35 percent humidity, the library stores its rarest books and manuscripts, trusting its engineers, for the stacks are below the water table. Unlike Boston’s Big Dig tunnels, quips acting dean Jay O. Light, these walls don’t leak.

Planners wished to enhance the library’s ability to serve as the intellectual hub of the campus. Much was done to foster interaction and informal meetings among faculty members, and to gather close the staff who support faculty research, teaching, and course development. The new Baker has 67 offices for professors, a net increase of 30. A faculty commons comprises three seminar rooms and a small dining room where one may have lunch. Scattered throughout the faculty precincts are three large conference rooms and six eight-person conference rooms. There are also 24 work stations for faculty assistants and 63 more compact work stations for research associates.

A new physical and virtual space, The Exchange, just inside the south entrance, invites students, faculty, and staff to pause to read newspapers from around the world, check e-mail at two computer stations, use eight two-screen Bloomberg terminals showing real-time and historical business data and information, or watch eight 42-inch plasma screens on the walls stream the latest business news and coverage of Business School events. From top to bottom, this building is wired.

The columned north façade facing the Charles River remains as it was, but the redefined south entrance is the main one now. It faces Allston and the future.

### Better-than-Balanced Books

**Faster revenue growth, plus expenses rising at almost the same rate, yielded an operating surplus of $43.6 million for Harvard’s fiscal year ended June 30, up slightly from the $36.8 million surplus reported for 2004. In reviewing the latter results a year ago, vice president for finance Ann E. Berman, Harvard’s chief financial officer, had forecast “probably similar” outcomes this fall. The bottom lines were similar, but not the paths that led there.**

Revenue rose 7.8 percent, to $2.8 billion. Reviewing the audited financial statements (the University’s formal report will appear, as usual, in November), Berman pointed to several surprises. In a competitive environment, federally sponsored research support, including overhead costs, rose nearly $8 million, or 7.9 percent. Gifts for current use jumped $34 million, or 22 percent (see “Generous Givers,” opposite). Other contributing factors included a $47-million increase in endowment income distributed for operations (this totaled $835 million, plus the special $106-million allocation of endowment capital for Allston campus development); a $21-million increase, to $308 million, in graduate-student income, driven by higher tuitions and slightly larger enrollments; and a $10-million gain in revenue from continuing and executive education.

Reported expenses grew 7.7 percent, to $2.76 billion—well above the 5 percent level of the preceding fiscal year. Salaries and wages (the University’s biggest category of expense, approaching $1.1 billion) increased 5.5 percent. Employment was virtually flat, reflecting some reductions in the workforce (in the central administration and Radcliffe Institute, for example), offset by hiring elsewhere. The $314-million employee benefits line rose just 3.1 percent—startling in an era of soaring healthcare and pension-funding costs. The cost trends are greater, Berman said, but the financial statements underestimate them: adoption of the new Medicare prescription-drug benefit reduced costs $11 million in fiscal 2005, and the University’s shift to self-insurance for its health plans also affected this expense line.

Offsetting those favorable expense factors were one unusual and two recurring items. “Other” expenses leaped more than 12 percent to $537 million; these included the $26-million settlement of a federal lawsuit concerning Harvard’s economic advisory services in Russia (see page 59). Among normal items, space and occu-
colleagues on September 23 that growth in come news. Faculty of Arts and Sciences tended into fiscal year 2007.

4.5 to 5.0 percent of market value, the re-
tment returns (see page 58) have pushed the distribution rate down to 4.3 percent, His work, Glauber said, was a mathematical approach to the theory of light explaining these effects: “That’s really all there is to it.” (Background papers are available at http://nobelprize.org.)

In his twenty-fifth anniversary class report, Glauber described his work as “papers on various aspects of quantum theory and nuclear theory.” And how. Twenty-five years later, he reported taking up undergraduate teaching after many years of focusing only at the graduate level. He remains so engaged, offering a freshman seminar, “The Atomic Nucleus on the World Stage” this fall, and the popular Core course, Science A-29, “The Nature of Light and Matter,” next spring. Tenured in 1956, he is the longest-serving currently active tenured member of the Faculty of Arts and Sciences.

Separately, on October 5, MIT professor Richard R. Schrock, Ph.D. ’72, was named a co-recipient of the Nobel Prize in chemistry.

pansy costs rose 11.4 percent, to $296 million, as new facilities came on line and en-
ergy and security costs increased; depre-
ciation increased in step, rising $14 million to $107 million. Undergirding the building boom, debt outstanding increased by a quarter-billion dollars, to more than $2.8 billion, with cash interest payments rising to $95 million in 2005, versus $77 million in the prior fiscal year.

Overall, Berman said, Harvard’s 2005 results reflected two prior years of fiscal caution, when weak investment results prompted the Corporation to curtail distributions from the endowment, the single largest source of operating revenue. Now, after the endowment distribution increased 5.8 percent in 2005 (with a planned aggregate rise of 8 percent in the current year), Berman is convinced that spending on faculty growth, financial aid, and construction “will rise faster in 2006.” And because back-to-back “great” endowment returns (see page 58) have pushed the distribution rate down to 4.3 percent, below the Corporation’s long-term goal of 4.5 to 5.0 percent of market value, the recent rate of increase in payout may be extended into fiscal year 2007.

In some quarters, that would be welcome news. Faculty of Arts and Sciences (FAS) dean William C. Kirby wrote to his colleagues on September 23 that growth in the professorial ranks—from 636 in January 2003 to a projected 700 by this New Year’s—had led him to at least tap on the brakes. The growth, while long sought, has “occurred even more rapidly than we had anticipated in our academic and financial planning.” Accordingly, he intended to “ensure that our numbers remain con-
stant or grow more moderately” this year.

That “financial planning” refers in part to physical facilities: laboratory buildings for scientists, other new faculty offices, li-

cence-oriented graduate schools (such as education, government, and public health).

The timing of a broad capital campaign has evidently been pushed back. Rapier cited the strength of Harvard Business School’s capital campaign, which accounted for more than one-fifth of the gifts recorded. Harvard Law School’s campaign continues on track, and the Faculty of Arts and Sciences (FAS) had steady results. “The sciences have engendered a lot of interest,” she said, with $30 million raised for the stem-cell institute and 10 professorships funded in the Division of Engineering and Applied Sciences, which held a “chair challenge.” Donor interest in financial aid focused on the initiative for low-income undergraduates and public-service-oriented graduate schools (such as education, government, and public health).

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Premier Physicist

Mallinckrodt professor of physics Roy J. Glauber ’45, Ph.D. ’49, has a new title: Nobel laureate. The Royal Swedish Academy of Sciences conferred the prize on October 4, recognizing Glauber for his elucidation of the quantum theory of light. Cowinners John L. Hall, of the University of Colorado, and Theodor W. Hänisch, of the Max Planck Institute, were cited for developing highly precise laser-based spectroscopy; Glauber praised the “exquisite ingenuity” of some of their experiments.

Glauber told reporters he was a child tinkerer who built a telescope and then a spectroscope, and found himself seduced by physics as a young teenager. At Harvard, he devoured the mathematics curriculum (so much so that he worked on the Manhattan Project as an undergraduate, making calculations about critical mass and the efficiency of atomic explosions) and discovered “all sorts of thrilling things.” With the invention of the laser, new experiments made it possible, and essential, to go beyond the prevailing wave theory and to encompass the “granular quality” of photons, better accounting for the nature and behavior of light. His work, Glauber said, was a mathematical approach to the theory of light explaining these effects: “That’s really all there is to it.” (Background papers are available at http://nobelprize.org.)

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Generous Givers

Donations to the University totaled $590 million in the fiscal year ended June 30—the second highest sum in Harvard’s history, according to Donella M. Rapier, vice president for alumni affairs and development. The previous peak, $658 million in 2001, came at the end of the $2.6-billion University Campaign. (Unlike the higher figures published in Harvard’s annual financial report, the development-office figures discount capital gifts for life income funds to their present value.)

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stellar Swan Song

ending his 15-year run as president of Harvard Management Company, Jack R. Meyer, M.B.A. ’69, and his investment colleagues turned in a rousing finale. For the fiscal year ended June 30, total investment return of 19.2 percent brought the value of Harvard’s endowment to $25.9 billion, after taking into account capital gifts received ($286 million), funds used (principally, $853 million distributed for University operations), and lesser accounting items. The comparable figure on June 30, 2004, was $22.6 billion (with a 21.1 percent return). The results appeared in a letter from James F. Rothenberg, chair of HMC’s board of directors and Treasurer of Harvard College, that was released on September 30, Meyer’s final day in Harvard’s employ. He and several colleagues—including top-performing domestic and foreign bond managers David R. Mittelman and Maurice Samuels—are setting up shop as Convexity Capital Management LP (see “Money-Manager Transition,” March-April, page 59).

In absolute terms (see chart), HMC equity performance was topped by emerging-markets and private assets; during fiscal year 2004, the mainstream domestic and foreign equity holdings were particularly strong (see “Endowment Gains: Last Hurrah?” November-December 2004, page 56). Commodities (HMC has been a significant investor in timber and natural gas) and real estate (a laggard in recent years) also produced outsized gains, and all the bond portfolios did even better than in the prior year. On a relative basis, private equities sharply outperformed the market benchmark for such assets, as did high-yield investments (an under-performer in 2004), commodities, and the big domestic and foreign bond portfolios.

<table>
<thead>
<tr>
<th>Fiscal Year 2005 Performance</th>
<th>HMC</th>
<th>Benchmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic equities</td>
<td>8.4 %</td>
<td>6.9 %</td>
</tr>
<tr>
<td>Foreign equities</td>
<td>16.4</td>
<td>14.3</td>
</tr>
<tr>
<td>Emerging markets</td>
<td>34.5</td>
<td>35.0</td>
</tr>
<tr>
<td>Private equities</td>
<td>34.7</td>
<td>23.8</td>
</tr>
<tr>
<td>Absolute return</td>
<td>11.1</td>
<td>8.6</td>
</tr>
<tr>
<td>High-yield</td>
<td>17.0</td>
<td>6.3</td>
</tr>
<tr>
<td>Commodities</td>
<td>25.2</td>
<td>15.2</td>
</tr>
<tr>
<td>Real estate</td>
<td>26.1</td>
<td>20.3</td>
</tr>
<tr>
<td>Domestic bonds</td>
<td>19.9</td>
<td>12.9</td>
</tr>
<tr>
<td>Foreign bonds</td>
<td>20.3</td>
<td>7.9</td>
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<tr>
<td>Inflation-indexed bonds</td>
<td>11.6</td>
<td>11.2</td>
</tr>
<tr>
<td>Total</td>
<td>19.2%</td>
<td>14.2%</td>
</tr>
</tbody>
</table>

For the year, according to Rothenberg’s letter, the 19.2 percent endowment return outpaced the market benchmark—returns expected for funds passively invested in HMC’s asset classes—by 5 percent points, worth $1.2 billion. According to preliminary data, Rothenberg wrote, median return for the 25 largest university endowments was 15.8 percent; at press time, only Yale (22.3 percent) and Stanford (19.5 percent) were known to have edged Harvard. The 2005 performance brought HMC’s five- and 10-year results to annualized rates of return of 9.5 percent and 16.1 percent, Rothenberg noted: 5.1 and 4.5 percentage points, respectively, in excess of market benchmarks for those periods.

Duplicating such results seems unlikely. Looking ahead, Rothenberg wrote, “a more realistic aspiration” would be an increment of about 1 percent per year better than market returns.

More immediate questions face HMC, too. Meyer’s successor has not yet been named, despite a long search. (HMC board and search-committee member Peter A. Nadosy ’68, former president of Morgan Stanley Asset Management, is serving as interim chief investment officer.) HMC’s annual disclosure of its president’s and top-performing professionals’ compensation, a lightning rod for criticism, may be a deterrent among elite money managers (see “Extraordinary Bonuses,” March-April 2004, page 69).

And the loss of personnel to Convexity deprives HMC of proven expertise. During the past fiscal year, the University disclosed, it downsized—to the tune of billions of dollars—much of what it called a “complex bond arbitrage portfolio,” assets at the heart of the departing fixed-income managers’ strategy. That step, apparently driven by market conditions and the need to shift to new personnel, preceded Rothenberg’s disclosure that “Harvard does plan to commit endowment assets for Convexity to manage,” as it has when other HMC staff have set up shop on their own. In the interim, Meyer and associates may play an advisory role, maintaining ties to an organization that helped increase the value of the endowment more than fivefold during his tenure.

a billion dollars. For FAS, that represents future debt service amounting to annual payments of $50 million or more by some estimates (not to mention added operating expenses), for which funding—and fundraising—must be secured.

Factors like these, duplicated to varying degrees in other Harvard faculties, underlie the probability that spending will accelerate—before counting Allston planning, debt, and construction costs. In light of Berman’s announced intention to step down next spring (see page 63), the responsibility for sustaining the University’s financial strength will fall to new hands.