research—augmented by national stimulus appropriations—soared 11 percent, increasing almost $62 million.

The report breaks out expenses in a new way. The 1 percent decline in total spending reflects the 8 percent increase in direct sponsored spending and a 2 percent decline in non-sponsored outlays. In their section of the report, vice president for finance Daniel S. Shore (Harvard’s chief financial officer), and University treasurer James F. Rothenberg characterize the latter as “more squarely within the University’s control, and demonstrating progress made in planned cost reductions.”

Excluding “certain costs that tend to be fixed in the near term (i.e., tenured faculty compensation, financial aid, depreciation, and interest)” and adjusting for one-time items in both fiscal years ($59 million of fiscal 2009 expenses for retirement incentives and severance and benefits costs associated with layoffs; and a $52-million item in fiscal 2010, discussed below), Harvard’s “controllable non-sponsored operating expenses decreased by 6 percent,” from $2.30 billion to $2.17 billion. In other words, expense reductions valued at $130 million were realized during the year—not an easy feat after routine increases in spending. Among the salient details:

- Given workforce reductions and a fiscal 2010 salary freeze for faculty and nonunion staff members, non-sponsored salaries and wages declined 3 percent, or $31 million.
- Sharp savings were effected in discretionary expenses, with non-sponsored costs for supplies and equipment, utilities and building maintenance, travel, and purchased services reduced by $88 million. The University did most of its budget dieting here, rather than in permanent changes in the workforce. Accordingly, it is now notably more challenging to add employees or to fill vacancies (the term of art is “position control”).
- But other expenses rose. Total interest expense increased 26 percent, to $265 million (accounting for more than 7 percent of the University’s spending in the year). Total indebtedness, $2.85 billion in fiscal 2005, climbed steadily in subsequent years before ballooning to $5.98 billion in fiscal 2009, when Harvard placed $2.5 billion of new debt issues to restore its impaired liquidity, refinance variable-rate debt, and unwind some of the costly interest-rate swaps. Interest expenses not associated with specific capital projects rose to $84.4 million in fiscal 2010, up from $56.6 million in the prior year (and just $33.3 million in fiscal 2008), reflecting the burden of servicing these new University-level obligations. Bonds and notes payable at the end of fiscal 2010 increased modestly, to a total of $6.28 billion, reflecting new issues, principally to pay for construction projects such as the Law School’s Northwest Corner building.
- During the year, capital spending was essentially cut in half, to $324 million. Although work continues at the Law School and on renovations of the Fogg Art Museum and the Fairchild Biochemistry Building (to outfit it for stem-cell researchers), the $1.4-billion Allston science complex has been suspended. For the foreseeable future, these projects and renovation of the physical plant seem likely to be the major capital initiatives. A new capital-planning process, overseen by executive vice president Katie Lapp and meant to provide a University-wide, five-year building program, will shape future commitments Harvard will make; there will surely be pressure to restrict new debt financing, despite current low interest rates (see “Back to the Bond Market,” below).

(To manage the process, Mark R. Johnson has been appointed vice president for capital planning and project management. His planning responsibilities span Cambridge, the Longwood Medical Area, and Allston, and he will direct the resulting construction projects—all within Harvard’s financial resources. Johnson has worked at Harvard since 2002, managing in turn the Business School’s Baker Library/Bloomberg Center project and now the Northwest Corner building under construction at the Law School, where he has also led campus master planning and a five-year capital plan.)

Among other items of interest, during fiscal 2010, the University entered into $695.5 million of additional swap agreements, all designed to offset existing swaps and so to reduce further long-term risk of loss if interest rates stay low or decline even more. It did so without laying out additional cash, by agreeing to new contracts that offset the terms of the original ones—but giving up the opportunity to recover past losses should rates increase over the life of the original contracts. To the extent possible, the University is getting out of the business of bearing interest-rate risk for those past contracts.

Continuing the emphasis on enhancing liquidity that was announced last year, the General Operating Account (GOA)—Harvard’s cash and operating funds—is now relatively less heavily invested along—