

Report of the Executive Vice President and Chief Operating Officer

Leonard W. Sandridge



These are difficult times for the Commonwealth of Virginia, which provide the University with a period of challenge and opportunity. Facing an accumulated budget deficit initially projected to be \$3.8 billion by 2004, our elected officials have had no choice but to make substantial cuts in funding to state agencies, including the University of Virginia. As President Casteen reports at the beginning of this document, we are dealing with reductions in state support of historic proportions.

We budgeted for reductions of \$25 million or 16 percent of our General Fund appropriations in 2002–2003, and \$33 million or nearly 21 percent of our state funding for 2003–2004. And as the state's financial picture grew dimmer, we prepared for more. On October 18, 2002, Governor Warner released plans that called for an additional 12 percent (\$16 million) in budget reductions for the current year and 14 percent (\$17.8 million) for 2003–2004. When added to the first round of cuts, the total reduction in our tax appropriation for the current year equals \$42 million, a 25 percent reduction, and nearly \$52 million for 2003–2004. Since making the most recent reductions, the governor has warned state agencies that more cuts may be necessary, particularly for 2003–2004.

I am often asked whether conditions today are worse than when we last faced severe cuts in the early 1990s. The answer is no. We are better organized to deal with adversity, we have instituted administrative efficiencies, and we have increased

and sustained the support we receive from non-state sources, including generous alumni and friends. If we continue to manage ourselves wisely and reduce our expenditures in ways that do not endanger the quality of our academic and patient-care programs, we will come out of this crisis stronger still.

Protecting Our People

Previous downturns have taught us that, in times like these, we must act quickly and firmly to cut costs. As we entered this fiscal year, we reduced the base budgets of academic departments by 4.35 percent and administrative departments by 4.6 percent. At mid-summer, as the magnitude of the revenue shortfalls in Richmond loomed larger than expected, we imposed a hiring freeze and put discretionary spending on hold.

The reductions in state funding do not affect all parts of the University equally. While the University as a whole now will receive less than 9 percent of its support from the Commonwealth, areas such as the University Library, the School of Architecture, and the College of Arts and Sciences rely on state general funds for a major share of their revenues. We must take this into account as we decide where to marshal our resources. We must also recognize that the University is an enterprise that depends on people for its success. As we reduce our budgets, we remain committed to protecting our investment in our faculty and staff. This is a key step in ensuring that all qualified students have access to a University education that is second to none.

Protecting the Quality of Care

In the University Health System, we must contend with state and federal cuts at a time when the costs of providing medical care are rising sharply, the number of uninsured patients continues to grow, and the need to train competent physicians and nurses is increasing. We have a strong team in place to deal with these difficulties, thanks in large part to steps taken by the Board of Visitors to reshape the Health System's governance and management structure. With Ed Howell as the new vice president and chief executive officer of the Medical Center and Dr. Tim Garson as vice president and dean of the School of Medicine, we have two seasoned

administrators who are working in partnership to meet our educational and patient-care goals.

Promising Sources of Support

It means a great deal to us that the voters of Virginia approved the general obligation bond issue that went before them in November. Providing \$846 million for higher education, including \$68 million for the University, this measure will take advantage of current interest rates and the state's substantial debt capacity to meet the facilities needs of public colleges and universities. For our part, these funds will allow us to move forward on building and infrastructure projects that are critical to our academic programs and that will enhance our ability to work collaboratively across disciplines.

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To help its public institutions offset the loss of state tax dollars, the Commonwealth has rescinded the in-state tuition freeze imposed in the mid-1990s.

Accordingly, one way we are addressing the shortfalls is to make use of our newly regained ability to manage our pricing structure. Increases in tuition replaced about half the money lost to the initial state funding cuts, but even at these new levels, our tuition rates remain substantially below prices charged by universities with which we traditionally compete for students. In fact, our in-state tuition rates remain below what they were in 1993-94. We will use a portion of the tuition increase to help maintain our commitment to meeting 100 percent of our students' demonstrated need for financial aid—a commitment we can live up to thanks in part to scholarships created by our donors. In recent days, the Board of Visitors has authorized a mid-year tuition surcharge to help offset a portion of the additional cuts that have been imposed on the University this year.

One reason we are better able to weather the state's

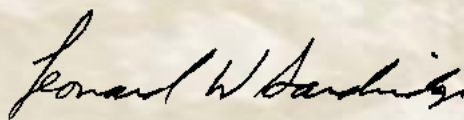
current financial setbacks is increased philanthropic support from alumni, friends, corporations, and foundations. Through the generosity of our donors, we can continue to expand and renovate our facilities, attract and retain distinguished faculty, meet the financial needs of our students, and build world-class programs across the Grounds. In 1999, we determined that we would have to raise \$250 million in philanthropic support annually by fiscal year 2005 to secure our place among the nation's finest institutions, public or private. In 2001-2002, we reached this benchmark, receiving \$255 million in gifts. We will work diligently to secure the continued loyalty of our donors and to assure them that we remain worthy of this extraordinary level of generosity.

Stewarding Our Resources

Our donors can look with confidence at how we manage the resources they invest in the academic enterprise. Excluding funds held by University-related foundations, our endowment stands at \$1.7 billion, a three-fold increase in the last ten years. Over the past three years, a time of broad market declines, we have achieved an annualized return on our endowment of 13.6 percent. This strong performance is the result of extraordinary management by the University of Virginia Investment Management Company (UVIMCO) board. The board and the UVIMCO management team limited our exposure to equities just as the stock market began to give ground in spring 2000.

Through continued innovation, disciplined management, dedicated employees, and diversification of our sources of support, we will come through this tough economic climate as a stronger and more confident institution. As we focus on near-term priorities, we will stay true to our long-term vision and our determination to leave our successors in 2020 a University that stands among the finest and best managed in the world.

Sincerely,



Leonard W. Sandridge
Executive Vice President
and Chief Operating Officer