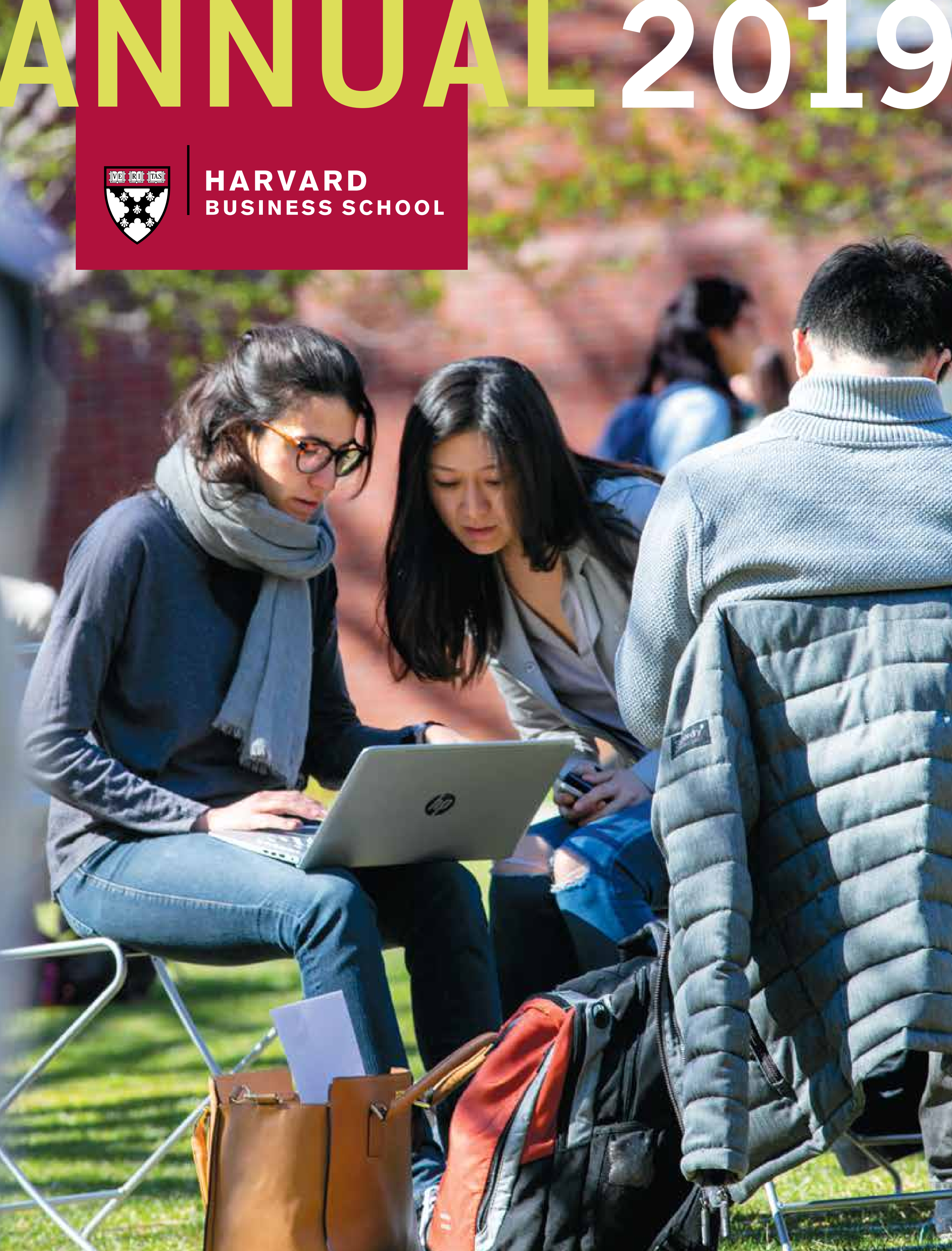
ANNUAL 2019

HARVARD
BUSINESS SCHOOL



DEAN OF THE FACULTY

Nitin Nohria

FACULTY LEADERSHIP

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Senior Associate Dean for University Affairs

C. Fritz Foley
Senior Associate Dean, Strategic Financial Planning

Janice H. Hammond
Senior Associate Dean, Culture & Community

Kathleen L. McGinn
Senior Associate Dean for Faculty Strategy & Recruiting

Das Narayandas
Senior Associate Dean for External Relations & HBS Publishing

Lynn S. Paine
Senior Associate Dean for International Development

Leslie A. Perlow
Senior Associate Dean for Research

Gary Pisano
Senior Associate Dean for Faculty Development

Jan W. Rivkin
Senior Associate Dean, Chair, MBA

David Scharfstein
Senior Associate Dean, Doctoral Programs

Debora Spar
Senior Associate Dean, Harvard Business School Online

Luis M. Viceira
Senior Associate Dean, Executive Education

EXECUTIVE DEAN FOR ADMINISTRATION

Angela Q. Crispi

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Chief Information Officer

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Associate Dean for Faculty & Academic Affairs

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Patrick Mullane
Executive Director, Harvard Business School Online

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Valerie Porciello
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Debra Wallace
Executive Director, Knowledge & Library Services

David A. Wan
President and Chief Executive Officer, Harvard Business Publishing

Harvard Business School is led by the Dean of the Faculty in conjunction with various advisory and oversight groups comprising faculty, staff, alumni, academics, and business practitioners. Harvard University appoints a Visiting Committee to review Harvard Business School's strategic goals and objectives and to provide advice and input to the Dean. The group meets biannually and reports to Harvard University's Board of Overseers.

FROM THE DEAN

Dear alumni and friends,

I am delighted to share with you the 2019 Annual Report for Harvard Business School. Each year, we provide highlights from the past year and a detailed look at the School's fiscal health. Our economic model—driven by MBA tuition, Executive Education and Publishing revenues, alumni gifts, and the endowment returns—enables us to invest in the core programs and activities of the School, including funding for faculty research, and to pursue innovations that will position HBS for leadership in the future.

We marked a number of exciting milestones and moments at Harvard Business School during 2018–2019—milestones that reflect the culmination of years of effort and planning, and moments that signal new and important beginnings. This was perhaps most evident with the dedication of Klarman Hall in October, an event focused on a daylong discussion about the state of American democracy that ushered in a new era of convening at Harvard Business School. Overnight, Klarman Hall has taken center stage as the place to showcase and discuss ideas from faculty and other thought leaders that have the power to change the role of business in the world.

Even as the School takes physical convening to the next level, our efforts to engage wider audiences via virtual platforms continue to build momentum. In January, HBX was renamed Harvard Business School Online, signaling a doubling down on our efforts to be a global leader in online management education. Over the past year, Online added 6 new programs and enrolled more than 19,000 learners—far more than those who come to campus annually. The HBX Live virtual classroom, where participants from around the world come together in real time for interactive case-based discussions, gained significant traction. Most importantly, since launching the online learning platform in 2014, we've learned a great deal about how to create and scale virtual courses that replicate the active, rigorous learning experience that is the hallmark of HBS.

Milestones were marked in other areas as well—including 20 years since the launch of the Asia-Pacific Research Center and 50 years since the launch of the African American Student Union at the School.

This Annual Report will be my last as dean of Harvard Business School. As I write this note, I am filled with optimism for the future of the School and the impact it will have in the world. And I am ever mindful that all of our efforts, past and future, are made possible by our incredible and generous alumni. For that support I am deeply grateful.

Nitin Nohria

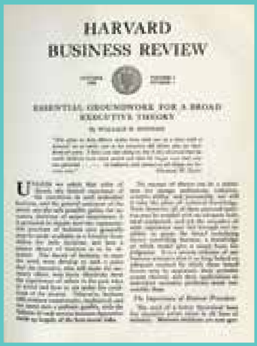
NITIN NOHRIA
DEAN OF THE FACULTY

THE YEAR IN REVIEW

FY19

SUMMER

While the rhythm of the academic year is familiar, with some activities unfolding with predictable regularity, other aspects of the School are continually refreshed and reimagined. Milestones like anniversaries offer one backdrop for this reinvention; changes in the world around us—both geopolitical and economic—provide additional impetus. As a result, Harvard Business School is both enduring and leading edge, as outlined in the pages that follow.

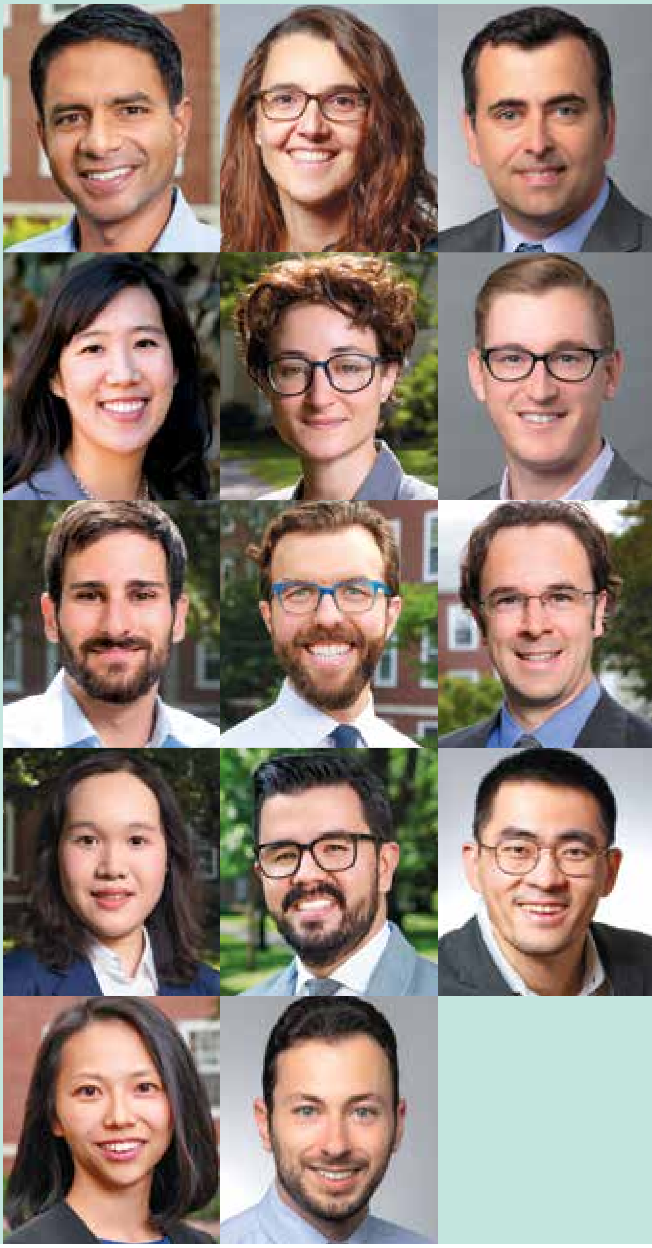


HARVARD BUSINESS REVIEW

Harvard Business Review, published in the US and with 12 regional editions, reached a milestone of more than 340,000 paid annual subscribers. Launched in 1922 by Dean Wallace B. Donham with an initial print run of 6,000 copies, the magazine struggled financially for its first 25 years, even as it gained a reputation for translating rigorous research into relevant reading for practicing mangers. Today the print magazine is supplemented by HBR.org, which averages nearly 7 million monthly visitors. The Publishing group also comprises Corporate Learning and Higher Education, offering tools like Harvard ManageMentor, case and reprint sales, podcasts, and webinars and other learning programs.

CHIEF INFORMATION OFFICER

Ron Chandler, with extensive experience in IT leadership, technology design, and management both in academia and in professional and financial services organizations, was announced as the School's new CIO. The HBS IT Group provides the administrative systems, platforms, tools, and infrastructure to support teaching, learning, engagement, and research (and its dissemination) at the School.



FACULTY START

New faculty members were welcomed to the School with an intensive 3-day orientation program, including sessions with junior and senior colleagues on their experiences in doing academic research and their career trajectories. Most relevant for those slated to begin teaching in the fall, START included an immersion in teaching by the case method where, working individually and in learning groups, faculty were given opportunities to prepare case studies and to practice a case opening and cold call.

New Faculty

(at left: left to right, top to bottom)

Full Professor

Amitabh Chandra, Technology & Operations Management *(joint appointment with Harvard Kennedy School)*

Associate Professors

Eva Ascarza, Marketing; **Alberto Cavallo,** Business, Government & the International Economy; **Laura Huang,** Organizational Behavior

Assistant Professors

Zoë Cullen, Entrepreneurial Management; **Mattias Fibiger,** Business, Government & the International Economy; **Daniel Green**, Finance; **Kyle Myers,** Technology & Operations Management; **Frank Nagle,** Strategy; **Trung Nguyen,** Accounting & Management; **Jorge Tamayo,** Strategy; **LT Zhang,** Organizational Behavior; **Ting Zhang,** Organizational Behavior; **Julian Zlatev,** Negotiation, Organizations & Markets

Faculty Promotions

(at right: left to right, top to bottom)

Ethan Bernstein
Associate Professor, Organizational Behavior

Rory McDonald
Associate Professor, Technology & Operations Management

Tsedal Neeley
Professor, Organizational Behavior

George Serafeim
Professor, Accounting & Management

STUDENTS ARRIVE

More than 9,000 applicants sought a place in the MBA Program and nearly 750 applicants in the Doctoral Programs; the acceptance rate for both was highly competitive, at 12% and 5%, respectively.

1,881
MBA Students

43%
Women

37%
International

27%
US Ethnic Minority

131
Doctoral Students

52%
Women

48%
International

24%
US Ethnic Minority

INCLUSION

Fellowships and financial aid are an important means of attracting a diverse student body and ensuring that graduates pursue careers where they feel their impact can be greatest. In the MBA Program, four Global Opportunity Fellowships were awarded to students taking their first jobs in Africa. The number of Forward Fellowships—aid for students facing unusual personal or family financial hardship—increased from 20 to 25.

$34.7M

Awarded in Fellowships

825

MBA Fellowship Recipients

$42,000

Average Fellowship per Recipient

FALL

KLARMAN HALL

The 120,000-square-foot convening facility opened in October with a dedication ceremony featuring remarks by Harvard President Larry Bacow, Governor Charlie Baker, and Beth and Seth (MBA 1982) Klarman; the afternoon also included a symposium on democracy, with a session on why competition in the politics industry is failing America, a panel discussion, and a fireside chat. Klarman Hall will host an array of events, including conferences (both academic and student club), classes, lectures, and performances and other entertainment. A highly technologically advanced building, it features an advanced audio system and seating design to accommodate groups of 250, 580, or 1,000. The lower-level concourse houses studios to support podcasts, webinars, and a black box room for video recording.

10TH ANNIVERSARY

The Global Financial Crisis Conference brought together 300 policy makers, investors, academics, and influencers to dissect the events—starting with the fall of Lehman Brothers in September 2008—that triggered the Great Recession. Over two days, guests and speakers—many of whom played key roles at the time, including former US Treasury Secretary Hank Paulson (MBA 1970), former president of the Federal Reserve Bank of New York and Paulson's successor at Treasury Tim Geithner, and former Director of the National Economic Council Larry Summers—examined the decisions they made and steps they took to try to stabilize the financial system. Professors Robin Greenwood and David Scharfstein co-chaired the conference to, in Greenwood's words, "better understand the past and prepare more effectively for what the future may hold."

PODCASTS

"Live from Klarman Studio" has become a familiar phrase to listeners of *Cold Call*, one of about a dozen podcasts produced at Harvard Business School. A powerful vehicle for featuring case studies, disseminating research, discussing news at the crossroads of business and culture, and fostering discussion, podcasts extend the reach and influence of the School's intellectual capital to millions of listeners around the world.

DOCTORAL STUDENT RESEARCH AWARDS

Four doctoral students were recognized for excellence and innovation in their dissertation research.

Wyss Award for Excellence in Doctoral Research

(Named in honor of Hansjörg Wyss, MBA 1965)

Daniel Brown (Management): impact of firms' measurement of value and performance on their stakeholders.

Alexandra Feldberg (Organizational Behavior): availability of information in technology systems and its effect on men's and women's everyday activities, performance outcomes, and relationship networks, as part of a broader study of gender, knowledge transfer, and discrimination within organizations.

Michael Lee (Management): effects of eliminating hierarchical authority on accountability, employees' work experience, and commitment to organization.

Martin Award for Excellence in Business Economics

(Established by Roger Martin, MBA 1981)

Oren Danieli (Business Economics): big data to optimize social experiments aimed at increasing income mobility and devising a new method to study wage polarization.

PHD IN BUSINESS ADMINISTRATION

The PhD in Business Administration (offered jointly with Harvard's Graduate School of Arts and Sciences) was approved and launched in Summer 2018, representing a transition from the Doctor of Business Administration (DBA) degree that had been awarded for many years.

100%

of Doctoral Programs graduates during FY19 were placed in academic, postdoc, or industry positions.

LEHMAN BROTHERS: A HISTORY, 1850–2008

Baker Library drew on its extensive Lehman Brothers Collection to launch an exhibit in the Library's lobby and online examining Lehman's rise, its reach into nearly every sector of the American economy, and the impact of its collapse. Baker's Special Collections, from which the exhibit was drawn, spans eight centuries and includes corporate archives, manuscripts, account ledgers, rare books, broadsides, photographs, films, electronic records, and company annual reports; it supports research in fields such as business, economic, social, and cultural history as well as the history of science and technology.

Harvard Business School Online

87%
Completion Rate

61
Net Promoter Score

HBX, the School's digital learning platform, was rebranded as Harvard Business School Online to help raise awareness of its offerings. New course offerings included *Strategy Execution* (HBX Live; Bharat Anand and Larry Culp), *Scaling Ventures* (HBX Live; Shikhar Ghosh and Jeffrey Rayport), *Leadership Principles* (Joshua Margolis and Anthony Mayo), and *Global Business* (Forest Reinhardt).

In partnership with the Harvard Graduate School of Education, Online also launched *Leading Change*, the first of four courses in the Certificate in School Management & Leadership Program aimed at helping preK-12 school leaders drive change. Additional modules of the certificate program will include *Leading Schools* (Fall 2019), *Leading People* (Summer 2020), and *Leading Learning* (Summer 2021).

A LIVING MODEL

Three hundred thirty-five staff positions were filled during 2018–2019, including 77 research associates. In total, the HBS workforce comprises approximately 1,100 FTEs, of whom 65% are women and 21% are minorities. Turnover at the School is 16%, reflecting a strong economy; 11% of staff received promotions.

EXECUTIVE EDUCATION

12,605
Participants

29%
Women

64%
International

New focused programs include Accelerating Innovation in Precision Medicine, Managing Sales Teams and Distribution Channels, and Building a Legacy: Family Office Wealth Management.

WINTER

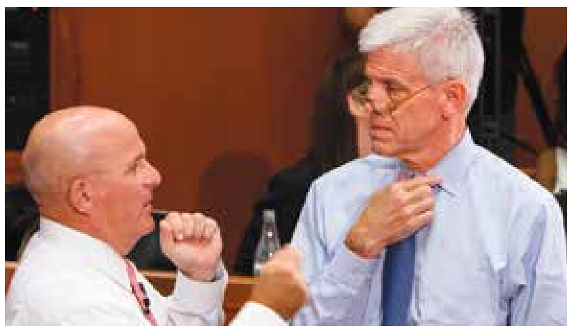
FORWARD-THINKING SUSTAINABILITY

In March, HBS joined the Leadership Circle at Farm Forward, a nonprofit that seeks to promote conscientious food choices that advance sustainable agriculture and support the humane treatment of animals. Working with Restaurant Associates, the campus's dining management company, the School will buy 100% of its eggs from farms certified as higher-welfare.

16
LEED-Certified Buildings

7
Green Roofs

4
Beehives



THE REFLECTIVE LEADER

This three-day residential Executive Education program offered approximately 60 senior-level, high-achieving MBA alumni roughly 10–15 years post-graduation an opportunity for personal development. Building on the belief that learning must continue beyond the two years of the MBA Program, The Reflective Leader represents an important step by the School to engage with and support alumni throughout their careers.

22ND ANNUAL NEW VENTURE COMPETITION

Student Business Track Winners

Dublier Grand Prize:
MyToolbox Technologies, Inc.
(shown) B2B labor marketplace for the construction industry.

Satchu-Burgstone Runner-Up Award:
Nom Pot
Clean-label frozen meals ready for one-pot cooking.

Student Social Enterprise Track Winners

Peter M. Sacerdote Grand Prize:
Hikma Health
Customized data management systems for healthcare providers caring for refugee patients.

Sacerdote Runner-Up Award:
Gramhal
Post-harvest services of storage, credit, and market linkage for smallholder farmers.

Alumni Winners

Grand Prize:
Blueland
Eliminate weight and waste from everyday products.

Runner-Up Award:
X-Cor Therapeutics
Extracorporeal CO_2 removal device that uses ultra-low blood flow to treat patients with hypercarbic respiratory failure.

266

Teams
66 Student Business
48 Student Social Enterprise
152 Alumni

200

Judges

$315,000

Cash Prizes

25 YEARS OF SOCIAL ENTERPRISE

The Social Enterprise Initiative marked its 25th anniversary with a two-day event, Frontiers of Change: 25 Years of Social Enterprise at HBS, which brought together over 300 alumni, students, faculty, staff, social entrepreneurs, government leaders, corporate executives, and experts in social innovation and change.

Sessions examined the evolving role of philanthropy and cross-sector partnerships; alumni leaders driving change across the public, private, and nonprofit sectors; building and leading best-in-class organizations; and the role of business and business leaders in social change.

Keynote speakers included Gerald Chertavian (MBA 1992 and Founder and CEO, Year Up), Stacey Childress (MBA 2000 and CEO, NewSchools Venture Fund), Max Hodges (MBA 2010 and Executive Director, Boston Ballet), Álvaro Rodríguez Arregui (MBA 1995 and Cofounder and Managing Partner, IGNIA), and Tracy Palandjian (MBA 1997, CEO and Cofounder, Social Finance).

VE RI TAS VE RI TAS

MS/MBA IN BIOTECHNOLOGY: LIFE SCIENCES

In collaboration with the Harvard's Graduate School of Arts and Sciences (GSAS), HBS approved a new joint degree program that aims to prepare students to develop transformative organizations that will advance new drug discoveries or therapeutics. The two-year program will welcome its first cohort of students in August 2020; their curriculum will include existing courses such as Online's CORe offering and the first year of the MBA, as well as newly designed courses such as Ethical Dilemmas in Biotechnology, Data Analytics and Technology, and NextGen Biotechnology. They also will have the opportunity to pursue a summer internship in life sciences or biotech.

PROBLEM SOLVING

Coauthors Russ Banham, Shirley Spence, and Sarofim-Rock Professor of Business Administration, Emeritus Howard Stevenson spent more than four years studying—through surveys, interviews, and extensive archival and secondary research—the impact of the School's alumni in education and learning, health and wellness, community and economic development, energy and the environment, and arts and culture. Their resulting coffee table book features more than 200 stories from around the world and highlights the breadth and depth of alumni support of social causes.

SPRING

COMMENCEMENT

At its 109th Commencement exercises in May, HBS awarded 935 MBA and 6 DBA degrees, and jointly awarded 14 PhD degrees.

At the annual Class Day celebration the day before, student speaker Brandon Rapp (above) explored the potential for courage to create a more just world.

"Class of 2019, I hope that we never forget the things that we are thankful for, and the 'what' and 'whom' we are courageously fighting for. I hope that we remember to be courageous. I hope that we choose to tap into that courage to fight for a better world and for each other, and to lean in to what we learned here: to speak truth even when your voice might quiver just a bit, and your hands might tremble."

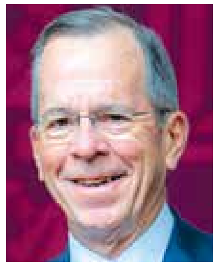
Brandon Rapp (MBA 2019)

Class Day Distinguished Speaker Michael Bloomberg (at right) emphasized the value of ethics and encouraged students to make decisions based not on their starting salary, but on their development and happiness. He offered up integrity as the solution to the country's economic and political woes, and exhorted the graduating class to take a leading role in restoring faith in the promise of America and the future of the American dream.

ALUMNI ACHIEVEMENT AWARDS

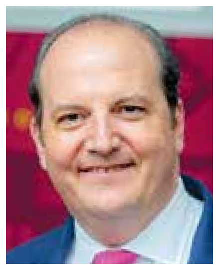
Marla Beck (MBA/MPA 1998)
CEO, Bluemercury, Inc.

Michael R. Bloomberg (MBA 1966)
Founder, Bloomberg LP & Bloomberg Philanthropies; three-term mayor of New York City



Michael G. Mullen (AMP 109, 1991)
17th Chairman, United States Joint Chiefs of Staff

Tracy P. Palandjian (MBA 1997)
CEO & Cofounder, Social Finance



Álvaro Rodríguez Arregui (MBA 1995)
Managing Partner, IGNIA

FACULTY AWARDS

Six faculty members were recognized by graduating MBA students for their exceptional contributions to the HBS experience: Ted Berk, Joshua Margolis, and Matt Weinzierl for outstanding teaching in the Required Curriculum, and David Moss, Tom Nichols, and Sophus Reinert for outstanding teaching in the Elective Curriculum.

Three faculty members were acknowledged with the Wyss Award for Excellence in Doctoral Mentoring: Anat Keinan, Jeff Polzer, and Dennis Yao. The student-sponsored award recognizes faculty members for their commitment to developing future scholars.

DEAN'S AWARD

Five graduating students were honored: Neel Ghose (MBA 2019), Lindsey Morrow (MBA 2019), Amanda Tyson (MBA 2019), Megan Williams (MBA 2019), and Alexandra Feldberg (PhD 2019). The Dean's Award celebrates the achievements of graduates who have had an extraordinary impact on the School, University, or broader community.

DIALOGUE

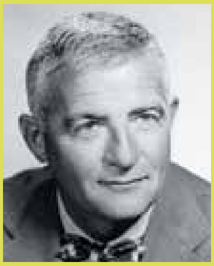
For two and a half days in June, the HBS campus was transformed into an immersive, creative living and learning experience—where content and substance were intertwined with art, and working sessions were interspersed with performance. More than 250 attendees gathered for conversations on topics at the intersection of business and society and to generate ideas for addressing society's complex challenges. Designed as a unique convening opportunity, Dialogue spurred imagination about the case method at scale and how to engage emerging and established thought leaders with the School.

IMMERSION IN AFRICA

Twenty-six faculty members spent a week in Nigeria and Kenya visiting and learning from nearly 20 companies, exploring the unique challenges these firms face as well as their innovative business practices. The Fung Global Symposium, held in Lagos, brought together more than 100 local alumni and business leaders from the region to learn about leading-edge faculty research. The School's Africa Research Center supported the immersion and will work with many of the faculty who participated on case studies and other research that emerged from the trip.

IN MEMORIAM

Henry (Hank) B. Reiling
Eli Goldston Professor of Business Administration, Emeritus



C. Wickham Skinner
James E. Robison Professor of Business Administration, Emeritus

FROM THE CHIEF FINANCIAL OFFICER

Harvard Business School's economic model performed impressively in fiscal 2019. For the fifth consecutive year, revenues grew faster than expenses, resulting in a double-digit increase in cash from operations. This cash flow enabled HBS to continue investing in core programs and strategic innovation, while still concluding the year in a strong financial position.

The HBS economic model is unique among the Harvard University schools and begins with our commitment to internally funded faculty research. Free from the constraints that can come with grants and other outside funding, HBS research budgets allow the School's faculty to pursue the questions that interest them most, and to interact in the field with managers who are engaged with the most timely business challenges and opportunities.

Through its Executive Education, Harvard Business Publishing (HBP, or Publishing), and Harvard Business School Online (Online) groups, the School leverages the intellectual capital created by the faculty to educate leaders and influence the practice of management on a global scale. Completing the cycle, net operating margin contributions from Executive Education, Publishing, and Online supplement revenues from MBA tuition and alumni gifts as key sources of research funding.

Total revenue in fiscal 2019 grew 8 percent from the prior year to $925 million, while operating expenses increased 7 percent to $821 million. As a result, total net margin contribution as a percentage of revenue grew to 11.2 percent, from 10.5 percent last year and 4.6 percent five years ago. Cash from operations—the School's operating surplus—increased more than 15 percent, from $90 million to $104 million. This surplus, beyond what it enables for HBS, plays an important role in the financial health of Harvard University and its ability to, for example, maintain its AAA bond rating. In fiscal 2019, the HBS surplus accounted for just over one-third of Harvard's $298 million surplus.

Concluding fiscal 2019 in a strong cash position enabled the School to invest $100 million in the HBS endowment reserve, following a $65 million investment in fiscal 2018. In contrast with alumni gifts to the endowment, which are largely earmarked for fellowships, professorships, and other key student and faculty activities, the long-term stream of income from internally generated funds invested in the endowment is unrestricted.

Building the balance of unrestricted funds in the endowment reserve is an important priority for HBS. Strategic initiatives and investments in campus construction have increased the School's fixed operating costs. At the same time, HBS is reliant on revenues from economically sensitive sources—current use giving, Executive Education, Publishing and, now, Online—to fund these higher expenses. Should revenues from these sources ever decline, annuity income from the endowment available for unrestricted purposes will be crucial to sustaining the School's operating model.

The School also holds unrestricted reserves outside of the endowment. These reserves are instrumental in providing the School with the liquidity necessary to execute on its mission and sustain the campus through economic cycles over the long term. HBS concluded fiscal 2019 with $129 million of unrestricted reserves held outside of the endowment—up from $118 million a year earlier, and well above the $100 million we have established as the School's liquidity management target.

One of our financial goals is for HBS to serve as a living example of a well-run organization, embodying the skills, tools, and frameworks taught across the School's educational programs. Transparency is intrinsic to achieving this goal, and to this end our fiscal 2019 financial results are reported in detail in the Supplemental Financial Information section that begins on page 24.

Sustaining this growth—as the ways knowledge is created, delivered, and consumed are changing, and as the marketplace for learning development is becoming more crowded—will not be easy. Publishing is investing in the development of digital platforms, channels, and content. Executive Education is exploring hybrid classroom/online program models that better serve an increasingly diverse and global participant base. Online is scaling its technology and business infrastructure to meet higher market demand.

The operating income these investments help to generate will be crucial to the School over the next several years. As explained in detail on page 26, income from the endowment is sensitive to long-term trends in the capital markets. Anticipating a period of muted investment returns worldwide, the University has advised HBS and the other Harvard schools to incorporate only modest endowment distribution growth, if any, into their five-year financial plans.

Income from unrestricted current use gifts will play a larger role as well. The Campaign for Harvard Business School, which concluded in fiscal 2018, spurred remarkable growth in unrestricted current use giving. After coming in at $40 million in fiscal 2019, income from unrestricted current use giving is expected to decline in fiscal 2020 as remaining Campaign pledges are fulfilled. Returning and sustaining annual giving to the HBS Fund at or above $40 million is a philanthropic priority. We are implementing creative approaches to engage the community of HBS alumni and friends in this effort.

At the same time, we are continuing to strengthen the core activity of MBA education at the School. Some of these initiatives add programmatic complexity or incremental costs.

For example, more students at HBS are seeking to integrate the skills they are learning in the MBA program with cross-disciplinary knowledge in areas such as biotechnology and engineering. As a result, HBS has invested in building six joint degree programs. The most recent is a joint MS/MBA, offered with Harvard's Graduate School of Arts and Sciences and Harvard Medical School, that prepares future leaders at the interface of life sciences and business. The School incurs additional operational and staff expenses to support these joint degree programs, including sharing with the partner Harvard schools a portion of the MBA tuition paid by the enrolled students. Fortunately, however, generous endowment gifts from HBS alumni have mitigated the associated financial impact.

Moreover, the School continues to seek a diverse applicant pool with respect to experience, gender, country of origin, and financial resources, among other dimensions. Beyond ensuring that the most talented future leaders apply, HBS also wishes to ensure students are supported while on campus and can pursue careers where they will have the most impact. In fiscal 2019, the School introduced a fellowship offering for MBA students with exceptional financial needs. Additionally, fellowship funds from restricted gifts were used to boost support for MBA graduates who pursue careers in Africa. These important programs add to the expense of MBA fellowships and financial aid.

Fellowships (in millions)	**MBA**	**Total***
FY 19	**$ 38**	**$ 51**
FY 18	37	50
FY 17	36	48
FY 16	34	47
FY 15	32	44

** Includes Doctoral Programs and Executive Education*

Investment in Research (in millions)	
FY 19	**$ 152**
FY 18	144
FY 17	136
FY 16	131
FY 15	123

FISCAL 2019 REVIEW

Fiscal 2019 was a year of strong financial performance. Revenues from Executive Education, Publishing, and Online were higher than expected. The resulting gains in operating leverage enabled HBS to make solid progress operationally and strategically, while still adding to the unrestricted reserves necessary to sustain the School's future success.

At Publishing, Harvard Business Review circulation continued to grow (counter to industry trends), and products launched by the Corporate Learning and Higher Education divisions were well-received. Leveraging space in new and newly renovated buildings, Executive Education added programs and grew participant enrollment. Online generated positive net cash flow for the first time, driven by additional market offerings and a growing learner base.

In an era when careers may extend 50 years and beyond, education and personal development no longer end in a person's 20s. The School is experimenting with new approaches to help MBA students realize that their two years at HBS mark only the start, not the end, of their learning journey. One new offering is The Reflective Leader, an Executive Education program aimed at the School's MBA alumni 15-25 years out who are contemplating their next phase of work and life. Over the next decade, HBS will invest further in a range of offerings designed to make lifelong learning a reality rather than an aspiration.

Faculty research, the foundation for the curriculum and for knowledge dissemination, has become more resource-intensive than in the past. The faculty's efforts to create new knowledge often involve complex projects, many of which are multi-year, global in scope, and team-based. Leading-edge computational and behavioral research methodologies, which are more expensive than traditional techniques, are gaining in usage, particularly among junior faculty. HBS typically receives few restricted gifts for faculty research in any given year, and therefore we fund nearly all direct and indirect costs with internally generated, unrestricted cash.

Before turning to the outlook for fiscal 2020 specifically, we offer a comment on the School's capital activity this past year and prospects for the near-term future.

The years since fiscal 2011 have seen a large number of construction and renovation projects at HBS. The School's capital investments in these major projects during this eight-year period have averaged $51 million annually. New buildings have added more than 250,000 square feet of learning, residential, and convening space to the campus, culminating in the substantial completion of Klarman Hall in fiscal 2018.

With the opening of Klarman, fiscal 2019 marked a shift toward what promises to be a multi-year focus on campus renewal and maintenance, versus the creation of new buildings, at the School. Total capital expenditures for fiscal 2019 decreased to $38 million, from $92 million in the prior year, reflecting lower costs for new construction. The School's capital activity during the year consisted primarily of small renewal and maintenance projects designed to prevent deferred maintenance and to enhance environmental sustainability.

FISCAL 2020 OUTLOOK

With the first quarter completed at this writing, HBS is positioned to deliver another year of solid financial performance in fiscal 2020. The School's income-generating groups are making good progress, operationally and strategically.

The current economic expansion in the United States—already the longest in its history—will come to an end at some point. The recent softening of growth in the global economy underlines this concern. With these dynamics in mind, HBS has undertaken detailed financial scenario planning—focusing on steps that can be taken in the near term to prepare for any number of economic outcomes.

The School has long been conservative in budgeting revenues and expenses. Our plan for fiscal 2020 reflects this sense of caution. If economic conditions remain favorable, the School's financial results are likely to outperform on both the top and bottom lines in fiscal 2020, as they have for the past several years.

Starting at the top of the Statement of Activity & Cash Flows (on page 22), the School's budget for fiscal 2020 assumes that total revenues will grow less than 1 percent from the $925 million reported for fiscal 2019. Combined revenue from Publishing, Executive Education, and Online is forecasted to increase approximately 2 percent.

Revenue from MBA tuition and fees is expected to be flat in fiscal 2020 for the first time in decades, reflecting the School's efforts to slow the rising cost of MBA education.

Philanthropy will remain essential to the School's financial health in fiscal 2020. The School's ability to continue investing in innovation depends on the HBS community's success in building on the achievements of the Campaign and sustaining recent momentum in current use giving.

We expect HBS to benefit from high single-digit growth in the endowment distribution for fiscal 2020. A portion of this growth relates to the increase in the University's distribution rate. The balance reflects growth in the size of the endowment as a result of endowment gifts and the School's fiscal 2019 investment in its endowment reserve.

Moving down the income statement to operating expenses, our fiscal 2020 financial plan targets an approximately 8 percent increase in the School's total spending, compared with fiscal 2019. As in the past few years, a portion of this increase reflects the inclusion of an expense contingency to cushion the impact of margin contribution shortfalls in the

Publishing Revenue (in millions)	
FY 19	**$ 262**
FY 18	240
FY 17	221
FY 16	217
FY 15	203

Executive Education Tuition (in millions)	
FY 19	**$ 222**
FY 18	207
FY 17	191
FY 16	176
FY 15	168

IT Investment (in millions; excludes capital expenses)	
FY 19	**$ 87**
FY 18	82
FY 17	85
FY 16	85
FY 15	72

event of a revenue slowdown. We will continue to closely monitor the School's actual financial performance versus budget as the year unfolds, hoping the expense contingency will not be necessary.

Our fiscal 2020 plan forecasts an increase of approximately 7 percent in total compensation expense, driven by the past year's growth in the size of the School's faculty and staff, as well as higher salaries and benefits costs. The plan also anticipates a higher cost of goods sold in Publishing, Executive Education, and Online as those groups continue to grow, as well as increased information technology spending for cybersecurity and infrastructure upgrades. The School's total capital budget for fiscal 2020 is $38 million, flat with fiscal 2019. Creating two new HBX Live studios for Online in Cumnock Hall, completing faculty office projects in Baker Library | Bloomberg Center and Cumnock as well as a renewal project in the Spangler Center, and implementing advanced campus security measures are among the largest capital projects planned for the year.

In summary, top-line growth and fiscal discipline enabled us to continue to execute on the School's mission in fiscal 2019 and deliver a robust operating surplus for the fifth straight year. By augmenting the School's reserves of unrestricted funds, this surplus positions HBS to further strengthen core programs and drive innovation over the long term. We remain committed to delivering sound and consistent financial results in fiscal 2020 and future years.

Richard P. Melnick

RICHARD P. MELNICK, MBA 1992
CHIEF FINANCIAL OFFICER
OCTOBER 1, 2019

Capital Investment (in millions)	
FY 19	**$ 38**
FY 18	92
FY 17	78
FY 16	113
FY 15	81

Building Debt Outstanding (in millions)	
FY 19	**$ 46**
FY 18	55
FY 17	64
FY 16	71
FY 15	78

FIVE-YEAR SUMMARY

FOR THE FISCAL YEAR ENDED JUNE 30,

Financial Data (in millions)	**2019**	**2018**	**2017**	**2016**	**2015**
Revenues	**$ 925**	$ 856	$ 800	$ 761	$ 707
Expenses	**821**	766	731	704	660
Cash from Operations	**104**	90	69	57	47
Capital Investments	**38**	92	78	113	81
Building Debt Outstanding	**46**	55	64	71	78
Unrestricted Reserves	**129**	118	145	103	125
Endowment	**3,985**	3,787	3,472	3,209	3,309
Total Assets	**$ 5,420**	$ 5,208	$ 4,821	$ 4,508	$ 4,587
MBA Program					
Applications	**9,228**	9,886	10,351	9,759	9,686
Percent Admitted	**12%**	11%	11%	11%	11%
Yield	**89%**	91%	91%	90%	91%
Enrollment	**1,881**	1,870	1,879	1,883	1,865
Tuition	**$ 73,440**	$ 72,000	$ 63,675	$ 61,225	$ 58,875
Average Fellowship Aid per Student	**$ 42,034**	$ 38,959	$ 37,312	$ 35,571	$ 32,919
Doctoral Programs					
Applications	**748**	864	915	843	749
Percent Admitted	**5%**	4%	4%	5%	4%
Yield	**81%**	64%	79%	66%	53%
Enrollment	**131**	134	132	134	147
Executive Education					
Enrollment	**12,605**	12,070	11,361	10,855	10,614
HBS Online					
Participants	**19,304**	12,936	9,142	6,634	3,471
Faculty					
Faculty Positions (full-time equivalents)	**233**	225	233	233	231
Teaching Materials	**626**	642	573	566	544
Research Articles on HBR.org	**177**	199	182	174	197
Books	**14**	11	14	23	13
Staff					
Staff Positions (full-time equivalents)	**1,761**	1,721	1,680	1,631	1,541
Publishing					
Cases Sold	**14,539,000**	15,062,000	14,859,000	13,468,000	13,223,000
Harvard ManageMentor Active Users	**2,837,000**	2,430,000	3,200,000	3,478,000	2,709,000
HBR.org Average Monthly Users	**6,916,000**	7,153,000	7,012,000	5,511,000	4,629,000

FISCAL 2019 HIGHLIGHTS

- Operating revenues grew 8 percent to $925 million, while operating expenses increased 7 percent to $821 million.
- The largest revenue growth drivers were Executive Education, Harvard Business Publishing (HBP, or Publishing), and Harvard Business School Online (Online).
- The major areas of expense growth were other expenses, resulting from accounting changes as well as salaries and benefits.
- New gifts and pledges totaled $150 million, compared with $214 million in fiscal 2018—the final year of The Campaign for Harvard Business School.
- The return on the School's endowment was 6.5 percent, compared with 10 percent in fiscal 2018.
- The value of the School's endowment (after the net impact of distributions from the endowment and the addition of new gifts) increased to $4 billion, from $3.8 billion a year earlier.
- Capital investments in campus facilities and new construction decreased to $38 million, from $92 million in fiscal 2018.
- The School generated an operating surplus of $104 million, compared with $90 million in the prior year.
- HBS ended fiscal 2019 with an unrestricted reserves balance of $129 million, compared with $118 million a year earlier.
- The School's total net assets increased to $5.1 billion, from $4.9 billion at the end of fiscal 2018, primarily reflecting the impact of growth in the market value of the endowment.

STATEMENT OF ACTIVITY & CASH FLOWS*

FOR THE FISCAL YEAR ENDED JUNE 30,

Revenues (in millions)	2019	2018	2017
MBA Tuition & Fees	**$ 140**	$ 138	$ 133
Executive Education Tuition	**222**	207	191
Publishing	**262**	240	221
Endowment Distribution	**162**	150	146
Unrestricted, Current Use Gifts	**40**	44	42
Restricted, Current Use Gifts	**28**	35	32
HBS Online	**43**	19	12
Housing, Rents, Interest Income, & Other	**28**	23	23
Total Revenues	**$ 925**	$ 856	$ 800

Expenses			
Salaries & Benefits	**$ 359**	$ 340	$ 327
Publishing & Printing	**77**	74	70
Space & Occupancy	**72**	71	68
Supplies & Equipment	**13**	12	12
Professional Services	**72**	68	63
Fellowships	**51**	50	48
University Assessments	**26**	24	24
Debt Service	**3**	3	4
Depreciation	**46**	42	40
Other Expenses	**102**	82	75
Total Expenses	**$ 821**	$ 766	$ 731

Cash from Operations	**$ 104**	$ 90	$ 69
Depreciation	**46**	42	40
Non-Cash Items	**—**	—	1
Cash Available for Capital Activities	**$ 150**	$ 132	$ 110

Capital Expenses	**$ (38)**	$ (92)	$ (78)
Change in Capital Project Pre-Funding	**(3)**	10	19
Use of Gifts for Capital Projects	**6**	3	51
Net Capital Expenses	**$ (35)**	$ (79)	$ (8)

New Borrowings	**$ 0**	$ 0	$ 0
Debt Principal Payments	**(9)**	(8)	(8)
Capitalization of Endowment Income	**(2)**	(2)	(4)
Decapitalization of Endowments	**2**	3	3
Other Non-Reserve Activity	**(95)**	(73)	(51)
Changes in Debt & Other	**$ (104)**	$ (80)	$ (60)

Increase (Decrease) in Reserves	**$ 11**	$ (27)	$ 42
Beginning Reserves Balance	**$ 118**	$ 145	$ 103
Ending Reserves Balance	**$ 129**	$ 118	$ 145

CONSOLIDATED BALANCE SHEET

FOR THE FISCAL YEAR ENDED JUNE 30,

Assets (in millions)	2019	2018	2017
Cash	**$ 105**	$ 89	$ 80
Current Use Reserves	**129**	118	145
Receivables, Loans, & Other Assets	**215**	214	177
Invested Funds:			
Endowment	**3,675**	3,453	3,140
Endowment Interest in Trusts Held by Others	**169**	164	157
Endowment Pledges	**138**	166	168
Undistributed General Investment Income	**3**	4	7
Current Use Investments	**75**	75	72
Current Use Pledges	**145**	151	151
Facilities, Net	**766**	774	724
Total Assets	**$ 5,420**	$ 5,208	$ 4,821

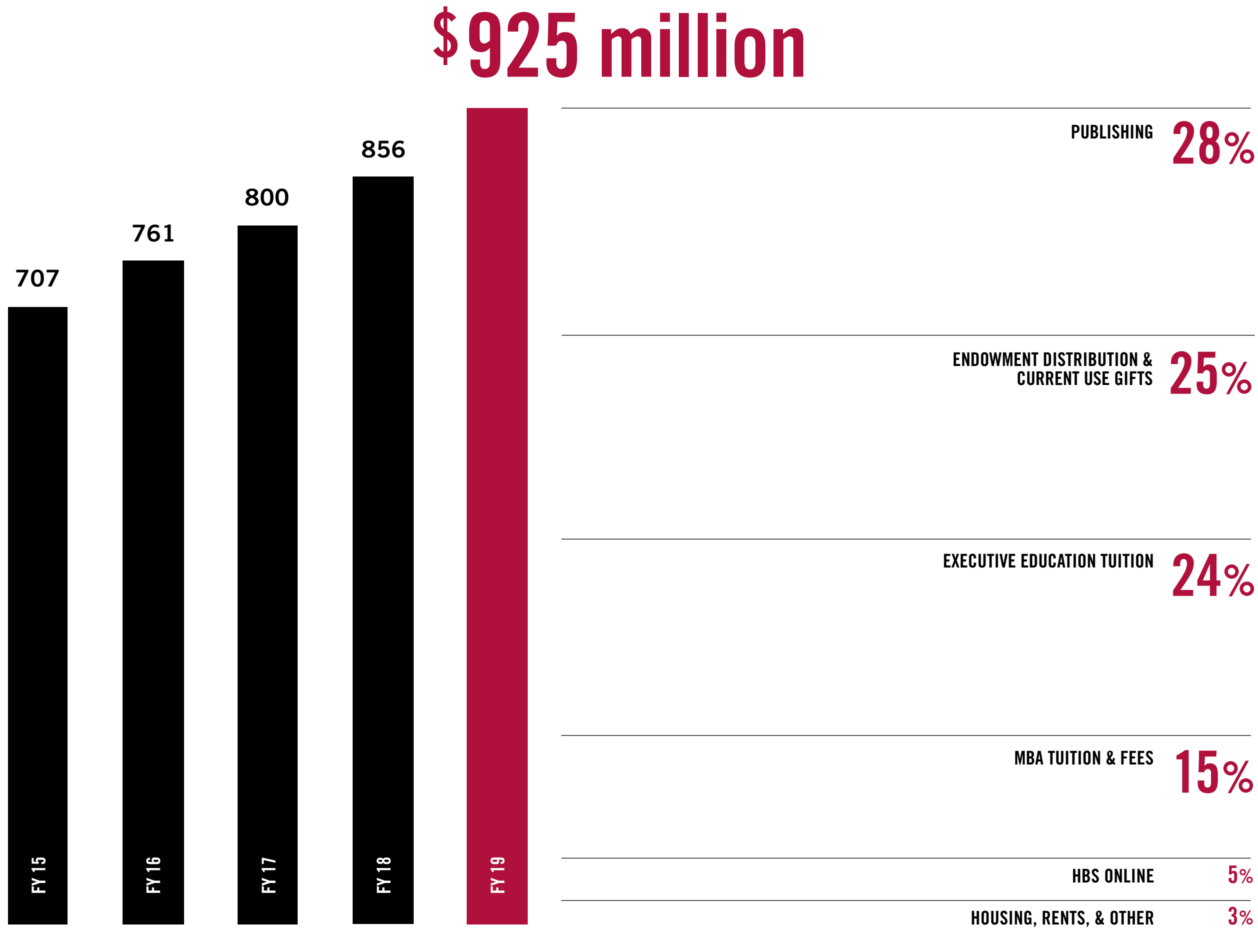
Liabilities			
Deposits, Advances, & Other	**$ 95**	$ 82	$ 69
Deferred Revenue	**183**	181	150
Other Debt Owed to University	**31**	27	26
Building Debt	**46**	55	64
Total Liabilities	**$ 355**	$ 345	$ 309

Net Assets			
Current Use Reserves	**$ 129**	$ 118	$ 145
Endowment Funds	**3,985**	3,787	3,472
Current Use Funds	**220**	226	223
Unexpended Endowment Income	**1**	1	1
Student Loan Funds	**10**	12	11
Investment in Facilities	**720**	719	660
Total Net Assets	**$ 5,065**	$ 4,863	$ 4,512

Total Liabilities + Net Assets	**$ 5,420**	$ 5,208	$ 4,821

* In pursuit of greater comparability across the Harvard schools, the University has asked all the schools to report their net results in accordance with generally accepted accounting principles (GAAP) in the United States. In addition to results for fiscal 2019, the School's results for fiscal years 2017 and 2018 are presented in accordance with GAAP within the Statement of Activity and Cash Flows on the opposite page.

SUPPLEMENTAL FINANCIAL INFORMATION



REVENUES

HBS funds its operations with cash from three primary sources: MBA tuition and fees, earned income (from Executive Education, Publishing, and Online), and philanthropic revenues (including current-use gifts and distribution from the endowment).

Earned income and philanthropy are sensitive to trends in the economy and the capital markets, which continued to perform well in fiscal 2019. The School's total revenues increased by $69 million, or 8 percent, to $925 million, from $856 million a year earlier.

This increase was primarily driven by growth at Executive Education, Publishing, and Online. All three groups delivered solid operating margin leverage on sales growth in fiscal 2019, and Online generated an operating surplus for the first time. Despite increases in compensation and other variable costs as revenues increased, as well as ongoing growth-focused investments, each group contributed more earned income to the School's fiscal 2019 operations than initially anticipated.

MBA Tuition & Fees

Student tuition and fee revenue from the MBA program increased to $140 million, from $138 million in fiscal 2018. First-year MBA tuition in fiscal 2019 was $73,440, compared with $72,000 last year. The School's combined tuition and fees for fiscal 2019 were near the midpoint among the seven peer schools tracked by HBS, and amounted to 15 percent of the School's total revenues, compared with 16 percent a year earlier.

Executive Education

Executive Education tuition revenue increased by $15 million, or 7 percent, from fiscal 2018, to $222 million, exceeding the School's forecast by 9 percent. As in the prior year, this growth was made possible by new and newly renovated buildings on campus, including Tata Hall, Esteves Hall, and the Chao Center. Leveraging the additional space in these facilities, HBS continued to expand its Executive Education program portfolio and increase the number of program participants in fiscal 2019, and total enrollment grew more than 4 percent to approximately 12,600.

In addition to increased participation in the School's comprehensive leadership programs, this enrollment growth reflected an increase in the number of focused programs, including the launch of three new focused programs during the year. Participation in custom programs was flat with fiscal 2018, as the group continued to diversify its custom portfolio across industries and geographies as well as by program type and size.

Global Executive Education program participation declined from fiscal 2018, while tuition revenue remained essentially flat. The group continued to expand its portfolio of longer, modular programs that include time spent both abroad and on the HBS campus by launching a new Senior Executive Leadership Program–China with solid enrollments. Executive Education delivered the second and third iterations of SELP–Middle East and SELP–India, generating continued regional interest.

Total Executive Education tuition revenue amounted to 24 percent of the School's total revenues in fiscal 2019, flat with the prior year.

Harvard Business Publishing

All three of Publishing's market-facing groups delivered stronger than anticipated revenues in fiscal 2019. Total revenue grew by $22 million, or 9 percent, to $262 million, from $240 million a year earlier, exceeding the School's cautious forecast for zero growth. International sales rose 14 percent, comprising 36 percent of Publishing's total annual revenues.

Harvard Business Review (HBR) group sales increased 7 percent from the prior year. The subscription model for HBR continued to gain market traction in fiscal 2019; paid circulation grew 6 percent to 340,000—the highest since *Harvard Business Review* began publication almost a century ago—driven by refined social media/digital campaigns and new subscription offers and options.

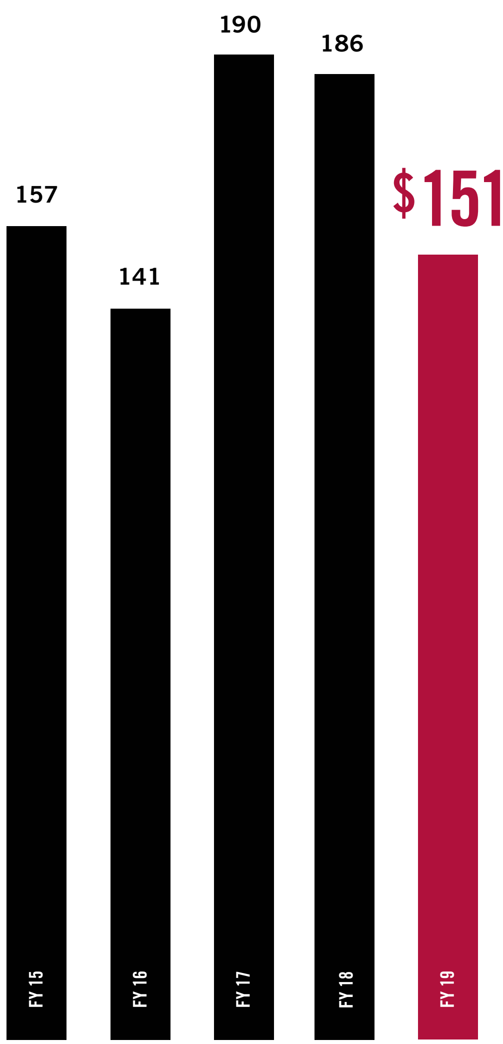
Corporate Learning continued to leverage its position as a provider of technology-enabled leadership development solutions for global corporations, and sales for fiscal 2019 were up 10 percent from a year earlier. The group updated more than 120 clients to its newly released Spark platform; benefited from improved renewal rates for its flagship product, Harvard ManageMentor; and delivered blended learning programs to a record 23,000 participants.

Higher Education sales of course materials grew 5 percent from fiscal 2018. The website launched by the group late in fiscal 2018 generated substantial growth in online course sales. In addition, the group experimented with new product/editorial formats, including podcasts, the HBR Visual Library, and website content focused on teaching, while also launching a simulation platform in partnership with external providers.

As in the prior year, total Publishing revenue amounted to 28 percent of the School's total revenues in fiscal 2019.

HBS Online

After posting deficits since its inception five years ago, in fiscal 2019 the Online group became a contributor to the School's internally generated cash from operations. Total revenue more than doubled to $43 million, from $19 million a year earlier,



CASH RECEIVED FROM GIFTS (in millions) resulting in an operating surplus of nearly $5 million. This compares with a $5 million operating deficit in fiscal 2018, and deficits exceeding $10 million for each of the four prior years.

Online continued to add courses in fiscal 2019, launching Global Business and Leadership Principles, and reached a total of more than 16,000 asynchronous participants across the portfolio during the year. Additionally, the group added a second cohort to its Harvard Business Analytics Program in conjunction with the Harvard John A. Paulson School of Engineering and Applied Sciences.

Online also launched Leading Change, the first course in the Certificate in School Management and Leadership Program offered with the Harvard Graduate School of Education. Moreover, HBX Live, the virtual classroom, hosted 192 synchronous sessions—a 90 percent increase from fiscal 2018—and generated 400 percent growth in revenue for the year.

Total Online revenue amounted to 5 percent of the School's total revenues in fiscal 2019, compared with 2 percent for the prior year.

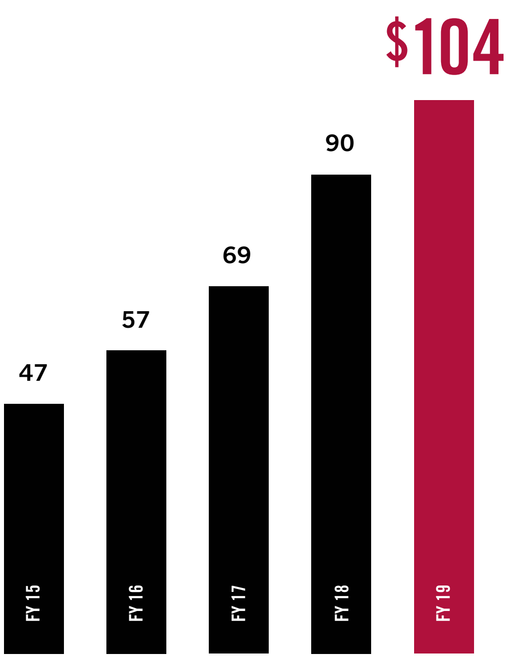
Gifts & Endowment

Philanthropic revenue has long been vital to sustaining the School's annual operations. In fiscal 2019, total revenue from the School's three philanthropic sources—distribution from the endowment, unrestricted current-use gifts, and restricted current-use gifts—was $230 million, compared with $229 million in fiscal 2018. This revenue amounted to nearly 25 percent of the School's total revenues, compared with 27 percent a year earlier. In contrast, for the University as a whole, philanthropic revenue for fiscal 2019 amounted to 43 percent of total operating revenues.

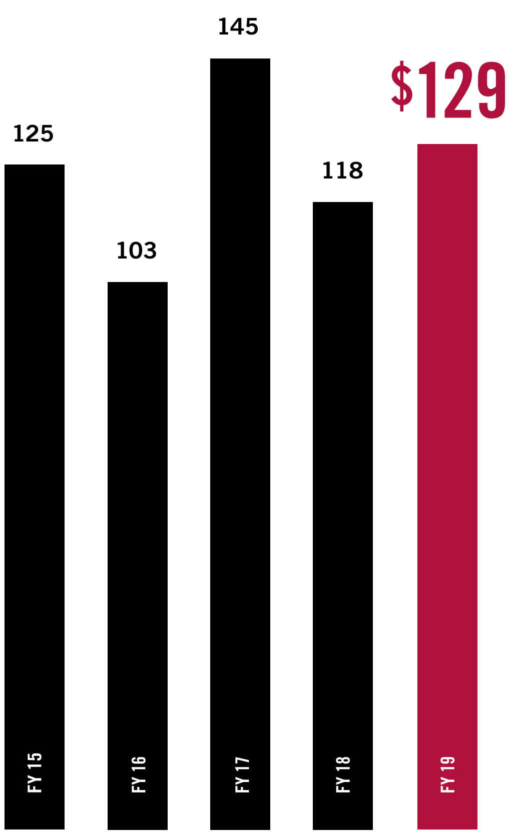
The School's annual endowment distribution for fiscal 2019 increased 8 percent from the prior year to $162 million, amounting to 17.5 percent of total revenue. The HBS endowment currently consists of more than 1,000 discrete funds established over the years by individual donors, corporations, and reunion classes. The School budgets the use of endowment distributions to support operations in accordance with the donors' intentions and the terms of each gift.

Harvard is obligated to preserve the purchasing power of the endowment by spending only a small fraction of its value each year. Spending more than that over time, for whatever reason, would privilege the present over the future in a manner inconsistent with an endowment's fundamental purpose of maintaining intergenerational equity.

The University executes on this obligation when determining each year's endowment payout rate—that is, the percentage of the endowment's fair market value withdrawn and distributed annually for operations and for one-time or time-limited strategic



CASH FROM OPERATIONS (in millions)



UNRESTRICTED RESERVES (in millions)

purposes. This rate applies to HBS and to all schools at Harvard.

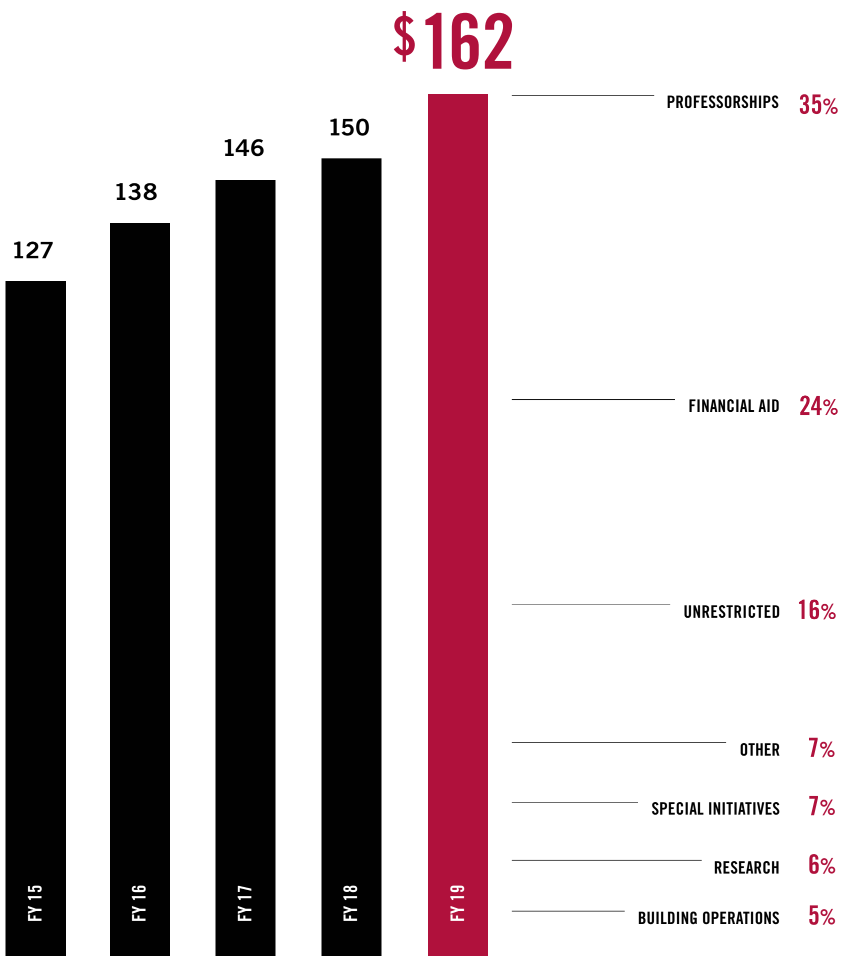
Consistent with the long-term goal of preserving the value of the endowment in real terms (after inflation) and generating a predictable stream of available income, the University's targeted annual payout range is 5.0 to 5.5 percent of market value. The payout rate for fiscal 2019 met that target at 5.1 percent, compared with 5.2 percent for the prior year.

Over the past 10 years, the rate has fluctuated from a low of 4.6 percent in fiscal 2009 to a high of 6.1 percent in fiscal 2010. This variation exists because the dollar amount of the distribution for the next fiscal year is determined well in advance of the start of the fiscal year and prior to knowing the market value at the end of it. This practice is followed to allow the University's schools and units adequate time for financial planning.

The utilization of a payout formula means that the annual payout rate is generally lower following years of relatively high investment returns, and higher following years of lower investment returns. Adjustments can be made in succeeding years, keeping in mind the long-term payout goals of balancing budgetary stability with the preservation of the endowment's purchasing power. Each year the Harvard Corporation approves the final distribution amount.

Harvard Endowment Returns

FY 19	**6.5 %**
FY 18	10.0
FY 17	8.1
FY 16	– 2.0
FY 15	5.8
FY 14	15.4
FY 13	11.3
FY 12	– 0.1
FY 11	21.4
FY 10	11.0



ENDOWMENT DISTRIBUTION (in millions)

ENDOWMENT (in billions)

Funds within the HBS endowment, along with those of the other Harvard schools, are managed by Harvard Management Company (HMC), a nonprofit, wholly owned subsidiary of the University. HMC has managed the Harvard endowment portfolio since 1974. Its mission is to help ensure the University has the financial resources to confidently maintain and expand its leadership in education and research for future generations.

HMC, as an organization, and the Harvard endowment portfolio, are about halfway through a five-year restructuring. HMC's early organizational efforts involved rebuilding its internal structure and culture, constructing a generalist investment team, establishing new investment processes, and putting in place new performance incentives.

HMC's investment portfolio is evolving in parallel. Repositioning of the portfolio's liquid assets—public equities and hedge funds—is well underway. Given the nature of HMC's illiquid investments—private equity, real estate, and natural resources—restructuring this portion of the portfolio will span multiple years.

The return on endowment assets for fiscal 2019, net of investment expenses and fees, was 6.5 percent, compared with 10 percent and 8.1 percent endowment returns, respectively, for the two prior fiscal years.

As in fiscal 2018, fiscal 2019 was a year in which asset allocation—or risk level—was a major factor in returns. Greater exposure to venture capital (a high-risk/high-reward asset class) would have resulted in a significantly higher return on the Harvard endowment. HMC's portfolio exposure to venture capital is notably small in the context of leading endowments.

As a result of the Tax Cuts and Jobs Act of 2017, fiscal 2019 was the first year in which Harvard, along with other large US colleges and universities, was liable for a new tax upon its endowment investment returns. The net impact on Harvard for fiscal 2019 was approximately 1 percent of total University revenues.

The value of the University endowment grew to $40.9 billion in fiscal 2019—an increase of 4.3 percent from $39.2 billion a year earlier. This value reflects investment returns, net of expenses and fees, as well as cash gifts to the endowment received during the year, net of the University's annual distributions and decapitalizations. The HBS endowment has comprised approximately 9 to 10 percent of the University endowment's total value over the past 10 years.

The fiscal 2019 year-end market value of the HBS endowment was $4 billion on June 30, 2019, compared with $3.8 billion a year earlier. This increase reflected the 6.5 percent net growth in market value and the subtraction of the School's annual distribution and decapitalizations, offset by the $76 million in endowment gifts received by HBS during the year, and the $100 million of internally generated cash transferred by the School to the endowment reserve.

HBS received gifts from more than 11,000 donors in fiscal 2019, including MBA, Doctoral, and Executive Education program alumni, as well as friends of the School. Approximately 24 percent of the School's MBA alumni gave to HBS in fiscal 2019.

Total cash received from gifts in fiscal 2019, including new endowment gifts and gifts for capital construction projects, payments on prior years' pledges, and restricted and unrestricted current-use giving, was $151 million, compared with $186 million in the prior year. Cash giving to the endowment decreased to $76 million, from $101 million in fiscal 2018. Cash giving for construction projects increased to $6 million, from $4 million.

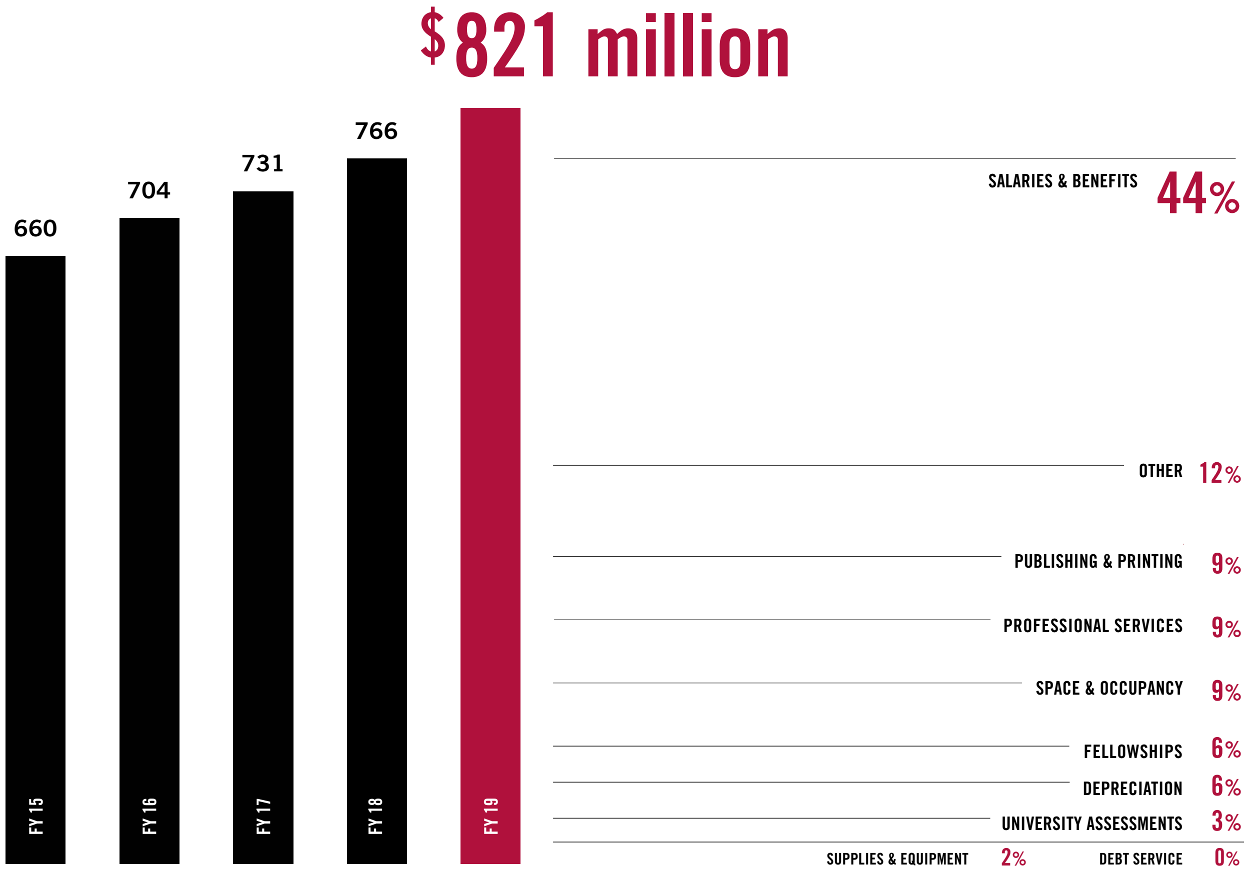
Current-use giving—both restricted and unrestricted—provides crucial funding for innovation across the School. Because current-use gifts can be spent immediately, they have a significant impact on cash from operations and, therefore, the School's ability to capitalize on emerging strategic opportunities. For example, current-use giving has enabled the School to roll out FIELD (Field Immersion Experiences for Leadership Development), support the faculty's ambitious research agenda, develop the Harvard i-lab ecosystem, and launch Online.

Growing unrestricted current-use giving to a sustainable annual level of $40 million was one of the major goals of The Campaign for Harvard Business School, which concluded in fiscal 2018. In the post-Campaign year of fiscal 2019, revenue from these flexible current-use gifts decreased 9 percent from $44 million a year earlier, matching the long-term target level of $40 million. Going forward, sustaining unrestricted current-use giving will be instrumental in achieving the mission of the School.

Restricted current-use giving typically varies from year to year in line with the School's changing fundraising priorities and strategic needs. Reflecting the conclusion of the Campaign, fiscal 2019 revenue from these restricted gifts decreased 20 percent from a year earlier to $28 million.

Housing, Rents, Interest Income, & Other

Total revenue from the Housing, Rents and Other category for fiscal 2019 increased by $2 million from the prior year to $23 million. The School reported interest income of $5 million, compared with $2 million in fiscal 2018, a reflection of gradually increasing interest rates. As in the prior year, total housing, rents, interest income, and other revenue amounted to 3 percent of the School's total revenues in fiscal 2019.



EXPENSES

Executive Education, Publishing, and Online operating costs, as well as the School's faculty research costs, cut across multiple expense line items in the Statement of Activity and Cash Flow on page 22.

Faculty research expenses include a portion of faculty salaries and benefits expense, as well as direct costs for faculty support staff and travel, and for the School's network of global offices. Additionally, HBS allocates a portion of the costs associated with library resources, campus facilities, technology, and administration to this category. Faculty research expenses totaled $152 million in fiscal 2019, comprising nearly 19 percent of the School's operating budget.

Although HBS characterizes costs charged to Executive Education, Publishing, and Online as operating expenses, in a profit-seeking enterprise they would in large part be considered as cost of goods sold. These expenses include direct costs for staff compensation, specialized outside professional services in information technology and other functional areas, marketing costs, and residence expenses for executive program participants.

The School's total operating expenses for fiscal 2019 were $821 million, up by $55 million, or 7 percent, from $766 million for fiscal 2018. This increase is attributable to several factors. A University-wide accounting change and higher costs in Online increased other expenses. Growth in the size of the School's faculty and staff, as well as higher compensation costs, resulted in a higher salaries and benefits expense.

Depreciation expense was up substantially, reflecting the opening of Klarman Hall. Increases in professional services and printing and publishing expenses were primarily attributable to growth-focused initiatives at Publishing and Online.

Salaries & Benefits

Compensation for faculty and administrative staff is the largest expense at HBS. The School's salaries and benefits expense for fiscal 2019 increased 5.6 percent to $359 million, from $340 million in fiscal 2018. As in the prior year, this represented 44 percent of the School's total operating costs.

Building the HBS faculty is a key strategic priority for the School. The total number of faculty, as measured in FTEs, can rise or fall in any given year, reflecting retirements, departures, and fluctuations in recruiting activity. Fiscal 2019 was a successful year for faculty recruiting and promotions. Fourteen candidates accepted assistant professor positions. Ten faculty members received promotions to associate or tenured positions. Net of retirements and departures, the size of the HBS faculty increased to 233 FTEs in fiscal 2019, from 225 FTEs a year earlier.

Recruiting administrative staff talent to fill open positions at HBS is becoming more challenging as the employment market tightens. The School's staff grew to a budgeted 1,761 FTEs in fiscal 2019, from 1,721 in the prior year. In addition to those aimed at capitalizing on growth opportunities in Publishing and Online, significant staff increases were seen in the Information Technology and External Relations groups, as well as in support of the Harvard i-lab and Global Initiative.

Fellowships

The School categorizes fellowships, or financial aid, as an expense line item on the Statement of Activity and Cash Flows. Making education at HBS affordable to a broad cross section of applicants, regardless of their financial circumstances, is a longstanding goal of the School.

The prospect of entering or returning to the work force with high levels of education debt can deter strong MBA candidates from applying to HBS and restrict their career choices upon graduation. This is particularly true for younger students, women, those from outside the United States, and students whose early career paths have not enabled them to reduce their undergraduate loans.

Consequently, the School strives to assist students in minimizing their debt at graduation by ensuring that fellowship support keeps pace with tuition and fees. Extending a long-term record of annual increases in financial aid, total Fellowships expense for fiscal 2019, including assistance for MBA students, Doctoral candidates, and a limited number of Executive Education participants, increased by $1 million, or 2 percent, from fiscal 2018 to $51 million. Fellowships amounted to 6 percent of the School's total operating costs in fiscal 2019, compared with 7 percent a year earlier.

Approximately half of the School's MBA students currently receive fellowships, which cover an average of more than 50 percent of a student's total tuition. About 27 percent of total tuition—nearly $38 million—was awarded as fellowships in fiscal 2019. This includes fellowships to more than 170 students in the classes of 2020 and 2021 who were the first in their families to attend college and now graduate school.

Average fellowship support per student increased 8 percent in fiscal 2019 to $42,000, from $38,959 in the prior year. Over the past five fiscal years, the School's average two-year MBA fellowship award has grown from $64,836 for the Class of 2015 to $80,400 for the Class of 2020.

Funding for fellowships comes from restricted endowment and current-use giving by HBS alumni and friends. These funds are supplemented by unrestricted funds as necessary, which totaled $4 million in fiscal 2019.

Publishing & Printing

This expense category includes a portion of Publishing's production costs plus a small amount of spending related to the School's printed materials and publications. The production costs include, for example, *Harvard Business Review*'s printing expense, which increased in fiscal 2019 as circulation continued to grow. These costs also include strategic investments in digital infrastructure and content designed to extend the group's record of consistent growth at a time of significant change in the way people consume information.

The School's publishing and printing expenses for fiscal 2019 increased by $3 million, or 4 percent, from the prior year, to $77 million. This amounted to 9 percent of the School's total operating costs, compared with 10 percent in fiscal 2018.

Space & Occupancy

The HBS campus includes 36 buildings encompassing more than 1.9 million square feet of occupied space. Space and occupancy expense includes costs related to maintaining and operating the School's buildings and campus infrastructure. Additionally, facilities improvement and renovation costs that do not qualify as capital expenses are generally categorized as space and occupancy.

Also included in this category are expenses related to dining facilities and other campus services, and costs associated with leased space for Publishing, Online, and the School's global offices. In addition, residence costs for Executive Education program participants are reported as space and occupancy expenses.

The School's space and occupancy expenses for fiscal 2019 grew by $1 million, or 1.4 percent, from the prior year to $72 million. Increases in dining and student housing costs and spending on small facilities projects were partially offset by lower utilities and support services expenses. As in the prior year, space and occupancy expenses amounted to 9 percent of the School's total operating costs.

Professional Services

A large portion of the School's professional services expense is related to spending that a for-profit business would categorize as cost of goods sold—including growth-focused investments at Publishing and Online, as well as compensation for faculty who teach Executive Education programs.

For fiscal 2019, a University-wide accounting change shifted a portion of the School's contingent labor costs to the Other Expenses category. As a result, professional services expenses for fiscal 2019 rose by a comparatively modest $4 million, or 6 percent, from the prior year to $72 million. As in fiscal 2018, professional services expenses amounted to 9 percent of total operating costs.

The increase in professional services expenses for fiscal 2019 primarily reflected costs for numerous projects designed to enhance the School's information technology (IT) capabilities. The School's IT infrastructure is becoming increasingly fundamental to operations. As a result, investments in IT have contributed to higher fixed costs at HBS in recent years. For fiscal 2019, the School's total IT investment grew by $5 million, or 6 percent, from fiscal 2018 to $87 million.

In addition to implementing new MBA classroom video and student engagement platforms during the year, the School made substantial faculty research computing and research information system investments. The School launched a community-wide video and web conferencing service; continued to roll out a new VoIP telephone system; and strengthened cybersecurity technologies, protocols, and resources across the campus.

IT spending represented nearly 11 percent of the School's total operating expenses in fiscal 2019. Consequently, controlling IT costs is an important financial priority for the School. Initiatives currently underway include shifting toward reliance on software as a service platforms and away from custom applications developed at the School, greater use of third-party IT service providers, and moving IT applications to the cloud.

Supplies & Equipment and Other Expenses

Supplies and equipment expenses for fiscal 2019 increased by $1 million, or 8 percent, from the prior year to $13 million, or 2 percent of the School's total operating costs. In the Other Expenses category, fiscal 2019 spending rose by $20 million, or more than 24 percent, from fiscal 2018 to $102 million. This amounted to 12 percent of the School's total operating costs, compared with 11 percent a year earlier.

Approximately $15 million of the increase in other expenses related to two types of outlays. First, costs for a wide range of contingent labor providers, formerly categorized by the School as professional services expenses, shifted to other expenses. Second, other expenses for fiscal 2019 reflected increased payments to an outside technology platform vendor at Online.

These payments were up substantially from fiscal 2018, reflecting both an accounting change and expansion in the group's portfolio of course offerings. Approximately $5 million of the fiscal 2019 growth in other expenses reflected increased spending in several areas, including advertising by Online and campus-wide catering costs and royalty fees.

Debt Service

HBS finances major capital projects with a mix of three sources of funding. The most important sources are gifts and unrestricted reserves of internally generated cash. The School may also make strategic use of debt financed through the University as appropriate.

The HBS balance sheet historically has been only modestly leveraged, and debt leverage remained low in fiscal 2019. Klarman Hall—the School's most recent large construction project—was substantially completed in fiscal 2018. As a result, total capital expenses for fiscal 2019 decreased to $38 million in fiscal 2019, from $92 million in the prior year. As in fiscal 2018, these investments were primarily funded by internally generated cash, and there were no new borrowings. HBS paid down $9 million in building debt in fiscal 2019, compared with $8 million a year earlier.

As a result, the School's year-end fiscal 2019 building debt-to-asset ratio decreased to 0.9 percent, from 1.1 percent in the prior year. Other university debt—mainly consisting of repayment obligations to the University for mortgage loans made by HBS as a faculty recruiting incentive—increased by $4 million from fiscal 2018 to $31 million.

The School's debt service expense consists of interest payments to the University, and is covered by using cash from operations. Fiscal 2019 debt service expense was $3 million, flat with the prior year. As in fiscal 2018, this expense was mainly associated with borrowings to finance prior years' campus expansion. Consistent with the three prior years, the interest portion of the School's debt service amounted to less than 1 percent of total operating costs in fiscal 2019.

University Assessments

The University assessments expense encompasses services provided to HBS by Harvard University, including payroll and benefits administration, processing of accounts receivable and payable, and legal services. The amount charged to HBS in any given year is primarily calculated as a percentage of the School's total expenses. As expected, the School's expense in fiscal 2019 for these assessments increased by $2 million from the prior year to $26 million, amounting to 3 percent of total operating costs.

Depreciation

The School computes depreciation using the straight-line method over the estimated useful lives of the assets. Depreciation expense for fiscal 2019 increased by $4 million, or 9.5 percent, from the prior year to $46 million. This increase primarily reflected the School's larger asset base following the opening of Klarman Hall. The School's depreciation expense for fiscal 2019 amounted to 6 percent of total operating costs, compared with 5 percent a year earlier.

CASH BEFORE CAPITAL ACTIVITIES

The School's cash from operations increased in fiscal 2019 by $14 million from the prior year to $104 million. As in fiscal 2018, this cash was largely generated by margin contributions from the School's competitive business units—Executive Education, Publishing and Online—as well as generous giving to the School by alumni and friends of HBS. In addition, depreciation is a non-cash item that added back $46 million to the School's cash flow in fiscal 2019, compared with $42 million in the prior year.

NET CAPITAL EXPENSES

Following the completion of Klarman Hall in fiscal 2018, the School's total capital investment decreased to $38 million in fiscal 2019, from $92 million in the prior year. Fiscal 2019 capital activity focused on multiple small projects designed to prevent deferred maintenance, reduce the School's environmental footprint, enhance sustainability, and preserve the value of the HBS campus for future generations. In addition to ongoing facilities renewal and maintenance, these projects included IT infrastructure and digital technology upgrades, as well as energy efficiency measures across the campus to meet the University's greenhouse gas reduction goals.

The School's net capital expenses for fiscal 2019 decreased to $35 million, from $79 million a year earlier, largely funded as in the prior year with internally generated cash. In addition to lower capital spending, the decrease reflected the timing of the receipt of cash gifts for capital projects, partially offset by planned increases in capital project pre-funding.

CHANGES IN DEBT & OTHER

The School's debt and other cash activities decreased by $104 million in fiscal 2019, compared with a decrease of $80 million in the prior year. The fiscal 2019 decrease primarily reflected a transfer of $100 million in unrestricted cash to the HBS endowment, made possible by the School's strong operating surplus. HBS made a comparable $65 million cash transfer to the endowment in fiscal 2018.

Because gifts, internally generated cash, and unrestricted reserves have been available and sufficient to finance capital activities, fiscal 2019 marked the School's eleventh consecutive year with no new borrowings. Debt principal payments increased by $1 million from the prior year to $9 million.

Capitalization of endowment income—or cash used to purchase endowment units—was a $2 million use of cash in fiscal 2019, flat with the prior year. In compliance with federal and state legal requirements, the School's objective is to spend as much of the endowment distribution as possible in any given year, according to the terms of each gift. Funds unspent as a result of gift restrictions are generally reinvested in the endowment.

In compliance with the law, HBS accesses the investment appreciation within existing endowment accounts when the terms of the gift require funds to be withdrawn at a rate higher than the University's payout rate in any given year. Decapitalization of endowment income—or cash drawn from endowment appreciation—was a source of $2 million in cash in fiscal 2019, compared with $3 million for the prior year.

ENDING BALANCE, UNRESTRICTED RESERVES

Nearly 57 percent of the School's revenues come from Executive Education, Publishing, and Online—business units that are highly sensitive to the economy. Consequently, maintaining an ample balance of unrestricted reserves outside of the endowment is crucial in providing HBS with sufficient liquidity to finance ongoing campus renewal and expansion projects, and to capitalize on emerging strategic opportunities through economic cycles over the long term.

Driven by the School's continued healthy cash from operations, fiscal 2019 was a successful year in this regard. After the $100 million of unrestricted, internally generated cash transferred to the endowment, HBS concluded fiscal 2019 with an unrestricted current-use reserves balance of $129 million, compared with $118 million a year earlier. This level is substantially above the $100 million in unrestricted reserves established by HBS as the School's long-term liquidity management target.

This document is intended to provide insight into the way Harvard Business School manages its resources and plans strategically for its future. Further information about the School can be found at www.hbs.edu.

We welcome questions and comments from our readers. Please direct correspondence to Richard P. Melnick, Chief Financial Officer: rmelnick@hbs.edu or to the Office of the Dean: officedean@hbs.edu.

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