

Financial Overview

From the Vice President for Finance and the Treasurer

We write to report on the University's financial position and results for the fiscal year ended June 30, 2015. The University's operating surplus of \$62 million is slightly more than 1% of University revenue, compared to last year's \$22 million, and again an approximate break even result. The University's net assets increased by \$1.4 billion, reflecting the strength of the University's ongoing capital Campaign and net growth in the market value of the endowment. Taken together, the results of this past fiscal year follow a recent trend of modest, but continued improvement in the University's overall financial health.

The progress we have achieved to date provides a strong foundation for the University to pursue its aspirations for the future. Harvard is committed to making critical investments in its academic program – expanded faculty; funding to support vital research; and new and modernized spaces that support research, teaching, and learning – that will help ensure the University's unparalleled excellence over the course of the next generation. Our donor community's contributions remain at the core of what enables us to drive our mission, and for that we are extremely grateful.

While the University is well positioned to invest in the future, it is with an acknowledgement of ongoing financial pressures, both in the world of higher education and at Harvard. Federal research funding has flattened, tuition growth is constrained by structural affordability issues, and capital market returns are uncertain and volatile. At the same time, a cost structure that is largely fixed makes quick changes difficult to effect. The University's commitment to financial aid, which is invaluable in making a Harvard education accessible at all income levels, and its deep commitment to research, with world-altering successes, also puts significant and continuing pressure on annual budgets. In recent years, Harvard has taken important steps to manage these pressures, by enhancing financial and capital planning, exploring alternative revenue sources, and establishing new financial practices and policies.

This kind of prudent financial management has enabled the University to begin investing now in several strategic priorities that will pay dividends in the future:

CAMPUS EXPANSION AND RENEWAL

After years of academic and logistical planning, Harvard's future in Allston has come into sharper focus in 2015. Over the course of the year, faculty have deeply engaged in the academic planning process with the aim of producing a prudently designed yet incomparably impactful and exciting new Science and Engineering Complex.

In Cambridge, the Faculty of Arts and Sciences is undertaking a multiyear effort to renew the undergraduate residential campus to meet the needs of the 21st-century student. Following completion of work to Stone Hall in 2013 and McKinlock Hall last year, Dunster House officially welcomed students back this fall, and pre-construction work began on Winthrop House. These famous buildings are now a magnificent mixture of old and new and designed to invigorate student life as well as student achievement.

NONTRADITIONAL SOURCES OF EDUCATION

Harvard is committed to an evolving learning strategy – including collaborations such as edX, University-wide efforts such as HarvardX and school-based activities like HBX, executive education programs, and the Division of Continuing Education. Novel pedagogical formats are attracting new types of students, such as pre-college students seeking a leg up; international and lifelong learners attracted by low or no residency requirements; and professionals and alumni looking to build career skills, expertise, or find an intellectual community. Moreover, our faculty have been eager to innovate and meet the changing interests of our residential students, through active and adaptive learning techniques and the introduction of new digital tools. Nurturing and furthering the University's longstanding tradition as a pioneer in

HIGHER EDUCATION REVENUE PRESSURES

In the wake of the global financial crisis and its aftermath, higher education in America has entered a new era in which primary and traditional sources of operating revenue are expected to grow modestly at best each year. Harvard is no exception. While the University is generating modest surpluses, we recognize and understand that pressure on traditional revenue streams are a new normal that we must account for as we plan our operations and financial management moving forward.

- Federal sponsored dollars remain under intense scrutiny, and with the expiration of the American Recovery and Reinvestment Act (ARRA), which offered short-term relief from spending cuts affecting government-funded research, federal spending, along with the overhead it helps support, has decreased in recent years. On aggregate, our revenue from federal and non-federal sponsored sources increased by 1%, but federal funding – which accounted for

approximately 72% of the total sponsored revenue – actually declined by 2%.

- The financial markets that drive the growth of our endowment continue to be volatile. While the University's endowment payout approach ensures that the impact of the investment results are smoothed into the operating budget over time, we continue to be mindful of the impact of building additional structural costs onto a volatile revenue source.
- Given our commitment to providing access to affordable higher education for all qualified candidates, the rate of revenue growth we previously derived from tuition has largely plateaued. In the midst of a growing debate about the levels of student loan debt, and as other colleges curtailed spending after 2008, Harvard has maintained its industry leading commitment to student support (\$520 million in fiscal year 2015).

pedagogy requires significant investment, and will be fundamental to our continuing success as a leader in higher education in the coming decades.

ENERGY AND ENVIRONMENT RESEARCH AND PRACTICE

The University's Climate Change Solutions Fund supports research initiatives intended to hasten the transition from carbon-based energy systems to those that rely on renewable energy sources, and to propel innovations needed to accelerate progress toward cleaner energy and a greener world. Broad efforts to raise funds for energy and environment research across the campus have already generated nearly \$120 million in committed support through the Harvard Campaign.

A key priority of Harvard's University-wide sustainability plan is an aggressive short-term, science-based goal to reduce greenhouse gas emissions 30% by fiscal year 2016, including growth. Harvard has upgraded the efficiency of its central utilities, including expanding combined heat and power

systems, and implemented campus-wide energy audits and conservation measures. As a result, absolute emissions have been reduced by 21% and energy by 2% from fiscal 2006 to fiscal 2014, even after accounting for an 11% increase in growth (excluding growth, greenhouse gas emissions were reduced 32% and energy was reduced 17%).



While new and innovative investments chart Harvard's future, the University remains steadfastly committed to the key elements supporting our teaching and research – our faculty and students. Attracting and supporting the most talented students and faculty, while providing them with the resources to do their best work, is a key priority of the ongoing Campaign. Increased faculty support, both through the establishment of new endowed professorships and funds supporting teaching and research, allows the University to retain and attract teachers and researchers at the tops of their fields. Similarly, the

THE HARVARD CAMPAIGN

In the second year since its formal launch in 2013, the Harvard Campaign continues to attract historic levels of support from our alumni community. Their generosity is evident in \$1 billion in current use, construction, and endowment gift receipts reported in fiscal year 2015.

The two largest endowment gifts in Harvard's history, both pledged in fiscal year 2015, will have significant future influence both on Harvard and the world.

- A \$350 million pledge from the Morningside Foundation, in the memory of the late T.H. Chan, will enable the Harvard T.H. Chan School of Public Health to support research on four global health threats: pandemics old and new, such as malaria, Ebola, cancer, and obesity; harmful physical and social environments such as those resulting from tobacco use, gun violence, and pollution; poverty and humanitarian crises such as those stemming from war and natural disasters; and failing health care systems around the world.

- John A. Paulson's pledge of \$400 million to the Harvard John A. Paulson School of Engineering and Applied Sciences will put the School on a firm financial footing, ensuring that Harvard faculty and students in these fields have the promise and the opportunity to tackle some of the most difficult problems facing humanity, from helping cure cancer to developing substantive solutions to climate change.

In the coming decades and centuries, funds from these two gifts will be invested alongside the approximately 13,000 other individual funds that make up the University endowment. We expect the returns from these investments along with those from our other generous donors to provide critical revenues for the University's faculty, students, and staff, so that they can achieve their academic goals and aspirations.

University's leading edge financial aid program, particularly at Harvard College, demonstrates a commitment to making a Harvard education accessible at all levels of income. In fiscal year 2015, in addition to maintaining total undergraduate aid at the record high mark of \$170 million, the Faculty of Arts and Sciences (FAS) introduced several investments in resources and programs developed in collaboration with current students, as well as new efforts to attract economically diverse students. These included: providing Spring Break meals on campus, programming for First Generation college students, and unveiling "The Harvard College Connection," which involves current College students in recruiting prospective students.

With a combination of constrained resources and high aspirations, new and ongoing University investments will require trade-offs and judicious cost management. To that end, we will continue to explore opportunities to both enhance University revenue streams and manage expenses. We will continue to plan carefully for today and tomorrow, prioritize, make choices, and steward our financial resources with great care so that

we can build on our historic and continuing excellence in research, teaching, and learning. We are confident in the future health and vigor of the University, and grateful for the support of our community.

We hope this introduction provides you with a helpful context for evaluating the University's financial report.



Thomas J. Hollister
VICE PRESIDENT FOR FINANCE



Paul J. Finnegan
TREASURER

October 29, 2015