

UNHCR

35th Meeting of the Standing Committee

Agenda Item 4. Programme Budgets and Funding

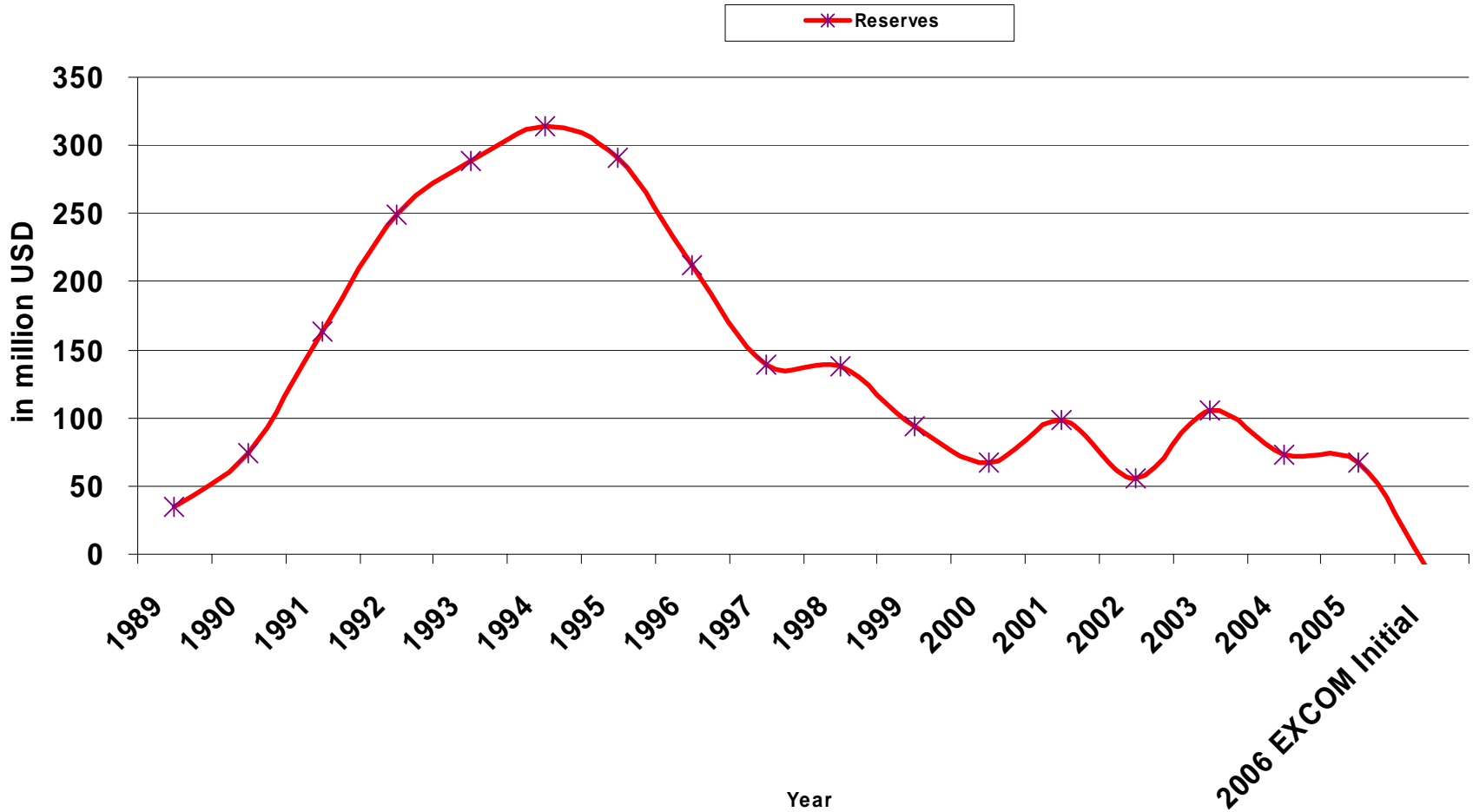
Presentation by the Controller

Tuesday, 7 March 2006

Key message:

The factors contributions to the current financial difficulty are: the depletion of reserves, the growing gap between the increasing budgets and funding, steadily increasing inflexible staff costs, concentration of expensive staff resources in Geneva, a weak defense mechanism against volatile foreign exchange market, among others. These are structural and systemic causes, therefore unless these root causes are properly addressed, UNHCR will face recurring financial crisis in the coming years.

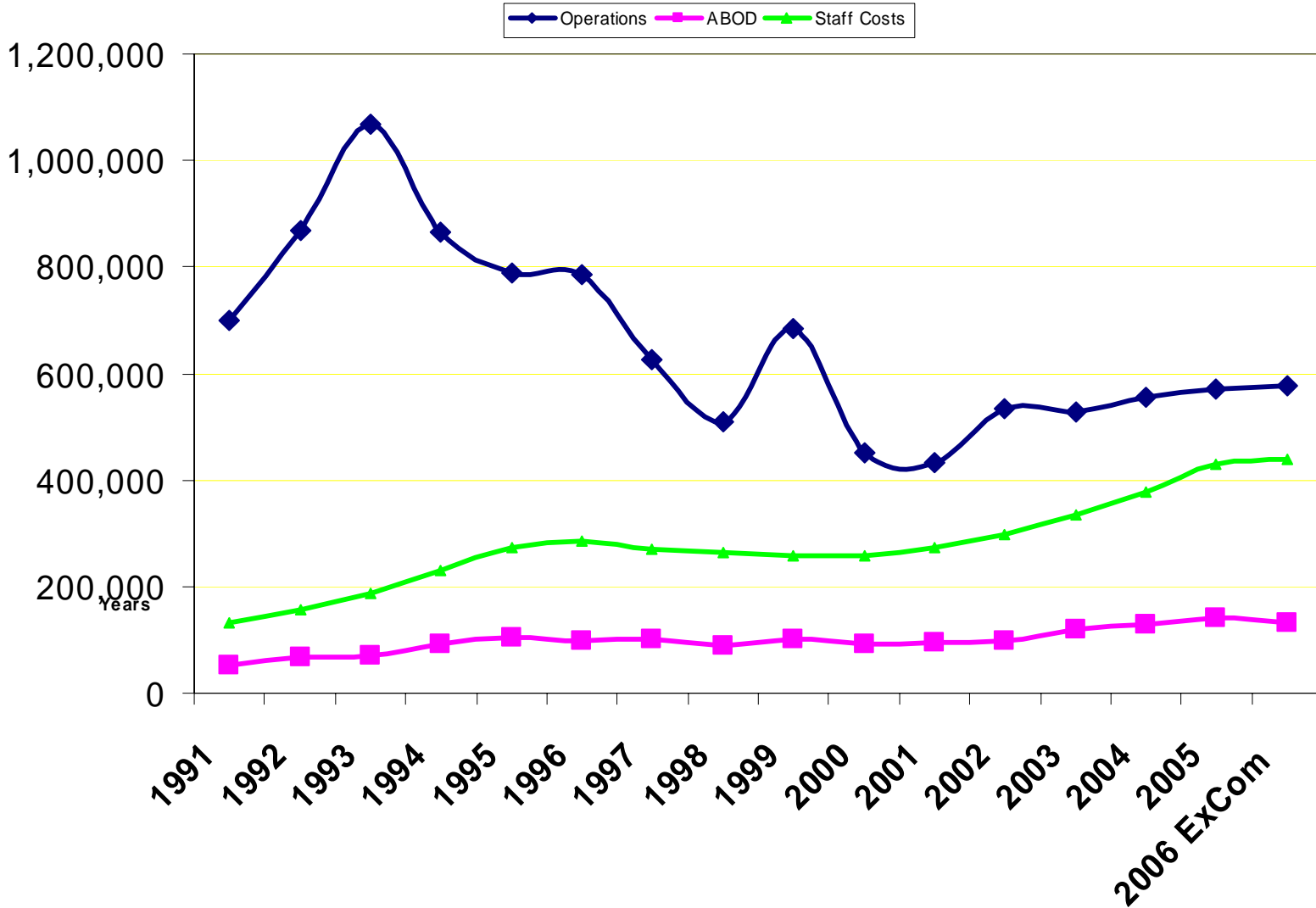
Fund Balance Trend: Unified Budget(AB+ SB+RB)



The total **reserves** have declined steadily since 1994 when they exceeded \$300M, becoming only 66M in 2005. We have no reserves to count on. From now on we must maintain strong fiscal discipline of not spending more than we earn, or earn more than we spend, otherwise financial crisis will recur every year.

This chart does not reflect **unfunded liabilities** (after-service health insurance, accrued annual leave and termination benefits) amounting to \$350M. They will be reported as liabilities under the Public Sector Accounting Standards applied to UNHCR latest by 2010. Had that been applied, our net reserve would be minus \$300M.

UNHCR EXPENDITURE - TRENDS BY CATEGORY
1991 - 2005 expenditure - 2006 EXCOM



Staff costs have been steadily increasing, particularly since 2000. In 2005 they counted close to 40%. The share of ABODs has remained steady at around 10%. The share of Operations has come down from 85% in 1990 to 62% in 2005.

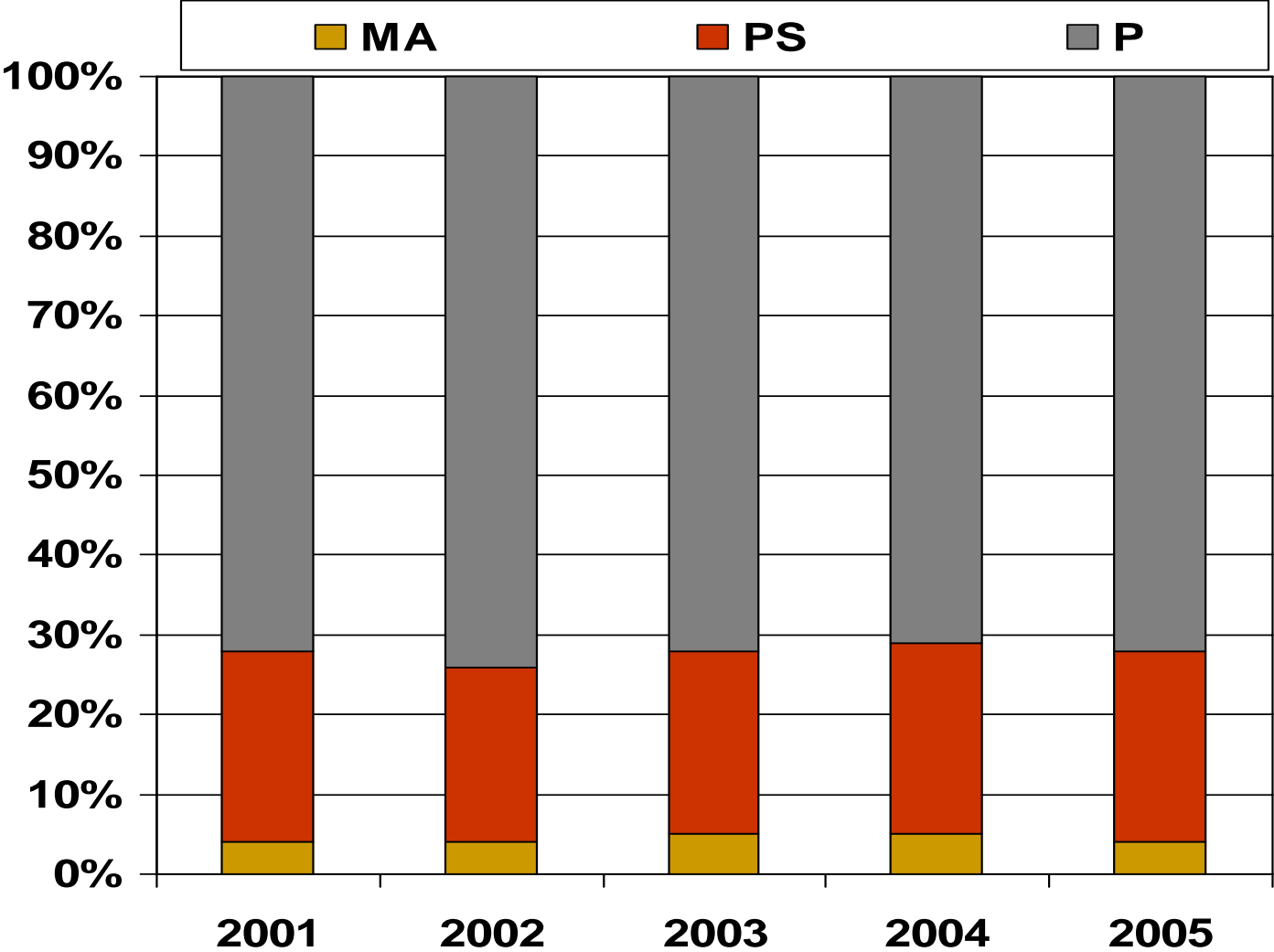
The steady increase in staff costs reflects changing needs. The need to have more protection staff and security officers in the Field is one. The regularization of so called “project staff” implemented recently is another.

The problem of staff costs is that they are "**fixed**" and inflexible in short term. UNHCR cannot engage in large scale staff reduction exercise at the time of acute funding shortfall, because **85%** of UNHCR staff members have indefinite contracts.

As a result, when funding falls short of expected levels, UNHCR has resorted to “capping” only allocations for ABODs and Operations. No staff costs have been capped. Repeated capping on Operations and ABODs meant a built-in bias or a structural bias for increasing share of staff costs (and decreasing share of Ops), leading to further loss of flexibility and worsening staff costs/Ops ratio. There are systemic problems here.

One important clarification: There is misperception that all staff costs are administrative cost, or that UNHCR is spending lots of money for itself. This is completely wrong, as the next slide shows.

Trend in Programme (P), Programme Support (PS) and Management & Administration (MA)



This slide presents another way to look at the UNHCR's overall cost structure in the last five years.

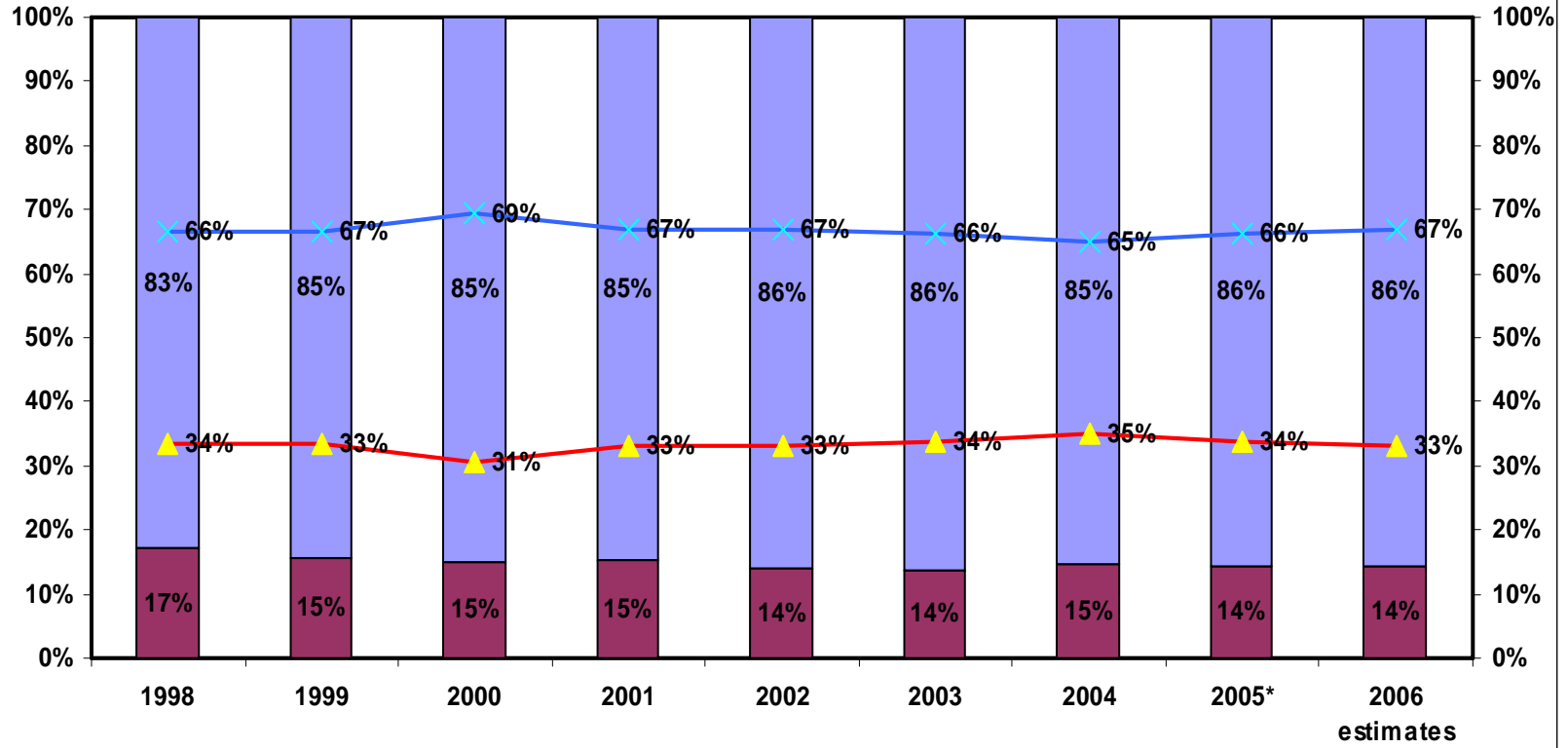
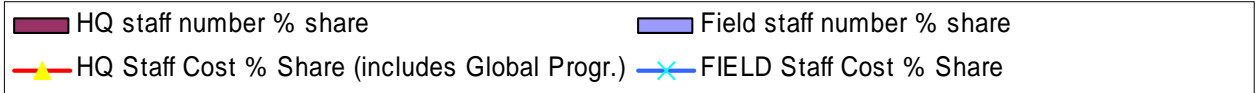
The grey part (72%) represents **Program costs** that include direct inputs for projects that affect refugees, such as protection officers and field offices in the Field. In terms of posts, **3000 positions fall under this category.**

Program Support costs are for the backstopping of development, formulation, delivery and evaluation of programs, including DIP and Dos at HQ and filed support positions. There are technical, thematic, logistical or administrative ones. **There are 2400 positions.**

The bottom yellow represents **Management and Administration costs (MA)**, found only at HQ, such as Executive Office or DHRM, DFSM. There are about **500 positions** (some 40% of the costs are covered by the UN Regular Budget).

UNHCR cost structure in terms of PG, PS and MA has been very stable. **Importantly, the administrative costs have been under control.**

HQ & Field Shares of Staff Numbers and Costs 1998 to 2006 (estimates)



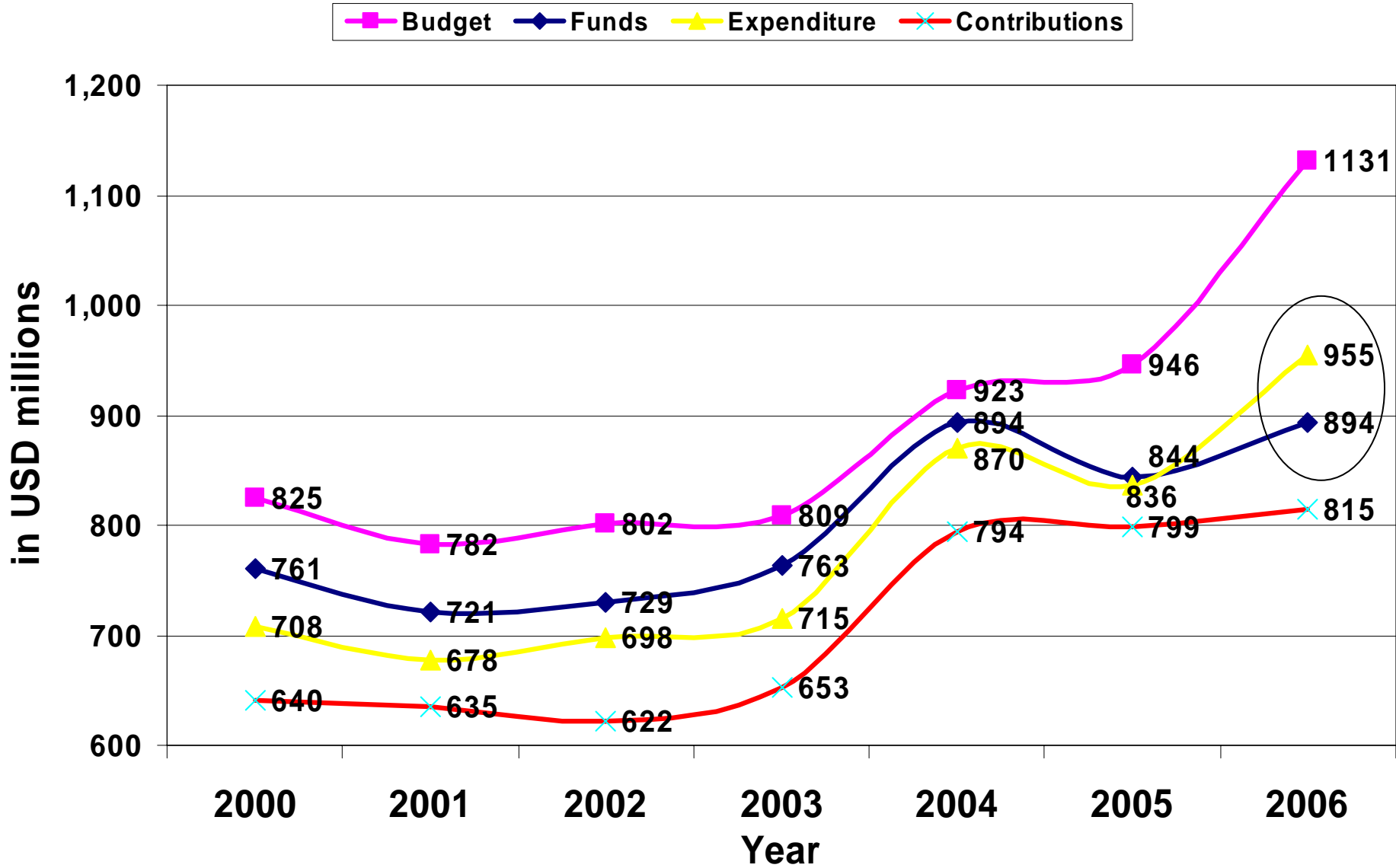
* In 2005, staff cost % share is estimate, and staff number % share is actual.

The total staff at HQ compared to total staff has been stable at around **14 %**, meaning that one out of six staff is at HQ. UNHCR is a relatively **decentralized organization** in terms of staff deployment.

However, the share of **staff costs at HQ** has been around **33%**. One reason is that some 30% of all professional staff members (450) are stationed in Geneva, one of the most expensive cities in the world. Second is GS salaries in Geneva are 3 times higher than those in the Field.

Presence of large number of (expensive) staff at HQ leads to larger premises, higher rents, higher utility costs, etc., resulting in higher fixed costs.

Annual Programme Budget 5-year Trend: 2000 - 2006

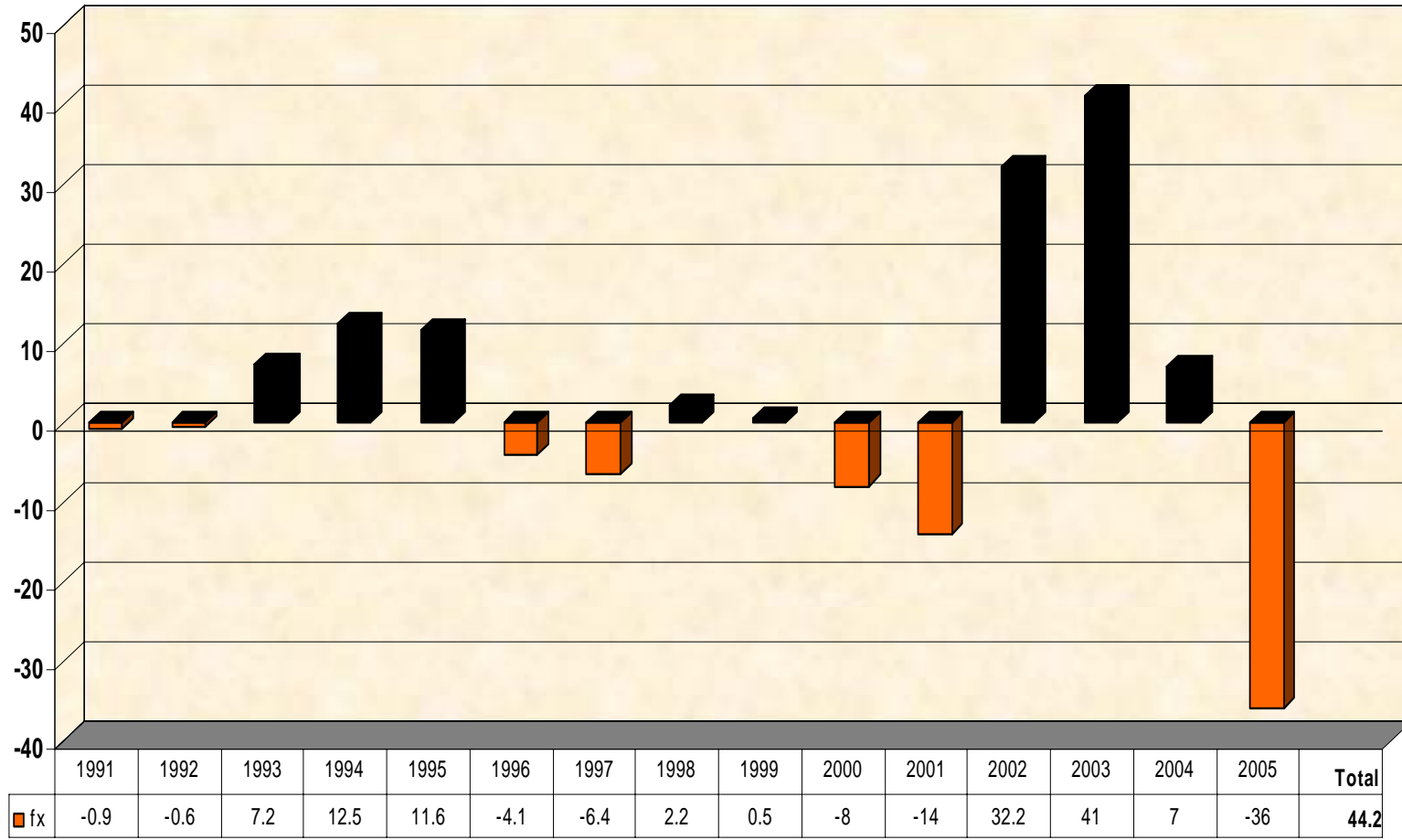


There is confusion as to the meaning of “**Deficit**”. What we mean by “deficits” is the gap between the “**funds**” and “**expenditures**” (the gap between the yellow line and the blue line). As for 2005, the gap (deficit) was \$12M and we financed this by borrowing from the Working Capital Fund.

There is a **widening gap** between the budgets and contributions.

The 2006 AB is much higher than 2005 AB due to mainstreaming of Chad / Burundi SBs as well as price changes. However, expected funding does not increase much, causing substantial deficit (even after 80% capping). The final deficit figure depends on the austerity measures and fund raising efforts.

UNHCR fx income: gains & losses (USD millions) 1991 - 2005



This slide shows the net exchange gains or losses over the last decade.

The long term impact of exchange rate fluctuation could be “neutral”, namely no gain, no loss. The sum of all foreign exchange gains and losses since 1991 is a positive \$44.2 million or an average of **\$3 million gains annually**. The exchange gains in 2002 and 2003 (32M and 41M) contributed to the relative financial stability in 2003 and 2004.

However, in the short term, UNHCR may face difficulty like 2005, when we lost \$36M. Unlike in the past when we had sufficient reserves, exchange loss of this magnitude easily triggers financial crisis. Nonetheless, foreign exchange fluctuations are part of life, and they are merely one of the contributing factors to the recent financial difficulty. It is not the cause.

Measures: One is the creation of a special account (or fund) to keep all gains and losses to spread risks across the years. Had we retained all exchange gains recorded in 2002 and 2003, that would have covered all losses in 2005. Another is to improve UNHCR’s budgetary control mechanism in such a way to dynamically increase / decrease budgetary allocations so as to control expenditures. Both can be called “natural hedging” approach. The third approach is to introduce more formal financial hedging mechanism, which is being considered.

For the moment, the better approach appears to be the current practice of taking advantage of the natural hedge positions.