

- 2 LETTER FROM THE PRESIDENT
- 4 LETTER TO THE BOARD OF OVERSEERS
- 8 Analysis of financial results
- 16 REVIEW OF ENDOWMENT RESULTS
- 18 REVIEW OF CAPITAL ACTIVITIES
- 22 ANNUAL REPORT OF THE HARVARD

 MANAGEMENT COMPANY
- 27 FINANCIAL STATEMENTS
- 53 SUPPLEMENTAL INFORMATION



FRESHMAN SEMINAR WITH PROFESSOR EVELYN BROOKS HIGGINBOTHAM

President Summers has set a goal of enabling all students to participate in a small faculty-led class during their first year at Harvard.

Towards this end, the Freshman Seminar Program has tripled in size in the past five years, now involving almost two-thirds of the

freshman class. In the coming year, 115 seminars will be offered in topics ranging from the efficacy of antibiotics to the literary influences of J.R.R. Tolkien. Students in Professor Higginbotham's seminar are examining and analyzing the northern civil rights movement.

To the Members of the Harvard Community:

I am pleased to present to you Harvard University's fiscal 2004 financial report. This past year the University has made significant progress in examining the undergraduate curriculum, charting new areas of growth in the sciences, and planning for development of our land in Allston. While making advances in these and other important areas, the University has maintained financial strength and realized an operating surplus for the year ended June 30, 2004.

The University has addressed the challenging economic conditions of the past several years with numerous steps to reduce costs and streamline operations. The past year saw a major review of the University's core central administration, resulting in level funding for fiscal 2005 and a subsequent redirection of funds to graduate student financial aid. Several schools, most notably the Medical School, the Radcliffe Institute for Advanced Study, and the Graduate School of Education, restructured operational areas to eliminate redundancies, improve effectiveness, and direct resources to high priority areas. In addition, the continuing generosity of our supporters, who contributed a total of \$592 million, and the exceptional performance of our endowment investments have allowed the University to maintain its existing strengths and develop in new and exciting areas.

We enter the coming year with an ambitious agenda. Besides the continuing review of the undergraduate academic experience, we are taking additional steps to ensure that the College attracts talented students from all economic backgrounds and, at the graduate level, that students who wish to pursue careers in public service are

not deterred because of finances. We hope to expand our research in important areas of scientific inquiry through such initiatives as the Harvard Stem Cell Institute and the Broad Institute collaboration with the Massachusetts Institute of Technology, the Harvard-affiliated hospitals, and the Whitehead Institute for Biomedical Research, and move forward with academic and physical planning for the eventual use of our land in Allston. These academic challenges and opportunities will require significant new resources. In addition, we must realize the maximum benefit from our existing resources by directing them to the areas of our highest priority and ensuring that we operate in a financially responsible manner.

In order to advance these common goals, the University community—faculty, staff, alumni, and students—must continue to work together to use our resources wisely. In doing so, I am hopeful that we can build an even stronger and brighter future for this great university.

Lawrence H. Summers

James H. Jumes

PRESIDENT

October 1, 2004

To the Board of Overseers of Harvard College:

Harvard University's financial health remains strong due in large measure to recent operational reviews and restructuring throughout the University. These efforts have allowed the University to achieve greater efficiencies and significant financial savings, particularly in central administrative services and purchasing. Following the lower investment returns of fiscal 2001 and 2002, income distributed from existing endowments rose only 2% in fiscal 2004, resulting in persistent pressure on operating budgets across the University. We enter fiscal 2005 with two years of improved investment returns, but with continued concerns for both revenue and expenses. Government support for sponsored research, rising health benefits and retirement costs for faculty and staff, and the increasing need to provide greater financial aid for students are areas that pose significant challenges. While the financial picture is improving, the University's agenda is no less ambitious than in prior years. We must remain committed to the sound financial management needed to achieve the University's goals. Continued fiscal discipline and increased administrative efficiency are essential to maximizing the resources available to support our teaching and research mission.

FINANCIAL HIGHLIGHTS

- The University ended the year with an operating surplus of \$37 million on \$2.6 billion of expenses. Unrestricted expenses exceeded income by \$12 million but were offset by a surplus of \$49 million in restricted funds (funds whose use is limited in future years to the purposes designated by the donors or sponsors).
- ❖ The Harvard Management Company had an excellent year, achieving a 21.1% total return for fiscal 2004 and raising the four-year return to an annualized 7.2%. Total market value of the endowment rose from \$19.3 billion to \$22.6 billion, contributing to the growth in total net assets from \$23.1 billion to \$26.9 billion.

- ❖ Through the generosity of alumni and friends, total giving reached an impressive \$592 million. Endowment gifts totaled \$258 million, current use gifts were \$154 million, and grants for research as well as gifts for loans, facilities, and life income funds comprised the remaining \$180 million.
- Student income, net of scholarships applied to tuition and fees, rose by 6%. As in fiscal 2003, total scholarships and other student awards grew by 11%. Financial aid for both undergraduate and graduate students continues to be one of the University's highest priorities.
- ❖ Sponsored funding for research and training rose 7%. This change reflects an increase in federal funding of 14% offset by a decline in support from non-federal sources of 13%. Our primary federal sponsor, the National Institutes of Health (NIH), did not experience a large growth in appropriation in fiscal 2004. Nonetheless, Harvard benefited from a 15% increase in funding from NIH as well as increased funding from other federal sponsors, including NASA and the National Science Foundation. Many of our non-federal sponsors suffered a decline in their investment performance, leading to reduced funding capacity and consequently fewer grants.
- Endowment income distributed for operations increased by 5% to \$808 million. This change is the result of a 2% increase in the distribution rate as well as distributions on additions to the endowment. The fiscal 2004 spending rate was 4.9%, within our targeted range of 4.5% to 5.0%.

Endowment income distributed for operations remained Harvard's largest source of income, constituting 31% of total operating income compared with 21% ten years ago. This growth reflects both the generous support of our alumni and friends as well as better capital markets and the strong performance of the Harvard Management Company.

❖ Total expenses grew by 5%. This change was primarily driven by significant increases in compensation and space and occupancy costs.

The University spent \$1.3 billion on compensation, an increase of 6% over fiscal

2003. Compensation growth included an increase in total salary and wage costs

of 5% and an 11% increase in benefits expenses. The growth in benefits expenses

resulted from increased pension and postretirement welfare costs as well as rising

health care costs.

❖ Space and occupancy expenses increased by 9%. In addition, the University spent

a total of \$410 million on physical renewal, new facilities, and acquisitions.

Significant construction expenditures were incurred for the new research building

in the Medical Area, the Center for Government and International Studies, the

Oxford Street garage, Baker Library, One Western Avenue, the Laboratory for

Integrated Science and Engineering, the new Dental School building, and 29

Garden Street graduate student and affiliate housing.

With the breadth of resources entrusted to the University by donors, the federal

government, students, and other supporters, the need for prudent fiscal oversight

is great. Working closely with the University's Governing Boards and our auditors,

we continue to review and improve our financial policies, procedures, and practices.

Such oversight will ensure the continued financial strength needed to pursue the

University's ambitious agenda in fiscal 2005 and beyond.

Ann E. Berman

an & Berman

VICE PRESIDENT FOR FINANCE

James F. Rothenberg

TREASURER

October 1, 2004



Analysis of financial results

The University ended fiscal 2004 in solid financial condition, with an operating surplus, strong endowment growth, and total net assets of \$26.9 billion.

OVERVIEW

In fiscal 2004, the University achieved a restricted operating surplus, partly offset by an unrestricted operating deficit. The University's restricted operating surplus of \$48.5 million was substantially less than the \$69.6 million surplus of fiscal 2003. The unrestricted operating deficit of \$11.7 million represents the second consecutive year of negative unrestricted operating results and, along with the decline in the restricted operating surplus, highlights the importance of continued discretion in

spending. In response to this concern and in order to redirect resources to the University's priorities in the areas of teaching and research, the core central administration undertook a budget review designed to improve efficiency and effectiveness and reduce costs. The review resulted in a flat central administration budget for fiscal 2005. At year-end, the University's total assets were \$60.0 billion, and total liabilities were \$33.1 billion. Net assets of \$26.9 billion included \$22.6 billion of endowment funds.

FINANCIAL RESULTS

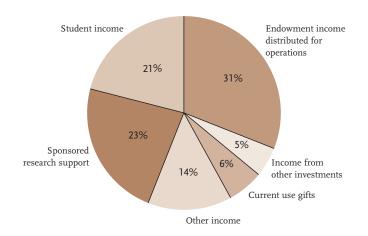
This section of the report analyzes revenue and expenses for fiscal 2004.

REVENUE The University's operating revenue totaled \$2.6 billion in fiscal 2004, a 5% increase over the prior year. Revenue includes student income, sponsored research support, gifts for current use, investment income, and other income, including revenue from the University's auxiliary activities.

Harvard University's many achievements over the past fiscal year extended from the areas of teaching and research to administration and public service. The highlights that follow provide a sampling of the accomplishments of each School and of the University as a whole.

STUDENT INCOME Student income totaled \$556.3 million in fiscal 2004, an increase of 6% over fiscal 2003. Revenue from undergraduate tuition rose 6%, mirroring the increase in the tuition rate for fiscal 2004. Graduate tuition revenue increased 8%, reflecting 6% average graduate tuition rate growth, higher health services fees, and additional graduate students in certain programs. Total student room and board income increased by 8%, primarily due to new housing for graduate students at One Western Avenue and 29 Garden Street, as well as a 4% increase in the undergraduate room and board rate. Continuing and executive education revenue

FISCAL YEAR 2004 OPERATING REVENUE



rose 5%, largely as a result of growth in the Business School's custom executive education programs. Scholarships applied to student income continued to grow faster than tuition, with a 10% increase in fiscal 2004 following a 9% increase in fiscal 2003.

Sponsored research grew 7% in fiscal year 2004 to \$589.2 million, representing a 14% increase in federal support and a 13% decrease in non-federal support. The University received 80% of its sponsored research funding from the federal government, 14% from foundations, and 6% from other sources, including corporations, foreign, state, and local governments, as well as research institutes.

Various agencies of the Department of Health and Human Services, including most notably the National Institutes of Health, funded \$367.9 million or 78% of the University's federal sponsored research in fiscal 2004, an increase from \$319.8 million or 77% of federal funding in fiscal 2003. The National Science Foundation supplied 8% of fiscal 2004 federal support, with the remainder awarded by other federal entities including the Departments of Defense, Energy, and Education, as well as the National Aeronautics and Space Administration. Approximately 95% of fiscal



FACULTY OF ARTS AND SCIENCES

The FAS focused on several major planning efforts this past year, with implications for the curriculum, the faculty, and the physical campus. In April, four working groups and a steering committee concluded a comprehensive review of the College curriculum. Their recommendations

will now undergo faculty review as a first step towards approval and implementation. Dean William Kirby also worked with the chair of the Life Sciences Executive Council and the divisional deans in the humanities, social sciences, and physical and applied sciences

to develop plans to expand the FAS faculty.

The physical campus changed as well.
Renovation of Widener
Library is nearly complete. The new Center
for Government and
International Studies,
a major expression of
the FAS's commitment
to international studies,

is well under construction. The sciences will gain support from several new buildings. In addition, the undergraduate Houses received upgrades to their recreational facilities, and the Malkin Athletic Center was improved.

Financial aid remains an important commit-

ment for the FAS. In addition to enhanced dissertation support for graduate students, a new initiative waives the parental contribution to undergraduate education costs for families who earn less than \$40,000 a year.

2004 federal sponsored funding, excluding financial aid, was received by three Schools: the Medical School, 43%; the School of Public Health, 28%; and the Faculty of Arts and Sciences, 24%.

The indirect costs of research include facility operations, depreciation, debt service, library use, and administrative costs. These costs are allocated as overhead to the direct costs of sponsored projects, enabling the University to recover a portion of such costs from the projects' funders. Other University resources finance the unrecovered overhead costs associated with research.

In fiscal 2004, indirect cost reimbursements totaled \$140.5 million. Federal indirect cost recovery rose 16%, and indirect cost reimbursements repre-

SUMMARY OF FINANCIAL RESULTS

sented 28% of total federal support. Predetermined federal indirect cost recovery rates have been established across the University through fiscal 2006.

Non-federal indirect cost recovery decreased 22%, significantly more than the 12% decrease in non-federal sponsored direct support, a result of non-federal sponsors reimbursing a smaller share of indirect costs. This trend is a concern, since unrecovered costs must be either eliminated or absorbed by other operating funds, placing stress on departmental operating budgets.

Two significant research centers expected to positively impact future sponsored research funding were formed in fiscal 2004. The University has partnered with the Massachusetts Institute of

Dollar amounts in millions					
	2000	2001	2002	2003	2004
Total revenue	\$ 2,022.6	\$ 2,228.2	\$ 2,349.0 ²	\$ 2,472.7	\$ 2,597.7
Total expenses	1,902.5	2,063.3	2,261.6 ²	2,432.9	2,560.9
Total gifts	505.0	707.1	477.5	562.4	591.8
Student notes receivable	172.9	159.0	151.3	136.7	128.6
Fixed assets at net historical cost	1,841.2 ¹	2,382.8	2,774.4	3,168.4	3,468.9
Bonds and notes payable	1,276.4	1,622.2	1,839.5	2,246.9	2,604.7

Net assets-General Operating Account 3.186.0 3,279.9 3.419.9 3,439.4 3,935.5 19,148.3 18,259.2 22,587.3 Net assets-endowment funds 17,518.0 19,294.7 (2.7%)Total return on general investments 32.2% (0.5%)12.5% 21.1% Degree student enrollment 18,847 19.539 19,536 19,638

²These numbers are restated to conform with fiscal 2003 presentation.



BUSINESS SCHOOL

Harvard Business School launched a required course in the MBA Program, *Leadership and Corporate Accountability*, that examines the legal, ethical, and economic responsibilities of leadership; achieving corporate accountability; and personal values and responsible leadership.

HBS and Graduate
School of Education
faculty are collaborating
on the Public Education
Leadership Project,
a three-year effort
involving joint research
and executive education
program delivery in
conjunction with nine
U.S. urban school
districts. Online,

self-paced tutorials in information technology and quantitative analysis were introduced.



SCHOOL OF DENTAL MEDICINE

HSDM is reaping the benefits of its recent strategic planning efforts. The School's outstanding accreditation report confirms the vitality of its integrated education, patient care, and research programs. Implementation of its strategic plan has resulted in a resurgence

of research and discovery, culminating in the opening of the new Research and Education Building in the fall of 2004.

¹This number is restated to conform with fiscal 2001 presentation.

Technology, the Whitehead Institute for Biomedical Research, and the Harvard-affiliated hospitals to form the Eli and Edythe L. Broad Institute. This joint venture will convene scientists from various disciplines and institutions to develop comprehensive tools for genomic medicine. The Broad Institute intends to make its research widely available to the scientific community and will utilize the results of this research to further the understanding, diagnosis, and treatment of diseases.

The past year also witnessed the creation of the Harvard Stem Cell Institute (HSCI). The mission of the Institute is the support of stem cell research with the goal of developing medically useful knowledge. In its initial phase, the HSCI will be a virtual center, supporting research and drawing together scientists who work in the Schools and at the affiliated hospitals. In the long run, the HSCI will identify significant funding sources to support its research and pioneer new medical treatments, while examining the ethical, religious, and political ramifications of this research.

GIFTS FOR CURRENT USE Current use gifts totaled \$153.5 million in fiscal 2004, a 1% increase over fiscal 2003. These gifts from alumni and friends provide crucial funding for the University's ongoing operations and priorities such as undergraduate and graduate student financial aid.

Investment income increased 2% to \$926.0 million. The largest component of investment income, endowment income distributed for operations, increased 5% to \$807.6 million. This increase was due to a 2% increase in the distribution rate as well as distributions on additions to the endowment. The modest increase in the distribution rate was set at the beginning of fiscal 2003 and reflected uncertainties regarding the economic climate. The distribution rate as a percentage of endowment market value was 4.9%, within the targeted spending rate of 4.5% to 5.0%. Endowment and related spending policies may be found in the section of this report beginning on page 16.



SCHOOL OF DESIGN

In June of 2004, Peter Rowe completed twelve distinguished years as Dean; Professor Alan Altshuler is currently serving as Acting Dean. After several years of deficit spending, the School realized a significant unrestricted surplus in fiscal 2004.

Work has been completed on facilities

that support the School's efforts to remain in the forefront of research and teaching related to technology in design. These include a wood shop, an environmental-testing lab, a new-materials library, a digital media lab, and state-of-the-art CAD-CAM facilities.



DIVINITY SCHOOL

Continuing a multi-year revision of its curriculum, HDS completed its review of and adopted new requirements and content for the Master of Divinity degree (MDiv). The MDiv is the target degree for one-third of HDS's students as they prepare for pastoral leadership and social-service ministries. The

greatest innovation in the MDiv curriculum is a series of team-taught introductory courses intended to provide new students with a common base from which they can be drawn more immediately into the intellectual life of the School. During fiscal 2005, the Faculty of Divinity will review the

Master of Theological Studies degree, the target degree for half of the HDS student body, and the doctoral programs jointly supervised with the Faculty of Arts and Sciences.

OTHER INCOME Other income consists primarily of rental and parking fees, publication revenue, royalties, health and clinic fees, and revenue from other auxiliary enterprises whose activities are consistent with the University's mission. In fiscal 2004, other income rose 11% to \$372.7 million, largely due to rental income at the Medical School's new research building, as well as increases in health fees and publication revenue.

EXPENSES The University's operating expenses totaled \$2.6 billion in fiscal 2004, a 5% increase over the prior year. Expense categories that rose significantly during the year included compensation and space and occupancy costs. Recent cost-cutting efforts restrained expense growth in many areas.

COMPENSATION As one of the foremost institutions of higher education in the world, the University strives to hire and retain outstanding faculty and staff. Accordingly, the University offers an attractive and competitive compensation and benefits package, which includes pension plans, health benefits for active and retired employees, dental plans, life insurance, tuition assistance, child and elder care resource services, mortgage and educational loan

programs, tax-deferred annuity programs, and free admission to the University's museums and libraries.

Compensation costs totaled \$1.3 billion in fiscal 2004, an increase of 6% over fiscal 2003. Compensation represented 52% of the University's expenses in both fiscal 2004 and 2003. Salaries and wages rose 5%, and benefits costs increased 11% in fiscal 2004. The salary expense growth reflects faculty hiring initiatives and additional personnel to support greater sponsored research activity, as well as pay increases and adjustments. The growth in benefits costs is the result of increased pension and postretirement welfare costs as well as rising health care expenses.

In addition to the standard benefits package, the Schools may offer educational and subsidized mortgage loans to their faculty members. The mortgage program helps faculty members cope with the high cost of housing in the Boston area. Total loans outstanding to faculty increased 6% to \$109.0 million in fiscal 2004 from \$103.0 million in the preceding year, reflecting larger loans resulting from continued increases in housing costs.



SCHOOL OF EDUCATION

In fiscal 2004, HGSE embarked on two innovative approaches to prepare the next generation of educational leaders: a pilot course focused on identifying education's core knowledge and skills taught in a case-based learning environment, and the Public Education

Leadership Project in

collaboration with Harvard Business School.

The School raised
\$2.5 million toward the
Learning Technologies
Center, a state-of-the-art
facility that offers the
HGSE community the
potential to research
and create innovative
resources that serve
educators and students
worldwide. Video- and

audio-conferencing capabilities enable users to address teachers, administrators, and policymakers across continents by hosting "virtual" meetings and conversations. In addition, the Harvard Club of Boston announced the funding of several new annual scholarships for HGSE students.



JOHN F. KENNEDY SCHOOL OF GOVERNMENT

David T. Ellwood was selected as the next Dean of the Kennedy School. One of the nation's most influential scholars of poverty, welfare, and family change, Dean Ellwood has been a member of the KSG faculty since 1980.

During this major election year, interest in elective office is increasing among KSC graduates. In addition to many graduates and current students working on campaigns, five graduates are running for seats in the U.S. Congress. KSC graduates were also recently elected as Prime Minister in both Singapore and Mongolia.

FINANCIAL AID Financial aid makes the possibility of attending Harvard University a reality for many students. Approximately 70% of financial aid is funded through gifts from generous alumni and friends, endowment income, and sponsored support, with the remaining 30% supported by other University operating funds. Expanding the financial aid programs for both undergraduate and graduate students continues to be one of the University's top priorities. In the coming year, one-third of the savings resulting from core central administration cost-cutting efforts will be redirected to fund financial aid for graduate students.

Scholarships and student awards, including amounts applied against student income, increased 11% to \$262.9 million in fiscal 2004, similar to the increase in fiscal 2003. In addition, the University spent \$51.9 million on student employment, loaned \$25.3 million to students, and acted as agent on behalf of specific student recipients for \$13.0 million in aid from outside sponsors.

In February 2004, President Summers announced a major new initiative designed to encourage talented students from families of low and moderate income to apply to and attend Harvard College. The new initiative has four major components: financial aid, recruitment, admissions, and a summer academic program designed to prepare

talented students from financially disadvantaged backgrounds for college. As part of this initiative, parents of families with annual income of less than \$40,000 will no longer be expected to contribute to the cost of their children's undergraduate education. In addition, the University will reduce the contributions expected of families with income between \$40,000 and \$60,000. This new initiative is the latest step in a progressive expansion of undergraduate financial aid.

Over the past ten years, the cost of attending the College has increased by 51%, from \$26,700 to \$40,450 per year. During that same ten-year period, the average annual scholarship award has grown 92%, from \$12,700 to \$24,400. Almost 70% of undergraduate students receive financial aid, with close to 50% qualifying for need-based scholarship assistance. The average undergraduate aid package consists of grants, loans, and employment, and represents almost two-thirds of the total cost of attendance. Over the past several years, financial aid enhancements have generated a significant decline in the median indebtedness among graduating seniors, from \$16,400 for the Class of 2000 to \$8,000 for the Class of 2004. These improvements have made Harvard College's financial aid program an exemplar for other institutions of higher education, while also enabling the College to further its



Law School

With the decision that the Law School would not be included in the University's Allston planning, HLS began ramping up development plans for its campus over the past year. In the summer of 2003, multiple classrooms were upgraded, and the central exterior

plaza was enhanced.
Planning moved into
high gear for the summer
2004 renovation of the
student center, Harkness
Commons, and for future
new construction in the
northwest corner of the
Law School campus.



MEDICAL SCHOOL

HMS celebrated the opening of a major new research building dedicated to the acceleration of medical progress through collaboration among scientists from many disciplines.

HMS also announced the creation of the Department of Systems Biology, its first completely new department in twenty years. Systems Biology seeks to build an understanding of how multi-cellular organs work as a system from current knowledge of genetic and molecular function.

Finally, faculty working groups have made significant progress on a comprehensive reform of the medical curriculum and educational process.

commitment to the dual principles of ensuring need-blind admissions and providing need-based financial aid.

Financial aid is also vital in attracting students to the graduate and professional schools. Between 67% and 91% of each School's students received financial support in fiscal 2004. The University implemented the following three significant financial aid initiatives for graduate and professional students during fiscal 2004.

The Presidential Scholars program will provide \$14.5 million in financial aid to doctoral students over the seven-year period beginning in fiscal 2004. The Schools are using the Presidential Scholars funds to meet their programs' greatest needs, ranging from reducing the loan burden for graduates pursuing public service or other low-income careers to providing stipends for students as they write their dissertations. The Presidential Scholars program is expected to provide incremental support to 220 students over the seven-year period.

The University Graduate-Student Aid Fund, the second financial aid initiative implemented in the past year, supports public service-related research and education across the University. Gifts to the fund will expand the Presidential Scholars program and increase financial aid within the individual Schools.

The third financial aid initiative is a low-cost, commercially funded loan program for graduate and professional students resulting from a partnership with a major financial institution. Though scholarship dollars rose again in fiscal 2004, graduate students continue to rely on educational loans or other financing to cover the costs of attendance. The new loan program is particularly important for international students, who are ineligible for federally subsidized education loans. This program assisted more than 1,700 graduate students by providing over \$29.0 million of below-market-rate loans in fiscal 2004. In the coming year, approximately \$33.0 million is expected to be loaned to 1,900 students.

The University also maintains its own student loan programs, which are funded through federal support, University capital resources, and donations. Outstanding loans from University funds to current and former students declined 6% to \$128.6 million in fiscal 2004. This decrease was due to a shift to external loans as well as low-interestrate student loan consolidations through the federal government and other lenders, resulting in full repayment of University loans. The University's student loan balance does not include loans made directly to students by the Federal Direct Student Loan Program and other non-Harvard entities.



RADCLIFFE INSTITUTE FOR ADVANCED STUDY

The Radcliffe Institute
Fellowship Program
brought a diverse group
of fifty-six scholars and
artists into the Harvard
community to explore
a broad range of topics
including art history,
theoretical computer
science, immigration,
and concepts of justice.

The Schlesinger Library marked its sixtieth anniversary by holding a conference on "Gender, Race, and Rights in African American Women's History" and undertaking renovations aimed at preserving and protecting its priceless collections for the future.



SCHOOL OF PUBLIC HEALTH

HSPH received a \$20.5 million federal biodefense grant to study the immune system response to pathogens. The goal of this research is to modulate the immune system to make vaccines more protective against microbial pathogens. Additionally, HSPH and the Kennedy School received CDC funding for

a National Preparedness
Leadership Academy for
government officials. A
new department was
formed focusing on
Genetics and Complex
Diseases. Basic research
combining molecular and
cellular biology with
genomics and proteomics
will address the environmental stresses that
contribute to complex

diseases like diabetes and cancer. Associate Professor Wafaie Fawzi and colleagues at Muhimbili University College of Health Sciences in Tanzania discovered that a simple low-cost daily multivitamin regimen could significantly delay progression of the AIDS virus and the need for antiretroviral drugs.

SUPPLIES AND EQUIPMENT In fiscal 2004, supplies and equipment expenses decreased slightly to \$198.3 million. University-wide contracts with vendor partners together with cost-conscious purchasing practices generated savings in this area. Vendor partnerships continued in the areas of office supplies, office furniture, and scientific supplies, and new partnerships were established for purchases of personal computers; watermark and recycled paper; facilities maintenance, repair, and operating supplies; and audiovisual equipment.

SPACE AND OCCUPANCY Space and occupancy costs totaled \$262.6 million in fiscal 2004, a 9% increase over the prior year. Facilities improvement and maintenance costs rose 16%, largely due to new facilities including the Medical School's new research building. Utility costs grew 16% from both increased usage and higher market rates. Energy prices rose substantially during fiscal 2004 due to global oil and gas demand as well as supply concerns. Utilities consumption increased as a result of new facilities and the slightly colder than normal winter weather conditions. Building operations costs rose 7% due to expenses associated with new space and increased spending on security. The University's rental costs also increased as a result of additional space requirements from growth in staff and programs, in addition to temporary relocations during the renovation of existing facilities.

OTHER EXPENSES Other expenses increased 1% in fiscal 2004 to \$488.1 million. This low level of expense growth was the result of cost-cutting efforts across the University as well as savings from purchasing initiatives. Vendor partnerships helped to reduce expenditures in the areas of temporary employment, express mail, travel, and offset printing. The savings from these purchasing initiatives are expected to grow in future years. The University continues to seek additional cost savings by consolidating vendors, negotiating contracts, and leveraging purchasing activity.

The largest components of other expenses in fiscal 2004 were purchased services of \$224.4 million, expenses subcontracted to other institutions for sponsored projects of \$79.8 million, publishing costs of \$51.0 million, travel expenses of \$49.7 million, and telephone costs of \$11.1 million. Certain items within other expenses are unique to the individual Schools, such as funds spent by the Medical School to reimburse its affiliated hospitals for the use of facilities and personnel.



THE UNIVERSITY

Groundbreaking for the Eli and Edythe L. Broad Institute occurred in the summer of 2004, an important milestone for the joint venture with MIT, the Harvard-affiliated hospitals, and the Whitehead Institute for Biomedical Research. In other interdisciplinary scientific efforts, the newly created Harvard

Stem Cell Institute and the Center for Brain Science will foster collaboration among faculty and researchers across the Schools and affiliates. Additionally, the Harvard Initiative for Global Health (HIGH) has begun to build interfaculty partnerships in a number of areas including mental health,

population science, and infectious and chronic diseases, as well as undergraduate education in these fields. The first major offshoot of HIGH, the Harvard Program on AIDS, will coordinate the University's research, education, and fundraising efforts to support prevention and treatment.

In the 2003-04 academic year, over 80% of the University's classes utilized the iCommons instructional computing software. iCommons provides a variety of tools to enhance course websites, including lecture notes, slides, and video footage; polling and file uploading capabilities; and

discussion threads.

Presidential Instructional
Fellows began to assist
the faculty in using the
iCommons tools during
the summer of 2004.
Usage is expected to
grow to over 90% in
the coming year.

Review of endowment results

The University's endowment represents the ongoing legacy of generous alumni and friends. Attaining an exceptional market value of \$22.6 billion at the end of fiscal 2004, the endowment continues to be a critical source of funding for the University's operations.

A STRONG ENDOWMENT

The endowment is the financial cornerstone of the University's continued excellence in education and research, providing long-term fiscal stability for student financial aid, the faculty, and academic programs. The endowment contains approximately 10,700 separate funds, the majority of which are restricted for specific purposes. The endowment's growth and the resulting income stream are reliant upon generous endowment giving and prudent investment management.

In fiscal 2004, endowment gifts totaled \$257.8 million, approximately 2% less than the prior year. This decline reflects several large one-time gifts received in fiscal 2003, offset by

increases in fiscal 2004 endowment giving for the Business School (HBS), Law School (HLS), and Medical School (HMS). HBS received \$60.1 million of endowment gifts as its capital campaign progressed. In addition, HBS endowment pledges grew to \$87.5 million as of the end of fiscal 2004. HLS'S capital campaign also continued, resulting in \$19.1 million of endowment gifts in fiscal 2004 and endowment pledges of \$86.8 million as of the end of the year. HMS'S endowment gifts increased 50% to \$33.2 million, primarily due to new endowed clinical professorships.

REAL	ENDOWMENT	GROWTH
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	Compound annual rate of growth				
	1974-84	1985-94	1995-04	1974-04	
Total general investment return	10.4%	12.3%	15.5%	13.2%	
Average per unit income distributed as a percent of unit value	(5.1)	(4.1)	(4.2)	(4.5)	
Total return reinvested	5.3	8.2	11.3	8.7	
Capital additions	3.3	1.5	2.1	2.3	
Total growth in endowment	8.6	9.7	13.4	11.0	
Inflation rate	(7.8)	(3.6)	(2.5)	(4.6)	
REAL ENDOWMENT GROWTH	0.8%	6.1%	10.9%	6.4%	

PERFORMANCE OVERVIEW

ENDOWMENT GROWTH*

In billions of dollars

Harvard Management Company (HMC) is responsible for investing the endowment assets. The unaudited *Annual Report of the Harvard Management Company* supplements the following review of the endowment's fiscal 2004 performance. HMC's report, beginning on page 22, discusses the University's investment philosophy and analyzes the endowment's performance in detail.

In fiscal 2004, total return of the endowment's general investments was 21.1%, compared with 12.5% in fiscal 2003. The market value of the endowment increased from \$19.3 billion to \$22.6 billion at the close of fiscal 2004, exceeding annual performance benchmarks by almost 5%. The change in market value includes all endowment activity: investment appreciation and depreciation; funds distributed to the Schools and departments for operations; new gifts and pledges; departmental

1989

984

1974 Principal and appreciation

1994

1999

Capitalized income

additions to the endowment from unrestricted fund and gift balances; and the use of endowment appreciation for specific purposes approved by the Corporation.

The University's endowment spending policy strives to maintain the purchasing power of the endowment while providing a reliable stream of income for operations. Accordingly, the University aims to distribute between 4.5% and 5.0% of the endowment's market value annually. In fiscal 2004, the endowment distributions resulted in a spending rate of 4.9%. Continuing donor support, superior investment management, and fiscal restraint will be required to ensure the endowment's future strength.

ENDOWMENT INCOME DISTRIBUTED

In millions of dollars

\$900 20 750 600 15 450 5 150

* To allow for comparability with years prior to fiscal 1995, this chart does not include pledge balances and interests in perpetual trusts.

Gifts and other changes

2004

- CPI growth

666

2004

994

Review of capital activities

In fiscal 2004, the University was engaged in 356 construction and renovation projects. The University maintains 21.6 million square feet of space in almost 600 buildings, as well as over 200 acres of land for long-term development.

APPROACH TO CAPITAL ISSUES

The University utilizes a comprehensive planning strategy to assess current and future space requirements while considering the impact of growth on the neighboring communities. In fiscal 2004, the University purchased several additional properties in Allston, representing strategic expansion of the University's holdings and progress in establishing an Allston campus.

During fiscal 2004, the planning process for the University's existing space as well as exploration of new opportunities for properties in Allston continued. The University Committee on Physical Planning and the Allston Initiative office completed a technical project involving a team of planning and engineering consultants who investigated the possibilities of transforming the Allston properties into an extended, integrated campus. The result was a series of land strategies for the University to consider as discussion and planning continue. President Summers charged several faculty task forces with developing program options for the Allston campus, based upon the broad areas of undergraduate life, science and technology, community life, and graduate and professional education. As a result of these efforts, a scope of work for an outside planning and design team was developed, and a team was selected to work on a framework plan for Allston in fiscal 2005.

Representatives from the Allston Initiative, the Office of the Vice President for Government, Community, and Public Affairs, and the Boston Redevelopment Authority are in the final stages of developing a North Allston Neighborhood Strategic Plan, the outcome of a multi-year community-planning process. Negotiations have occurred throughout the past year around critical issues

involving the University's ability to use the land in Allston for the creation of a new teaching, research, and residential campus. The coming year will provide additional opportunities for the internal and external communities to engage in discussions regarding the University's future plans for its properties in Allston.

To demonstrate its commitment toward the Allston community, the University granted \$2.5 million to the City of Boston to support the construction of affordable housing in Allston. The Brian J. Honan Apartment Complex groundbreaking occurred in December of 2003.

Developments also transpired in Cambridge during fiscal 2004. The University continued to participate in discussions with neighbors and officials regarding planned construction in the area north of the main Cambridge campus for Law School and Faculty of Arts and Sciences (FAS) facilities projects. Several FAS building projects in this area are underway. Discussions have centered on the creation of open space, pedestrian circulation, management of traffic and construction impacts, as well as University goodwill contributions for the benefit of the community. While none of the proposed projects has required traffic analysis, the University undertook a comprehensive north campus transportation study to assess the cumulative impacts of the proposed development.

During fiscal 2004, the University continued to make progress toward its goal of expanding graduate student and affiliate housing, increasing the number of available accommodations by 382 or 12%. Construction of One Western Avenue and renovations at 29 Garden Street were both completed. In Boston, the University became a participant in

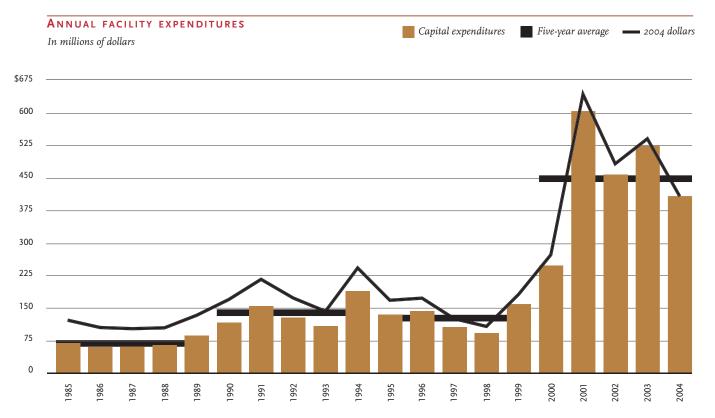
the Fenway mixed-use project, which will include affiliate apartments. The University is in the final stages of planning for the development of new housing in two locations in the Riverside area of Cambridge, after years of negotiations with residents of the surrounding neighborhood. Incremental living space for graduate students and affiliates will continue to alleviate the campus-area housing shortage.

THE PHYSICAL PLANT

The University owned 21.6 million square feet of space at the end of fiscal 2004. The University's physical plant must accommodate diverse needs, including security, energy efficiency, accessibility, and 24-hour use. Student housing occupies 6.6 million square feet; offices and classrooms, 4.9 million square feet; laboratories, 3.7 million square feet; libraries, 1.6 million square feet; and other facilities including athletic, health care, and administrative facilities, as well as museums and commercial space, 4.8 million square feet.

In fiscal 2004, the University invested \$409.9 million in 356 active capital projects and acquisitions, compared with \$526.1 million and 434 active projects during fiscal 2003. The investments in plant were allocated as follows: 60% for new construction and renovation of laboratories,

classrooms, and offices; 13% for libraries, museums, and assembly spaces; 12% for housing; and 15% for athletic and other facilities. Capital projects were funded by \$47.2 million of unrestricted balances, \$15.5 million of gifts, and \$4.1 million of endowment, with the remainder financed by debt. For more than 20 years, the University has employed a strategy of financing capital projects with bonds. This strategy has enabled the continuous renewal and improvement of existing facilities, while allowing payments for the improvements to occur over time and avoiding the encumbrance of considerable endowment and operating funds. The University's outstanding debt totaled \$2.6 billion at the end of fiscal 2004, a 16% increase over the \$2.2 billion balance at the close of fiscal 2003.



NEW CONSTRUCTION AND ACQUISITIONS

New construction and acquisitions accounted for 57% and 6%, respectively, of the University's capital expenditures during fiscal 2004. The University purchased five properties containing 104,000 square feet in Allston. These properties are positioned strategically within the University's existing holdings. Additionally, the One Western Avenue graduate student housing and garage complex in Allston was completed during the year, providing housing for graduate students primarily from the Business School (HBS) and the Kennedy School of Government. The Medical School finished construction on its new research building in the Longwood Medical Area. In Cambridge, the new building at 60 Oxford Street was finished, and the FAS completed the addition to the Science Center.

Two fas construction projects in the north campus began during fiscal 2004: the Laboratory for Interface Science and Engineering (LISE) and the Biology Research Infrastructure (BRI) building. Progress at the LISE included excavations and the rerouting of active existing campus utilities in the work area. This facility will enable interaction among faculty and students in the areas of physics, chemistry, biology, engineering, and material science. The LISE will also include laboratory space for the

Center for Imaging and Mesoscale Structures. The BRI building, located under the Biological Laboratories courtyard, will house a multiscientist support facility for FAS research.

Planning has begun for a new 460,000 square-foot FAS laboratory building in the northwest campus, which will house the Center for Brain Science as well as other multidisciplinary scientific efforts.

Significant progress was made on the Center for Government and International Studies. This project will permit the co-location of the Government Department and various centers for regional and international studies and will accommodate a range of academic and administrative uses, including faculty offices, graduate student workspace, lecture halls, various seminar rooms, a library, the Harvard-MIT Data Center (a research center for quantitative social science data), and a cafe.

Major construction work continued on the new Research and Education Building at the Dental School, a 68,000 square-foot facility that will house the Laboratories for Molecular Dental Medicine. Research in this state-of-the-art building will focus on three critical areas: bone and joint biology and disease, mucosal biology and disease, and clinical research.

RENOVATION AND RENEWAL

With a physical plant whose history spans nearly four centuries, the University is committed to renovation and renewal as a means to preserve its architectural assets and to creatively adapt space to meet evolving needs. Investment in the existing physical plant represented 37% of total capital expenditures in fiscal 2004.

Throughout the year, renovation and renewal addressed the need for improved student facilities. Renovations were completed at 29 Garden Street, providing additional housing for both graduate students and affiliates. Major renovations occurred at Harkness Commons at the Law School during the summer of 2004 and included repairs, changes in layout, and new mechanical systems. The improvements are intended to provide an up-to-date facility for dining, social gatherings, and student

activities. Within the FAS, renovations occurred at the Malkin Athletic Center (MAC) and Loker Commons during the summer of 2004. Improvements to the MAC included expanding exercise space as well as total cosmetic refurbishment of the exercise and locker room areas. New exercise machines have been added, nearly doubling the amount of available equipment. Loker Commons is located below Annenberg Hall, the freshman dining facility, and functions as a social gathering spot for undergraduate students. The Loker Commons renovations consisted of constructing a late night grill and increasing the amount of space available for student gatherings and functions. The Harkness Commons, мас, and Loker Commons projects were completed in September of 2004.

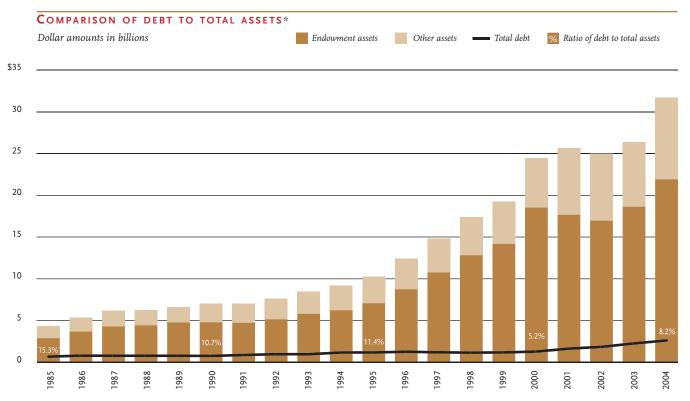
The Radcliffe Institute for Advanced Study began renovating Schlesinger Library in January of 2004. In addition to allowing the Library to revive some of its historic spaces, the renovation will include installation of many modern amenities for students and researchers. The Schlesinger Library project is expected to be completed in February of 2005.

Phase two of the Widener Library project continued during fiscal 2004, resulting in public and administrative space reconfigurations with busy, interactive spaces separated from reading rooms. Phase two includes renovation to the periodicals reading room on the first floor, creation of a microform reading room adjacent to the periodicals reading room, restoration of the second floor reading room to its original configuration, and installation of climate control, sprinklers, fire alarms, and new wiring and lighting in the library's public spaces. Additionally, original architectural features and finishes are being restored throughout Widener. Work on the project's second phase was approximately 80% complete as of the end of fiscal 2004.

Major renovations to the Faculty Club were completed during fiscal 2004. The project created an

expanded kitchen facility, a new employee dining room and improved employee locker rooms, relocated administrative offices, and a new glass conservatory on the north terrace that allows for year-round use.

At нвя, renovations to Aldrich Hall and Baker Library continued during fiscal 2004. In Aldrich Hall, seven classrooms and adjacent hallways and study alcoves were updated. The new classrooms incorporate technology for audio and video capture as well as improvements intended to enhance the learning environment for students and faculty. The alcoves provide flexible space for small team projects and study group meetings. In the Baker Library/Academic Center project, the historic lobby, reading room, and north facade are being restored, and a new academic center is being constructed to accommodate faculty, library, and research offices as well as book stacks, seminar rooms, and informal student gathering spaces. Ultimately, the Academic Center's entrance will be oriented toward Allston and the University's developing campus.



^{*} Assets are net of pledges, interests in perpetual trusts, and securities pledged to counterparties.

Annual report of the Harvard Management Company

Harvard Management Company (HMC), a wholly owned subsidiary of Harvard University, was founded in 1974 to manage the University's endowment, pension assets, working capital, and deferred giving accounts. HMC is governed by a Board of Directors that is appointed by the President and Fellows of the University.

HMC currently manages \$27.3 billion, of which \$25.4 billion resides in the General Investment Account (GIA), a pooled fund that consists primarily of endowment assets. The information presented below relates to the GIA.

THE POLICY PORTFOLIO

The cornerstone for the management of the GIA is the Policy Portfolio, the long-term asset mix that is most likely to meet the University's long-term return goals with the appropriate level of risk. It serves as the benchmark against which the performance of the actual portfolio is measured. The components of the Policy Portfolio at the end of fiscal 2004 are shown below:

TOTAL	100%
Cash	(5)
Inflation-indexed bonds	6
Foreign bonds	5
Domestic bonds	11
Real estate	10
Commodities	13
High-yield securities	5
Absolute return funds	12
Private equities	13
Emerging markets	5
Foreign equities	10
Domestic equities	15%

Several points about the Policy Portfolio are worth noting. First, it is a well-diversified portfolio with an attractive expected return-to-risk ratio. It includes a higher allocation to foreign securities and commoditybased assets and a lower allocation to domestic fixed-income assets than the typical institutional fund. Second, while performance will be measured against the Policy Portfolio, the actual asset mix in the portfolio may differ from the Policy Portfolio at any point in time. For instance, if domestic equities are perceived to be overvalued, the actual portfolio may hold only 12% in domestic equities compared with the 15% weight in the Policy Portfolio. If these tactical asset allocation decisions are correct, on balance, the actual portfolio will tend to outperform the Policy Portfolio. Also, if нмс succeeds in outperforming the benchmarks for the individual asset classes (for example, the Lehman 5+ year Treasury Index for the domestic bond sector), the actual portfolio will outperform the Policy Portfolio. The Policy Portfolio is regularly reviewed and modifications are made periodically in light of experience and changing circumstances.

FISCAL 2004 INVESTMENT RESULTS

Total return on the GIA for the year ended June 30, 2004 was 21.1%. This figure is net of all fees, expenses, and negotiated fee offsets, and compares with a 16.4% return on the Policy Portfolio.

The table below shows total return on the GIA for each of the past ten years. The Policy Portfolio is shown for comparison, as is the Trust Universe Comparison Service (TUCS) Median, a universe of more than 100 funds with assets of over \$1.0 billion. As the numbers indicate, endowment returns on average have exceeded returns on the Policy Portfolio and the TUCS Median by a substantial margin.

TOTAL RETURN			
	Harvard	Policy	TUCS
Fiscal year	GIA*	portfolio	median
1995	16.8%	17.2%	16.1%
1996	26.0	22.3	17.6
1997	25.8	20.0	20.3
1998	20.5	17.1	17.9
1999	12.2	18.9	11.2
FIVE-YEAR ANNUAL RATE	20.1	19.1	16.6
2000	32.2	18.6	10.4
2001	(2.7)	(9.8)	(5.7)
2002	(0.5)	(4.5)	(5.9)
2003	12.5	8.3	4.0
2004	21.1	16.4	16.2
FIVE-YEAR ANNUAL RATE	11.8	5.2	3.8
TEN-YEAR ANNUAL RATE	15.9%	11.9%	10.1%

^{*}Net of all fees, expenses, and negotiated fee offsets

ASSET ALLOCATION

The table below shows the breakdown by asset category of the General Investment Account as of June 30, 2004 and 2003 (dollar amounts in millions):

	20	2003		
Domestic equities	\$ 4,779	18.8%	\$ 3,830	18.3%
Foreign equities	3,447	13.6	2,713	13.0
Emerging markets	1,829	7.2	1,385	6.6
Private equities	1,968	7.7	1,817	8.7
Subtotal	12,023	47.3	9,745	46.6
Absolute return funds	2,907	11.4	2,495	11.9
High-yield securities	1,497	5.9	1,509	7.2
Commodities	2,986	11.8	1,991	9.5
Real estate	1,420	5.6	1,111	5.3
Subtotal	8,810	34.7	7,106	33.9
Domestic bonds	1,708	6.7	2,385	11.4
Foreign bonds	826	3.3	1,193	5.7
Inflation-indexed bonds	1,446	5.7	1,392	6.7
Cash	595	2.3	(901)	(4.3)
Subtotal	4,575	18.0	4,069	19.5
TOTAL	\$ 25,408	100.0%	\$ 20,920	100.0%

RESULTS BY ASSET CLASS

The following section discusses the investment management approach for each of the asset classes of the General Investment Account as well as fiscal 2004 investment results.

DOMESTIC EQUITIES In fiscal 2004, the domestic equity program returned 22.8% compared with 21.5% for the domestic equity benchmark. The largest portion of the domestic equity portfolio is managed by an external management group that spun out from HMC in July 2001. This group outperformed their benchmark in fiscal 2004 by 2.2%. Four other external managers, retained to manage small capitalization equities, had mixed results. An internal strategy focusing on arbitrage strategies—merger arbitrage, convertible arbitrage, and pairs trading—outperformed its benchmark by 3.2%.

FOREIGN EQUITIES The foreign equity program returned 36.1% in fiscal 2004, compared with 34.0% for the foreign equity benchmark. The internally managed foreign equity portfolio, which focuses on arbitrage opportunities, outperformed the benchmark by 8.0%. The two external managers retained to manage foreign equities also outperformed the benchmark in fiscal 2004.

EMERGING MARKETS Three strategies are used to manage equities in emerging markets—countries in which the capital markets are smaller and less developed than those in the foreign equity sector. The first strategy is an internally managed fund that has concentrated on closed-end funds selling at a discount to net asset values. This fund outperformed the benchmark in fiscal 2004 by 4.1%. The second strategy employs an external manager and outperformed the benchmark by 2.2%. Finally, a small portion of emerging market equities is in private equity funds. This strategy underperformed its benchmark in fiscal 2004. Overall, the emerging market equity program returned 36.6% compared to 33.9% for the benchmark.

PRIVATE EQUITIES Private equity returns in fiscal 2004 were 20.8%, compared with 20.3% for the benchmark, a broad index of private equity funds. At the end of fiscal 2004, the private equity portfolio consisted of 170 funds managed by 60 different external management teams.

ABSOLUTE RETURN FUNDS Seven external managers are employed to provide positive returns without regard to a specific security index. These managers typically focus on merger arbitrage, convertible arbitrage, pairs trading, and balance sheet arbitrage, with a sprinkling of absolute value trades. Ideally, these managers are sufficiently hedged to generate positive returns in either up or down markets. In fiscal 2004, this program returned 15.7%, exceeding the benchmark by 5.8%.

HIGH-YIELD SECURITIES The domestic portion of the high-yield portfolio is managed externally by two firms that emphasize flexibility and situations where debt securities appear to be incorrectly valued. One external manager slightly outperformed its benchmark in fiscal 2004, while the other manager sharply underperformed. The emerging market debt portion of the high-yield program is managed internally and returned 9.9%, outperforming the benchmark by 5.1%. Overall, the high-yield portfolio underperformed its benchmark in fiscal 2004 by 2.9%.

COMMODITIES The commodity portfolio has two components. The first strategy attempts to outperform an index of publicly traded commodities by discovering and exploiting mispricings among similar securities. This strategy outperformed its benchmark by 6.5% in fiscal 2004. The second component of the commodities program is a portfolio of timber properties. This strategy outperformed its benchmark by 6.2% in fiscal 2004.

REAL ESTATE The real estate portfolio returned 16.0% in 2004 compared with 16.8% for the benchmark. The real estate portfolio is focused on opportunity funds where managers strive to find undervalued assets and add significant value through aggressive management. These opportunity funds have not performed as well as fully leased core real estate assets over the past several years. Over the longer term, the opportunity funds are expected to prevail.

Domestic bonds The domestic bond portfolio returned 9.2% in fiscal 2004 compared with (3.4)% for the benchmark. The entire domestic bond portfolio is managed internally with a focus on arbitrage situations—the opportunity to buy relatively cheap securities and simultaneously sell overvalued securities with similar characteristics. Since the overall maturity structure and duration of the portfolio is kept close to the benchmark index, interest rate movements typically have little influence on relative performance.

FOREIGN BONDS The foreign bond portfolio returned 17.4% in fiscal 2004 compared with the benchmark return of 7.6%. As with domestic bonds, the emphasis is on arbitrage. Duration and country allocation do not vary substantially from the benchmark.

INFLATION-INDEXED BONDS Inflation-indexed bonds were added to the Policy Portfolio in fiscal 2000. These securities, which the U.S. Treasury first issued in January 1997, provide a guaranteed rate of return over the CPI inflation rate. The return on the inflation-indexed bond portfolio was 4.2% in fiscal 2004, slightly ahead of the benchmark return of 3.9%.

RISK MANAGEMENT

The active management of a diverse portfolio involves inherent risks essential to meeting the long-term return objectives of the endowment. The primary risk factors include market risk, credit risk, liquidity risk, and operational risk. The management of these risks is the responsibility of the Board of Directors, its subcommittees, and senior management, who determine the objectives and policies that guide the management of the endowment. Subcommittees include the Corporate Governance and Nomination Committee, the Finance Committee, the Valuation Committee, the Compliance Committee, and the Compensation Committee.

Collectively, HMC has implemented a series of risk management processes to identify and quantify the risks to which the University is exposed, establish the proper mitigating controls, and monitor compliance with risk mitigation strategies. Risk management techniques are structured around fundamental principles including clearly defined policies and procedures; segregation of duties with clear reporting lines; strong management information systems, measurement and analytical tools; disciplined relationship management; and independent review.

- 1) Market risk is defined as the sensitivity of income and capital to variations in interest rates, foreign exchange rates, equity prices, commodity prices, and other market-driven rates and prices. Market risk also considers the correlation risk among investments and the liquidity of the underlying positions. Market risk is measured as the potential gain or loss resulting from a price change at a given probability over a specific time period; this is also described as value at risk. Value at risk is monitored and reviewed frequently by the Board of Directors and senior management to ensure that exposures are consistent with approved limits and guidelines. Stress tests are also conducted to determine how potential changes in market conditions could impact the market risk of the portfolio.
- 2) Credit risk is defined as the risk of loss arising from a counterparty's failure or inability to meet payment or performance terms of a contract. HMC manages credit risk by establishing strict credit policies, setting concentration limits and approval procedures, and monitoring exposure continuously. HMC enters into arrangements with counterparties believed to be creditworthy and requires collateral to the maximum extent possible. Limits are established for each counterparty based on their creditworthiness.
- 3) Liquidity risk considers the risk of loss arising from the inability to meet funding commitments. The objective of liquidity risk management is to ensure the ability to meet the endowment's financial obligations. Effective management of liquidity risk requires the ability to project and understand all cash flows and potential future commitments. It also involves the identification and prioritization of sources of liquidity. Cash is managed actively by a centralized staff responsible for understanding funding requirements and evaluating sources of liquidity. Liquidity measures are employed to ensure that the University maintains adequate liquidity and is prepared for periods of stress.
- 4) Operational risk is the risk of loss resulting from inadequate or failed internal processes or systems, errors by employees, or external events. The management of these risks is primarily the responsibility of the business line managers in each functional area. HMC manages operational risk by identifying areas of risk, monitoring compliance, promoting best practices, and implementing internal controls and robust systems. The results of these activities are reviewed frequently by senior management, and an extensive review of these controls is performed during the external audit process.

FINANCIAL STATEMENTS BALANCE SHEETS

28

29 STATEMENTS OF CHANGES IN NET ASSETS

WITH GENERAL OPERATING ACCOUNT DETAIL

30 STATEMENTS OF CHANGES IN NET ASSETS
OF THE ENDOWMENT

31 STATEMENTS OF CASH FLOWS

32 Notes to financial statements

52 REPORT OF INDEPENDENT AUDITORS

STEM CELL RESEARCH IN THE LABORATORY OF PROFESSOR DOUGLAS MELTON

The University founded the Harvard Stem Cell Institute during the past year, an example of the significant strides made in important areas of scientific inquiry. Led by Professors Douglas Melton and David Scadden, the Institute will facilitate collaboration among scientists across the University and the affiliated hospitals,

ultimately raising funds for research and the development of new medical treatments. The Institute will also serve as a forum for discussing the ethical, religious, and political dilemmas associated with stem cell research.

Balance sheets

with summarized financial information for the year ended June 30, 2003

		June 30
In thousands of dollars	2004	2003
ASSETS:		
Cash and cash equivalents (Notes 3 and 4)	\$ 1,404,626	\$ 1,746,843
Working capital investments, at market (Notes 3 and 4)	1,866,964	882,375
Receivables (Note 5)	146,246	199,456
Prepayments and deferred charges	64,686	66,260
Notes receivable:		
Students (Note 6)	128,611	136,726
Faculty and staff	108,994	102,952
Other	19,556	19,260
Total notes receivable	257,161	258,938
Pledges receivable (Note 7)	721,803	732,715
Fixed assets, net of accumulated depreciation (<i>Note 8</i>)	3,468,897	3,168,426
Interests in perpetual trusts held by others (Note 9)	245,277	215,317
Investment portfolio, at market (Notes 3 and 4)	24,472,444	20,035,262
Market value of securities pledged to counterparties (Notes 3 and 4)	27,401,077	35,714,633
TOTAL ASSETS	60,049,181	63,020,225
LIABILITIES:		
Accounts payable	424,482	414,881
Deposits and other liabilities	293,753	257,148
Securities lending and other liabilities associated with the investment portfolio (Notes 3 and 4)	28,897,526	36,251,907
Liabilities due under life income fund agreements (Note 10)	492,138	419,415
Bonds and notes payable (Note 11)	2,604,714	2,246,910
Pension and other accrued retirement obligations (Note 12)	343,282	278,253
Government loan advances (Note 6)	56,045	55,455
TOTAL LIABILITIES	33,111,940	39,923,969
NET ASSETS	\$ 26,937,241	\$ 23,096,256

		Temporarily	Permanently		June 30
	Unrestricted	restricted	restricted	2004	2003
NET ASSETS:					
General Operating Account (Note 13)	\$ 2,824,375	\$ 1,030,947	\$ 80,152	\$ 3,935,474	\$ 3,439,377
Endowment (Note 9)	3,374,635	15,456,102	3,756,568	22,587,305	19,294,735
Life income funds (Note 10)	0	140,248	274,214	414,462	362,144
TOTAL NET ASSETS	\$ 6,199,010	\$ 16,627,297	\$ 4,110,934	\$ 26,937,241	\$ 23,096,256

The accompanying notes are an integral part of the financial statements.

Statements of changes in net assets with General Operating Account detail

with summarized financial information for the year ended June 30, 2003 For the year ended Temporarily Permanently June 30 In thousands of dollars Unrestricted restricted restricted 2004 2003 **REVENUE:** Student income: Undergraduate program 190,619 190,619 179,689 Graduate programs 287.102 287,102 266.785 Board and lodging 106 736 106.736 99 008 Continuing education and executive programs 145,281 145,281 137,754 Scholarships applied to student income (Note 6) (173,437)(173,437)(158, 350)Total student income 0 0 556.301 556,301 524,886 Sponsored research support (Note 14): Federal government—direct costs 342,026 342.026 302.432 Federal government-indirect costs 131,474 131,474 113,723 Non-federal sponsors—direct costs 27,588 79,033 106,621 121,180 Non-federal sponsors-indirect costs 5,295 3,753 11,542 0 Total sponsored research support 506,383 82,786 589,169 548,877 Gifts for current use (Note 15) 61,795 91,723 153,518 151,941 Investment income: Endowment income distributed for operations (Note 9) 681,247 807,645 770,670 126,398 Income on working capital investments distributed for operations 97,763 14,070 111,833 133,274 Interest received on student, faculty, and staff loans 6,544 7.744 6.544 Total investment income 230,705 695 317 0 926,022 911,688 Other operating income (Note 16) 372,696 372,696 335,300 Net assets released from restrictions (Note 2) 821,352 (821, 352)0 **TOTAL REVENUE** 2,549,232 48,474 0 2,597,706 2,472,692 **EXPENSES:** Salaries and wages 1,036,028 1,036,028 986,196 Employee benefits (Note 12) 304,281 304,281 274,187 Scholarships and other student awards (Note 6) 89,414 89,414 79,510 Supplies and equipment 198,310 198,310 199,112 Space and occupancy 262,633 241,162 262.633 Depreciation (Note 8) 182.138 182,138 168.072 Other expenses (Note 17) 488,115 488,115 484,705 TOTAL EXPENSES 2,560,919 0 0 2,560,919 2,432,944 NET REVENUE/(DEFICIT) (11,687)48,474 0 36,787 39,748 OTHER PROVISIONS AND CREDITS: 437.861 Change in appreciation, net of operating distribution 11.838 449,699 21.083 Change in undistributed general investment income (23,686)(43,162)(66,848)(150,520)Other changes (Note 2) 9,885 TOTAL OTHER PROVISIONS AND CREDITS 414,175 (31, 324)382,851 (119,552)CAPITAL CHANGES: Net change in pledge balances (Note 7) (10,098)(10,098)(3,065)Capital gifts for loan funds and facilities (Note 15) 28,485 1,305 29,790 28,867 Transfers between General Operating Account and endowment 66,473 (12,301)(3,037)51,135 72.175 Transfers between General Operating Account and life income funds (Note 10) 5,249 383 5,632 1,339 Non-operating net assets released from restrictions (Note 2) 41.155 (44,488)3.333 0 **TOTAL CAPITAL CHANGES** 107,628 1,984 76,459 99.316 (33,153)GENERAL OPERATING ACCOUNT NET CHANGE DURING THE YEAR 510,116 (16,003)1,984 496,097 19,512 Endowment net change during the year 490,302 2,530,918 271,350 3,292,570 1,776,714 Life income funds net change during the year (Note 10) 28,969 23,349 52,318 23,632 NET CHANGE DURING THE YEAR 2,543,884 1.000,418 296,683 3.840.985 1.819.858 Balance, beginning of year 14,083,413 21,276,398 5,198,592 3,814,251 23,096,256 BALANCE, end of year \$ 6,199,010 \$ 16,627,297 \$ 4,110,934 \$ 26,937,241 \$ 23,096,256

Statements of changes in net assets of the endowment with summarized financial information for the year ended June 30, 2003

with summarized financial information for the year ended June 30, 200	03			For the	year ended
		Temporarily	,		ne 30
In thousands of dollars	Unrestricted	l restricted	restricted	2004	2003
Gifts for capital (Note 15)	\$ 14,774	\$ 39,376	\$ 203,617	\$ 257,767	\$ 262,368
Investment return (Notes 3 and 9):					
Endowment income from general investments	29,852	162,991		192,843	252,524
Change in realized and unrealized appreciation during year	558,996	3,048,681		3,607,677	1,807,171
Total investment return	588,848	3,211,672	0	3,800,520	2,059,695
Endowment income distributed for operations	(126,398)	(681,247)		(807,645)	(770,670)
Change in undistributed general investment income	9,543	50,138		59,681	126,475
Net investment return after distributions	471,993	2,580,563	0	3,052,556	1,415,500
Transfers between endowment and General Operating Account:					
Unexpended income capitalized/(decapitalized)	(1,581)	12,150	4,416	14,985	(968)
Gifts capitalized	1,036	1,518	1,145	3,699	3,812
Other	(65,928)	(1,367)	(2,524)	(69,819)	(75,019)
Total transfers	(66,473)	12,301	3,037	(51,135)	(72,175)
Capitalization of life income funds (Note 10)		1,985	7,487	9,472	20,796
Net change in endowment pledge balances (Note 7)		(16,601)	15,013	(1,588)	96,980
Net change in interests in perpetual trusts held by others (<i>Note 9</i>)		,	29,960	29,960	(7,184)
Other changes	(26)	(1,930)	(2,506)	(4,462)	60,429
Net assets released from restrictions (Note 2)	70,034	(84,776)	14,742	0	0
NET CHANGE DURING THE YEAR	490,302	2,530,918	271,350	3,292,570	1,776,714
Balance, beginning of year	2,884,333	12,925,184	3,485,218	19,294,735	17,518,021
BALANCE, end of year	\$ 3,374,635	\$ 15,456,102	\$ 3,756,568	\$ 22,587,305	\$ 19,294,735

The accompanying notes are an integral part of the financial statements.

Statements of cash flows

	For the	he year ended June 30
In thousands of dollars	2004	2003
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 3,840,985	\$ 1,819,858
Adjustments to reconcile change in net assets to net cash provided by/(used by) operating activities:		
Provision for depreciation	182,138	168,072
Change in pension and retirement obligations	65,029	37,995
Change in interests in perpetual trusts held by others	(29,960)	7,184
Change in liabilities due under life income fund agreements	72,723	(8,092)
Net gain on sale of investments	(2,157,674)	(1,100,000)
Net unrealized appreciation on investments	(2,069,157)	(945,748)
Gifts restricted for capital purposes	(352,870)	(311,092)
Changes in operating assets and liabilities:		
Working capital investments	(984,589)	685,694
Receivables	53,210	128,735
Prepayments and deferred charges	1,574	(9,985)
Pledges receivable	10,912	(93,917)
Accounts payable	9,601	27,659
Deposits and other liabilities	36,605	9,822
NET CASH PROVIDED BY/(USED BY) OPERATING ACTIVITIES	(1,321,473)	416,185
CASH FLOWS FROM INVESTING ACTIVITIES: Loans made to students, faculty, and staff	(51,425)	(53,243)
Payments received on student, faculty, and staff loans	53,498	62,233
Change in other notes receivable	(296)	17,211
Proceeds from sale of investments	33,928,651	23,057,775
Purchase of investments	(26,116,555)	(38,987,889)
Net additions to fixed assets	(482,609)	(562,090)
NET CASH PROVIDED BY/(USED BY) INVESTING ACTIVITIES	7,331,264	(16,466,003)
	,,,,,	(3, 33,333)
CASH FLOWS FROM FINANCING ACTIVITIES: Proceeds from issuance of debt	371,913	421,030
	•	•
Debt repayment	(14,109)	(13,630)
Gifts restricted for capital purposes	352,870	311,092
Advances under security lending agreements	15,708,183	26,992,825
Payments under security lending agreements	(22,771,455)	(10,683,883)
Change in government loan advances	590	167
NET CASH PROVIDED BY/(USED BY) FINANCING ACTIVITIES	(6,352,008)	17,027,601
NET CHANGE IN CASH AND CASH EQUIVALENTS	(342,217)	977,783
Cash and cash equivalents, beginning of year	1,746,843	769,060
CASH AND CASH EQUIVALENTS, end of year	\$ 1,404,626	\$ 1,746,843

 $\label{the accompanying notes are an integral part of the financial statements.$

Notes to financial statements

1. UNIVERSITY ORGANIZATION

Harvard University is a private, not-for-profit institution of higher education with approximately 7,000 undergraduate and 12,650 graduate students. Established in 1636, the University includes the Faculty of Arts and Sciences, ten graduate schools, the Radcliffe Institute for Advanced Study, the Division of Continuing Education, a variety of research museums and institutes, and an extensive library system to support the teaching, learning, and research activities of the Harvard community. The President and

Fellows of Harvard College (the Corporation), a governing board of the University, has oversight responsibility for all of the University's financial affairs. The Corporation delegates substantial authority to the schools and departments for the management of their individual resources and operations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements include the activities of Harvard University as a whole, including all significant affiliated organizations.

On July 1, 2002, the Rowland Institute for Science (the Rowland Institute) became part of Harvard University. The Rowland Institute is an interdisciplinary research institute focused on experimental rather than theoretical science. The addition of the Rowland Institute's investment in plant and equipment, as well as its operating balances, are included in the "Other changes" line of the fiscal 2003 Statement of Changes in Net Assets with General Operating Account Detail. The addition of the Rowland Institute's endowment is included in the "Other changes" line of the fiscal 2003 Statement of Changes in Net Assets of the Endowment.

For the purposes of financial reporting, the University classifies resources into three net asset categories pursuant to any donor-imposed restrictions and applicable law. Accordingly, the net assets of the University are classified and defined in the accompanying financial statements in the categories that follow.

PERMANENTLY RESTRICTED net assets are subject to donorimposed stipulations that they be invested to provide a perpetual source of income to the University. Generally, donors of these assets require the University to maintain and invest the original contribution in perpetuity, but permit the use of some or all investment earnings for general or specific purposes. TEMPORARILY RESTRICTED net assets are subject to legal or donor-imposed stipulations that will be satisfied either by actions of the University, the passage of time, or both. These net assets include gifts donated for a particular purpose, amounts subject to time restrictions such as funds pledged for future payment, or amounts subject to legal restrictions such as portions of otherwise unrestricted capital appreciation, which must be reported as temporarily restricted in accordance with Massachusetts law.

UNRESTRICTED net assets are not subject to donor-imposed restrictions. Funds invested in fixed assets and funds functioning as endowment comprise 74% of unrestricted net assets. In addition, this category includes unrestricted gifts and endowment income balances, University-designated loan funds, and other unrestricted designated and undesignated current funds (see *Notes 9* and 13).

Revenues received, expenses incurred, and income distributed for operations for the purpose of conducting the programs and services of the University are presented as "Net revenue/(deficit)" in the *Statements of Changes in Net Assets with General Operating Account Detail*. Net revenue/(deficit) is the measure of operating activity of the University.

Revenue from sources other than contributions are generally reported as increases in unrestricted net assets. Expenses are reported as decreases in unrestricted net assets. Income earned by restricted fund and gift accounts is initially classified as temporarily restricted and reclassified as unrestricted when expenses are incurred for the intended purpose.

Unconditional pledges are reported as increases in the appropriate category of net assets in accordance with donor restrictions (see *Note 7*). Gains and losses on investments are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets are reported as reclassifications from temporarily restricted net assets to unrestricted net assets. Funds transferred to the University on behalf of a specific beneficiary are reported as agency transactions and are not included in the *Statements of Changes in Net Assets*.

The *Balance Sheets* display both the assets and corresponding liabilities generated by securities lending transactions. These are transactions executed to support the investment activities of the Harvard Management Company. The University has also separately reported the fair value of assets for which the counterparty has the right to pledge or exchange the collateral it has received; assets of the investment portfolio that are unencumbered are reported as "Investment portfolio, at market" in the *Balance Sheets*.

The University's vast array of museums and libraries houses priceless works of art, literary works, historical treasures, and artifacts. These collections are protected and preserved for public exhibition, education, research, and the furtherance of public service. They are neither disposed of for financial gain nor encumbered in any manner. Accordingly, such collections are not recorded or capitalized for financial statement purposes.

The University is a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code.

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect reported amounts and disclosures. Actual results could differ from those estimates. The financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the University's financial statements for the year ended June 30, 2003, from which the summarized information was derived. Certain prior year amounts have been reclassified to conform to current year presentation.

3. INVESTMENT HOLDINGS

The University's investment holdings as of June 30, 2004 and 2003 are summarized in the following tables (in thousands of dollars):

		2004		2003
	Pooled			
	general	Other		
	investments	investments	Total	Total
Short-term investments*	\$ 2,871,952	\$ 399,638	\$ 3,271,590	\$ 2,629,218
Investment portfolio	24,032,158	440,286	24,472,444	20,035,262
Securities pledged to counterparties	27,401,077	0	27,401,077	35,714,633
Securities lending and other liabilities associated				
with the investment portfolio	(28,897,526)	0	(28,897,526)	(36,251,907)
TOTAL INVESTMENT HOLDINGS	\$ 25,407,661	\$ 839,924	\$ 26,247,585	\$ 22,127,206

Investment holdings are comprised of:

26,772 97,913 79,727	0 (33,389)	97,913 46,338	73,029 (18,650)
97,913	0	97,913	73,029
20,772	Ü	20,772	27,870
26 772	0	26,772	27,876
482,044	424,556	906,600	781,559
21,849,253	49,119	21,898,372	18,634,174
\$ 2,871,952	\$ 399,638	\$ 3,271,590	\$ 2,629,218
investments	investments	Total	Total
general	Other		
Pooled			
			2003
	general investments \$ 2,871,952 21,849,253 482,044	Pooled general Other investments	Pooled general investments Other investments Total \$ 2,871,952 \$ 399,638 \$ 3,271,590 21,849,253 49,119 21,898,372 482,044 424,556 906,600

^{*}Short-term investments include working capital investments and cash and cash equivalents. Cash and cash equivalents consist principally of funds deposited in cash management accounts with maturities when purchased of fewer than 90 days.

The University employs a unit method of accounting for pooled general investments. Each participating fund enters and withdraws from the pooled investment account based on monthly unit market values. Changes in the market value of investments are distributed proportionately to each fund that participates in the investment pool. Net general investment income

distributed during the year is allocated on a per unit basis to each participating fund (see *Note 4*).

The changes in the market value and income of participating units for the years ended June 30, 2004 and 2003 were as follows:

	2004	2003
Unit value at end of year	\$ 1,215.68	\$1,013.51
Unit value at beginning of year	1,013.51	914.78
Change in realized and unrealized appreciation	202.17	98.73
Net income earned on general investments	10.79	13.88
TOTAL UNIT RETURN ON POOLED GENERAL INVESTMENTS	\$ 212.96	\$ 112.61
TOTAL UNIT RETURN PERCENTAGE USING MONTHLY COMPOUNDING	21.1%	12.5%

Other investments are managed separately from the pooled general investment account. These investments consist primarily of fixed-income securities, principally government securities and certificates of deposit held for the University's working capital needs, and various

managed bond and equity portfolios associated with life income funds. Those investments that are not readily marketable are carried either at cost or a nominal value. Income on other investments is recorded and distributed when received.

4. POOLED GENERAL INVESTMENTS

The following are the significant accounting policies of the University related to pooled general investments:

- A) Investments are presented at fair market value based on trade date positions as of June 30. Instruments listed or traded on a securities exchange are valued at the last sale price on the primary exchange where the security is traded. Investments in publicly traded securities that are subject to restrictions limiting their salability are discounted from the current public market price to levels that reflect the estimated cost of those restrictions. Non-exchange traded debt instruments are valued by independent pricing services or by broker/dealers who actively make markets in these securities. Options contracts, forward contracts, interest rate exchange agreements, and interest rate cap and floor agreements are valued using validated models with externally verifiable model inputs, or by using independent broker quotes. Private equity, real estate, commodities, and absolute return funds consist primarily of investments that are not readily marketable. Investments in these categories, which are managed externally, are valued utilizing the most current information provided by the general partner. Direct investments are valued utilizing discounted cash flow and other industry standard methodologies. Where applicable, independent appraisers and engineers are utilized to assist in the valuation. These values are determined under the direction of, and subject to approval by, the Valuation Committee of the Harvard Management Company Board of Directors.
- B) The preparation of consolidated financial statements requires management to make estimates and assumptions about the effect of matters that are inherently uncertain. The accounting policies considered potentially significant in this respect are the valuation of derivative instruments, private equities, real estate, and certain commodities. Values for these instruments are often estimated using techniques such as discounted cash flow analysis and comparisons to similar instruments. Estimates developed using these methods are subjective and require judgment regarding significant matters such as the amount and timing of future cash flows and the selection of discount rates that appropriately reflect market and credit risks. Estimates, by their nature, are based on judgment and

available information. Changes in assumptions could have a significant effect on the fair value of these instruments. Actual results could differ from these estimates and could have a material impact on the financial statements.

- c) The University amortizes bond premiums and accretes bond discounts where such expense or income is significant.
- **D)** The University utilizes a number of subsidiary entities to support the investment activities of the endowment. The consolidated financial statements include all assets and liabilities associated with these entities.

The University's investment strategy incorporates a diversified asset allocation approach and maintains, within defined limits, exposure to the movements of the world equity, fixed-income, commodities, real estate, and private equity markets. The core investment portfolio is structured to mirror the market exposures defined by the Policy Portfolio and is considered to be "unhedged." (The Policy Portfolio is described in the unaudited Annual Report of the Harvard Management Company, which begins on page 22.) In addition, the University seeks to enhance the returns of certain asset classes through strategies designed to capture mispricings in specific financial instruments without changing the fundamental risk profile of the core investment account. These strategies generally involve several distinct but highly correlated financial instruments that are weighted to neutralize market risk. Depending on the characteristics of the financial instruments, the specific positions within a given strategy may be recorded on the asset or liability sections of the following table.

The following table delineates securities pledged to counterparties, where the counterparty has the right, by contract or custom, to sell or repledge the securities. The fair value of collateral pledged to counterparties that cannot be sold or repledged as of June 30, 2004 was \$688.5 million and as of June 30, 2003 was \$922.9 million. The fair value of collateral accepted by the University as of June 30, 2004 was \$3,757.1 million and as of June 30, 2003 was \$2,157.6 million. The portion of this collateral that was sold or repledged as of June 30, 2004 was \$1,020.8 million and as of June 30, 2003 was \$1,307.1 million.

The summarization of pooled general investment assets and liabilities as of June 30, 2004 and 2003 is as follows (in thousands of dollars):

POOLED GENERAL INVESTMENT LIABILITIES		28,897,526		36,251,907
Cash collateral held under security lending agreements ³		27,029,032		34,092,304
7 1		1,868,494		2,159,603
Options Total financial instruments sold, not yet purchased, under hedge transactions		746,820		636,932
Fixed-income securities		424,267		629,852
Equity and convertible securities		697,407		892,819
Financial instruments sold, not yet purchased, under hedge transactions:		607.105		200 0
LIABILITIES:				
POOLED GENERAL INVESTMENT ASSETS		54,305,187		57,171,443
Accounts receivable/(payable), net ²		848,595		(1,712,198
Securities pledged to counterparties	9,113	1,094,470	13,582_	1,174,553
Cash and short-term investments	1,085,357	1.004.476	1,160,971	1 174 550
Collateral advanced under security borrowing agreements	2 005 057	1,195,850	1 1 60 071	1,013,020
Total financial instruments purchased under hedge transactions		28,055,665		36,872,062
Commodities		336,965		11,867
Options		2,268,210		2,076,990
Securities pledged to counterparties	22,733,300	23,997,107	31,174,723	33,321,472
Fixed-income securities	1,263,807	•	2,146,749	
Securities pledged to counterparties	59,617	1,453,383	30,472	1,461,733
Financial instruments purchased under hedge transactions: Equity and convertible securities	1,393,766		1,431,261	
Total investments		23,110,607		19,824,006
Securities pledged to counterparties	973,030	1,326,684	997,243	1,382,845
Inflation-indexed bonds	353,654		385,602	
Commodities		2,197,088		1,190,322
Real estate		1,457,203		1,161,096
Private equities		1,980,619		1,886,163
Absolute return funds		2,630,057		1,991,165
Securities pledged to counterparties	361,971_	1,176,230	278,713	1,324,341
High-yield securities	814,259		1,045,628	
Securities pledged to counterparties	17,449	1,653,936	0	1,318,407
Emerging markets equity and debt	1,636,487		1,318,407	
Securities pledged to counterparties	137,547	149,702	81,511	117,922
Foreign fixed-income securities	12,155		36,411	
Securities pledged to counterparties	2,349,446	2,424,888	2,660,202	2,719,320
Domestic fixed-income securities	75,442		59,118	
Securities pledged to counterparties	590,064	3,482,610	236,505	2,809,043
Foreign equity and convertible securities	2,892,546		2,572,538	0.000.040
Securities pledged to counterparties	169,540	4,631,590	241,682	3,923,382
Domestic equity and convertible securities	\$ 4,462,050		\$ 3,681,700	
Investments:				
ASSETS:	2.	2004		
(in thousands of donars):	2.	2004		

The collateral advanced under security borrowing agreements is in the form of cash or publicly traded equity securities.

As of June 30, 2004, accounts receivable and payable relating to undistributed income and purchases and sales of securities were \$1,547,256 and \$698,661, respectively. The amounts at June 30, 2003 were \$660,846 and \$2,373,044, respectively. As of June 30, 2004, of the \$1,547,256 of accounts receivable, gross receivables relating to off-balance sheet instruments were \$787,463, and of the \$698,661 of accounts payable, gross payables relating to off-balance sheet instruments were \$220,529. As of June 30, 2003, of the \$660,846 of accounts receivable, gross receivables relating to off-balance sheet instruments were \$1,48,924, and of the \$2,373,044 of accounts payable, gross payables relating to off-balance sheet instruments were \$1,964,598.

The minimum collateral the University requires by contract on each stock loan and repurchase agreement is 100% of the market value of the security loaned. Collateral is moved as is required by fluctuations in the market value of the security loaned.

The University uses a variety of financial instruments with off-balance sheet risk involving contractual or optional commitments for future settlement. These include futures, options, interest rate exchange agreements, interest rate cap and floor agreements, and forward purchase and sale agreements, which are exchange traded or executed over-the-counter. These instruments are primarily used in the arbitrage strategies that enhance the returns of certain asset classes without increasing the market risk to the underlying asset class (see "hedged" market exposure in the following tables). The market risk of a strategy is influenced by the relationship between the financial instruments with off-balance sheet risk and the offsetting positions recorded on the balance sheet. (For a detailed analysis of the market exposure of the portfolio as of June 30, 2004, see the supplemental information on Pooled General Investments beginning on page 54.) The University controls market

risk through the use of industry standard analytical tools that measure the market exposure of each position within a strategy. The strategies are monitored daily and positions are frequently adjusted in response to changes in the financial markets. Financial instruments with off-balance sheet risk are also used by the University to adjust the market exposure of a given asset class without disturbing the underlying instruments in the core investment portfolio (see "unhedged" market exposure in the following tables).

The following table summarizes the market exposure (expressed in cash market equivalents as discussed below), net ending fair value, net average fair value, and credit exposure relative to the financial instruments with off-balance sheet risk as of June 30, 2004 (in thousands of dollars):

TOTAL	\$ 2,882,446	\$ 34,943,536	\$ (48,551,494)	\$ 27,132	\$ 2,293,724	\$ 1,200,869	\$ 70,729
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real estate investments	5,000	0	0	0	0	0	0
Private put agreements related to							
Currency options	0	5,210,907	(1,860,145)	0	448,477	580,751	1,071
,			(, , , ,	•	,	•	
Currency forwards	1,071,187	2,075,857	(3,127,351)	7,121	12,572	5,905	73
Total commodity instruments	880,000	670,132	(850,048)	0	176,951	29,406	6,662
Commodity exchange agreements	880,000	547,438	(490,189)	0	92,133	200	4,988
Commodity options	0	122,694	(273,490)	0	84,818	29,206	13
Commodity futures	0	0	(86,369)	0	0	0	1,661
Total fixed-income instruments	352,812	26,860,524	(41,558,785)	23,675	1,611,844	528,746	8,557
Interest rate caps and floors	7,894	17,843,634	(1,558,156)	20,684	328,015	481,597	3,301
Interest exchange agreements	314,976	7,074,374	(33,870,004)	968	571,309	(628,713)	805
Fixed-income forwards	0	0	0	0	0	0	0
Fixed-income options	531	1,828,160	(5,809,972)	2,023	712,500	676,278	2,651
Fixed-income futures	29,411	114,356	(320,653)	0	20	(416)	1,800
Total equity instruments	373,447	120,110	(1,133,103)	(3,004)	+3,000	30,001	34,500
Total equity instruments	573,447	126,116	(1,155,165)	(3,664)	43,880	56,061	54,366
Equity options Equity exchange agreements	333,440	31,492	(268,753)	(15,521)	17,544	43,943 8,954	377
Equity rutures Equity options	11.857	87,014	(38,055)	11,857	26,524	43,943	1,026
Equity futures	\$ 228,150	\$ 7,610	hedged \$ (848,357)	\$ 0	Hedged \$ (188)	\$ 3,164	exposure ⁷ \$ 52,963
	Long unhedged	hedged		Unhedged	Hodood	value	
	Long	Long	Short	OII-Dalatice S	neet positions	average fair	Credit
		Market exposu	1*0		heet positions		
				Net ending	fair value of	Net	

^{*} Credit exposures primarily represent cash or securities advanced by the University to meet legal margin requirements in connection with future, forward, and option contracts.

The following table summarizes the market exposure (expressed in cash market equivalents as discussed below), net ending fair value, net average fair value, and

credit exposure relative to the financial instruments with off-balance sheet risk as of June 30, 2003 (in thousands of dollars):

				Net ending	fair value of	Net		
	Market exposure			off-balance sl	neet positions	average		
	Long	Long	Short			fair	Credit	
	unhedged	hedged	hedged	Unhedged	Hedged	value	exposure*	
Equity futures	\$ 24,943	\$ 4,474	\$ (591,960)	\$ 3,939	\$ 3,342	\$ 22,704	\$ 54,976	
Equity options	0	14,483	(40,746)	0	5,379	51,474	2,803	
Equity exchange agreements	163,171	162,364	(450,776)	8,707	(11,984)	(4,765)	42	
Total equity instruments	188,114	181,321	(1,083,482)	12,646	(3,263)	69,413	57,821	
Fixed-income futures	47,763	100,837	(179,139)	0	0	1,406	3,570	
Fixed-income options	22,933	2,339,293	(7,695,028)	2,085	558,498	409,213	11,587	
Fixed-income forwards	0	2,333,233	(7,055,020)	0	0	(3,512)	0	
Interest exchange agreements	300,902	8,835,423	(43,380,781)	10,677	(2,082,796)	(960,200)	2,106	
Interest rate caps and floors	529,801	15,312,692	(955,161)	24,475	464,035	308,522	14,219	
Total fixed-income instruments	901,399	26,588,245	(52,210,109)	37,237	(1,060,263)	(244,571)	31,482	
Commodity futures	0	0	0	0	0	0	0	
Commodity options	0	89,819	(59,017)	0	(10,137)	(4,259)	511	
Commodity exchange agreements	800,000	307,272	(307,150)	0	122	9,465	4,577	
Total commodity instruments	800,000	397,091	(366,167)	0	(10,015)	5,206	5,088	
Currency forwards	952,707	3,878,253	(4,796,735)	(14,898)	49,123	2,885	12,645	
Currency options	0	6,013,832	(2,175,485)	0	628,433	461,882	7,050	
Private put agreements related to								
real estate investments	5,000	0	0	0	0	0	0	
TOTAL	\$ 2,847,220	\$ 37,058,742	\$ (60,631,978)	\$ 34,985	\$ (395,985)	\$ 294,815	\$ 114,086	

^{*} Credit exposures primarily represent cash or securities advanced by the University to meet legal margin requirements in connection with future, forward, and option contracts.

Financial instruments with off-balance sheet risk are recorded on the balance sheet at fair value. Fair value is a function of the characteristics of the individual financial instruments and their relationship to current market conditions, as well as the length of time each instrument has been held. For example, domestic futures contracts, which expire periodically, are subject to daily cash settlements, and as such, the end of day fair value of these contracts is zero. In contrast, interest rate exchange agreements may be held for the life of a strategy and may reflect significant unrealized gains and losses depending on the change in value since the inception of the contract. The cash market equivalent of exposure represents the notional value of the off-balance sheet instrument adjusted for its correlation to its underlying index or asset.

Market exposure is only meaningful when related to the corresponding positions recorded on the balance sheet. Fair value and market exposure do not accurately measure risk. A more appropriate indicator of market risk is the net exposure of all positions (on and off-balance sheet) expressed in market risk equivalents, or value at risk. (For a more comprehensive discussion of market risk of the portfolio, see the unaudited *Annual Report of the Harvard Management Company*, which begins on page 22.)

Financial instruments with off-balance sheet risk necessarily involve counterparty credit exposure. The policy of the University is to require collateral to the maximum extent possible under normal trading practices. Collateral is moved on a daily basis as is required by fluctuations in

the market. The collateral is generally in the form of debt obligations issued by the U.S. Treasury. In the event of counterparty default, the University has the right to use the collateral to offset the loss associated with the replacements of the agreements. The University enters into arrangements only with counterparties believed to be creditworthy. Specific credit limits are established for each counterparty, based on their individual credit rating. Credit limits are monitored daily and are adjusted according to policy.

The asset allocation of the University's portfolio involves exposure to a diverse set of markets. The investments within these markets involve various risks such as interest rate, market, sovereign, and credit risks. The University anticipates that the value of its investments may, from time to time, fluctuate substantially as a result of these risks.

The University has entered into debt service put agreements in connection with its real estate investments. Under specific circumstances, these put agreements

grant those who lend to certain investments held in these portfolios the right to sell senior secured loans to the University at a designated price. These put agreements have been valued by the University under policies previously described. The University has also entered into agreements, primarily with private equity partnerships, that require periodic cash contributions totaling approximately \$3,457.6 million through 2014.

For the year ended June 30, 2004, the total return on the pooled general investments was 21.1%, or \$4,391.7 million, net of all expenses and fees, and including the impact of revenue-sharing agreements with certain fund managers. This compares with 12.5%, or \$2,312.4 million for fiscal 2003. The investment return is a result of the performance of the core investment portfolio, adjusted for the net results of the internal value-added strategies. The fiscal 2004 investment results by asset class are described in detail in the unaudited *Annual Report of the Harvard Management Company*.

5. RECEIVABLES

The major components of receivables, net of reserves for doubtful accounts of \$2.5 million and \$1.5 million, as of June 30, 2004 and 2003, respectively, were as follows (in thousands of dollars):

		2004	2003
Investment income	\$	0	\$ 53,260
U.S. Government,			
principally related to research	1	36,080	36,440
Non-federal sponsored research		5,044	6,364
Students		9,102	6,290
Other	9	96,020	97,102
TOTAL RECEIVABLES	\$ 14	46,246	\$ 199,456

6. STUDENT FINANCIAL AID

Financial aid granted to students totaled \$353.1 million in fiscal 2004: \$262.9 million of scholarships and other student awards, \$25.3 million of loans, \$51.9 million of student employment, and \$13.0 million of aid from sponsors for which the University acts as an agent for the recipient. Of the \$262.9 million of scholarships and other student awards, \$89.4 million represents stipends and other payments made directly to students, and \$173.5 million represents financial aid applied to student income. Approximately 70% of this financial aid is funded by gifts, endowment income, and sponsored support.

In addition to administering institutional loan programs, the University participates in various federal loan programs. Notes receivable from students as of June 30, 2004 and 2003 were as follows (in thousands of dollars):

	2004	2003
Federally insured loans	\$ 13,149	\$ 21,245
Government revolving loans	63,211	62,045
Institutional loans	52,251	53,436

TOTAL STUDENT NOTES RECEIVABLE \$ 128,611 \$ 136,726

Federally insured loans are generally repaid over a ten-year period and earn interest at an adjustable rate that approximates the 90-day U.S. Treasury Bill rate plus 3.0%. Principal and interest payments on these loans are insured by the American Student Assistance Corporation and are reinsured by the federal government.

Government revolving loans are funded principally with federal advances to the University under the Perkins Loan Program and certain other programs. These advances totaled \$56.0 million and \$55.5 million as of June 30, 2004 and 2003, respectively, and are classified as liabilities. Interest earned on the revolving and institutional loan programs is reinvested to support additional loans. The repayment and interest rate terms of the institutional loans vary considerably.

Notes receivable under federally guaranteed student loan programs are subject to significant restrictions. Accordingly, it is not practicable to determine the fair value of such amounts.

7. PLEDGES RECEIVABLE

Unconditional promises to donate to the University in the future are recorded as pledges receivable in the year promised at the present value of expected cash flows, net of an allowance for unfulfilled pledges. Pledges receivable included in the financial statements as of June 30, 2004 and 2003 are expected to be realized as follows (in thousands of dollars):

PLEDGES RECEIVABLE	\$ 721,803	\$ 732,715
unfulfilled pledges	(87,780)	(75,955)
Less: discount and allowance for		
More than five years	275,599	280,174
Between one and five years	427,187	422,797
Within one year	\$ 106,797	\$ 105,699
	2004	2003

A discount of \$42.4 million and \$52.9 million for the years ended June 30, 2004 and 2003, respectively, was calculated using a discount factor based on the appropriate U.S. Treasury Note rate. Pledges receivable have been designated for the following purposes (in thousands of dollars):

TEDGES RECEIVABLE	J 721,003	\$ 732,713
PLEDGES RECEIVABLE	\$ 721,803	\$ 732,715
Endowment	443,656	445,244
General Operating Account balances	278,147	287,471
Loan funds and facilities	35,270	53,207
Non-federal sponsored research	108,154	136,516
Gifts for current use	\$ 134,723	\$ 97,748
	2004	2003

Because of uncertainties with regard to their realizability and valuation, bequest intentions and other conditional promises are not estimated by management and are recognized as assets if and when the specified conditions are met.

8. FIXED ASSETS

Fixed assets are shown at cost or at fair value as of the date of the gift, net of accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

The major categories of fixed assets as of June 30, 2004 and 2003 are summarized as follows (in thousands of dollars):

Estimated

FIXED ASSETS, net	\$ 3,468,897	\$ 3,168,426	
Less: accumulated depreciation	(1,494,263)	(1,318,822)	
SUBTOTAL AT COST	4,963,160	4,487,248	
Equipment	334,999	268,973	***
Construction in progress	328,749	526,970	-
Other facilities and land	795,677	765,691	**
Service facilities	200,593	141,773	35
Athletic facilities	106,274	104,899	35
Museums and assembly facilities	205,579	200,103	35
Libraries	242,057	222,769	35
Classrooms and offices	751,653	682,251	35
Research facilities	1,198,698	894,953	*
Housing	\$ 798,881	\$ 678,866	35
	2004	2003	(in years)
			useful life
			Estimated

Estimated useful lives of components used for calculating depreciation range from 10 to 45 years.

Fixed assets include both facilities and equipment. Equipment includes general and scientific equipment, computers, software, furniture, and vehicles.

The costs of research facilities are separated into the shell, roof, finishes, fixed equipment, and services. These components are separately depreciated. The average useful life for research facilities is 19 years.

Certain University facilities are subject to restrictions as to use, structural modifications, and ownership transfer.

9. ENDOWMENT FUNDS

Harvard's endowment consists of approximately 10,700 separate funds established over many years for a wide variety of purposes. Endowment fund balances, including funds functioning as endowment, are classified and reported as either permanently restricted, temporarily restricted, or unrestricted, in accordance with donor specifications. Net losses on permanently restricted endowment funds are classified as a reduction to unrestricted net assets until such time as the market value equals or exceeds book value. Although funds functioning as endowment are not subject to permanent donor restrictions, the decision to spend their principal requires

the approval of the Corporation. All but a small fraction of the endowment is invested in the pooled general investment account (see *Notes 3* and 4).

The University is also the beneficiary of certain perpetual trusts held and administered by others. The estimated fair values of trust assets, which approximate the present values of expected future cash flows from the trusts, are recognized as assets and revenue when the trusts are established.

^{**} The estimated useful life of other facilities is 35 years.

^{***} Estimated useful lives of equipment range from 3 to 8 years.

Endowment funds as of June 30, 2004 and 2003 are summarized below (in thousands of dollars):

	2004				2003	
		Temporarily	Permanently			
	Unrestricted	restricted	restricted	Total	Total	
Endowment funds	\$ 0	\$ 13,441,532	\$ 3,151,772	\$ 16,593,304	\$ 14,094,860	
Funds functioning as endowment:						
Departmental funds	2,521,874	1,878,787	0	4,400,661	3,767,414	
University funds	852,761	51,646	0	904,407	771,900	
Pledge balances	0	84,137	359,519	443,656	445,244	
Interests in perpetual trusts held by others	0	0	245,277	245,277	215,317	
TOTAL	\$ 3,374,635	\$ 15,456,102	\$ 3,756,568	\$ 22,587,305	\$ 19,294,735	

The University's endowment income distribution policies are designed to preserve the value of the endowment in real terms (after inflation) and to generate a predictable stream of spendable income. Endowment investments are managed to achieve the maximum long-term total return. As a result of this emphasis on total return, the proportion of the annual income distribution funded by dividend and interest income or by capital gains may vary significantly from year to year. Amounts withdrawn from endowment capital gains to fund the fiscal 2004 and 2003 distributions totaled \$644.9 million and \$471.7 million, respectively.

The portion of investment returns earned on endowment and distributed each year is based on a rate (stated in dollars per unit) that is approved by the Corporation. This rate is not set based on a specific formula, nor is it directly tied to current investment returns. Rather, it reflects expectations about long-term returns and inflation rates and seeks to maintain the distribution rate at between 4.5% and 5.0% of the market value of the endowment. The table below shows the total return on endowment for the past five fiscal years, as well as the distribution rate for the following fiscal years.

Endowment income capitalized to endowment principal is available to meet future spending needs, subject to the approval of the Corporation.

Endowment investment returns (dollar amounts in thousands)					Distril	oution rate ^{1,3}
Fiscal	Interest and	Net	Total	Total		As a % of
year	dividends	appreciation	return ²	return % ³	Per unit	market value
2004	\$ 192,843	\$ 3,607,677	\$ 3,800,520	21.1%	\$ 54.17	4.5%
2003	252,524	1,807,171	2,059,695	12.5	49.70	4.9
2002	378,999	(474,416)	(95,417)	(0.5)	47.11	5.1
2001	354,368	(844,638)	(490,270)	(2.7)	45.32	4.8
2000	268,797	4,192,691	4,461,488	32.2	32.92	3.3
FIVE-YEAR T	ГОТАL \$ 1,447,531	\$ 8,288,485	\$ 9,736,016			

¹Since current year interest and dividends are used to fund the following year's distribution, these represent distribution rates for the following fiscal year.

42

²Total return is net of all expenses and fees, and includes the impact of revenue-sharing agreements with certain fund managers.

³Total return % and distribution rate per unit and as a % of market value amounts relate to pooled general investments.

10. LIFE INCOME FUNDS

As of June 30, 2004, the University held life income funds—pooled funds, gift annuities, and charitable remainder trusts—for approximately 2,000 donors. These funds are held in trust for one or more beneficiaries, and generally pay lifetime income to those beneficiaries, after which the principal is made available to the University in accordance with donor intentions. When a trust is established, life income fund net assets are recorded at fair market value, net of related liabilities for the present value of estimated future payments due to beneficiaries and net of obligations under charitable remainder trusts

due to other institutions. As of June 30, 2004, life income fund assets totaled \$906.6 million, with corresponding liabilities for amounts due to beneficiaries of \$420.1 million and amounts due to institutions of \$72.0 million, respectively. Gifts for capital to life income funds are presented at full value. The discounted present value of these gifts is \$23.1 million and \$9.0 million for fiscal 2004 and 2003, respectively. The changes in life income fund net assets for fiscal 2004 and 2003 were as follows (in thousands of dollars):

		2004		2003
	Temporarily	Permanently		
	restricted	restricted	Total	Total
Gifts for capital (Note 15)	\$ 36,614	\$ 28,699	\$ 65,313	\$ 19,857
Investment return:				
Investment income	6,222	13,407	19,629	17,607
Change in realized and unrealized appreciation	31,306	67,465	98,771	41,979
Total investment return	37,528	80,872	118,400	59,586
Payments to annuitants	(13,809)	(29,759)	(43,568)	(41,768)
Life income funds capitalized to endowment	(1,985)	(7,487)	(9,472)	(20,796)
Life income funds transferred to General Operating Account	(5,249)	(383)	(5,632)	(1,339)
Change in liabilities due under life income agreements	(24,130)	(48,593)	(72,723)	8,092
NET INCREASE DURING THE YEAR	28,969	23,349	52,318	23,632
Balance, beginning of year	111,279	250,865	362,144	338,512
BALANCE, end of year	\$ 140,248	\$ 274,214	\$ 414,462	\$ 362,144

11. BONDS AND NOTES PAYABLE

Bonds and notes payable as of June 30, 2004 and 2003 are summarized as follows (in thousands of dollars):

	Fiscal	Remaining	One-year			
	year	years to	effective	Outstanding	g principal	
	of issue	maturity	interest rate	2004	2003	
TAX-EXEMPT BONDS AND NOTES PAYABLE:						
Variable-rate bonds and notes:						
Series L - Weekly	1990	20	4.5%	\$ 71,140	\$ 71,140	
Series R - Weekly	2000-2004	45	0.9	103,670	90,765	
Series Y - Weekly	2000	31	5.3	117,905	117,905	
Series BB - Weekly	2001	30	0.9	196,700	196,700	
Series HH - Weekly	2004	30	5.7	92,235	0	
Commercial Paper (Series EE)	Various	29	1.0	519,434	212,298	
Total variable-rate bonds and notes			2.0	1,101,084	688,808	
Fixed-rate bonds:						
Series N	1992	16	6.3	78,771 *	78,679	
Series P	1995	28	5.5	104,730	105,830	
Series Z	2001	12	5.1	110,194 *	118,174	
Series AA	2001	5	5.5	24,769 *	29,403	
Series DD	2002	31	5.0	134,852 *	134,819	
Series FF	2003	33	5.1	275,968 *	275,962	
Radcliffe College Series 1997	1998	2	4.7	575	1,100	
Total fixed-rate bonds			5.3	729,859	743,967	
TOTAL TAX-EXEMPT BONDS AND NOTES PAYABLE			3.3	1,830,943	1,432,775	
TAXABLE BONDS AND NOTES PAYABLE:						
Commercial paper	Various		5.1	336,977	377,386	
Fixed-rate bonds	1992	3	8.1	115,000	115,000	
Series CC	2001	27	7.0	247,000	247,000	
TOTAL TAXABLE BONDS AND NOTES PAYABLE			6.3	698,977	739,386	
OTHER NOTES PAYABLE	Various	38		74,794	74,749	
TOTAL BONDS AND NOTES PAYABLE			4.1%	\$ 2,604,714	\$ 2,246,910	

^{*} Series N ,DD and FF principal are net of \$1.2 million, \$1.0 million and \$0.2 million of discounts, respectively. Series Z and AA principal include premiums of \$1.8 million and \$0.9 million, respectively.

Interest payments on a cash basis totaled \$77.1 million and \$70.8 million for fiscal 2004 and 2003, respectively. Interest expense was \$76.8 million for both fiscal 2004 and 2003. Excluding maturity of commercial paper and other notes payable, scheduled principal payments are (in thousands of dollars):

Fiscal year	Principal payments
2005	\$ 14,380
2006	13,960
2007	129,395
2008	14,175
2009	14,725
Thereafter	1,486,625
TOTAL	\$ 1,673,260

The University initiated its affiliate housing bond program in fiscal 2004 with the issuance of \$92.2 million of Series HH tax-exempt weekly variable-rate bonds. Also in fiscal 2004, the University reauthorized its existing tax-exempt commercial paper program (Series EE). With this action, the authorized limit on the program was raised from \$300 million to \$650 million. The series had \$519.4 million in outstanding notes as of June 30, 2004.

In fiscal 2003, the University issued \$276.2 million in fixed-rate Series FF bonds to finance a variety of capital facilities and equipment projects. The University also initiated a tax-exempt commercial paper program to finance construction period spending for large capital projects (Series EE). Also during fiscal 2003, the University recorded

an obligation to purchase certain property with payments that extend over 20 years. The present value of this obligation was \$6.4 million as of June 30, 2004.

Based on quoted market prices, the estimated fair value, including accrued interest, of Harvard's bonds and notes payable issued in the capital market as of June 30, 2004 and 2003 was \$2,582.7 million and \$2,277.1 million, respectively.

In July 2004, the University issued \$205.9 million in taxexempt weekly variable-rate Series GG-1 bonds and \$58.5 million in taxable weekly variable-rate Series GG-2 bonds to finance a new research facility. The Series GG-1 and Series GG-2 bonds mature in July 2029 and 2013, respectively.

Interest rate exchange agreements The University has entered into various interest rate exchange agreements in order to convert variable-rate borrowings to a fixed rate, thereby managing the interest cost and risk associated with its outstanding debt. The interest rate exchange agreements were not entered into for trading or speculative purposes. Under the terms of these agreements, the University pays a fixed rate, determined at inception, and receives a variable rate on the respective notional princi-

pal amounts. Each of these exchanges is collateralized, as described in *Note 4*. The interest rates in the preceding schedule reflect any applicable exchange agreements.

The fair value of interest rate exchange agreements is the estimated amount that the University would have received or (paid), including accrued interest, to terminate the agreements on the dates of the Balance Sheets, taking into account the creditworthiness of the underlying counterparties. The notional amount and fair value of interest rate exchange agreements were \$1,376.6 million and \$(58.4) million, respectively, as of June 30, 2004 and \$720.5 million and \$(120.0) million, respectively, as of June 30, 2003. The fair value of these agreements is included in "Investment portfolio, at market" in the Balance Sheets. The change in unrealized depreciation that was recognized for the interest rate exchange agreements was approximately \$61.7 million and \$78.6 million for fiscal 2004 and 2003, respectively. The loss realized from the monthly settling of these agreements was \$28.7 million and \$25.8 million for fiscal 2004 and 2003, respectively. All unrealized and realized gains and losses from interest rate exchange agreements are included in the "Change in appreciation, net of operating distribution" line in the Statements of Changes in Net Assets with General Operating Account Detail.

12. EMPLOYEE BENEFITS

The University offers current employees a choice of health plans, dental plans, short-term and long-term disability plans, life insurance, tuition assistance, and a variety of other benefits such as subsidized passes for public transportation and for Harvard athletic facilities. In addition, the University has pension plans covering substantially all employees.

The University uses a measurement date of June 30 for its pension and postretirement health plans.

PENSION BENEFITS Faculty members and certain long service administrative officers participate in defined contribution plans that are funded on a current basis. All staff and hourly employees are covered by a retirement program that includes a defined benefit component, a defined contribution component, or a combination of the two.

Effective July 1, 2002, certain union employees do not receive further compensation credits to their cash balance accounts, and the compensation credits to their individual investment accounts are increased.

In accordance with ERISA requirements, the University has established a trust to hold plan assets for its defined benefit pension plans. The market value of the trust's assets was \$640.0 million and \$575.4 million as of June 30, 2004 and 2003, respectively. In addition, the University has internally funded and invested \$26.8 million and \$27.9 million as of June 30, 2004 and 2003, respectively, for its defined benefit pension plans. The University recorded expenses for its defined contribution plans of \$61.6 million and \$71.3 million as of June 30, 2004 and 2003, respectively.

POSTRETIREMENT HEALTH BENEFITS The University provides defined benefit postretirement health coverage and life insurance to substantially all of its employees. As of June 30, 2004, the University invested \$97.9 million to fund the postretirement health benefit accrued liability of \$316.5 million. As of June 30, 2003, the University invested \$73.0 million to fund an accrued liability of \$250.4 million.

	2004	2003	2004	2003
In thousands of dollars	Pensio	n benefits	Other benefits	
CHANGE IN BENEFIT OBLIGATION				
Benefit obligation at beginning of year	\$ 583,588	\$ 508,061	\$ 491,656	\$ 379,017
Service cost	14,737	11,921	23,080	15,857
Interest cost	34,796	35,368	29,949	28,063
Plan participants' contributions	0	0	2,868	2,523
Amendments	0	(14,454)	0	0
Actuarial (gain)/loss	(18,941)	76,207	(28,247)	78,809
Benefits paid	(33,723)	(33,515)	(14,341)	(12,613)
BENEFIT OBLIGATION AT END OF YEAR	\$ 580,457	\$ 583,588	\$ 504,965	\$ 491,656

The accumulated benefit obligation for pension benefits in 2004 and 2003 was \$495.7 million and \$518.2 million, respectively.

CHANGE IN PLAN ASSETS				
Fair value of plan assets at beginning of year	\$ 575,366	\$ 585,394	\$ 0	\$ 0
Actual return on plan assets	98,309	23,487	0	0
Employer contribution	0	0	11,473	10,090
Plan participants' contributions	0	0	2,868	2,523
Benefits paid	(33,723)	(33,515)	(14,341)	(12,613)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	\$ 639,952	\$ 575,366	\$ 0	\$ 0
Funded status	\$ 59,494	\$ (8,221)	\$ (504,965)	\$ (491,656)
Unrecognized actuarial (gain)/loss	(51,632)	20,397	120,987	165,703
Unrecognized portion of net obligation at transition	0	0	54,560	60,622
Unrecognized prior service cost/(credit)	(34,634)	(40,052)	12,908	14,954
NET AMOUNT RECOGNIZED	\$ (26,772)	\$ (27,876)	\$ (316,510)	\$ (250,377)
AMOUNTS RECOGNIZED IN THE BALANCE SHEETS CONSIST OF:				
Prepaid benefit cost	\$ 0	\$ 0	\$ 0	\$ 0
Accrued benefit liability	(26,772)	(27,876)	(316,510)	(250,377)
NET AMOUNT RECOGNIZED	\$ (26,772)	\$ (27,876)	\$ (316,510)	\$ (250,377)

WEIGHTED-AVERAGE ASSUMPTIONS USED TO DETERMINE BENE	FIT OBLIGATIONS AS OF JU	JNE 30:		
Discount rate as of June 30	6.25%	6.00%	6.25%	6.00%
Rate of compensation increase as of June 30	4.00%	5.00%		

For measurement purposes, a 10.0% annual rate of increase in the per capita cost of covered health care

benefits was assumed for 2005, decreasing gradually to a 5.0% annual rate in 2010 and all years thereafter.

	2004	2003	2004	2003
In thousands of dollars	Pensio	n benefits	Othe	er benefits
COMPONENTS OF NET PERIODIC BENEFIT COST				
Service cost	\$ 14,737	\$ 11,921	\$ 23,080	\$ 15,857
Interest cost	34,796	35,368	29,949	28,063
Expected return on plan assets and reserves	(48,160)	(49,776)	(6,083)	(4,509)
Amortization of:				
transition obligation/(asset)	0	0	6,062	6,062
prior service cost/(credit)	(5,418)	(5,418)	2,046	2,046
actuarial loss/(gain)	(3,127)	(6,433)	6,620	3,386
Net periodic benefit cost/(income)	(7,172)	(14,338)	61,674	50,905
Investment return on invested reserves	6,068	4,251	15,932	7,267
TOTAL PERIODIC COST/(INCOME)	\$ (1,104)	\$ (10,087)	\$ 77,606	\$ 58,172

WEIGHTED-AVERAGE ASSUMPTIONS USED TO DETERMINE THE NET PE	RIODIC BENEFIT CO	ST FOR THE YEARS	ENDED JUNE 30:	
Discount rate as of June 30	6.00%	7.25%	6.00%	7.25%
Expected return on plan assets for the year	7.75%	7.75%	7.75%	7.75%
Rate of compensation increase as of June 30	5.00%	5.00%	5.00%	5.00%

The expected return on plan assets is determined by utilizing Harvard Management Company's capital markets model, which takes into account the expected real return, before inflation, for each one of the pension portfolio's asset classes, as well as the correlation of any one asset class to every other asset class. This model runs the real returns and correlations and derives an expected real return for the entire portfolio, given the percentage weighting allocated to each asset class. After calculating this expected

real return, an assessment is made to accommodate the expected inflation rate for the forthcoming period. The final expected return on assets is the aggregate of the expected real return plus the expected inflation rate.

Assumed health care trend rates have a significant effect on the amounts reported for the health care plan. A one percentage point change in assumed health care trend rates would have the following effects:

	2004		2003	
	One percentage	One percentage	One percentage	One percentage
In thousands of dollars	point decrease	point increase	point decrease	point increase
Effect on total of service cost and interest cost components	\$ (9,420)	\$ 12,332	\$ (7,071)	\$ 9,087
Effect on the postretirement benefit obligation	(70,573)	88,900	(63,055)	78,266

ASSET ALLOCATION BY CATEGORY FOR THE PENSION PORTFOLIO

TOTAL ALL ASSET CATEGORIES	100.0%	100.0%	100.0%
Other	21.0	21.3	15.7
Real estate	9.0	8.8	8.8
Debt securities	20.0	20.6	22.6
Equity securities	50.0%	49.3%	52.9%
	2005 Target	2004 Actual	2003 Actual

The University's investment strategy for the pension portfolio is to manage the assets across a broad and diversified range of investment categories, both domestic and international. The objective is to achieve a risk-adjusted return, which is in line with the long-dated

obligations that the University has to the pension plan beneficiaries. The investment program is also managed to comply with all ERISA regulations. The "Other" asset category consists of absolute return funds, commodities, and cash.

thousands of dollars Pension benefits		Other benefits
EXPECTED CASH FLOWS		
Employer contributions:		
2005 expected to plan assets, net of income from invested reserves	\$ (2,507)	\$ 10,351
2005 expected to participants	32,951	17,065
Expected benefit payments:		
2005	32,951	17,065
2006	33,503	18,662
2007	33,664	20,181
2008	34,623	21,621
2009	35,451	23,161
2010-2014	201,919	142,273

The Medicare Prescription Drug Improvement and Modernization Act of 2003 (the Act) was signed into law in December of 2003. The Act provides certain prescription drug-related benefits for retirees as well as subsidies for employers providing actuarial equivalent subsidies to their retirees. In January of 2004, the Financial Accounting Standards Board issued a Staff Position permitting companies to defer accounting for the effects of the Act. The University has elected this deferral. As such, the University's postretirement benefit obligation and

net periodic postretirement benefit cost do not reflect the effects of the Act. Guidance on the accounting for the federal subsidy under the Act has been issued effective for fiscal 2005. However, specific guidance on the eligibility for and amount of any employer subsidy available under the Act has not yet been finalized. When final guidance is available, the University may modify previously reported information to reflect the subsidies and other changes resulting from the Act.

13. GENERAL OPERATING ACCOUNT

The General Operating Account (GOA) consists of the general or current funds of the University as well as the assets, liabilities, and obligations related to student and faculty loans and facilities. The GOA accepts, manages, and pays interest on deposits made by University departments, invests surplus working capital, makes loans, and arranges external financing for major capital projects.

It is used to manage, control, and execute all University financial transactions, except for those related to investment activities conducted by the Harvard Management Company.

The major components of GOA net asset balances are summarized in the following table (in thousands of dollars):

		20	04		2003
		Temporarily	Permanently		
	Unrestricted	restricted	restricted	Total	Total
Departmental balances:					
Unexpended endowment income	\$ 63,121	\$ 387,388	\$ 0	\$ 450,509	\$ 488,865
Unexpended gift balances	65,405	273,906	0	339,311	334,102
Pledge balances	0	263,313	0	263,313	282,818
Loan funds	30,883	0	80,152	111,035	112,092
Funds for construction	0	48,382	0	48,382	30,552
Funds invested in fixed assets	1,189,028	0	0	1,189,028	1,106,497
Other departmental purposes	407,743	0	0	407,743	486,977
Total departmental balances	1,756,180	972,989	80,152	2,809,321	2,841,903
University balances	1,068,195	57,958	0	1,126,153	597,474
TOTAL	\$ 2,824,375	\$ 1,030,947	\$ 80,152	\$ 3,935,474	\$ 3,439,377

14. SPONSORED RESEARCH

Total expenditures funded by U.S. government sponsors or by institutions that subcontract federally sponsored research to the University were \$473.5 and \$416.2 million in fiscal 2004 and 2003, respectively. Approximately 95% of federal research support for the year ended June 30, 2004 was received by the Medical School, the School of Public Health, and the Faculty of Arts and Sciences. The University's principal source of federal research funds is the Department of Health and Human Services. The University also has many non-federal sources of sponsored support, including corporations, foundations, state and local governments, foreign governments, and research institutes.

Research grants and contracts normally provide for the recovery of direct and indirect costs. The University recognizes revenue associated with direct costs as the related costs are incurred. Recovery of related indirect costs is generally recorded at fixed or predetermined rates negotiated with the federal government and other sponsors. Predetermined federal indirect cost rates have been established for the University Area, the Medical School, and the School of Public Health through fiscal 2006. Funds received for federally sponsored research activity are subject to audit.

15. GIFTS

Gifts that are available for current purposes are classified as "Gifts for current use." Gifts that have been restricted by the donor or designated by the Corporation for construction, loan funds, endowment, or similar purposes are classified as "Gifts for capital." Both gifts for current use and gifts for capital are classified as unrestricted, temporarily restricted, or permanently restricted in accordance with donor specifications.

Gifts for the years ended June 30, 2004 and 2003 are summarized as follows (in thousands of dollars):

TOTAL GIFTS	\$ 591,833	\$ 562,370
Total gifts for capital	352,870	311,092
Loan funds and facilities	29,790	28,867
Life income funds*	65,313	19,857
Endowment funds	257,767	262,368
Gifts for capital:		
Total gifts for current use	238,963	251,278
Support for non-federal projects	85,445	99,337
Current use gift funds	\$ 153,518	\$ 151,941
Gifts for current use:		
	2004	2003

^{*} Gifts for capital to life income funds are presented at full value. The discounted present value of these gifts is \$23,062 and \$9,007 for fiscal 2004 and 2003, respectively.

16. OTHER OPERATING INCOME

The major components of other operating income for the years ended June 30, 2004 and 2003 were as follows (in thousands of dollars):

	2004	2003
Publications	\$ 76,901	\$ 71,213
Rental and parking	81,954	63,154
Royalties from patents,		
copyrights, and trademarks	50,697	47,883
Other student income	20,698	13,926
Health and clinic fees	12,313	10,991
Other	130,133	128,133
TOTAL OTHER OPERATING INCOME	\$ 372,696	\$ 335,300

17. OTHER EXPENSES

The major components of other expenses for the years ended June 30, 2004 and 2003 were as follows (in thousands of dollars):

	2004	2003
Services purchased	\$ 224,424	\$ 244,001
Subcontract expenses		
under sponsored projects	79,794	73,664
Publishing	51,020	53,631
Travel	49,744	45,799
Telephone	11,110	12,196
Other	72,023	55,414
TOTAL OTHER EXPENSES	\$ 488,115	\$ 484,705

18. FUNCTIONAL CLASSIFICATION OF EXPENSES

Expenses are allocated functionally on a direct basis. Interest, depreciation, and operations and maintenance expenses are allocated based on square footage. Operations and maintenance costs allocated to functional categories totaled \$217.5 million and \$198.6 million for the years ended June 30, 2004 and 2003, respectively.

Expenses by functional classification for the years ended June 30, 2004 and 2003 were as follows (in thousands of dollars):

	2004	2003
Instruction	\$ 710,870	\$ 672,960
Research	585,623	535,916
Libraries	164,055	156,265
Academic support	211,074	235,996
Scholarships and other student awards	89,414	79,510
Student services	119,181	100,292
Institutional support	389,722	343,546
Auxiliary services	290,980	308,459

TOTAL EXPENSES \$ 2,560,919 \$ 2,432,944

19. COMMITMENTS AND CONTINGENCIES

The University receives funding from federal government agencies for research conducted under government grants and contracts. The grants and contracts provide for reimbursement of direct and indirect costs. The costs recovered by the University in support of sponsored research are subject to audit and adjustment.

In July of 1999, the University commenced a comprehensive investigation of the most recent years of the administration of a specific training grant funded by the National Institute on Aging. The University entered into an agreement with the government to resolve this matter during fiscal 2004.

In April of 1997, the Harvard Institute for International Development (HIID) learned of an investigation by the Inspector General's Office of the U.S. Agency for International Development (USAID). USAID had awarded amounts to HIID under two cooperative agreements to provide assistance to Russia in implementing economic and legal reforms. In September of 2000, the United States filed an eleven-count civil complaint against the University and others. The district court has since dismissed or entered judgment for the University on all counts against it, except for one count alleging breach

of contract. Regarding this breach of contract count, the court issued summary judgment for the government on liability during fiscal 2004. It is not possible to predict what damages, if any, the government may receive as a result of the court's finding.

While it is not possible to predict accurately or determine the eventual outcome of the above described legal matters or various other legal proceedings involving the University, management believes that the outcome of these proceedings will not have a material adverse effect on the University's financial position, results of operations, or cash flows.

In the spring of 2004, the University together with the Massachusetts Institute of Technology (MIT) and the Whitehead Institute for Biomedical Research established the Eli and Edythe L. Broad Institute. The Broad Institute is a collaborative biomedical research institute within MIT that is jointly governed by the University, MIT, and the Broad Foundation. The Institute is focused on applying knowledge of the human genome to clinical medicine and making such knowledge widely available to the scientific community.

In connection with the founding of the Broad Institute, the University and MIT agreed to try to jointly raise \$20 million per year in gifts and non-federal grants and awards to support the Institute's endeavors. In the event this fundraising goal is not reached, the University has agreed to provide MIT with a portion of the shortfall, subject to certain conditions. The University's obligation for such payments will not exceed \$20 million over the initial five-year term of the Institute, or \$30 million in total if the term is extended for a second five years. The University will make payments and record the corresponding expenses as these conditions are met. The University made no such payments to MIT for the Broad Institute during fiscal 2004.

The University and MIT will equally share certain laboratory construction costs for the Broad Institute's new building, which is expected to be completed in fiscal 2006. The University's portion of these costs is expected to be approximately \$10 million. If the University's participation in the collaboration terminates under certain circumstances, the University may also be obligated to pay MIT up to \$5 million to compensate MIT for expenses incurred in connection with the lease for the new building. In addition, the University expects to share with MIT in ongoing facilities improvement costs of approximately \$4 million per year for up to ten years. Some of the University's contributions to these capital costs may be reimbursed in the future through indirect cost recoveries associated with the Institute's grant funding.

Report of independent auditors

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To the Board of Overseers of Harvard College:

In our opinion, the accompanying Balance Sheet and the related Statements of Changes in Net Assets with General Operating Account Detail, Changes in Net Assets of the Endowment, and Cash Flows present fairly, in all material respects, the financial position of Harvard University (the "University") at June 30, 2004, and the changes in the net assets of its general operating account and endowment funds and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the University's fiscal 2003 financial statements, and in our report dated September 25, 2003, we expressed an unqualified opinion on those financial statements. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

October 1, 2004

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SUPPLEMENTAL INFORMATION

- 54 POOLED GENERAL INVESTMENTS
- 56 GIFTS FOR CURRENT USE
- 57 GIFTS FOR CAPITAL
- 58 ENDOWMENT FUNDS BY DEPARTMENT
- 60 ENDOWMENT AND INCOME INFORMATION

FOR THE TEN SCHOOLS

MENTORING IN THE CRIMSON SUMMER ACADEMY

The Crimson Summer Academy is a critical component of the University's new undergraduate financial aid initiative. Designed to help local students from financially disadvantaged backgrounds attend top colleges, the Academy brought 30 high school sophomores to Harvard for an intensive four-week session in its

inaugural year. The students pursued a broad curriculum while receiving mentoring from current Harvard students. The three-year program will include events and advising throughout the school year in addition to summer sessions.

Pooled general investments

The "Asset allocation" for the General Investment Account is based on the Policy Portfolio as described in the unaudited Annual Report of the Harvard Management Company. The Policy Portfolio is the asset mix that is most likely to meet the long-term needs of the University with the appropriate level of risk. While the Policy Portfolio defines the University's market risk profile, Harvard Management Company (нмс) undertakes a number of diversified arbitrage activities to enhance the returns without changing the portfolio's risk profile. These trades are subtle and complex and tend to have a long volatility bias. The focus of these return enhancement strategies is to identify mispricings of specific financial instruments relative to other similar instruments. Once these mispricings are identified, a series of long and short transactions are undertaken to capture the mispricings and to remain neutral to changes in the value of the underlying asset class. These offsetting positions are taken in both instruments recorded on the summary of assets and liabilities (balance sheet cash positions) and in off-balance sheet products (futures, options, over-the-counter exchange agreements, and forwards), as exhibited in Note 4 to the University's financial statements.

The accompanying table combines the balance sheet and the off-balance sheet financial instruments in a form consistent with HMC's approach to the management of the General Investment Account. The table categorizes the information presented in the financial statements into groupings reflecting the type of strategy. There are several key points to be noted:

- A) The "Balance sheet cash positions" are the assets and liabilities shown on the summary of assets and liabilities included in *Note 4* to the University's financial statements.
- **B**) The on-balance sheet and off-balance sheet positions, both long and short, net to the core market exposure of the portfolio, which approximates the market exposure of the Policy Portfolio.
- **c**) The off-balance sheet amounts represent the market exposure on the notional value of the forwards, futures, options, and exchange agreements included in *Note 4* to the University's financial statements.

D) From a market exposure standpoint, HMC uses on-balance sheet and off-balance sheet financial instruments interchangeably.

The "Asset class" column describes the basic assets of the Policy Portfolio broken down into its major categories with the addition of a series of diversified arbitrage accounts related to the equity, commodity, and fixed-income portfolios. The arbitrage accounts represent the positions taken in value-added strategies to enhance the returns of the underlying Policy Portfolio. The "Other" asset class represents on-balance sheet and off-balance sheet positions that are not subject to market risk, but which may be subject to credit risk. Included in this category are financial instruments such as cash, premiums paid or received on option positions, and balances related to securities lending (collateral held under security lending agreements) and securities borrowing (collateral advanced under security borrowing agreements).

The remainder of the schedule shows the on-balance sheet and off-balance sheet positions of the specific investment categories. The "Balance sheet cash positions" columns show the financial positions that are reported on the pooled general investment balance sheet. These columns include ownership or short sells in stock and bond positions, as well as investments in real estate, commodities, and private equities, either directly or through limited partnerships.

The "Forwards," "Futures," "Options," and "Exchange agreements" columns represent the long and short values of the off-balance sheet positions. Option positions have been adjusted to reflect the market exposure of the underlying assets. Fixed-income futures have been adjusted to reflect duration weighting where appropriate. The positions in these categories are primarily used for the value-added arbitrage transactions, but may also be used to adjust the core asset mix in a nondisruptive and cost-effective manner.

The "Net market exposure" column aggregates long and short exposure across all types of instruments and may differ from the "Asset allocation" as reported in the unaudited *Annual Report of the Harvard*

Management Company. The balance sheet cash positions and off-balance sheet amounts are reported in accordance with generally accepted accounting principles and don't necessarily reflect "market risk" exposure amounts. For instance, in the equity area, the University owns convertible debt positions hedged by equity. The balance sheet reflects the market value of the convertible debt: however. depending on the conversion features of the bond and the volatility of the underlying equity, the convertible debt will have significantly less equity market exposure than the amount recorded on the balance sheet. In the fixed-income area, a fully hedged strategy designed to capture shifts in the yield curve may reflect a mismatch in long and short market exposure due to the duration qualities of the underlying instruments. In some instances, option strategies have been employed to take advantage of market volatility. While these strategies may appear to generate unhedged market exposure, the potential losses are limited to the option premium, which is comparatively small relative to the indicated exposure. The activities of arbitrage accounts are focused on adding value to the Policy Portfolio, taking advantage of mispricings in a variety of financial instruments, and creating a well-diversified set of specific strategies. The market, credit, legal, operational, and liquidity risks associated with these strategies are monitored on a daily basis by an internal independent risk management group. This risk management group utilizes a number of different methodologies to evaluate and control the various risks of the core portfolios and value-added strategies. Individual strategies and portfolios are reviewed to monitor value at risk, compliance with cash and margin requirements, and adherence to credit risk limits established by нмс for each counterparty. All positions other than private equity, certain commodities, and real estate are marked-to-market on a daily basis. with applicable profit and loss statements generated for each strategy. Risk monitoring and control is described in greater detail in the unaudited Annual Report of the Harvard Management Company, found on page 22.

			Mari	ET EXPOSU	RE OF OFF-E	BALANCE SH	EET INSTRUM	MENTS		То	TAL		
				Furupec		0		EXCHANGE				Net	
CASH F	OSITIONS	ITIONS FORWARDS	VARDS	- FUIUKES	OPTIONS	AGREEMENTS		EXPOSURE		market	Asset		
Long	Short	Long	Short	Long	Short	Long	Short	Long	Short	Long	Short	exposure	allocation
4,632	-	-	-	228	-	-	-	-	-	4,860	-	4,860	4,779
2,630	-	-	-	-	-	-	-	-	-	2,630	-	2,630	2,907
3,483	-	-	-	-	-	-	-	-	-	3,483	-	3,483	3,447
1,654	-	-	-	-	-	12	-	333	-	1,999	-	1,999	1,829
1,453	(697)	-	-	8	(848)	87	(38)	31	(269)	1,579	(1,852)	(273)	-
13,852	(697)	-	-	236	(848)	99	(38)	364	(269)	14,551	(1,852)	12,699	12,962
2,425	-	-	-	-	-	-	-	-	(708)	2,425	(708)	1,717	1,708
150	-	-	-	-	-	362	(16)	315	(350)	827	(366)	461	826
1,176	-	-	-	29	(37)	1	-	-	(37)	1,206	(74)	1,132	1,497
1,327	-	-	-	-	-	-	-	-		1,327	-	1,327	1,446
23,997	(1,381)	-	-	114	(284)	19,317	(7,352)	7,074	(32,775)	50,502	(41,792)	8,710	-
29,075	(1,381)		-	143	(321)	19,680	(7,368)	7,389	(33,870)	56,287	(42,940)	13,347	5,477
2,197	-	-	-	-	-	-	-	880		3,077	-	3,077	2,986
337	-	-	-	-	(86)	123	(273)	547	(490)	1,007	(849)	158	-
2,534	-	-	-	-	(86)	123	(273)	1,427	(490)	4,084	(849)	3,235	2,986
1,981	-	-	-	-	-	-	-	-	-	1,981	-	1,981	1,968
1,457	-	-	-	-	-	-	-	-	-	1,457	-	1,457	1,420
48,899	(2,078)	-	-	379	(1,255)	19,902	(7,679)	9,180	(34,629)	78,360	(45,641)	32,719	24,813
1,094	-												595
1,196	-												-
-	(26,073)												
849	-												-
2,268	(747)												
5,407	(26,820)												595
54.306	(28.898)												25,408
	Long 4,632 2,630 3,483 1,654 1,453 13,852 2,425 150 1,176 1,327 23,997 29,075 2,197 337 2,534 1,981 1,457 48,899 1,094 1,196 - 849 2,268	4,632 - 2,630 - 3,483 - 1,654 - 1,453 (697) 13,852 (697) 2,425 - 150 - 1,176 - 1,327 - 23,997 (1,381) 2,197 - 337 - 2,534 - 1,981 - 1,457 - 48,899 (2,078) 1,094 - 1,196 - (26,073) 849 - 2,268 (747) 5,407 (26,820)	CASH POSITIONS FORW	BALANCE SHEET CASH POSITIONS FORWARDS	BALANCE SHEET FORWARDS FUT Long	BALANCE SHEET CASH POSITIONS FORWARDS FUTURES	BALANCE SHEET CASH POSITIONS	RALANCE SHEET CASH POSITIONS FORWARDS FUTURES OPTIONS	CASH POSITIONS	BALANCE SHEET CASH POSITIONS FORWARDS FUTURES OPTIONS ACREEMENTS	BALANCE SHEET CASH POSITIONS	BALANCE SHEET CASH POSITIONS	BALANCE SHEET CASH POSITIONS FORWARDS FUTURES OPTIONS CACREEMENTS CASREEMENTS CASRE

Gifts for current use

Year ended June 30, 2004 (in thousands of dollars)	
FACULTIES:	
Faculty of Arts and Sciences	\$ 59,642
Business School	14,570
School of Dental Medicine	607
School of Design	2,264
Divinity School	1,127
School of Education	7,701
John F. Kennedy School of Government	27,968
Law School	18,170
Medical School	53,962
School of Public Health	23,519
Radcliffe Institute for Advanced Study	2,554
TOTAL FACULTIES	212,084
OTHER ACADEMIC DEPARTMENTS:	
Arnold Arboretum	365
Harvard University Art Museums	2,668
Joint Center for Housing Studies	1,694
Nieman Foundation	877
Villa I Tatti	727
TOTAL OTHER ACADEMIC DEPARTMENTS	6,331
SERVICE DEPARTMENTS:	
Harvard University Press	6
University Health Services	30
TOTAL SERVICE DEPARTMENTS	36
CENTRAL ADMINISTRATION:	
Memorial Church	554
President's Initiatives	18,773
University Library	1,035
University Unrestricted	150
TOTAL CENTRAL ADMINISTRATION	20,512
TOTAL GUETA FOR GUIDDENIT HAS	
TOTAL GIFTS FOR CURRENT USE	\$ 238,963

Gifts for capital

Year ended June 30, 2004 (in thousands of dollars) funds funds funds Total FACULTIES: Faculty of Arts and Sciences \$ 92,853 \$ 2,391 \$ 46 \$ 52,902 84,222 </th <th></th> <th>Endowment</th> <th>Construction</th> <th>Loan</th> <th></th>		Endowment	Construction	Loan	
Paculty of Arts and Sciences	Year ended June 30, 2004 (in thousands of dollars)	funds	funds	funds	Total
Business School 60,111 24,056 55 84,222 School of Dental Medicine 114 292 406 School of Dental Medicine 114 292 406 School of Dental Medicine 1,074 6 1,080 Divinity School 1,177 1,130 1 2,548 John F. Kennedy School of Government 3,528 100 764 20,175 John F. Kennedy School of Government 3,528 100 764 20,175 John F. Kennedy School of Government 3,327 5 439 33,673 School of Public Health 3,327 5 439 3,3673 School of Public Health 3,327 169 245,297 OTHER ACADEMIC DEPARTMENTS: Armold Arboretum 188 8 188 Barvard University Art Museums 768 2 2 Nieman Foundation 5 24 2 2 Villa I Tatti 137 12 149 149 TOTAL OF L	FACULTIES:				
School of Dental Medicine 114 292 406 School of Design 702 702 Divinity School 1,074 6 1,080 School of Education 1,417 1,130 1 2,548 John F. Kennedy School of Government 3,528 100 3,628 Law School 19,111 300 764 20,175 Medical School 33,229 5 439 33,673 35,278 33,273 33,273 33,273 33,273 33,273 33,279 33,273 33,273 33,275 33,275 33,273 33,275 32,48,29 30,275 31,28 37,275 32,48,29 37,275 32,28,29 33,275<	Faculty of Arts and Sciences	\$ 92,853	\$ 2,391	\$ 46	\$ 95,290
School of Design 702 702 Divinity School 1,074 6 1,080 School of Education 1,417 1,313 1 2,548 John F, Kennedy School of Government 3,528 100 3,628 Law School 19,111 300 764 20,175 Medical School 3,327 5 439 33,627 School of Public Health 3,327 169 3,246 TOTAL FACULTIES 218,543 28,49 1,305 248,295 TOTAL FACULTIES 28 28,449 1,305 248,295 TOTAL FACULTIES 188 188 188 Harvard University Art Museums 768 5 24 29 Villa 1 Tati 137 12 149 104 TOTAL TATUTION 1,098 36 0 1,134 TOTAL SERVICE DEPARTMENTS 7,002 8 2,002 University Health Services 13 0 7,002 CENTRAL ADMINISTRATION: 862	Business School	60,111	24,056	55	84,222
Divinity School 1,074 6 1,080 School of Education 1,417 1,130 1 2,548 John F. Kennedy School of Government 3,528 100 3,628 Law School 19,111 300 764 20,175 Medical School 33,229 5 439 33,673 School of Public Health 3,327 69 3,246 School of Public Health 3,377 169 3,246 TOTAL FACULTIES 218,543 28,449 1,305 248,297 OTHER ACADEMIC DEPARTMENTS: University Park Museums 768 2 2,82 New John Compartments 188 188 Haryard University Art Museums 768 2 2 Nieman Foundation 5 24 29 Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS 7,002 2 7	School of Dental Medicine	114	292		406
School of Education 1,417 1,130 1 2,548 John F. Kennedy School of Government 3,528 100 3,628 Law School 19,111 300 764 20,758 Medical School 33,229 5 439 33,673 School of Public Health 3,327 169 3,246 TOTAL FACULTIES 218,543 28,449 1,305 248,297 OTHER ACADEMIC DEPARTMENTS: Armold Arboretum 188 8 188 Nieman Foundation 5 24 29 Villa 1 Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS SERVICE DEPARTMENTS 7,002 7,002 7,002 CONDEPARTMENTS 13 13 13 CENTRAL ADMINISTRATION: 862 862 862 CENTRAL ADMINISTRATION: 862 862 862 Universi	School of Design	702			702
School of Education 1,417 1,130 1 2,548 John F. Kennedy School of Government 3,528 100 3,628 Law School 19,111 300 764 20,758 Medical School 33,229 5 439 33,673 School of Public Health 3,327 169 3,246 TOTAL FACULTIES 218,543 28,449 1,305 248,297 OTHER ACADEMIC DEPARTMENTS: Arrange Minersity Art Museums 188 8 188 Nieman Foundation 5 24 29 Villa 1 Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS 7,002 7,002 7,002 CHARRAGE MINISTRATION: 13 13 13 CENTRAL ADMINISTRATION: 862 862 862 President's Initiatives 26,985 8 26,985 University Library 823	Divinity School	1,074	6		1,080
John F. Kennedy School of Government 3,528 100 3,628 Law School 19,111 300 764 20,175 Medical School 33,229 5 439 33,273 School of Public Health 3,327 169 3,246 TOTAL FACULITIES 218,543 28,449 1,305 248,297 COTAL FACULITIES COTHER ACADEMIC DEPARTMENTS: Transl Act Movements 188 28,449 1,305 248,297 COTHER ACADEMIC DEPARTMENTS: Transl Act Multiversity Art Museums 768 5 24 29 Villa I Tatti 137 12 29 19 Villa I Tatti 137 12 29 Villa I Tatti 137 12 49 Villa I Tatti 137 12 9 Villa I Tatti 137 12 9 Villa I Tatti 137 12 9 7 7,002 <td< td=""><td>,</td><td>1,417</td><td>1,130</td><td>1</td><td>2,548</td></td<>	,	1,417	1,130	1	2,548
Law School 19,111 300 764 20,175 Medical School 33,229 5 459 33,673 School of Public Health 3,327 169 3,246 TOTAL FACULTIES 218,543 28,449 1,305 248,297 OTHER ACADEMIC DEPARTMENTS: Arnold Arboretum 188 28,449 1,305 248,297 OTHER ACADEMIC DEPARTMENTS: 768 6 768 Nieman Foundation 5 24 29 Villa 1 Tatit 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS: Harvard University Press 7,002 7,002 7,002 University Health Services 13 13 13 TOTAL SERVICE DEPARTMENTS 2,015 0 7,002 University Health Services 13 2 82 CENTRAL ADMINISTRATION: 862 82 82 University Librar	John F. Kennedy School of Government	·	100		·
Medical School 33,229 5 439 33,673 School of Public Health 3,277 169 3,246 TAGACHIF Institute for Advanced Study 3,077 169 2,48,297 OTHER ACADEMIC DEPARTMENTS: Arnold Arboretum 188 3,84 188 Harvard University Art Museums 768 24 29 Nilean Foundation 5 24 29 Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS 7,002 7,002 7,002 CUNIVERSITY Press 7,002 7,002 7,002 CUNIVERSITY Press 7,015 0 7,002 7,002 CUNIVERSITY Press 8 2 862 862 862 862 862 862 862 862 862 862 862 862 862 862 862 862 862 862 862	•	·	300	764	·
School of Public Health 3,327 169 3,247 Radciffe Institute for Advanced Study 3,077 169 3,246 TOTAL FACULTIES 218,543 28,449 1,305 248,297 OTHER ACADEMIC DEPARTMENTS: Arnold Arboretum 188 8 188 Harvard University Art Museums 768 6 26 Nieman Foundation 5 24 29 Villa 1 Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS: Harvard University Press 7,002 7,002 7,002 University Health Services 13 3 13 3 13 13 13 13 13 13 13 13 13 13 13 13 13 13 13 13 13 13 14 14 14 14 14 14 14 14 14 14 14 <					·
Radcilife Institute for Advanced Study 3,077 169 3,246 TOTAL FACULTIES 218,543 28,449 1,305 248,287 OTHER ACADEMIC DEPARTMENTS: Arnold Arboretum 188 188 Harvard University Art Museums 768 2 29 Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS: 3 6 0 1,134 SERVICE DEPARTMENTS: 13 2 7,002 University Health Services 13 0 7,002 University Health Services 13 0 7,015 CENTRAL ADMINISTRATION: 862 862 President's Initiatives 26,985 26,985 University Library 823 28 University Unrestricted 2,441 2,441 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$ 25,767 \$ 28,485 \$ 1,305 287,557 LIFE INCOME FUNDS: 5 52,767		·			,
TOTAL FACULTIES 218,543 28,449 1,305 248,297 OTHER ACADEMIC DEPARTMENTS: 8 188 188 Harvard University Art Museums 768 768 768 Nieman Foundation 5 24 29 Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS: Harvard University Press 7,002 7,002 7,002 University Health Services 13 13 13 TOTAL SERVICE DEPARTMENTS 7,015 0 0 7,015 CENTRAL ADMINISTRATION: Wemorial Church 862 862 862 President's Initiatives 26,985 26,985 26,985 University Library 823 23 24 24 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$25,767 \$28,485 \$1,305 287,5		·	169		•
OTHER ACADEMIC DEPARTMENTS: Arnold Arboretum 188 188 Harvard University Art Museums 768 768 Nieman Foundation 5 24 29 Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS: TOTAL University Press 7,002 7,002 7,002 University Health Services 13 13 13 13 13 10 13 10 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 7,015 0 0 2,015	· · · · · · · · · · · · · · · · · · ·	· · · · · · · · · · · · · · · · · · ·		1,305	
Arnold Arboretum 188 188 Harvard University Art Museums 768 768 Nieman Foundation 5 24 29 Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS 7,002 7,002 7,002 13 14 14 14 14 14 14 14 14 14 14 14 14 14 14 14 14 14 14 14		,	,	,	
Harvard University Art Museums 768 768 Nieman Foundation 5 24 29 Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS: Harvard University Press 7,002 7,002 7,002 University Health Services 13 13 13 TOTAL SERVICE DEPARTMENTS 81 3 13 CENTRAL ADMINISTRATION: Wemorial Church 862 862 President's Initiatives 26,985 26,985 University Unrestricted 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$257,767 \$28,485 \$1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts \$2,217 50 Grift Annuities \$2,845 \$1,305 287,557 Harvard Balanced Fund	OTHER ACADEMIC DEPARTMENTS:				
Nieman Foundation 5 24 29 Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS: Harvard University Press 7,002 7,002 7,002 University Health Services 13 0 0 7,015 CENTRAL ADMINISTRATION: Memorial Church 862 862 862 President's Initiatives 26,985 26,985 26,985 University Unrestricted 2,441 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$257,767 \$28,485 \$1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 50 50 30 30 30 30 30 30 30 30 30 30 30 30 30 30 31 30	Arnold Arboretum	188			188
Villa I Tatti 137 12 149 TOTAL OTHER ACADEMIC DEPARTMENTS 1,098 36 0 1,134 SERVICE DEPARTMENTS: Harvard University Press 7,002 7,002 7,002 University Health Services 13 13 13 TOTAL SERVICE DEPARTMENTS 7,015 0 0 7,015 CENTRAL ADMINISTRATION: Memorial Church 862 862 862 President's Initiatives 26,985 26,985 26,985 University Library 823 823 823 University Unrestricted 2,441 0 0 31,111 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$257,767 \$28,485 \$1,305 287,557 LIFE INCOME FUNDS Charitable Remainder Annuities and Unitrusts \$2,217 36 30 30 30 30 30 30 30 30 30 <td>Harvard University Art Museums</td> <td>768</td> <td></td> <td></td> <td>768</td>	Harvard University Art Museums	768			768
SERVICE DEPARTMENTS:	Nieman Foundation	5	24		29
SERVICE DEPARTMENTS: Harvard University Press 7,002 7,002 University Health Services 13 13 TOTAL SERVICE DEPARTMENTS 7,015 0 0 7,015 CENTRAL ADMINISTRATION: Memorial Church 862 862 862 President's Initiatives 26,985 26,985 26,985 University Library 823 823 823 University Unrestricted 2,441 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$257,767 \$28,485 \$1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 536 Harvard Balanced Fund 70 70 Harvard Growth Fund 98 Harvard Life Return Fund 98 TOTAL LIFE INCOME FUNDS 65,313	Villa I Tatti	137	12		149
Harvard University Press 7,002 7,002 13 13 13 13 13 13 15 15	TOTAL OTHER ACADEMIC DEPARTMENTS	1,098	36	0	1,134
Harvard University Press 7,002 7,002 13 13 13 13 13 13 15 15					
University Health Services 13 13 TOTAL SERVICE DEPARTMENTS 7,015 0 0 7,015 CENTRAL ADMINISTRATION: Memorial Church 862 862 President's Initiatives 26,985 26,985 University Library 823 823 University Unrestricted 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$257,767 \$ 28,485 \$ 1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 \$ 26 \$ 26 \$ 27,217 <th< td=""><td>SERVICE DEPARTMENTS:</td><td></td><td></td><td></td><td></td></th<>	SERVICE DEPARTMENTS:				
TOTAL SERVICE DEPARTMENTS 7,015 0 0 7,015 CENTRAL ADMINISTRATION: Memorial Church 862 862 President's Initiatives 26,985 26,985 University Library 823 823 University Unrestricted 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$ 257,767 \$ 28,485 \$ 1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 Gift Annuities 12,536 Harvard Balanced Fund 70 Harvard Growth Fund 98 Harvard Life Return Fund 392 TOTAL LIFE INCOME FUNDS 65,313	Harvard University Press	7,002			7,002
CENTRAL ADMINISTRATION: Memorial Church 862 862 President's Initiatives 26,985 26,985 University Library 823 823 University Unrestricted 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$ 257,767 \$ 28,485 \$ 1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 50ff Annuities 12,536 Harvard Balanced Fund 70 70 70 70 Harvard Growth Fund 98 70	University Health Services	13			13
Memorial Church862862President's Initiatives26,98526,985University Library823823University Unrestricted2,4412,441TOTAL CENTRAL ADMINISTRATION31,1110031,111TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS\$ 257,767\$ 28,485\$ 1,305287,557LIFE INCOME FUNDS:Charitable Remainder Annuities and Unitrusts52,217Gift Annuities12,536Harvard Balanced Fund70Harvard Growth Fund98Harvard Life Return Fund392TOTAL LIFE INCOME FUNDS65,313	TOTAL SERVICE DEPARTMENTS	7,015	0	0	7,015
Memorial Church862862President's Initiatives26,98526,985University Library823823University Unrestricted2,4412,441TOTAL CENTRAL ADMINISTRATION31,1110031,111TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS\$ 257,767\$ 28,485\$ 1,305287,557LIFE INCOME FUNDS:Charitable Remainder Annuities and Unitrusts52,217Gift Annuities12,536Harvard Balanced Fund70Harvard Growth Fund98Harvard Life Return Fund392TOTAL LIFE INCOME FUNDS65,313	CENTRAL ADMINISTRATION.				
President's Initiatives 26,985 26,985 26,985 University Library 823 823 823 University Unrestricted 2,441 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$257,767 \$28,485 \$1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 Gift Annuities 12,536 Harvard Balanced Fund 70 Harvard Growth Fund 98 Harvard Life Return Fund 392 TOTAL LIFE INCOME FUNDS 65,313		963			9.63
University Library 823 University Unrestricted 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$257,767 \$28,485 \$1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 Gift Annuities Harvard Balanced Fund 570 Harvard Growth Fund 598 Harvard Life Return Fund 599 TOTAL LIFE INCOME FUNDS 65,313					
University Unrestricted 2,441 2,441 TOTAL CENTRAL ADMINISTRATION 31,111 0 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$257,767 \$28,485 \$1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 Gift Annuities 52,217 Gift Annuities 70 Harvard Balanced Fund 70 Harvard Growth Fund 98 Harvard Life Return Fund 392 TOTAL LIFE INCOME FUNDS 65,313		·			•
TOTAL CENTRAL ADMINISTRATION 31,111 0 0 0 31,111 TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$ 257,767 \$ 28,485 \$ 1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts \$ 52,217 Gift Annuities \$ 12,536 Harvard Balanced Fund \$ 70 Harvard Growth Fund \$ 98 Harvard Life Return Fund \$ 392 TOTAL LIFE INCOME FUNDS \$ 65,313	, ,				
TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS \$ 257,767 \$ 28,485 \$ 1,305 287,557 LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts 52,217 Gift Annuities 12,536 Harvard Balanced Fund 70 Harvard Growth Fund 98 Harvard Life Return Fund 392 TOTAL LIFE INCOME FUNDS 65,313		· · · · · · · · · · · · · · · · · · ·			· · · · · · · · · · · · · · · · · · ·
LIFE INCOME FUNDS: Charitable Remainder Annuities and Unitrusts Gift Annuities Harvard Balanced Fund Harvard Growth Fund Harvard Life Return Fund TOTAL LIFE INCOME FUNDS S2,217 52,217 62,217 62,217 62,217 63,318	TOTAL CENTRAL ADMINISTRATION	31,111	0	0	31,111
Charitable Remainder Annuities and Unitrusts52,217Gift Annuities12,536Harvard Balanced Fund70Harvard Growth Fund98Harvard Life Return Fund392TOTAL LIFE INCOME FUNDS65,313	TOTAL ENDOWMENT, CONSTRUCTION, AND LOAN FUNDS	\$ 257,767	\$ 28,485	\$ 1,305	287,557
Charitable Remainder Annuities and Unitrusts52,217Gift Annuities12,536Harvard Balanced Fund70Harvard Growth Fund98Harvard Life Return Fund392TOTAL LIFE INCOME FUNDS65,313	LIFE INCOME FUNDS:				
Gift Annuities 12,536 Harvard Balanced Fund 70 Harvard Growth Fund 98 Harvard Life Return Fund 392 TOTAL LIFE INCOME FUNDS 65,313					52 217
Harvard Balanced Fund Harvard Growth Fund Harvard Life Return Fund TOTAL LIFE INCOME FUNDS 70 65,313					
Harvard Growth Fund 98 Harvard Life Return Fund 392 TOTAL LIFE INCOME FUNDS 65,313					,
Harvard Life Return Fund 392 TOTAL LIFE INCOME FUNDS 65,313					
TOTAL LIFE INCOME FUNDS 65,313					
, , , , , , , , , , , , , , , , , , ,					
TOTAL GIFTS FOR CAPITAL \$ 352,870	TOTAL LITE INCOME FORDS				05,515
	TOTAL GIFTS FOR CAPITAL				\$ 352,870

Endowment funds by department

Year ended June 30, 2004 (dollar amounts in thousands)

_ 1		
Endowment	principal	

1eur enueu june 30, 2004 (uouur amounis in inousuri	us)	1	ildowillellt billicil	Jd1	
	D11	Gifts and	D11	Manlantanlan	Participating
	Book value July 1, 2003	other changes	Book value June 30, 2004	Market value	units
FACULTIES:	July 1, 2003	other changes	June 30, 2004	June 30, 2004	June 30, 2002
Faculty of Arts and Sciences	\$ 2,367,906	\$ 123,194	\$ 2,491,100	\$ 10,256,052	8,423,517
Business School	511,079	61,920	572,999	1,602,580	1,307,762
School of Dental Medicine	29,518	154	29,672	140,214	115,338
School of Design	58,838	930	59,768	283,266	233,010
Divinity School	77,463	(1,096)	76,367	400,107	329,122
School of Education	91,333	1,848	93,181	342,062	281,375
John F. Kennedy School of Government	217,473	2,273	219,746	672,674	547,420
Law School	279,190	22,102	301,292	1,099,556	902,360
Medical School	704,411	46,466	750,877	2,463,945	2,026,055
School of Public Health	149,543	9,471	159,014	743,238	2,020,033
Radcliffe Institute for Advanced Study	180,911	21,651	,	•	•
TOTAL FACULTIES			202,562	355,221	292,115
TOTAL FACULITES	4,667,665	288,913	4,956,578	18,358,915	15,069,450
OTHER ACADEMIC DEPARTMENTS:					
Arnold Arboretum	37,282	1,745	39,027	191,917	157,868
Harvard University Art Museums	99,781	4,831	104,612	414,429	338,852
Joint Center for Housing Studies	0	0	0	0	C
Nieman Foundation	15,232	6	15,238	90,946	74,811
Villa I Tatti	44,021	1,034	45,055	169,845	139,712
TOTAL OTHER ACADEMIC DEPARTMENTS	196,316	7,616	203,932	867,137	711,243
SERVICE DEPARTMENTS:					
Harvard University Press	9,253	7,001	16,254	62,900	51,740
University Health Services	3,592	18	3,610	27,246	22,412
University Operating Systems	563	255	818	3,537	2,910
TOTAL SERVICE DEPARTMENTS	13,408	7,274	20,682	93,683	77,062
	,	- ,=- :		75,005	77,002
Central Administration	519,623	22,351	541,974	2,578,637	2,115,101
SUBTOTAL	5,397,012	326,154	5,723,166	21 909 272	17,972,856
SUBTUTAL	3,397,012	320,134	3,723,100	21,898,372	17,372,636
Pledges outstanding	445,244	(1,588)	443,656	443,656	
Interests in perpetual trusts held by others	215,317	29,960	245,277	245,277	
TOTAL	\$ 6,057,573	\$ 354,526	\$ 6,412,099	\$ 22,587,305	17,972,856
	4 -,,	÷ == :,520	¥ •,=,•,,	·,, ,505	,

Year ended	Tune 20 200	(in thousan	ds of dollars)
1 cur criucu	TUNE 30. 2002	i iri iriousurii	us oi uonaisi

Endowment income

Year enaea June 30, 2004 (in thousanas of aouars)			Endowment incom	e	
	Unexpended	Investment			Unexpended
	income	income	Other receipts	Fund income	income
	July 1, 2003	distributed	and transfers	availed of	June 30, 2004
FACULTIES:					
Faculty of Arts and Sciences	\$ 105,036	\$ 347,456	\$ (44,542)	\$ (308,511)	\$ 99,439
Business School	429	54,385	2,956	(57,424)	346
School of Dental Medicine	608	4,791	(13)	(4,493)	893
School of Design	1,647	9,723	1,511	(11,576)	1,305
Divinity School	6,143	13,852	714	(14,074)	6,635
School of Education	2,064	11,610	(52)	(10,974)	2,648
John F. Kennedy School of Government	8,899	22,789	3,609	(23,881)	11,416
Law School	10,244	37,113	(540)	(36,836)	9,981
Medical School	66,090	84,025	3,538	(70,755)	82,898
School of Public Health	33,349	26,010	(5,041)	(19,606)	34,712
Radcliffe Institute for Advanced Study	6,063	10,822	(2,265)	(9,932)	4,688
TOTAL FACULTIES	240,572	622,576	(40,125)	(568,062)	254,961
OTHER ACADEMIC DEPARTMENTS:					
Arnold Arboretum	2,072	7,528	(126)	(7,741)	1,733
Harvard University Art Museums	5,776	14,086	(3,750)	(10,915)	5,197
Joint Center for Housing Studies	0	0	41	0	41
Nieman Foundation	2,165	3,166	16	(3,271)	2,076
Villa I Tatti	2,123	5,797	(344)	(5,110)	2,466
TOTAL OTHER ACADEMIC DEPARTMENTS	12,136	30,577	(4,163)	(27,037)	11,513
SERVICE DEPARTMENTS:					
Harvard University Press	4,593	2,121	5,492	(7,796)	4,410
University Health Services	201	938	(1)	(994)	144
University Operating Systems	153	86	(83)	0	156
TOTAL SERVICE DEPARTMENTS	4,947	3,145	5,408	(8,790)	4,710
	-		<u> </u>	,	•
Central Administration	33,548	87,516	(29,247)	(50,397)	41,420
TOTAL	\$ 291,203	\$ 743,814	\$ (68,127)	\$ (654,286)	\$ 312,604
	,	,	. (,)	. (,)	,

Endowment and income information for the ten schools

The charts and graphs in this section present summaries of endowment and income information for each of the University's ten schools, as well as for the University as a whole.

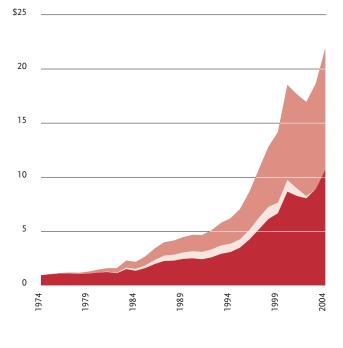
The endowment graphs show the growth since 1974 of the major components of the endowment: 1974 appreciated principal, capitalized income, and gifts and other changes. To allow for comparability

with years prior to fiscal 1995, endowment values exclude pledge balances and interests in perpetual trusts.

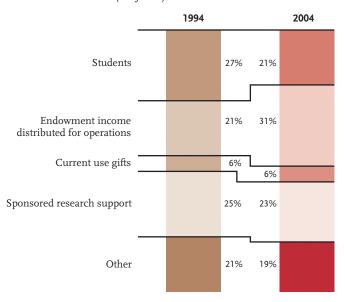
The income charts show the major components of income in fiscal 1994 and 2004. Shown below each of these charts is the ten-year compound growth rate after inflation for total income.

UNIVERSITY





Sources of income (% of total)



Real growth rate of income 1994-2004: 4.5%

and appreciation



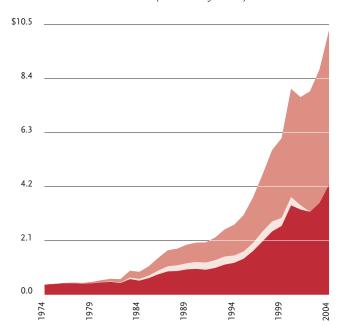




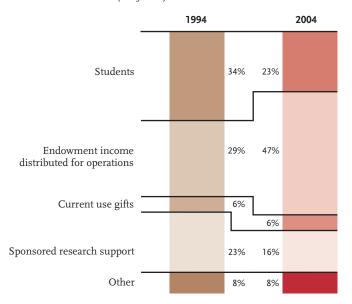
changes

FACULTY OF ARTS AND SCIENCES

ENDOWMENT GROWTH (in billions of dollars)



Sources of income (% of total)



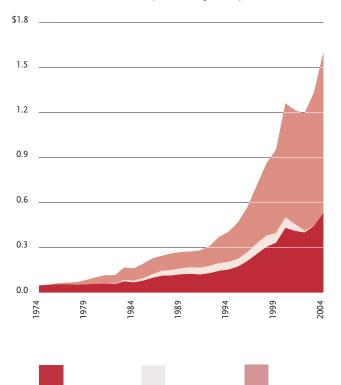
Real growth rate of income 1994-2004: 3.9%

BUSINESS SCHOOL

1974 Principal

and appreciation

ENDOWMENT GROWTH (in billions of dollars)

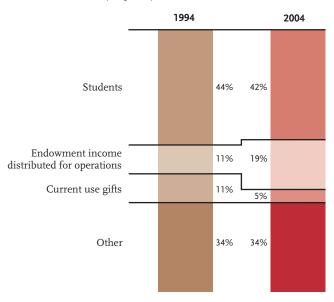


Capitalized income

Gifts and other

changes

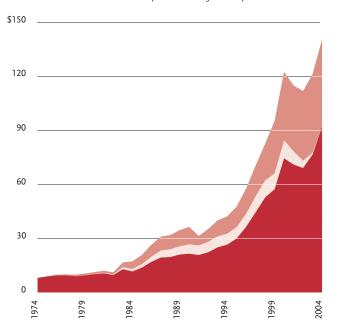
Sources of income (% of total)



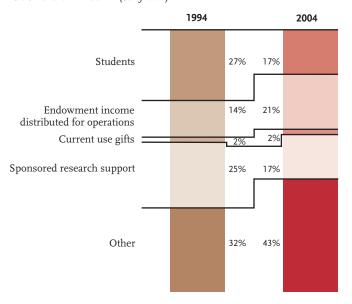
Real growth rate of income 1994–2004: **4.2**%

SCHOOL OF DENTAL MEDICINE





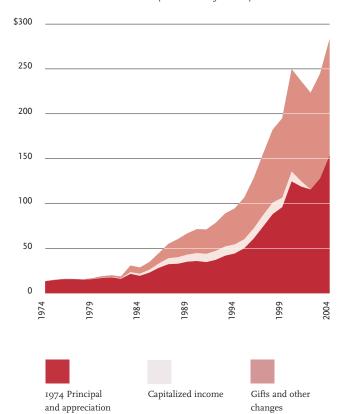
Sources of income (% of total)



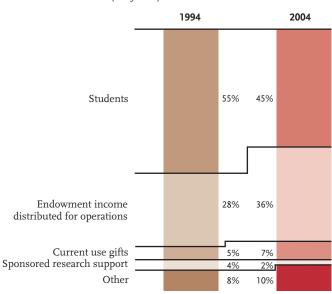
Real growth rate of income 1994-2004: 4.4%

GRADUATE SCHOOL OF DESIGN

ENDOWMENT GROWTH (in millions of dollars)



Sources of income (% of total)



Real growth rate of income 1994-2004: 5.2%

DIVINITY SCHOOL

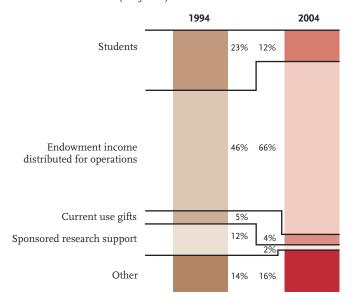


\$450 360 270 180 979 1989 666

1994

2004

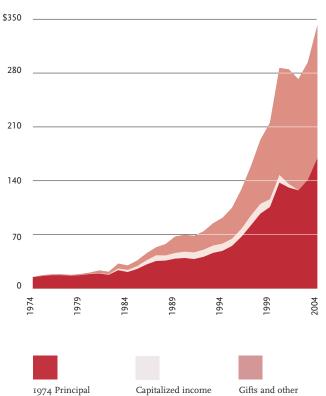
Sources of income (% of total)



Real growth rate of income 1994-2004: 5.0%

GRADUATE SCHOOL OF EDUCATION

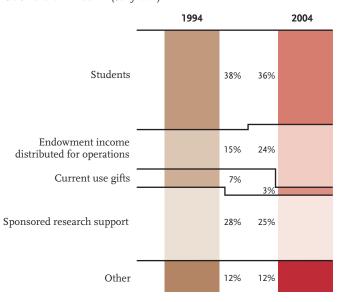
ENDOWMENT GROWTH (in millions of dollars)



changes

and appreciation

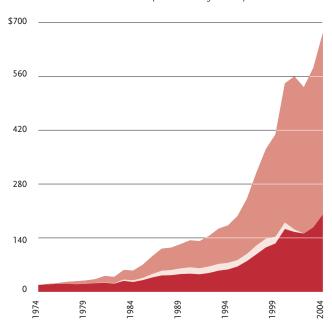
Sources of income (% of total)



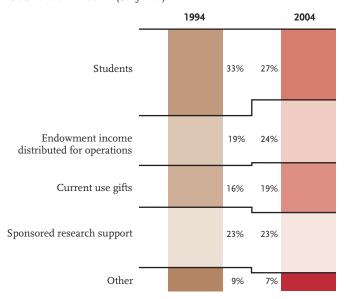
Real growth rate of income 1994-2004: **5.2**%

JOHN F. KENNEDY SCHOOL OF GOVERNMENT

ENDOWMENT GROWTH (in millions of dollars)



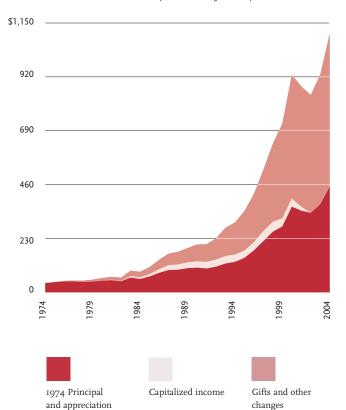
Sources of income (% of total)



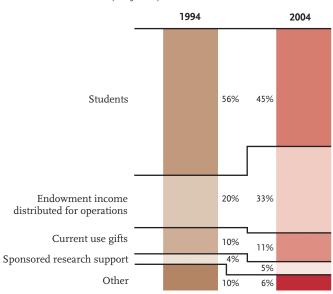
Real growth rate of income 1994-2004: 8.0%

LAW SCHOOL

ENDOWMENT GROWTH (in millions of dollars)



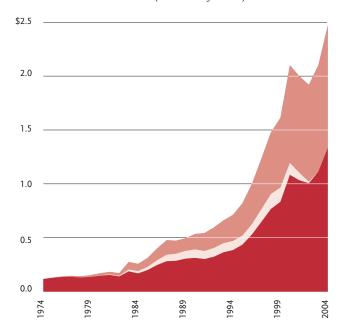
Sources of income (% of total)



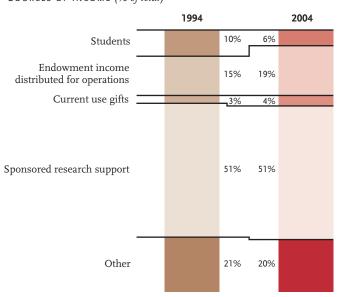
Real growth rate of income 1994-2004: 4.7%

MEDICAL SCHOOL

ENDOWMENT GROWTH (in billions of dollars)



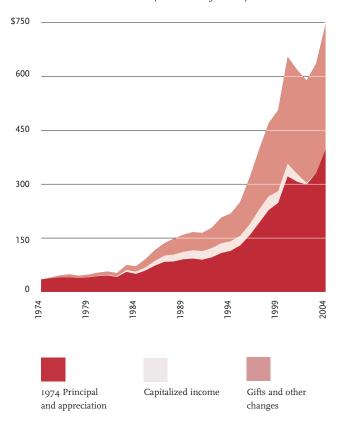
Sources of income (% of total)



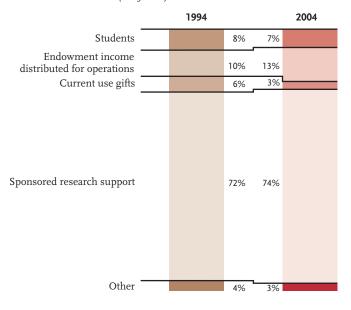
Real growth rate of income 1994-2004: 6.6%

SCHOOL OF PUBLIC HEALTH

ENDOWMENT GROWTH (in millions of dollars)



Sources of income (% of total)



Real growth rate of income 1994–2004: **6.2**%



Harvard continues to expand graduate and affiliate housing in order to alleviate the campus-area housing shortage. In the past year, available accommodations increased by 12%. Renovations at 29 Garden Street included new apartment formats, updated indoor and outdoor gathering spaces, as well as modernized building systems. In Allston, the new graduate housing complex was completed at One Western Avenue. The University's properties in Allston will be an important center for future housing development.

