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United Nations Office for Project Services

Progress report of the Executive Director on the activities of the United Nations Office for Project Services*

Summary

The report provides an overview of projected 2004 budget performance, the revised budget estimates for 2005 and updates on the evolving corporate strategy.

Elements of a decision

The Executive Board may wish to:

(a) Welcome the significant level of business acquisition in 2004, demonstrating demand for UNOPS services;

(b) Note the preliminary 2004 statement of revenues and expenditures;

(c) Note the revised 2005 budget estimates which demonstrates that UNOPS will operate within a balanced budget;

(d) Note the evolution of the corporate strategy;

(e) Request that the Executive Board be kept informed of progress achieved in business acquisition and delivery; and

(f) Request that UNOPS present to the September 2005 session of the Board a report on further measures to be taken in 2006 to implement the corporate strategy, enhance the efficiency of business operations and reduce the cost base of UNOPS.

* The compilation of data required to provide the Executive Board with the most current information has delayed the submission of the present report.

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I. Introduction

1. Pursuant to Executive Board decision 95/1 of 10 January 1995, the present report has been reviewed by the Management Coordination Committee.

2. The United Nations Office for Project Services (UNOPS) projects that it will complete 2004 with a year-end fund balance of $9.21 million, including $6 million held in the operating reserve. While earned revenues fell below projections, change management expenditures were contained and the implementation of some change initiatives was deferred. Business acquisition was encouraging, standing at $663 million as of 30 November 2004. Portfolio growth was strong in post-conflict transition countries, while among clients, international financial institutions represented the strongest growth trend. The achievement of UNOPS in growing and diversifying its business portfolio demonstrates, inter alia, that there is demand for UNOPS services and recognition of the added value that UNOPS provides.

3. In 2004, UNOPS reorganized its client service and procurement operations. Significant human resource capacity was decentralized to better serve clients. A new management team was hired in mid-2004. The implementation of the Atlas system was initiated – with some difficulties, which are being addressed through the Atlas stabilization and optimization project. As part of ongoing efforts to strengthen internal governance and control mechanisms, a planning and budget advisory committee, an audit committee and an information and communications technology (ICT) steering committee were established.

4. UNOPS management recognizes that 2005 remains a critical year in the organization's turn-around. UNOPS recognizes the need for a balanced budget to ensure that, as a self-financing entity, expenditures are fully covered from revenues earned and thus submits a projection for 2005 of revenue of $53.77 million and expenditures of $50.86 million. With a projected 2004 year-end fund balance at $9.21 million, the year-end fund balance for 2005 is projected to reach $12.12 million.

5. In 2005, plans for the UNOPS multi-year change programme will focus on critical and essential actions responding to the recommendations of the United Nations Board of Auditors (DP/2005/12), on refining the corporate strategy and defining further business process and structural changes to take place in 2006.

II. Budget performance 2004

A. Overview

6. This section presents the preliminary estimates for the year-end revenue and ending fund balance for UNOPS (see annex). The projected year-end revenues and expenditures constitute a 'most likely case' scenario. The estimates were derived from the UNOPS financial management systems, Atlas, and the integrated management information system, and are based on best available data combined with estimates and assumptions as of 30 November 2004.

7. In 2004, as approved by the Executive Board in January 2004, UNOPS proceeded with the implementation of an internal change process (DP/2004/7).

The plan was to address: (a) business acquisition and strategy; (b) enhancement of mission, vision and values; (c) project management and pricing; (d) organizational structure; and (e) business process improvements. However, in his progress report to the Executive Board in September 2004 (DP/2004/45), the Executive Director noted that the priorities for change would be amended to focus more clearly on the recommendations in the report of the United Nations Board of Auditors. At that time the new challenges arising from the External Auditors' disclaimer on UNOPS financial statements were seen as (a) clarifying corporate and business strategies to position the organization towards a value-adding and sustainable future, and (b) defining a multi-year management and investment effort to address financial and other systems deficiencies. Those initiatives constituted a first necessary phase in the repositioning of UNOPS. That phase was also preparatory to a more fundamental realignment, which is expected to take place in 2006.

8. UNOPS refined its mission and vision by early 2004 and implemented an aggressive business acquisition initiative throughout the year. It also proceeded with the decentralization of project portfolios to improve services to clients. New management was installed. UNOPS reorganized its client service and procurement operations and decentralized staff out of New York into regional structures. The reorganization affected 194 positions and, combined with the introduction of Atlas, was disruptive in the short term and a factor contributing to below-target delivery of project budgets and services for the calendar year. As a result, according to current projected actuals of revenue and expenditure, expenditure will exceed revenue by $13.99 million (including $3.5 million in installation expenditure payments for the Atlas rollout).

9. The fund balance at the end of 2004 is being estimated at $ 9.21 million, comprising an operating reserve balance of $6 million and a working capital of $3.21 million.

B. Delivery: project portfolio of services

10. As of 30 November 2004, UNOPS estimates that total 2004 delivery will be $381.59 million.

C. Revenue analysis

11. UNOPS generates revenue from several sources. These include: portfolio revenue (fees earned on the provision of implementation services for clients); services revenue from the International Fund for Agricultural Development (IFAD); revenues from reimbursable service agreements, the Global Fund to Fight AIDS, Tuberculosis and Malaria (GFATM) and the Global Alliance for Improved Nutrition (GAIN); the servicing of the Programme of Assistance to the Palestinian People (PAPP), and other revenue (rent and interest).

12. 2004 revenue is projected at $38.41 million. Broken down in percentage terms, the revenue generated from the project portfolio of services is estimated at 60.1 per cent; revenue generated from direct service provision is estimated at 36.5 per cent; and revenue from rental and interest represents 3.4 per cent of total projected 2004 revenue.

D. Expenditure analysis

13. Total expenditures for the year are projected at a level of $52.41 million.

14. Of total projected expenditures, salaries and benefits are estimated at $26.16 million and general and administrative expenditures are estimated at $12.05 million. Reimbursements to UNDP and other United Nations organizations for 2004 are estimated to reach $8.52 million, including the Atlas-related payment to UNDP. The latter payment will be $3.5 million, or $1 million higher than initially projected.

15. Expenditures under the approved change management budget are projected to stand at $4.88 million. The combined total expenditure of $4.88 million remains below the approved $8.1 million 2004 budget for change initiatives.

III. Business acquisition in 2004

A. Overview

16. Business acquisition in 2004, encompassing acquisition for delivery in 2004 as well as in subsequent years, was encouraging, and particularly strong growth took place for project portfolios in post-conflict transition countries and with international financial institutions.

17. As of 30 November 2004, new business acquired under the project portfolio of services reached $663 million. Budget increases in the ongoing project portfolio of services are not recorded in this figure. Some $458 million relates to business acquisition in post-conflict and transition environments, with notable acquisitions in Afghanistan; $191.5 million in acquisition relates to development support activities; and $13.7 million to global services.

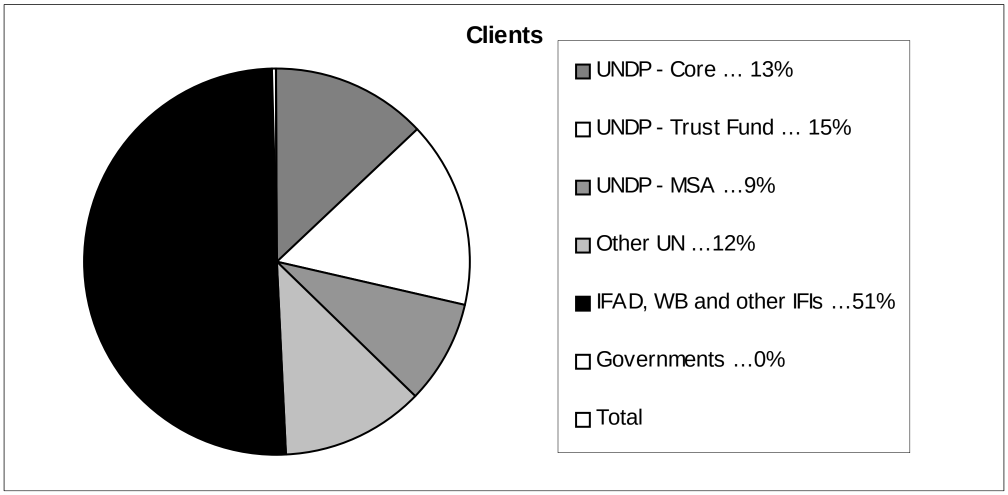
18. The Afghanistan Project Implementation Facility (APIF) had acquired new business in the amount of $331.3 million as of 30 November 2004. The Global Projects Division, the Eastern and Southern Africa Division and the Central Asia, North Africa and Near East Division acquired business totalling $252.8 million. Business acquisition efforts in Latin America and the Caribbean, West and Central Africa and the Asia-Pacific region total some $79.1 million.

19. A detailed analysis of targeted markets will be undertaken in 2005 to determine, inter alia, what direction UNOPS will elect to take in Latin America and the Caribbean as well as in the Asia-Pacific region. The low level of UNOPS activity in West and Central Africa requires urgent attention, and will be the subject of review early in 2005.

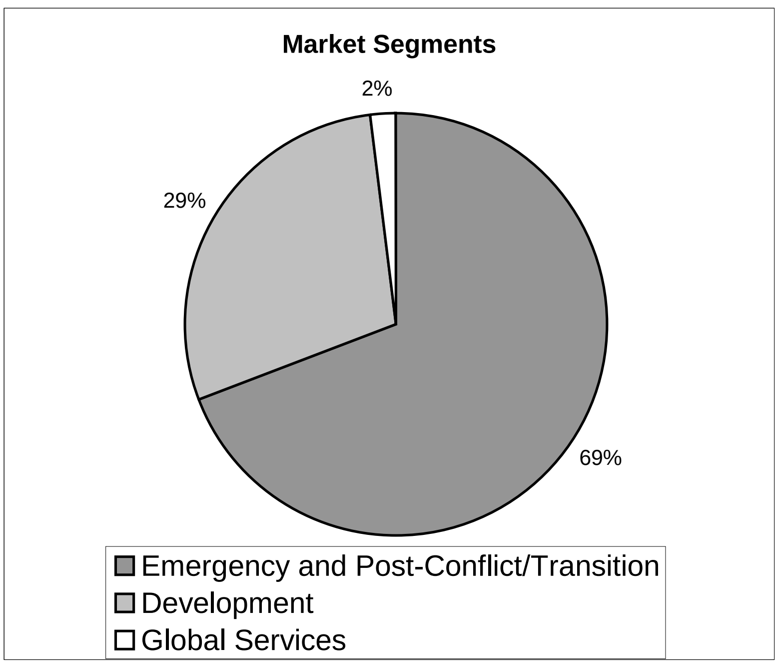
B. Client and market segment analysis

20. *Graph 1* below, shows business acquisition by client share; g*raph 2* groups acquisition into its market segments; and *graph 3* illustrates the trend in acquisitions from 2000 to 30 November 2004. UNOPS business acquisition shows considerable growth in emergency and post-conflict or transition projects. The development project portfolio continued to grow at a steady rate and accounts for about $191.5 million in new project budgets. While the shift in the composition of the UNOPS portfolio towards emergency, post-conflict and related activities is evident, UNOPS remains heavily involved in servicing activities in support of development. It is encouraging to note that new business acquired from international financial institutions in 2004 in the post-conflict and development markets is equivalent to $134 million in project budgets.

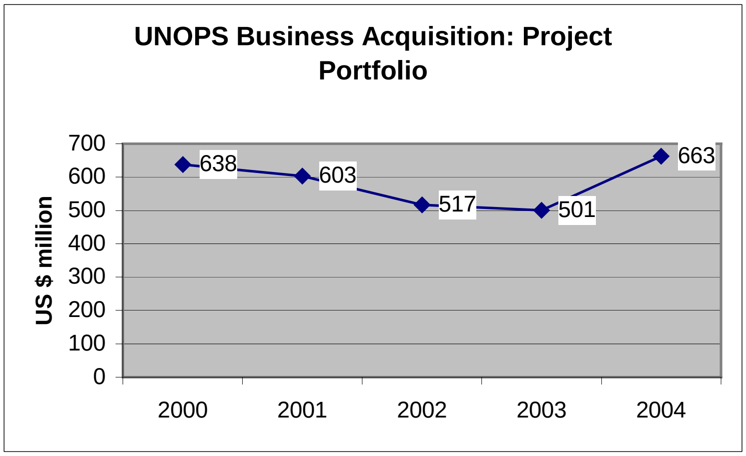
Graph 1. 2004 business acquisition under the project portfolio, by client



Graph 2. 2004 Business acquisition under the project portfolio, by market segment



Graph 3. Trends in business acquisition under the project portfolio, 2000-2004 (as of 30 November 2004)



IV. Business objectives and revised budget estimates for 2005

A. Overview

21. The 2005 budget proposal foresees revenues in the amount of $53.77 million and expenditures of $50.86 million, resulting in a projected net income of $2.91 million. As a result, based on the projected ending fund balance for 2004 of $9.21 million, the total 2005 year-end cumulative fund balance is projected at $12.12 million.

B. Objectives for 2005

22. As a result of a successful business acquisition drive during 2004, UNOPS expects to achieve revenue growth in 2005. The portfolio will be managed along two tracks. The t*rack 1* operations are comprised of large-scale post-crisis and reconstruction projects, building on the operating model applied in Afghanistan during 2002-2004. Delivery in 2005 is estimated at about $226.6 million from this track (see table 1 below).

23. Essentially, the model is based on building up a substantial portfolio of large-scale projects, achieving high levels of delivery and efficiency over a short period of time through efficient project management. UNOPS works with several types of clients, including host governments in the infrastructure and public works fields, and with and the World Bank. UNOPS recruits the best available expertise in specialized areas such as engineering, logistics, administration, information technology, communications and elections. These contractors are hired on a short-term basis; and, once their project has been implemented, they are either redeployed to another project or released from UNOPS employment. The benefits of this model are: higher net revenues than for other types of projects implemented by UNOPS; lower fixed costs; and speedy, visible results that satisfy clients and lead to more business.

24. UNOPS provides start-up funds from its administrative budget only in order to leverage the first one or two projects. Thereafter, the earnings from these projects serve to leverage additional projects and to replenish the administrative budget.

25. UNOPS anticipates that major donor investment in the post-crisis and transitional programmes, including Afghanistan, Haiti, Liberia and Sudan, as well as in Iraq, will provide the opportunity in 2005 to increase business volume in infrastructure, public works and related activities.

26. The business model described above will be evaluated during 2005 and if successful, will become the basis for transforming UNOPS' project management methodology and organizational arrangements in future years.

27. The *track 2* portfolio covers project implementation services and is restricted to projects in the areas of environment, governance, rural development, agriculture and other projects in countries pursuing the achievement of the Millennium Development Goals (MDGs). The 2005 estimated portfolio is $414.8 million in project budgets and services contracts. UNDP continues to be the main client for the track 2 portfolio, the relative decline of which, within the overall project portfolio of UNOPS, is expected to continue in future years. Nevertheless, the World Bank and other international financial institutions (IFIs) account for a growing proportion of the portfolio. The long-standing UNOPS partnership with IFAD, and services for GFATM and GAIN, will continue in 2005.

C. Project delivery estimates

28. The project delivery forecast for 2005 is $641.40 million. This is comprised of already approved budgets and project funds shortly to be received, and for which a documented exchange of communication between the client and UNOPS is on record as a precursor to project formulation.

29. The table below presents established delivery targets grouped by UNOPS business unit. These units have sizeable business recorded in the Atlas system. It is recognized that possible instability in post-conflict transition countries where UNOPS has significant portfolios may affect delivery targets.

2005 project portfolio delivery projections, by business unit (rounded in millions of dollars)

Business unit	Signed project budgets (A)	Hard pipeline (B)	Total (A) + (B)	Projected 31/12/05 Delivery	Delivery projection as percentage of total (A) + (B)
Latin America & Caribbean RO (LAC)	51	75	126	77.7	61.7
West & Central Africa RO (WCARO)	25	7	32	20.1	62.8
East & Southern Africa RO (ESARO)	12	31	43	30.2	70.2
C. Asia, N. Africa, N. East &EU RO (CANANE)	65	76	141	118.8	84.3
Asia-Pacific RO (APRO)	39	0	39	25.5	65.4
Global/Interregional Office (GLO/INT)	113	117	230	142.5	62.0
APIF (Incl. Afghanistan., Haiti, Liberia & Sudan)	371	63	434	226.6	52.2
Total	676	369	1,045	641.4	61.4

D. Revenue estimates

30. Estimated 2005 total revenue is $53.77 million, which is composed of: (a) revenue derived from project portfolio implementation services at $42.14 million; (b) service revenue of $9.82 million derived from supervision and loan administration services to IFAD projects and from GFATM, for which UNOPS is the local fund agent in various countries; and (c) rental revenue derived from subleasing UNOPS headquarters premises, interest income and other miscellaneous income totalling $1.81 million.

31. Planned revenue is higher in 2005 than 2004 levels for three reasons. First, during 2004, and particularly in the last quarter, UNOPS acquired a substantial portfolio of projects for delivery in 2005. In fact, Table 1 shows that by the end of 2004 there was already a significant 'hard pipeline' for 2005. Planned delivery in 2005 is estimated to approximately average 61.4 per cent of total budgets (including 'hard pipeline'). This is considered to be achievable given that delivery rates in 2003 and before have generally exceeded the 70 per cent level.

32. Second, ongoing multi-year projects will continue into 2005 (including carry-overs from 2004). Under-delivery in 2004, caused by various factors, has resulted in a significant carry-over to 2005.

33. Third, staff can focus on delivery, and not be diverted by the kind of major operating system rollout and organizational restructuring that took place in 2004.

34. One important measure that will be implemented in 2005 is to delegate to regional directors and division chiefs authorities and accountability in accordance with their responsibilities. The managers of decentralized offices will be so delegated in January 2005, providing the framework for these offices to operate in a businesslike manner, without the need for time-consuming approvals from headquarters. Planned improvements in management reporting and internal controls – in accordance with the recommendations of the external auditors – are essential for such delegation of authority to become effective. Performance contracts between members of the Senior Management Team and the Executive Director are proposed for implementation in 2005.

35. Business development for 2006 and beyond remains a priority, and UNOPS will engage more actively in United Nations system activities so that the organization participates fully when programming and service provision decisions are taken.

E. Expenditure estimates

36. Total 2005 expenditures are estimated at $50.86 million, comprised of the following elements: (a) Salaries and benefits: $28 million; and (b) General and administrative costs: $10.05 million, for a total of $38.05 million. Change management expenditures are estimated at $4.70 million as well as a provision of $0.7 million for doubtful accounts. Reimbursements to UNDP and other United Nations organizations for 2005 are estimated at $7.41 million, including Atlas-related payments to UNDP.

37. Salaries and benefits will increase by $1.84 million over 2004 projected actuals. Increases in salaries reflect anticipated changes in post adjustment and

some increase in staffing levels to handle peak activities associated with the projected demands of higher delivery levels.

38. UNOPS will reduce ongoing operating expenses by $2 million in 2005 as compared to current estimates for 2004. Atlas-related payments to UNDP and reimbursements to United Nations organizations will account for $7.41 million. Other projected expenditures totalling $4.70 million are related to the continued implementation of the change management programme approved by the Executive Board in January 2004, including Atlas stabilization and activities to address the systems deficiencies identified in the report of the Board of Auditors. These are detailed in the UNOPS report on implementation of the recommendations of the Board of Auditors for the biennium 2002-2003 (DP/2005/12).

F. Projected movement of operational reserve and fund balance

39. Under the above 2005 plan and budget estimates, the 2005 year-end net income from operations is $2.91 million. The 2005 year-end fund balance is forecast to be $12.12 million, building upon an expected 1 January 2005 opening balance of $9.21 million.

G. Conclusion

40. UNOPS management views the 2005 plan and budget as underpinning an interim strategy that will force a more radical realignment of UNOPS operations in 2006. UNOPS management proposes to work out a strategy to address the fundamental problems of income volatility and high fixed costs that characterize the existing organizational arrangements. In this connection, the UNOPS management is following the advice of the Management Coordination Committee and will evaluate the options for configuring future UNOPS operations.

V. Corporate strategy: Vision 2006-2007

41. At its second regular session, in September 2004, the Executive Board requested the Executive Director to articulate a strategy for attaining financial viability. Considerable diagnostic analysis of the organization has been undertaken through the conduct of the Independent Review and other studies. The findings have been discussed with the Executive Board, which approved a number of change management measures that are currently being implemented. Further analysis has subsequently been undertaken, and UNOPS has developed a set of strategic business development objectives for market positioning. Through a combination of increased responsiveness to market trends, portfolio expansion and greater internal efficiencies, UNOPS intends to move towards sustained financial viability in 2006-2007 through the achievement of four strategic objectives:

(a) Revenue growth;
(b) Increased operational efficiency;
(c) High client satisfaction; and
(d) Good governance and oversight.

42. UNOPS is a United Nations entity that provides project management services to United Nations departments and organizations, to the World Bank and regional development banks, and, in the field of infrastructure and public

works, directly to partner governments. The services that UNOPS provides are: (a) programme support and complex project management; (b) loan administration and project supervision; and (c) procurement of goods and services, including human resources administrative and advisory services. Through these services UNOPS helps its clients to achieve their own mandates, which include: promoting peace, national reconstruction and state-building, equitable development, and capacity-building worldwide.

43. UNOPS operates in two primary market segments: (a) rapid-response, complex logistics and reconstruction activities in countries transitioning from crisis and conflict; and (b) development support activities to UN system clients, international financial institutions and host governments (the latter related to infrastructure development) in countries addressing poverty reduction and the achievement of the MDGs.

44. More specifically, in countries transitioning from crisis and conflict, UNOPS has demonstrated the ability to respond quickly and deliver effectively on a large scale, under varying conditions of security. Indeed, the 2004 business acquisition level may testify not only to the demand for UNOPS services but also to the value that the speed, flexibility, project mentality and results-orientation of UNOPS adds to the work of its clients.

45. It is therefore the goal of UNOPS to work with other United Nations system entities, international financial institutions and host governments to expand its role in large-scale, rapid-response reconstruction projects and complex logistical initiatives in countries transitioning beyond crisis and conflict. Based on the lessons of the operating model applied in Afghanistan during 2003-2004, UNOPS anticipates that major donor investment in the post-crisis programme countries will provide the funding base within which other United Nations entities, and in some cases the host governments, will continue to request UNOPS services.

46. The existing portfolio of development projects and services-only provision will continue to evolve over the next two years. For this market segment, UNDP remains the predominant client of UNOPS. While UNOPS will seek to continue improvements to the quality of service delivery to UNDP, it expects continued erosion in the portfolio as direct execution is expanded. Management services agreements (MSAs) may also decline in value as UNOPS undertakes direct contracts with IFIs and with governments for infrastructure works.

47. A new, more diversified approach is required if UNOPS is to maintain and increase service provision volume in support of existing clients that work with governments to address poverty reduction, sustainable development and achievement of the MDGs. In 2005, UNOPS will continue to pursue market expansion to work directly with governments in infrastructure and public works, as well as with the World Bank and regional financial institutions. UNOPS will actively pursue additional partnerships with the full range of United Nations entities. At the same time, the durable viability of UNOPS will require a reduction in the cost base of its operations.

48. Finally, some opportunities emerged during 2004 in the area of United Nations system common services to support missions and country teams, particularly in post-conflict and transition countries. UNOPS has become a member of the Working Group on Common Services, to which it will contribute its experience in this area.

49. UNOPS is valued for its ability to provide professional solutions to help clients achieve their objectives. Clients appreciate UNOPS speed, transparency and cost effectiveness. However, UNOPS must continuously seek to increase its value to United Nations system and other clients by: (a) bringing projects to completion within time and cost budget; (b) providing timely reporting on and management of project finances; (c) having well-developed expertise in translating expressed client requirements into feasible activities; (d) developing a reputation for being trustworthy, ethical and easy to work with; and (e) operating in full compliance with the principles of the United Nations. This presents a considerable challenge to UNOPS; in order to deliver on client expectations, UNOPS must proceed expeditiously in creating new capacities.

50. UNOPS intends to put in place new business processes that are both cost-effective and driven by appropriate information and communication technologies. Furthermore, to keep operating expenditures under control; UNOPS must reorganize its internal operations and restructure its cost base in 2006. This may require further relocation of certain functions to more economic cost centres, as well as the aggressive reduction of the cost base.

Annex

Statement of revenues, expenditures and changes in fund balance

2004 budgeted and projected actuals and 2005 (budgeted)

(in millions of dollars)

Section 1: Delivery

	2004 budget	2004 projected actuals	2005 (budgeted)
Delivery Amount	485.00	381.59	641.40

	2004 budget	2004 projected actuals	2005 (budgeted)
Section 2: Revenues and expenditures			
Revenue from implementation of project portfolio			
Excluding UNDP MSAs		22.38	
UNDP MSAs		4.71	
Total project revenue	35.00	27.09	42.14
Revenue from "service only"	8.00	8.86	9.82
IFAD		7.57	
PAPP		0.18	
Reimbursable service agreements		1.12	
Other revenue (interest, rent)	1.00	1.28	1.81
Savings on prior biennium purchase orders		3.20	
Estimated revenue reduction from 2004 unliquidated obligation cancellations		(2.02)	
Total revenue	**44.00**	**38.41**	**53.77**
Salaries and benefits		26.16	28.00
General and administrative		12.05	10.05
Salaries and benefits, general and administrative	44.00		
Change management	10.00	4.88	4.70
Subtotal – ongoing operating expenses	54.00	43.09	42.75
Provision for doubtful accounts	0.00	0.80	0.70
Subtotal - doubtful accounts	0.00	0.80	0.70
Atlas-related payments to UNDP	2.50	3.50	3.50
Reimbursements made to United Nations entities		3.91	3.91
Other accrued liabilities – outstanding United Nations invoices		1.11	0.00
Subtotal – United Nations entity payments	2.50	8.52	7.41
Total expenditures	**56.50**	**52.41**	**50.86**
Income/(Loss) from operations	**(12.50)**	**(13.99)**	**2.91**
Section 3: Fund balance roll-forward			
Beginning fund balance, including $6 million operating reserve	23.20	23.20	9.21
Income/(Loss) from operations	(12.50)	(13.99)	2.91
Ending fund balance, including $6 million operating reserve	**10.70**	**9.21**	**12.12**
Section 4: Contingent liabilities			
After -service health insurance	4.00	4.00	4.00
Total contingencies	**4.00**	**4.00**	**4.00**