Looking forward, HBS plans to begin implementing its long-term campus plan in fiscal 2010. At that point, the School expects to see a return to the previous pattern of cash from operations falling short of net capital expenses. As in the past, HBS will ensure through its financial planning that sufficient resources—including unrestricted reserves—are available to service the School’s debt and execute on its capital investment strategy.

NET CAPITAL EXPENSES

The most recent period of significant investment in the HBS campus concluded in fiscal 2005, when capital expenses reached $79 million. The School’s capital expenses declined to $49 million in fiscal 2006 and to $20 million in fiscal 2007 as the major projects initiated earlier in the decade neared completion. In fiscal 2008, capital expenses rose to $40 million, largely reflecting the $18 million invested in completing the majority of the renovations of MBA residence space in Gallatin Hall.

Other large capital projects in fiscal 2008 included the completion of a project to renew classroom space for executive programs in McCollum Hall, and the installation of new life safety systems in Morris Hall. The School also completed a multiyear upgrading of the Technology Operations Center and the replacement of an outdated and inefficient heating and air-conditioning infrastructure. Capital expenses for these projects totaled approximately $8 million.

To protect the long-term value of the physical plant, HBS continues to invest in the renewal and maintenance of its buildings, facilities, and IT infrastructure. In fiscal 2008, the School’s aggregate spending on these numerous smaller projects totaled $7.6 million.

The $40 million in fiscal 2008 capital expenses was funded with $13 million in internally generated cash, substantially all of the School’s $22 million in new borrowings, and $5 million in gifts for capital projects. In fiscal 2007, sources of funding for capital expenditures included $10 million in internally generated cash, new borrowings of $7 million, and $3 million in gift payments for specific capital projects.

CHANGES IN DEBT & OTHER

HBS uses debt strategically as a means of optimizing its capital structure. The School borrows only on qualified capital projects, carefully considering the interest rate environment and expectations for the performance of the Harvard endowment. The School’s policy is to borrow when market conditions make accepting the incremental debt service obligation preferable to using endowment principal and appreciation.

New borrowings rose to $22 million in fiscal 2008, from $7 million a year earlier, primarily to finance the Gallatin Hall renovation. Debt principal payments rose to $9 million, from $7 million in fiscal 2007, reflecting scheduled payments as well as payments made possible by large restricted gifts received during the year.

Other non-reserve activity was $33 million in fiscal 2008, compared with $22 million in fiscal 2007. In fiscal 2008, as in the prior year, HBS transferred $25 million of current use reserves to the unrestricted endowment reserve established several years ago in order to capture higher investment returns. Reflecting these additional funds and the performance of the endowment, the market value of this reserve grew to $126 million at June 30, 2008, from $94 million a year earlier. Other non-reserve activity for fiscal 2008 also reflected a one-time, non-cash accounting adjustment of $8 million required by the University.