

# Financial Overview

From the Vice President for Finance and the Treasurer

The University's financial performance in 2018 was solid, with revenue rising to \$5.2 billion based on 4% growth, an operating surplus of \$196 million, and endowment returns of 10%. Consequently, the net assets of the University, the most fundamental measure of resources, increased this past year by \$3 billion from \$44 billion to \$47 billion. This 7% increase in net assets is primarily driven by endowment returns and gifts, which enable the University to continue to advance in teaching and research.

These results were achieved through considerable care in managing resources throughout the University as evidenced by an increase in operating expenses of less than 3% during the year. Careful management of resources is necessary for Harvard, as it is for all colleges and universities, in the current environment. In last year's letter, we commented that higher education has matured as an industry. Revenues are under pressure as the number of students has plateaued, tuition costs have reached limits of affordability, federal research support is uncertain, and expectations for returns in the investment markets are muted. For these and other reasons, Moody's and Standard & Poors both issued within the last year a "Negative Outlook" for higher education in the U.S.

Harvard is well positioned to manage through this period due to a healthy balance sheet, modest recent operating surpluses, established financial discipline, and Harvard's primary strength—faculty and staff—who create one of the world's most exciting learning and research environments. Nonetheless, the University is cognizant of economic pressures, and recognizes its obligation to our students, donors, and research sponsors to ensure that every dollar under University stewardship is efficiently and effectively managed in support of our teaching and research mission. We thank our faculty and staff for wisely managing resources over the past year.

With only 22% of revenues coming from net tuition, Harvard's annual funding is deeply dependent upon its generous donors with 44% of annual revenues arising from donations, past and present: endowed distributions represent 35% of revenues and current-year gifts represent 9% of revenues. The success of the Capital Campaign has been broadly reported elsewhere, but we add our thanks as well to Harvard's thoughtful donors. From a financial perspective, philanthropy is the critical driver of the excellence to which Harvard aspires in transformative teaching and ground-breaking research.

The operating surplus of \$196 million equaled 3.8% of revenues, a comparable percentage to other AAA-rated universities. Generating a surplus is helpful as it will add a small cushion to reserves in preparation for an inevitable economic downturn, particularly in light of the current extended economic expansion—one of the longest in history. At Harvard, most reserves are managed locally as every school and unit within Harvard is accountable for its own budget results, with local control over resources and decision-making. Consequently, the \$196 million surplus is the consolidation of individual school and unit results—some with surpluses and others losses. As one example, the Faculty of Arts & Sciences (FAS), Harvard's largest individual enterprise, showed a surplus of \$3.1 million this year, overcoming several recent years of operating losses thanks to sustained and careful stewardship.

The passage of the Tax Cuts and Jobs Act adds a new series of tax cost burdens to the University. We believe the provisions applying to higher education are bad public policy. Our country's philanthropic history has helped create leading universities, hospitals, and social service agencies that serve our communities in ways that are the envy of the world. The step of levying a federal tax on public good, non-profit charities is deeply concerning as it reduces the money available

for the underlying missions of these organizations, and establishes an unsound precedent for other levels of government. The Act has added several new tax burdens on the University, the largest of which is a new tax on endowment income. Although we do not have final guidance from the U.S. Treasury, we have estimated that these related provisions will ultimately cost the University \$40-\$50 million on an annual basis. This policy will increase the cost of education and damage the University's teaching and research mission. In Harvard's case, the tax is approximately 25% of this past year's undergraduate financial aid grant budget. We believe these dollars are better spent enabling our educational mission.

Student aid this past year enabled one out of five undergraduates to receive 100% of their tuition, room and board paid by the University, as they come from families with annual incomes of less than \$65,000. Across the student body, 54% of undergraduates receive financial aid, and on average their families paid \$12,000 for tuition, room and board. The University hopes to continue this level of affordable access to a Harvard education for students.

As mentioned above, the endowment earned a 10% return for the year. This is gratifying as it is 2% above our 8% long-term target return. Similar to recent years, this result is roughly equal to the average return of larger college and university endowments, but not yet our immediate peers. We are very encouraged by the steps that Narv Narvekar and his Harvard Management Company colleagues have taken to reposition the endowment for long term success, knowing that the positive impact of these changes will take time to unfold.

With Drew Faust having stepped down as President at the end of the fiscal year, we would like to thank her for her farsighted financial stewardship—especially during times of financial constraint. During President Faust's tenure, the Corporation Committee on Finance was established, consistent budgeting practices were installed across the campus, decision-making has been guided by new multi-year financial and capital planning processes, and clear policies have been created with respect to University liquidity, operating reserves, philanthropy for capital, and facilities renewal spending. Through both her championing of sound financial practices and her leadership role in the success of the Capital Campaign, President Faust's legacy of financial stewardship will benefit the University for generations to come.

In closing, we want to again thank each and every donor to the University—past and present—for understanding that Harvard's excellence in teaching and research is made possible through your philanthropy. We also want to thank Harvard's faculty and staff for their vital contributions, on a daily basis, in making Harvard one of the world's preeminent institutions.



Thomas J. Hollister  
VICE PRESIDENT FOR FINANCE



Paul J. Finnegan  
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