

برنامج
الأغذية
العالمي



Programme
Alimentaire
Mondial

World
Food
Programme

Programa
Mundial
de Alimentos

**Executive Board
First Regular Session**

Rome, 4–6 February 2008

RESOURCE, FINANCIAL AND BUDGETARY MATTERS

Agenda item 6

*For information**



Distribution: GENERAL
WFP/EB.1/2008/6-D/1
25 January 2008
ORIGINAL: ENGLISH

UPDATE ON THE WFP MANAGEMENT PLAN (2008–2009)

* In accordance with the Executive Board's decisions on governance, approved at the Annual and Third Regular Sessions, 2000, items for information should not be discussed unless a Board member specifically requests it, well in advance of the meeting, and the Chair accepts the request on the grounds that it is a proper use of the Board's time.

This document is printed in a limited number of copies. Executive Board documents are available on WFP's WEB site (<http://www.wfp.org/eb>).

NOTE TO THE EXECUTIVE BOARD

This document is submitted to the Executive Board for information.

The Secretariat invites members of the Board who may have questions of a technical nature with regard to this document to contact the WFP staff focal points indicated below, preferably well in advance of the Board's meeting.

CFO* and Director, Finance and Legal Division: Mr A. Abdulla tel.: 066513-2401

Director, FLB**:

Mr S. O'Brien tel.: 066513-2682

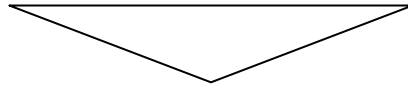
Should you have any questions regarding matters of dispatch of documentation for the Executive Board, please contact Ms C. Panlilio, Administrative Assistant, Conference Servicing Unit (tel.: 066513-2645).

* Chief Financial Officer

** Office of Budget and Financial Planning



DRAFT DECISION*



The Board takes note of “Update on the WFP Management Plan (2008–2009)” (WFP/EB.1/2008/6-D/1).

* This is a draft decision. For the final decision adopted by the Board, please refer to the Decisions and Recommendations document (WFP/EB.1/2008/15) issued at the end of the session.



INTRODUCTION

1. With the approval of the WFP Biennial Management Plan (2008-2009), the Secretariat reaffirmed its commitment to providing updates on the implementation of the Plan during the biennium. This is the first update for the current biennium.

BACKGROUND

2. The Biennial Management Plan (2008–2009) outlined the expected requirements of current operations and programmes for the biennium, which totalled US\$5.4 billion. The Programme Support and Administrative (PSA) budget of US\$345 million took into consideration the level of indirect support cost (ISC) income that could be expected from these requirements, based on historical funding levels and predicted reserve balances.
3. Recognizing that in a voluntarily funded organization funding required may not be available from donors, the Secretariat continuously reviews WFP's operational level, the expected level of associated funding and ISC income and the associated reserve balances, to ensure the PSA expenditure levels are sustainable.
4. The objective of this note is to update the Executive Board on these issues. Since the operational component of the Management Plan was finalized in June 2007 there have been unprecedented shifts in global markets, affecting many WFP operational inputs. The rapid increase in food prices, combined with fuel price rises and a continued decline of the US dollar against many other WFP operating currencies over the past six months, has changed many of the assumptions on which the operational Programme of Work was based.
5. This update note provides an overview of the changes in the Programme of Work since the approval of the Management Plan; an overview of the projected resource level to fund the programme of work; and a forecasted opening and closing balance of the PSA equalization account based on the approved PSA appropriations. It also outlines issues related to the US\$/Euro exchange rate and the effect this may have on the PSA budget.

CHANGES IN THE PROGRAMME OF WORK

6. The operational requirements outlined in the Management Plan 2008–2009 were US\$5.414 billion, for an intended distribution of 7.8 million mt of food. Since the compilation of the Plan, world markets – particularly for food commodities – have fundamentally changed. These unprecedented changes have led to significant cost increases, particularly for food and transport. In addition, a number of new operational requirements have emerged.

Re-Costing the 2008–2009 Programme of Work

7. The original WFP operational requirements for 2008–2009 were compiled between January and June 2007, using cost assumptions formulated at that time. The following section outlines the potential impact of subsequent market changes on the WFP Programme of Work.



⇒ *Commodity price increases*

8. Over the past year commodity markets have experienced unprecedented price growth and uncertainty. During 2007, the prices of wheat and maize (which traditionally represent almost half of WFP's commodity food basket) have reached record highs on international markets, with the international price of wheat doubling between May and September.¹
9. The FAO *Food Outlook* report from November 2007 highlighted:
 - an annual increase in “the FAO food price index ... of roughly 37 percent [with] the surge in prices being led primarily by dairy and grains”;
 - “the concurrence of the hike in world prices of, not just a selected few, but of nearly all major food and feed commodities”;
 - the price hike was “accompanied by much higher price volatility than in the past, especially in the cereals and oilseeds sector [highlighting] the prevalence of greater uncertainty”; and
 - the changes in the cereal market wheat prices were the “main protagonist”.²
10. Although “no straightforward” prediction of future commodity price changes can be made, the International Food Policy Research Institute (IFPRI) has concluded that “these high prices do not appear likely to fall soon”.³
11. As a result, the Secretariat has re-examined the pricing of WFP's commodity requirements for 2008–2009. The average commodity prices used in the original Management Plan were compared to the actual prices during late 2007. For all commodity groups, prices had increased between 15 and 25 percent.
12. Re-costing the original Programme of Work outlined in the Management Plan would result in US\$519.9 million of additional commodity costs for implementing the requirements outlined in the Plan. The cost of existing commodity requirements for 2008–2009 would increase from US\$2,426.9 million to US\$2,946.8 million.

⇒ *Landside transport, storage and handling (LTSH)*

13. More than 85 percent of WFP's landside transport, storage and handling (LTSH) expenditures are incurred in Africa. Operating expenses are continually and severely affected by increases in local costs due to inflation and exchange rate fluctuations. These increases affect LTSH in particular at the port entry level through higher port charges, levies and handling costs. Ports are more frequently congested and discharge of vessels is delayed, resulting in higher port services and forwarding fees on the land side and increased storage costs. The impact of the continuing weakening of the US dollar is estimated to add US\$43.9 million in LTSH requirements for 2008–2009.
14. Higher fuel, tyre and lubricant costs are additional factors contributing significantly to increases in transport costs. Fuel costs influence approximately 25 percent of total LTSH costs. Oil prices have increased by 35 percent since operational figures for the Management Plan were finalized in June 2007, adding US\$133 million of LTSH requirements to the existing budget. Relatively poor road conditions in Africa contribute further to high maintenance costs for the truck fleets. To prevent deterioration of the

¹ *Economist*. The end of cheap food. 6 December 2007

² *Food Outlook: Global Market Analysis*. 2007. November 2007

³ IFPRI. 2007. “The World Food Situation: New Driving Forces and Required Actions”



national road networks, governments are increasingly imposing axle weight limitations, increasing the number of trucks needed to transport a given amount of food.

15. For these reasons, the LTSH requirements outlined in the Management Plan are likely to increase significantly; the total increase is now estimated at US\$176.9 million.

⇒ *Direct support costs (DSC) and other direct operational costs (ODOC)*

16. The value of the US dollar relative to other currencies also has a direct impact on direct support costs (DSC) and other direct operational costs (ODOC), because a significant portion of expenditures for these cost categories (including local staff charges, recurring office costs and implementing partner costs) are also incurred in-country and mostly denominated in local currencies.⁴

17. As a result of the continued weakening of the US dollar against many local currencies during the second half of 2007, WFP will potentially have to revise upward its DSC budget by 5 percent and its ODOC budget by 2 percent. The re-costing is likely to increase the DSC budget from US\$626.1 million (as originally estimated in the Management Plan 2008–2009) to US\$657.7 million; and the ODOC budget from US\$292.1 million to US\$298 million.

⇒ *Summary of Impact*

18. While the above sections outline a conservative overall estimate of the likely impacts of rising food and fuel prices and the weakening dollar on existing 2008–2009 requirements, a comprehensive project-by-project technical budget review has been initiated by the Secretariat to formalize these increases and ensure they are correctly reflected in all project budgets. The results of this review will be communicated in the Management Plan update to the 2008 Annual Session of the Executive Board.
19. The Secretariat will continue to examine the impact of market and economic factors on WFP's Programme of Work. Given the current market uncertainties it is expected that the Programme of Work will be re-costed several times during the current biennium.

Additional Requirements

20. In addition to potential increases due to changes in the cost structure of the original requirements outlined in the Management Plan, as of December 2007 the Programme of Work had increased by US\$228 million, or 4 percent, as a result of new or increased operational requirements.
21. Half of the increase of US\$228 million is due to unforeseen projects, mainly emergency operations, and a number of projects originally planned to end in 2007 that were extended into 2008. These include:
- a new emergency operation to respond to Cyclone Sidr in Bangladesh, requiring US\$37.1 million;
 - a protracted relief and recovery operation in Pakistan to assist food-insecure households, requiring US\$14.7 million;
 - an existing emergency operation to assist drought-affected people in Kenya, extended until June 2008 and requiring US\$13.8 million;

⁴ Refer to "Analysis of WFP Cost Components" (WFP/EB.A/2006/6-G/1)



- an existing emergency operation in the Philippines, extended until March 2008 and requiring US\$4.2 million; and
 - other unforeseen projects to support emergencies in Bolivia, the Dominican Republic, the Gambia, Ghana, Nicaragua, Pakistan, Peru, the Syrian Arab Republic and Yemen.
22. In addition, increased requirements have been identified for projects in Ethiopia (US\$26.4 million) and Zimbabwe (US\$97.5 million).
23. The potential revisions to the Programme of Work, including all of the above changes, are shown in Table 1.

TABLE 1: POTENTIAL REVISED PROGRAMME OF WORK				
	Original Management Plan	Estimated re-costing	Additional operational requirements	Total
Operational budget by cost component (US\$ million)				
Commodity cost	2 426.9	2 946.8	128.4	3 075.2
External transport	593.2	593.2	18.1	611.3
LTSH	1 475.8	1 652.7	5.3	1 658.0
ODOC	292.1	298.0	38.0	336.0
DSC	626.1	657.7	38.2	695.9
Total operational budget	5 414.1	6 148.4	228.0	6 376.4
Programme of work (including 7% ISC)	5 793.1	6 578.8	243.9	6 822.7

Potential Additional Requirements

24. For WFP, the impact of higher food and fuel prices will be reflected in higher operational costs and also a possible increase in demand for food aid. There are signs that price rises could sharply increase both the incidence and depth of food insecurity.⁵
25. The profile of hunger may also be changing as households that depend mostly on markets face deteriorating conditions. These households will spend more on food to the detriment of non-food expenditures (such as education and health). This means that the effects of price increases might be detected first in lower school-attendance rates or worsening health indicators, rather than in an immediate drop in food consumption.

⁵ This section draws from the following publications:

Johnson, S. 2007. The (Food) Price of Success. *Finance and Development*, 44(4). International Monetary Fund (IMF).

IMF. 2007. *World Economic Outlook: Globalization and Inequality*.

IFPRI. 2007. *The World Food Situation: New Driving Forces and Required Actions*.

IFPRI. 2007. *The World's Most Deprived: Characteristics and Causes of Extreme Poverty and Hunger*.

IFPRI. 2007. *Taking Action on the World's Poor and Hungry People: A Way Forward*.

World Bank. 2007. *World Development Report 2008: Agriculture for Development*.

FAO. 2007. *Food Outlook: Global Market Analysis*, June.



26. However, in the poorest households, a direct and immediate impact of price increases on food insecurity is already evident. This is because the poorest households buy more food than they sell, spend a larger share of their income on food and have fewer coping mechanisms to fall back on. Groups most affected include the rural landless, pastoralists and small farmers; yet it is among the urban poor where we may well see the most acute impact.
27. Already, the poorest households consume predominantly cereals and only very small quantities of other nutritious foods. Higher prices translate into even poorer diets, as families shift the meagre income spent on other foods to purchases of energy-dense cereals. Moreover, literature shows that households reduce their food expenditures by 0.75 percent for every 1 percent increase in food prices, so we are likely to see more and more households also reducing the number and size of their meals.
28. This evidence suggests that we are entering a new era of hunger at a time when the absolute number of hungry people in the world continues to increase. While there are few global estimates of the impact of higher food prices on food security, a wide range of institutions, including WFP, the Food and Agriculture Organization of the United Nations (FAO), IFPRI, the United States Department of Agriculture, the World Bank and the International Monetary Fund (IMF) are focused on, and deeply concerned by, actual and potential impacts on the poorest households. WFP will continue to work with these institutions to quantify the implications and will keep the Executive Board apprised of specific increases in food-insecure populations that might result.

Projected Resource Levels

29. Donor response, as well as operational, cost and other uncertainties, will have a significant impact on the resources generated during the biennium.
30. While the Management Plan (2008–2009) was based on an overall income projection of US\$5.2 billion, the impact on funding levels of the above changes to the Programme of Work – in particular, the impact of increased food and fuel prices, and the continued weakening of the US dollar – has yet to be determined.
31. However, given the 20 percent increase in the Programme of Work, unless resource availability rises correspondingly, WFP will have to either reduce rations to beneficiaries or reduce the number of beneficiaries being assisted. Until the impact of the above changes on funding levels becomes clearer, the Secretariat is not proposing any change to the ISC income forecast or the PSA level.

STATUS OF THE PROGRAMME SUPPORT AND ADMINISTRATIVE EQUALIZATION ACCOUNT

32. The latest forecast for the PSA equalization account, based on the approved PSA appropriation, is therefore unchanged from the Management Plan (2008–2009) as shown in Table 2.



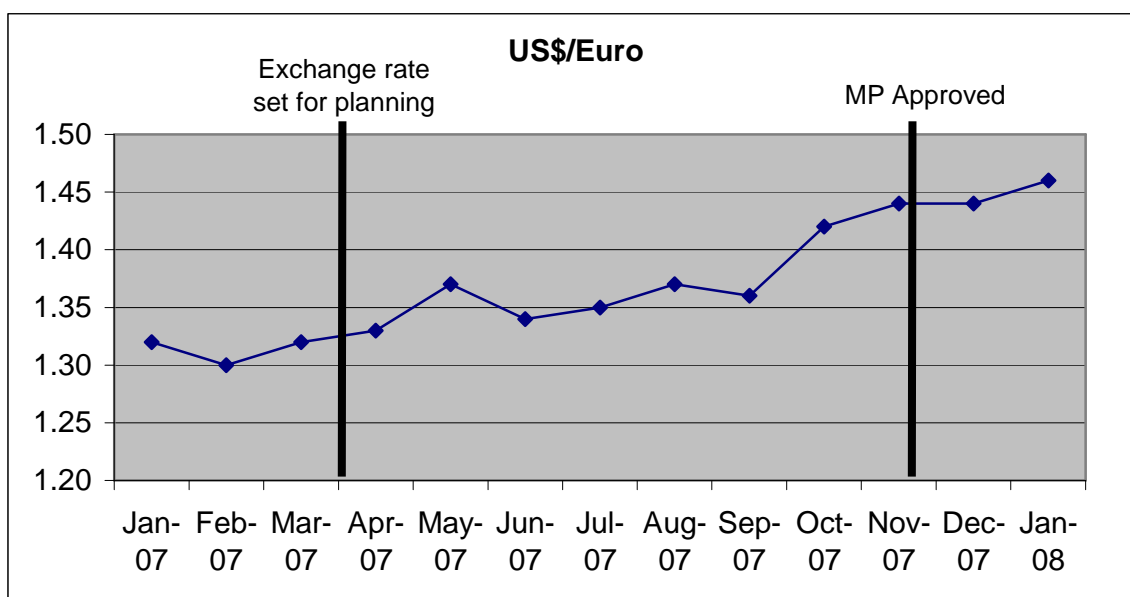
TABLE 2: PSA EQUALIZATION ACCOUNT, 2008–2009	
	PSA Equalization Forecast 2008–2009
1 January 2008 estimated opening balance	11
Transfer of DSCAF*	24.1
2008–2009 ISC income	311
2008–2009 PSA expenditure	(345)
Income from unforeseen emergency operations	-
31 December 2009 forecast	1.1

* Direct Support Cost Advance Facility

33. The forecasted balance of the PSA Equalization Account for the end of the biennium is currently estimated to be in line with the Management Plan, before the impact of exchange rate fluctuations outlined below is taken into account.
34. The Secretariat recognizes the importance of keeping a healthy positive balance in the PSA Equalization Account and will continue to monitor both ISC income and PSA expenditures to ensure that they are in line with projections. The Executive Board will be updated on the status of the account throughout the biennium.

Impact of Exchange Rate Fluctuations

35. Exchange rate changes can have a major impact on the PSA budget. As outlined in the Management Plan, the current PSA budget appropriation of US\$345 million is built on the assumption of a US\$/Euro exchange rate of 1.33. Most PSA costs are incurred in Euros although the budget appropriation – and consequently the authority given by the Board to the Secretariat – is expressed in dollars.
36. The figure below outlines the evolution of the exchange rate between the US\$ and the Euro, based on the official United Nations rate of exchange.



37. During and subsequent to the formulation and approval of the Management Plan 2008–2009, the exchange rate between these currencies has changed significantly and presents a challenge for budgetary management. The rate in mid-January 2008 was US\$/Euro 1.46, which is 0.13 cents above the Management Plan rate.
38. The Secretariat has calculated that every one-cent change in the US\$/Euro rate has an impact of US\$1.06 million on the PSA budget. If the exchange rate between the US\$ and the Euro remains, on average, at the current level of 1.46 for the full biennium this would have an impact of approximately US\$13.8 million in additional expenditure.
39. In order to provide exchange rate certainty on the Euro-based portion of the PSA budget, a decision on hedging would need to be made in March or April of the year in which the Management Plan is prepared, the point at which the exchange rate is set for the purposes of constructing the budget. However, the budget is normally presented to and approved by the Executive Board in October or November.
40. The Secretariat will review the decisions and approvals required to enable a hedge earlier in the budget preparation process and fully mitigate the foreign exchange risk of Euro-based PSA expenditure. The findings will be presented to the Executive Board in due course for the preparation of the next Management Plan.

ACRONYMS USED IN THE DOCUMENT

DSC	direct support costs
DSCAF	Direct Support Cost Advance Facility
FAO	Food and Agriculture Organization of the United Nations
IFPRI	International Food Policy Research Institute
IMF	International Monetary Fund
ISC	indirect support cost
LTSH	landside transport, storage and handling
ODOC	other direct operational costs
PSA	Programme Support and Administrative