



Financial Statement Discussion And Analysis

**For the Year Ended
March 31, 2020**

CONSOLIDATED FINANCIAL STATEMENT DISCUSSION AND ANALYSIS YEAR ENDED MARCH 31, 2020

(in millions of dollars)

The consolidated financial statement discussion and analysis should be read in conjunction with the University of Alberta audited financial statements. The university's financial statements have been prepared in accordance with Canadian Public Sector Accounting Standards. For more in-depth discussion and analysis of the university's goals and objectives please refer to the following documents:

For the Public Good, Comprehensive Institutional Plan, Investment Reports.

<https://www.ualberta.ca/reporting>

The consolidated financial statement discussion and analysis provides an overview of the university's:

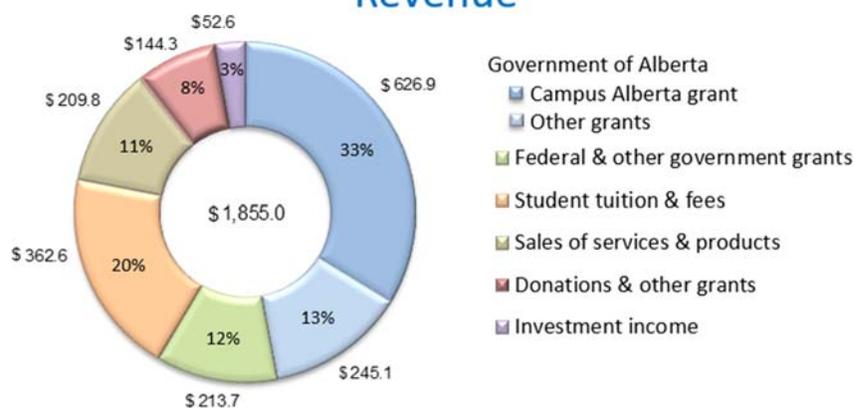
- Summary of Financial Results
- Revenue and Expense
- Capital Acquisitions
- Net Assets and Net Debt
- Areas of Significant Financial Risk

Summary of Financial Results

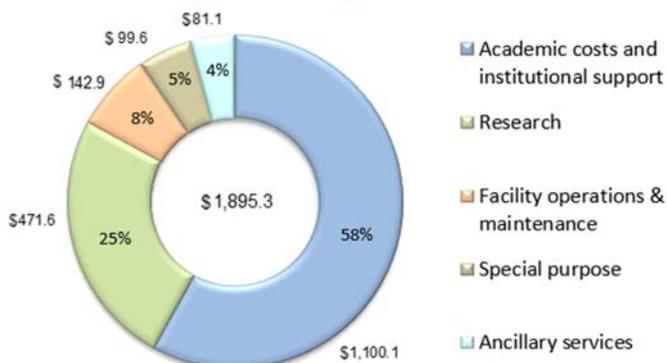
The university ended the year with an annual deficit of \$14.7 million. Of this amount \$25.6 million are donations directed to endowments and endowment capitalized investment income and therefore are not available for spending. The annual operating deficit was \$40.2 million; 2.2% of total revenue (budget annual operating surplus: \$37.7; 1.9% of total revenue). This decrease from the prior year annual operating surplus of \$123.3 was primarily due to a decrease in the Campus Alberta operating grant, lower investment income from realized capital losses and higher pension expense caused by higher plan expenses (current services costs and interest expense).

Net assets of \$1,982.8 million decreased from the prior year (2019: \$2,179.5). The decrease is mainly due to a decrease in the fair value of endowments.

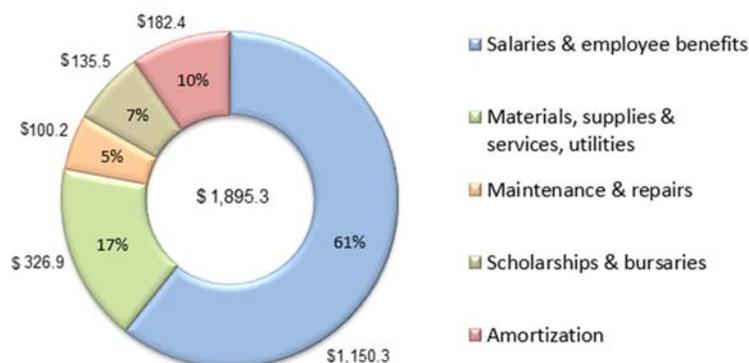
Revenue



Expense by Function



Expense by Object



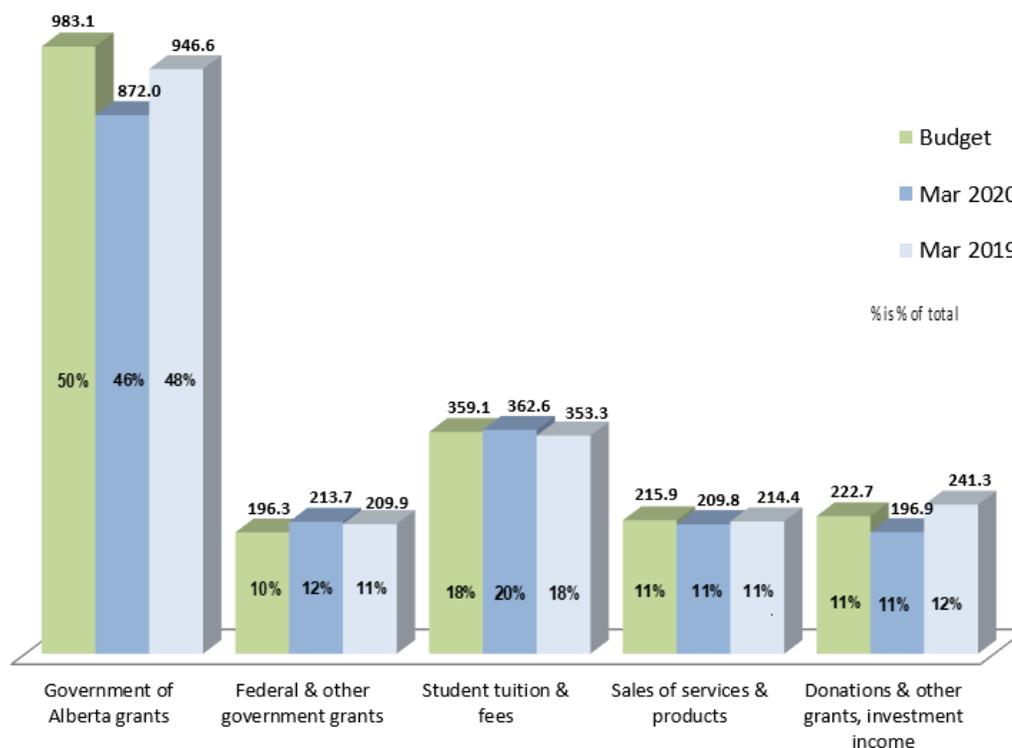
CONSOLIDATED FINANCIAL STATEMENT DISCUSSION AND ANALYSIS

YEAR ENDED MARCH 31, 2020

(in millions of dollars)

Revenue

Total revenue for the year was \$1,855.0 million, a decrease of \$110.5 million over the prior year and \$122.1 million (6.2%) less than budget.



Government of Alberta grants

Government of Alberta grants (GoA) represent the single largest source of funding for university activities at 46% of total revenue. GoA grant revenue of \$872.0 million was \$74.6 million lower than prior year and \$111.1 million lower than budget. The decrease over prior year is primarily due to a 6.9 percent reduction in the Campus Alberta operating grant (\$44.4 million) and a one year cancellation of the Infrastructure Maintenance Program grant (\$34.9 million). These two items are also the primary reasons for the decrease compared to the budget for GoA revenue.

Federal and other government grants

Federal and other government grants primarily support the university's research activities. Federal and other government grants revenue of \$213.7 million was \$3.8 million higher than prior year and \$17.4 million higher than budget. The increase over prior year and the budget is due to increased research funding from the Government of Canada, including funding for research on COVID-19 of \$5.3 million.

Student tuition and fees

Student tuition and fees includes instructional fees, market modifiers, program differential fees, international student fees, and mandatory non-instructional fees. Student tuition and other fees revenue of \$362.6 million was \$9.3 million higher than prior year and \$3.5 million higher than budget. The increase over prior year and the budget is mainly due to higher international student enrolment. In the October 2019 provincial budget the GoA announced that the freeze of domestic tuition fees has been lifted and institutions can raise domestic tuition beginning in fiscal year 2021 by up to 7% per year for the next three years.

Sales of services and products

Sales of services and products revenues are generated by ancillary services and faculties and administrative units to both individuals and external organizations to support university activities. Sales of services and products revenue of \$209.8 million was \$4.6 million lower than prior year and \$6.1 million lower than budget. There was no one individually significant item that has caused the reduction.

Donations and other grants

Donations and other grants support many university activities. Donations and other grants revenue of \$144.3 million was \$2.3 million less than prior year but was \$6.3 million more than budget. There was no one individually significant item that accounted for these variances.

CONSOLIDATED FINANCIAL STATEMENT DISCUSSION AND ANALYSIS

YEAR ENDED MARCH 31, 2020

(in millions of dollars)

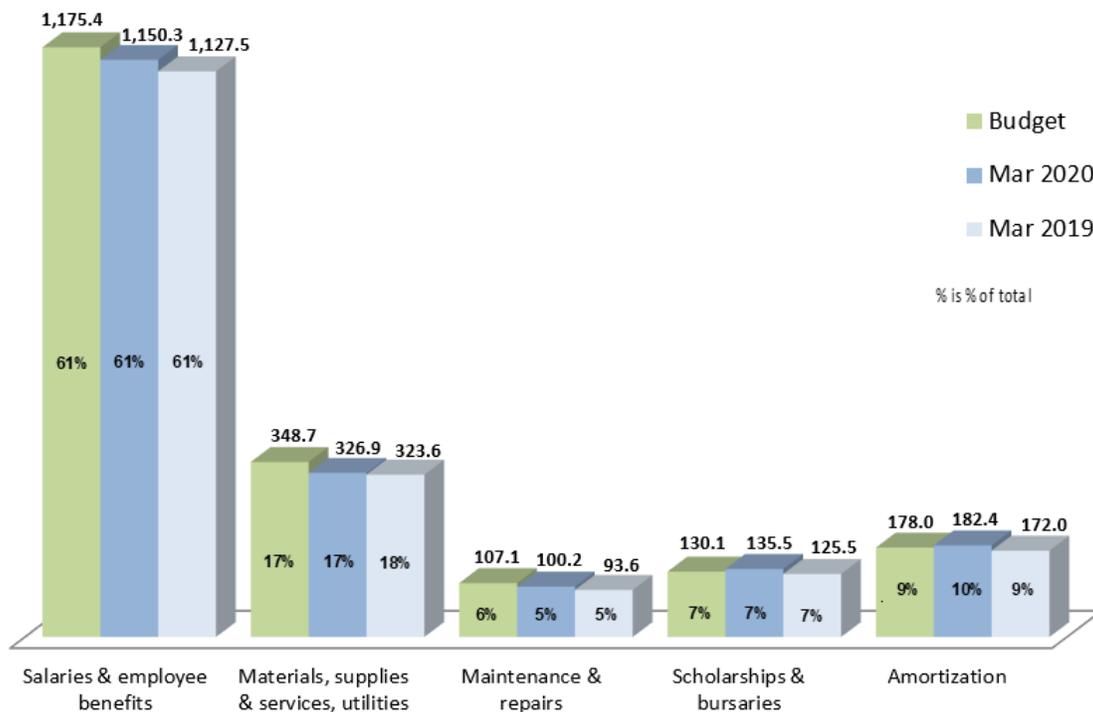
Investment income

Investment income supports many university activities. Investment income revenue of \$52.6 million was \$41.9 million lower than prior year and \$32.1 million lower than budget. The decrease over prior year and the unfavorable to budget was due to the realization of a capital loss on the disposal of two oil and gas indexed funds. Investments fall into two categories, the University Endowment Pool (UEP) and the Non-Endowed Investment Pool (NEIP). The UEP had a loss of 10.2% (2019: 5.9% return) and represents the majority of the university's long-term investment strategy. The NEIP investments which are allocated to short-term, mid-term and long-term investment strategies had a loss of 1.3% (2019: 3.5% return).

Expense

Total expense for the year was \$1,895.3 million, an increase of \$53.1 million over the prior year and \$44.1 million (2.3%) less than budget. Salaries and employee benefits are the single largest expense representing 61% of total expense.

Expense by Object



Salaries and employee benefits

Salaries and employee benefits of \$1,150.3 million was \$22.8 million more than prior year and \$25.1 million less than budget. The increase over prior year is mainly due to higher pension expense caused by higher plan expenses (current services costs and interest expense). The decrease compared to budget is mainly due to lower salary costs across a number of areas.

Materials, supplies and services and utilities

Materials, supplies and services, and utilities of \$326.9 million was \$3.3 million more than prior year and \$21.8 million less than budget. Materials, supplies and services, and utilities was comparable to prior year and less than budget due to units restricting their spending due to GoA funding cuts.

Maintenance and repairs

Maintenance and repairs of \$100.2 million was \$6.6 million more than prior year and \$6.9 million less than budget. The increase over prior year was due to the recognition of an environmental liability for the remediation of the university's snow bank facilities. Maintenance and repairs was less than budget due to units restricting their spending due to GoA funding cuts.

Scholarships and bursaries

Scholarships and bursaries of \$135.5 million was \$10.0 million more than prior year and \$5.4 million more than budget. The increase over prior year and increase over budget was due to funding from endowments and GoA grants for both undergraduate and graduate awards. This expense aligns with the University's goal to attract and support undergraduate and graduate students.

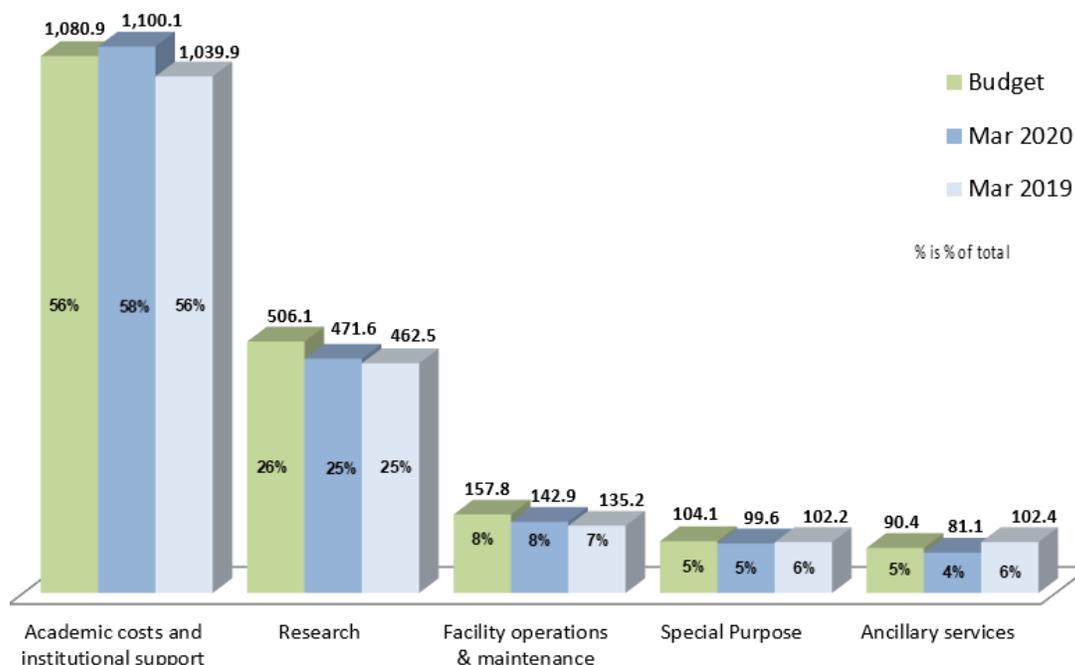
CONSOLIDATED FINANCIAL STATEMENT DISCUSSION AND ANALYSIS YEAR ENDED MARCH 31, 2020

(in millions of dollars)

Amortization

Amortization of \$182.4 million was \$10.4 million more than prior year and \$4.4 million more than budget. The increase over prior year and the increase over budget was due to an adjustment of the useful life of a number of buildings.

Expense by Function



Academic costs and institutional support

Academic costs and institutional support expenses effectively represents the operating activities of the university. A significant component of this category is salary and employee benefit costs. Expenses for this category of \$1,100.1 million was \$60.2 million more than prior year and \$19.2 million more than budget. The increase over prior year was mainly due to higher pension expense and higher internally funded scholarships. The increase over budget was mainly due to higher pension expense caused by higher plan expenses (current services costs and interest expense).

Research

Research expenses are funded by restricted grants and donations along with internal funds designated for research related activities. Research expenses of \$471.6 was \$9.1 million more than prior year and was \$34.5 million less than budget. The increase over prior year has no one individually significant item. The decrease over budget was mainly due to lower expenditures for salaries on research activities.

Facility operations and maintenance

Facility operations and maintenance represents the cost of maintaining university facilities and grounds. Facility operations and maintenance expense of \$142.9 million was \$7.7 million more than prior year and \$14.9 million less than budget. The increase over prior year is due to the recognition of an environmental liability for the remediation of the university's snow bank facilities. The decrease over budget was mainly due to lower maintenance and repairs caused by the one year cancellation of the GoA Infrastructure Maintenance Program grant.

Special purpose

Special purpose expenses are for student awards and bursaries and other programs involving teaching and learning, and community service specifically funded by restricted grants and donations. Special purpose expense of \$99.6 million was \$2.6 million less than prior year and \$4.5 million less than budget. No one individually significant item is accountable for these variances.

Ancillary services

Ancillary services include the university bookstore, parking services, utilities and student residences. Ancillary services expense of \$81.1 million was \$21.3 million less than prior year and was \$9.3 million less than budget. The decrease over prior year is mainly due to lower maintenance costs for residences and lower input costs for the utilities ancillary. The decrease over budget is attributable to the same reasons.

CONSOLIDATED FINANCIAL STATEMENT DISCUSSION AND ANALYSIS YEAR ENDED MARCH 31, 2020

(in millions of dollars)

Capital Acquisitions

The university expended \$157.6 million (2019: \$124.6) on construction and other tangible capital asset acquisitions.

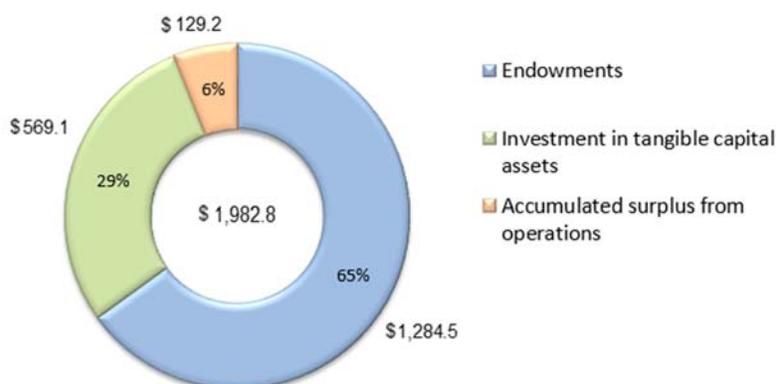
The most significant construction and capital asset acquisitions in 2020 are:

- Lister Centre renewal – a multi-year project to upgrade three residence towers in the Lister Centre complex.
- Dentistry and Pharmacy Renewal and Repurpose - a multi-year project to renovate the Dentistry Pharmacy building.
- Natural Resources Engineering Facility (NREF) Renewal and Renovation project – a multi-year project to repurpose a number of floors of the facility to high tech research laboratory space.

Net Assets and Net Debt

Net assets

The net asset balance is an important indicator of financial health for the university. The net assets measure provides the economic position of the university from all years of operations. The university's net assets include endowments of \$1,284.5 million. Endowments represent contributions from donors that are required to be maintained in perpetuity, as well as capitalized investment income that is also required to be maintained in perpetuity to protect the economic value of the endowment. Endowments are not available for spending. Of the remaining \$698.3 million in net assets, \$569.1 million represents funds invested in tangible capital assets.



	Unrestricted	Internally restricted	Investment in tangible capital assets	Endowments	Total
Net assets, beginning of year	\$ 138.3	\$ 55.1	\$ 553.8	\$ 1,432.3	\$ 2,179.5
Annual operating deficit	(40.2)	-	-	-	(40.2)
Endowments contributions and capitalized income	-	-	-	25.5	25.5
Transfer to endowment	(2.3)	-	-	2.3	-
Tangible capital assets	(15.3)	-	15.3	-	-
Transfer from endowments	30.5	-	-	(30.5)	-
Transfer from internally restricted	15.0	(15.0)	-	-	-
Change in accumulated remeasurement gains	(36.9)	-	-	(145.1)	(182.0)
(Decrease) increase	(49.2)	(15.0)	15.3	(147.8)	(196.7)
Net assets, end of year	\$ 89.1	\$ 40.1	\$ 569.1	\$ 1,284.5	\$ 1,982.8

The decrease in accumulated surplus from operations is mainly due to the annual operating deficit (\$40.2) and to a decrease in the fair value of portfolio investments causing a decrease in the unrealized remeasurement gains (\$36.9). The university also transferred \$2.3 million from accumulated surplus to endowments for capitalization of unrestricted gains and transferred \$30.5 million from endowments to accumulated surplus for unfunded endowment expenditures.

CONSOLIDATED FINANCIAL STATEMENT DISCUSSION AND ANALYSIS YEAR ENDED MARCH 31, 2020

(in millions of dollars)

The university has an internally restricted investment income reserve (\$40.1). The purpose of the reserve is to create a buffer for risk management purposes; that is, to ensure that future financial obligations can be fulfilled in the event of significant investment losses. The reserve target is 17% of the underlying obligations (investment cost), currently \$87 million, which allows for fluctuations in capital and equity markets to the degree experienced during the financial crisis in 2008-09. Once the reserve target is met, allocations will be made to a Strategic Initiatives Fund that will be used to support long-term institutional goals. This year the university withdrew \$15.0 million from the reserve to replace funding for committed capital initiatives that were impacted by the one year cancellation of the Infrastructure Maintenance Program grant.

The increase in investment in tangible capital assets of \$15.3 million consists of additions (\$87.3) and debt repayments (\$14.5), less new financing (\$20.0) and amortization (\$66.5). These additions include construction projects, equipment, furnishings, computer hardware/software and library resources.

The university's endowment spending policy provides for an annual spending allocation (2020: \$53.0; 2019: \$49.0) to support a variety of key initiatives in the areas of academic programs, chairs and professorships, scholarships, bursaries and research. The decrease in endowments of \$147.8 million is due to a decrease in fair value (\$145.1) and a transfer of endowment principal to unrestricted net assets to cover unfunded endowment expenditures (\$30.5), partially offset by new contributions (\$25.5) and a transfer of miscellaneous sales revenue from unrestricted net assets (\$2.3). During the year the university's investment income earned from endowment investments was not sufficient to fund the annual spending allocation of \$53.0 million along with the investment management and administration fees of \$18.8 million. Total investment income was \$13.8 million leaving an unfunded allocation of \$58.0 million. Of this amount, \$30.5 million was spent by the endowment holders and was funded by a transfer from endowments net assets to unrestricted net assets. The remaining \$27.5 million represents unspent allocation per the University Endowment Pool (UEP) Spending policy and is being managed by the university as a future commitment.

Net debt

The university's liquidity needs are met primarily through operating cash flows, working capital balances and capital expansion funding received through grants or long-term debt. Net financial assets (net debt) is a measure of an organization's ability to use its financial assets to cover liabilities and fund future operations.

The net debt (excluding portfolio investments restricted for endowments) indicates that the university has a \$168.6 million deficiency (2019: \$97.8). The deficiency can be attributed to the acquisition of prepaid expenses \$9.3 (2019 - \$8.1), tangible capital assets acquired by debt financing \$288.5 (2019 - \$283.1), partially offset by the accumulated operating surplus \$129.2 (2019 - \$193.4). Net debt has increased mainly due to the acquisition of tangible capital assets.

Areas of Significant Financial Risk

Fiscal Uncertainty

The Campus Alberta grant is the primary source of funding for the university's day-to-day operating activities. Government support is under pressure given the impacts of COVID-19, the drop in oil prices and the province's fiscal outlook. Grants, tuition and other revenue generation initiatives are largely under government control, which puts significant pressure on university finances. The impact to university revenue of a 1% change to the Campus Alberta base operating grant is \$6.2 million and a 1% change to domestic tuition is \$2.0 million.

The COVID-19 pandemic has had a large impact in how the university conducts its operations. The major operational change was the change to on-line delivery of instructional courses to students. It is anticipated that there will be negative impacts to major revenue streams, especially with regards to enrollment (international students) and fundraising. Staffing levels will be impacted as the university and the Non-Academic Staff Association (NASA) agreed to a Letter of Understanding regarding temporary layoffs on April 15, 2020. The full financial impact to the university has yet to be established and won't be known for a period of time. The liquidity position of the university is strong so there are no immediate cash flow concerns.

Unfunded Pension Liability

The university participates with other Alberta post-secondary institutions in the Universities Academic Pension Plan (UAPP) to provide pensions for the university's participating employees. The unfunded deficiency in the UAPP is currently being funded by a combination of employee and employer contributions and the Government of Alberta. The deficiency is required to be eliminated by 2043. At March 31, 2020, based on actuarial assumptions, the university has recorded a UAPP employee future benefit liability of approximately \$116 million.

The impact to the university's share of the unfunded liability of a 1% increase in the inflation rate assumption would be an increase of approximately \$83 million, a 1% increase in the salary escalation assumption would be an increase of approximately \$17 million, while a decrease of 0.25% in the discount rate assumption would lead to an increase of approximately \$47 million.

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Deferred Maintenance

As the largest and oldest post-secondary institution in the province, the university's deferred maintenance obligations continue to increase. As of December 2019, the liability stood at \$309 million and is estimated to increase to approximately \$872 million over the next five years. As part of the fiscal 2020 budget, the government eliminated the Infrastructure Maintenance Program (IMP) grant (\$35 million) which was a main source of funding in dealing with the deferred maintenance issue. This funding was re-established in the fiscal 2021 provincial budget. The university continues to identify and address priority deferred maintenance issues through joint renewal and repurposing projects to maintain the functionality of our building inventory.