UNIVERSITY OF CALGARY

Management Discussion & Analysis

For the Year Ended
March 31, 2016

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Management Discussion and Analysis Overview

This Management Discussion and Analysis ("MD&A") should be read in conjunction with the University of Calgary's ("the University") consolidated financial statements and accompanying notes for the year ended March 31, 2016. The MD&A and consolidated financial statements are reviewed and approved by the University's Board of Governors on the recommendation of the University's Audit Committee. The University's consolidated financial statements have been prepared in accordance with Canadian Public Sector Accounting Standards ("PSAS") and are expressed in Canadian dollars.

The MD&A is an overview of the University's financial results for the fiscal year ending March 31, 2016 and offers analysis of the University's:

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Operating Environment

The University of Calgary is Canada's leading next-generation university: a dynamic and youthful institution that embraces change and opportunity with a can-do attitude in Canada's most enterprising city. As evidence, in the 2015 QS World University Rankings of universities established in the last 50 years, the University of Calgary was ranked first in Canada, first in North America, and twelfth in the world.

In large part, this success is driven by the University of Calgary community's commitment to the Eyes High strategic vision:

> *"The University of Calgary will be a global intellectual hub located in Canada's most enterprising city. In this spirited high-quality learning environment, students will thrive in programs made rich by research and hands-on experiences. By our 50th anniversary in 2016, we will be one of Canada's top 5 research universities, fully engaging the communities we both serve and lead."*

We are realizing our Eyes High vision by focusing on three foundational commitments: 1) sharpening our focus on research and scholarship; 2) enriching the quality and breadth of learning, and 3) fully integrating the university with the community.

The development of our institutional Academic Plan and Research Plan in 2011-12 resulted in seven academic and three research priorities that have provided a roadmap for the achievement of our Eyes High vision. The vision and priorities established at the University of Calgary are designed to show our community the benefits and rewards of integrating teaching, learning and research in an environment where discovery, creativity, and innovation are central to the mission. Our priorities have guided human, financial, and capital resource allocations for the foreseeable future. This trio of documents (Eyes High strategy, Academic Plan, Research Plan), produced through broad consultation processes on our campus, has resulted in strong strategic decision-making that has moved the institution forward, while at the same time placed focus on prudent fiscal management.

Changes in Financial Presentation

During the fiscal year ended March 31, 2016, the University adopted the presentation of the Net Financial Asset indicator in the Consolidated Statement of Financial Position. In adopting this presentation, the University, along with other Post-secondary Institutions in Alberta, received direction from the Controller of the Province of Alberta relating to the classification and presentation of portfolio investments restricted for endowments along with the recording of endowment contributions and related investment income capitalized on an annual basis into the endowed balance. The impact of this direction results in:

1. Presentation of Net Financial Assets on the Statement of Financial Position that includes portfolio investments restricted for endowments; and,
2. The inclusion of endowment contributions and related capitalized endowment investment income in the Statement of Operations after annual surplus from operations. These amounts were not previously recorded in the Statement of Operations, but as direct increases into net assets.

The impact of presenting portfolio investments restricted for endowments is discussed in more detail in the following Net Asset and Net Financial Asset section.

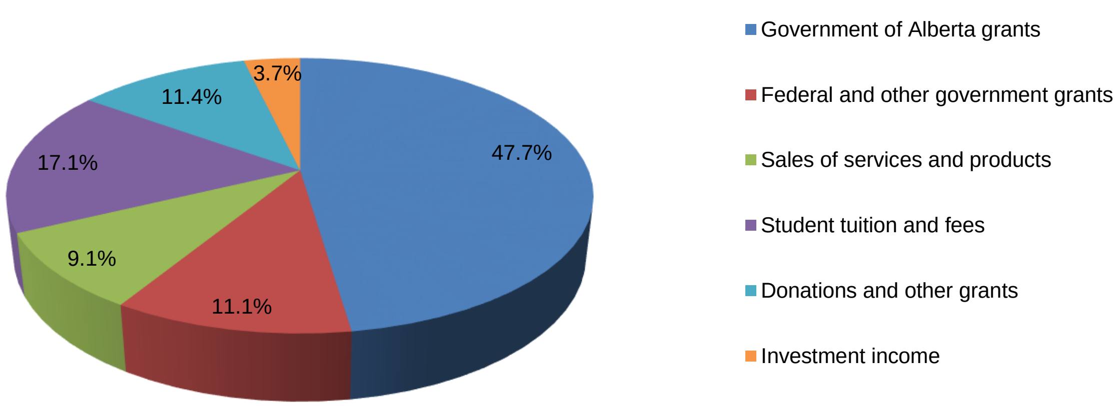
Financial Results

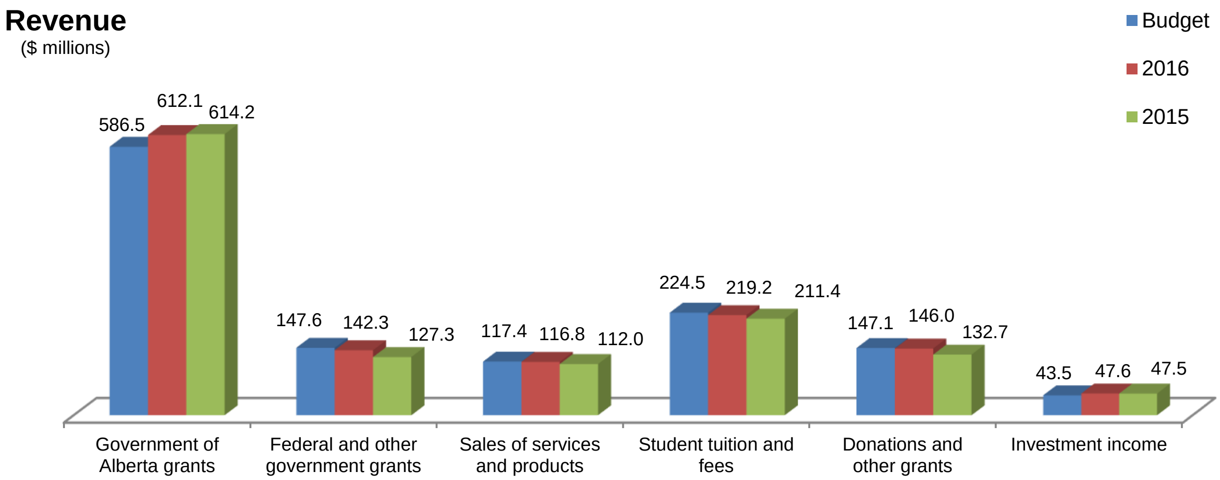
For the year ended March 31, 2016, the University's revenues exceeded expenses by $11.3 million. This annual operating surplus decreased from the $53.9 million surplus in 2015 mainly due to increased spending on strategic research, academic and support initiatives combined with inflationary pressures exceeding operating funding increases.

The $11.3 million in annual operating surplus combined with $31.1 million in additions to endowments and $57.7 million decrease in remeasurement gains as a result of a decrease in unrealized gains on working capital and endowment investments, resulted in total net assets of $1,381.4 million for the year ended March 31, 2016. This represents a decrease of $15.4 million from March 31, 2015.

Revenue

Total revenues for the year ended March 31, 2016, were $1,284.1 million, an increase of $38.9 million (3.1%) over the prior year and $17.4 million (1.4%) over budget. Revenue from the Government of Alberta represents the University's single largest source of income, at 47.7% of total University revenue in 2016, and plays a key role in the ability to fund University activities. Major components of revenue are as follows:





Government of Alberta grants

Government of Alberta grant revenue of $612.1 million was $25.6 million higher than budgeted primarily due to additional funding received from the Government of Alberta to compensate for the provincial tuition freeze, market modifier replacement funding, recovery of past funding decreases, and enrollment growth funding. This additional operating funding from the Government of Alberta was offset by reductions in other funding relating to research, donor-matching grants from the province, and grants from Alberta Health and Wellness and Alberta Health Services resulting in a $2.1 million net drop in revenues compared to 2015.

Federal and other government grants

Although grant revenue from federal and other government sources of $142.3 million was $5.3 million less than budgeted, revenues increased over the prior year by $15.0 million. The increase from the prior year is primarily due to $7.3 million increase in previously deferred contribution revenues recognized from research and special purpose activities, $4.0 million from a one-time federal GST recovery, and $2.9 million increased funding related to the Nursing program in Qatar.

Sales of services and products

In providing services to the community, students, and staff, the University continues to develop alternative sources of revenue to fund operations and strategic initiatives. Sales of services and products revenue of $116.8 million was $4.8 million higher than the prior year and consistent with budgeted expectations.

Student tuition and fees

Student tuition and fees represent another important component of the University's funding of educational goals. For the year ended March 31, 2016, student tuition and fees of $219.2 million were $5.3 million below budget primarily due to the Government of Alberta's freeze of tuition rate increases and market modifier revenues. Revenue continued to increase from the prior year by $7.8 million as a result of increased enrolment, international students, and summer camp program fees.

Donations and other grants

While donation and other grant revenues of $146.0 million were $1.1 million less than budgeted, donation and other grant revenues exceeded prior year amounts by $13.3 million. The increase from prior year is primarily due to $8.4 million increased recognition of revenue from research and special purpose activities, as well as $5.1 million of income through the University's partnership with Tri-University Meson Facility which operates a subatomic physics research facility with eleven other Universities.

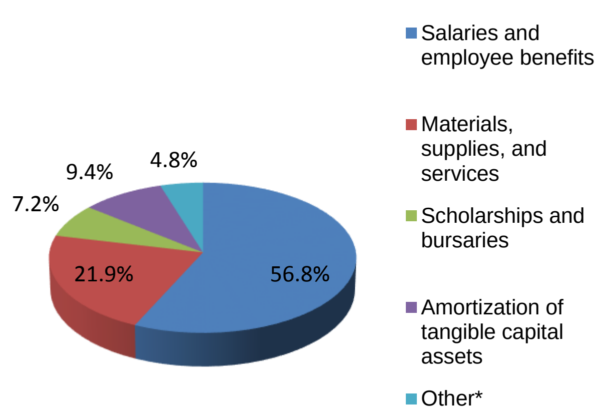
Investment income – Including Investment loss in government business enterprises
While Investment income of $47.6 million including investment loss from government business enterprises ("GBE's") remained relatively unchanged from the prior year, investment income was $4.1 million higher than budgeted primarily as a result of higher than expected endowment income from endowment spending, partially offset by higher than budgeted losses on investments in West Campus Development Corporation ("WCDC") and University Technologies Group. Current year GBE losses are mainly driven by continued development costs incurred by WCDC which will be recovered from revenues once WCDC lands have been developed and commercialized for use.

Expense

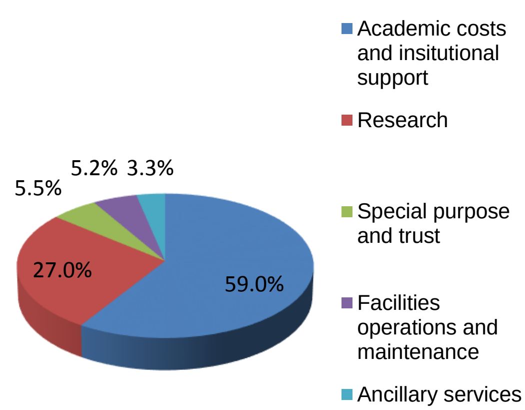
For the year ended March 31, 2016, the University recorded $1,272.8 million in expenses representing an increase of $81.5 million (6.8%) over the prior year and $6.2 million (0.5%) higher than budget. Salaries and benefits are the largest expenditure component at the University, representing 56.8% of the University's expenses. Compensation expense continues to be a challenge when making budgeting decisions, especially during times where increases in operating grants do not adequately cover the increase in salaries that are often governed by union and faculty agreements.

Academic costs and institutional support represents the single largest function at the University, with this function representing 59.0% of the University's expenses. This includes instruction, non-research academic and administrative support activities, effectively representing the operating activities of the University.

Expense by Object

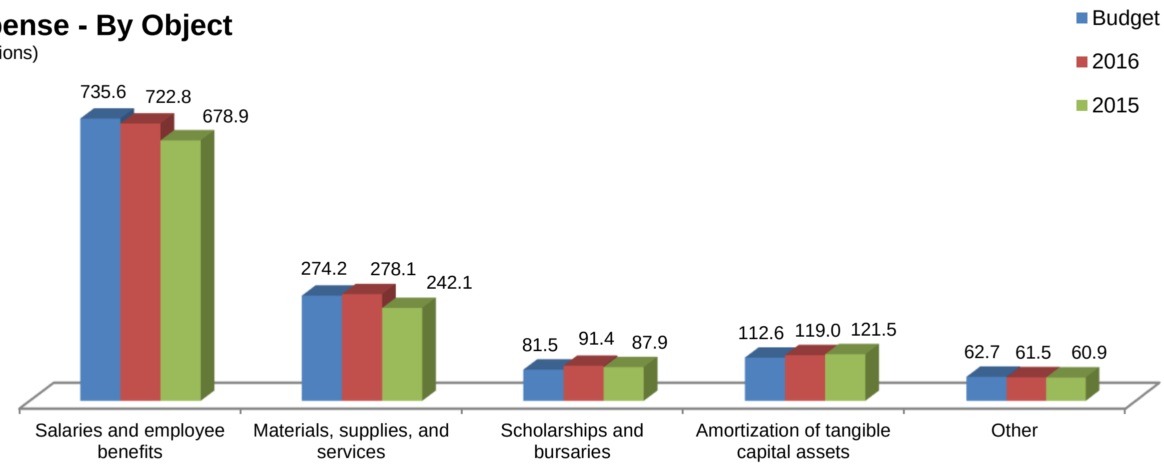


Expense by Function



*Other expenses include: Utilities; Maintenance and repairs; and Cost of goods sold.

Expense - By Object
($ millions)



Salaries and employee benefits

Of the total compensation expense of $722.8 million, salaries comprise $606.3 million and employee benefits comprise $116.5 million. Salaries and employee benefits have increased by $43.9 million over the prior year but are $12.9 million less than budget. The increase from the prior year includes higher salaries expense of $13.6 million related to increase in support staff costs resulting from negotiated union agreement increases, new positions, and filled vacancies. Additional increases of $26.4 million are related to the hiring of new Postdoctoral Scholars, accelerated hiring of academic positions, negotiated academic salary increases, as well as new positions and filled vacancies related to Management and Professional staff. Increases in benefits are related to increased salaries, new positions, and filled vacancies.

Materials, supplies and services

Materials, supplies and services of $278.1 million represents the second largest expense component of the University with current year costs being $36.1 million higher than the prior year and $3.9 million higher than budget. The current year increase is primarily a result of increased spending of prior year internally restricted surplus balances on new strategic research and operating initiatives such as the classroom and facilities upgrades, Network Renewal Program and upgrade of campus wireless.

Scholarships and bursaries

Scholarships and bursaries of $91.4 million were $3.5 million higher than 2015 and $10.0 million above budget. These higher expenses are in line with University goals for attracting and supporting students, especially graduate scholarships related to Eyes High doctoral recruitment and the University's MBA program.

Amortization of tangible capital assets

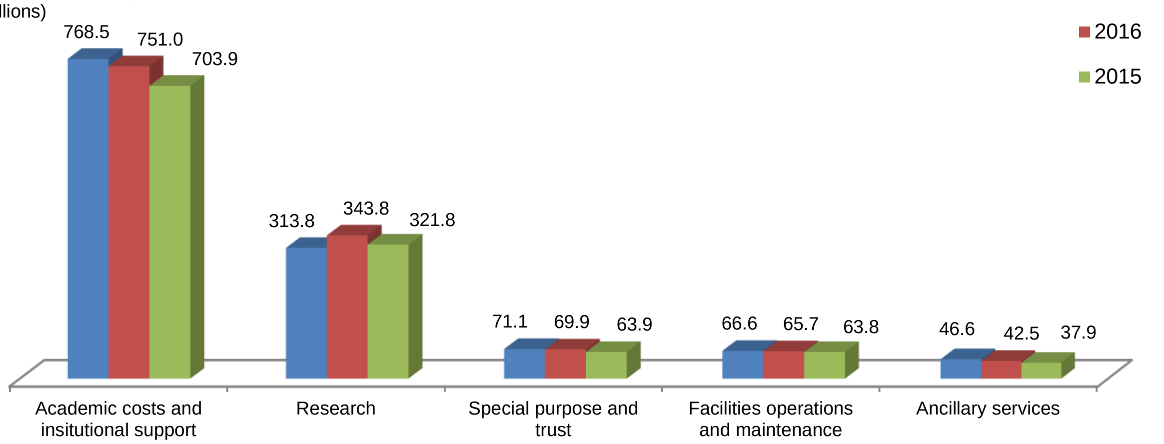
Amortization of tangible capital assets expense of $119.0 million decreased by $2.5 million from the prior year and is $6.4 million over budget. During the year, capitalization of new projects including two residence buildings, Education tower completions, and various IT projects resulted in increased amortization expense of $4.9 million. One-time amortization charges that occurred in the prior year relating to the decommissioning of older residences, in preparation for new residences, resulted in year over year decreases.

Other

Other expenses totaling $61.5 million were relatively consistent with the prior year amounts.

Expense - By Function

($ millions)



Academic costs and institutional support

While Academic costs and institutional support expense of $751.0 million has increased $47.1 million over the prior year, the total academic costs and institutional support expense was $17.6 million below budget. The increase from prior year is primarily due to additional spending on strategic initiatives relating to the hiring of new Postdoctoral Scholars, accelerated hiring of academic positions, services supporting researchers in commercializing research, improvements to the University's IT network and wireless accessibility, upgrading of institutional budgeting systems and processes, and improvements to classrooms and study spaces. The budgetary savings of $17.6 million were experienced as a result of unspent budgeted amounts and higher than budgeted vacant employee positions during the year.

Research; and Special purpose and trust

Research costs of $343.8 million were $22.0 million higher than prior year and $30.0 million higher than budget. This increase is due to the University's strategic focus on directing resources and activities towards research initiatives in 2016 in support of *Eyes High* goals for increasing research across many faculties of the University. Special purpose and trust costs of $69.9 million were $6.0 million higher than prior year and comparable to budgeted amounts. The increase from the prior year is primarily as a result of increased scholarship payments.

Facilities operations and maintenance; and Ancillary services

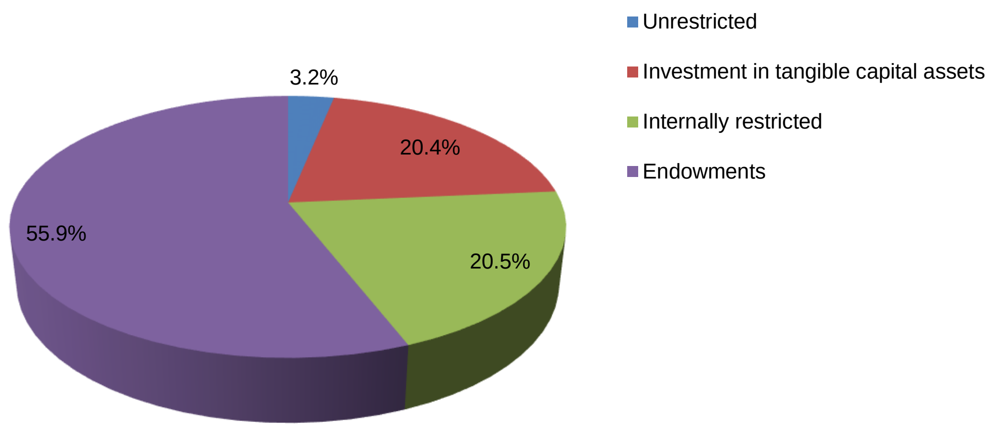
Facilities operations and maintenance costs of $65.7 million were comparable to budget and $1.9 million higher than prior year primarily as a result of increased salaries and benefit costs. Ancillary expenditures of $42.5 million were $4.5 million higher than prior year due to increases in salary and benefit costs offset by savings on utility costs and decrease in the cost of consumables.

UNIVERSITY OF CALGARY

Net Assets and Net Financial Assets

Net Assets

The University's net asset balance is an important indicator of financial health for the University. Prudent financial planning and decision making combined with increased endowment contributions from donors have all contributed to the University's success. Endowments continue to represent the largest component of Net Assets. Endowments must be maintained in perpetuity with investment income earned funding specific research, scholarship and donor supported initiatives on campus. Of the $1,381.4 million in net assets, $283.3 million are formally restricted by the University's Board of Governors for spending on strategic initiatives in support of student learning, research, capital projects, and community service. After Board of Governors restrictions, $43.9 million has been maintained for unforeseen events and future strategic decision making. Remaining net asset balances represent funds that have either been already spent on investments in capital assets, or are required to maintained in perpetuity as endowments and are not available for spend. Net assets at March 31, 2016 are comprised of the following balances and related summarized transactions:



Net Assets ($ thousands)	Unrestricted	Investment in Capital Assets	Internally Restricted	Endowments	Total
Balance at March 31, 2015	72,192	237,184	296,786	790,568	1,396,730
Annual operating surplus	11,250	-	-	-	11,250
Transfer to internally restricted net of expenditures	(40,261)	-	40,261	-	-
Endowment contributions and capitalized income	-	-	-	31,118	31,118
Net capital asset acquisition, amortization and debt financing	9,107	44,637	(53,744)	-	-
Change in accumulated remeasurement gains	(8,384)	-	-	(49,349)	(57,733)
Balance at March 31, 2016	43,904	281,821	283,303	772,337	1,381,365

Net Financial Assets

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. The Net Financial Asset indicator is intended to identify the availability of net financial resources an organization has to fund future operations after considering liabilities owed to third parties. The University presents the Net Financial Asset indicator in a manner as directed by the Controller of the Province of Alberta. The presentation includes $772.3 million of investments that are restricted for endowments. Endowment restricted investments must be maintained in perpetuity and are therefore not available to pay for University liabilities, nor can the University use the endowment portfolio investments to pay for future operating or capital purchases. As a result, University management monitors an adjusted Net Financial Asset indicator, which represents a clearer picture of Net Financial Assets available for future spending.

Adjusted Net Financial Assets ($ thousands)		2016	2015
Net Financial Assets (as presented in Statement of Financial Position)	$	823,702	898,493
Less portfolio investments – restricted for endowments		(772,337)	(790,568)
Adjusted Net Financial Assets	$	51,365	107,925

During the fiscal year, the Adjusted Net Financial Asset balance decreased by $56.6 million primarily as a result of cash flow timing related to capital expansion being partially offset by the $11.3 million annual operating surplus. The University continues to have sufficient positive Adjusted Net Financial Assets, demonstrating financial strength and commitment to managing the University's financial position.

Capital Expansion and Renewal

Capital expansion and renewal projects remain a critical priority for the University, contributing not only to the student learning experience and the quality of research activity, but also positively to the Calgary economy. In 2016, the University expended $204.1 million (2015 - $208.3 million) on construction and other capital asset acquisitions. This capital activity represents the continuation of the University's multi-year capital building program through construction of new buildings as well as redevelopment, renovation, and numerous instructional facility upgrade projects.

The following represents progress on the top six major construction projects on campus:

Major Capital Project Costs ($ thousands)		2016		Project to Date		Total Budget
Schulich School of Engineering Expansion	$	63,422	$	119,714	$	172,700
Crowsnest Hall Graduate Residence		8,113		51,283		51,900
The Taylor Institute for Teaching and Learning		15,709		36,370		40,000
Aurora Hall undergraduate Residence		7,362		36,159		35,600
Mobility and Joint Health		6,276		11,915		14,015
Education Tower Restack Plan		7,607		14,127		15,310

Schulich School of Engineering Expansion and Renovation – During 2013-14, construction began on this $172.7 million initiative to construct an 18,300 square meter expansion to the Canadian Natural Resources Limited Engineering Complex, along with major renovations to 15,000 square meters of the existing building footprint. The building expansion includes high intensity research labs and support spaces, undergraduate engineering teaching labs, group workrooms, low intensity research facilities, and classroom and theatre spaces and is expected to be completed in the fall of 2016.

Crowsnest Hall Graduate Residence; Aurora Hall Undergraduate Residence – These projects are part of the University's goal to increase on-campus student accommodation to 15.0% of undergraduate full-load enrolment by 2022. The projects are complete and the residences were occupied in August 2015. Crowsnest Hall Graduate Residence is a 390 bed facility for graduate and professional faculty students while Aurora Hall Undergraduate Residence is a 268 bed undergraduate residential building.

Taylor Institute for Teaching and Learning – The University started construction in 2013-14 to transform the former Nickle Arts Museum site into the $40.0 million Taylor Institute for Teaching and Learning. The Taylor Institute for Teaching and Learning is a leading-edge facility and signature building on the University main campus. Conceived with the specific objective of maximizing natural light and weaving the most advanced learning technology throughout the space, the new facility serves as an ideal platform to promote advances in teaching and learning. The structure breaks free of the classroom mold by incorporating the latest advances in learning spaces. It includes a simulation centre for teaching research and professional development, multi-purpose facilities to promote collaboration and the sharing of best practices for related research and institutional support teams. The University and community celebrated the opening of the Taylor Institute for Teaching and Learning in early spring of 2016.

Mobility and Joint Health – This project includes the renovation of approximately 400 square metres of existing space to create a clinical state of the art diagnostic imaging facility dedicated to advancing bone and joint research. The construction phase is complete and final equipment deliveries to occur in July 2016.

Education Tower Restack Plan – Given the age and condition of the University's Education Tower, extensive renovations were completed for the majority of the floors of this fourteen floor structure to create collaborative academic and research environments. Renovations were completed in spring of 2016.

Areas of Significant Financial Risk

Deferred Maintenance

The University directs significant resources to ensure that University buildings are updated with relevant technology, operate efficiently, and meet contemporary standards. The University has an outstanding deferred maintenance balance of nearly $487.3 million (2015 - $481.0 million). Infrastructure Maintenance Program ("IMP") funding from the province slightly increased to $11.0 million (2015 - $9.9 million) as compared to the prior year. While the University recognizes that there are budgetary constraints facing the Government of Alberta, lack of increases to IMP funding significantly impacts the University's ability to proactively manage and address its deferred maintenance risk.

Unfunded Pension Liability

The University participates with other Alberta post-secondary institutions in the Universities Academic Pension Plan ("UAPP") to provide pensions for participating faculty and staff. The extrapolated actuarial deficiency for the pension plan at March 31, 2016 was $868.7 million (2015 - $1,129.9 million) of which the University's portion is $108.9 million (2015 - $147.3 million). This unfunded deficiency in the UAPP is currently being funded by the Government of Alberta, employee and employer contributions in order to eliminate the unfunded deficiency by 2043.

Other employees at the University participate in the Public Sector Pension Plan ("PSPP"). Given the large number of employers participating in PSPP and the resultant complexities in calculating accurate information relating to each participant's share of any unfunded liability, employers are unable to isolate their portion of the total unfunded deficiency at December 31, 2015 of $133.2 million (2014 - $803.3 million). Although this unfunded liability has decreased from the prior year, the continued unfunded balance represents a risk that both employer and employee contribution rates could increase in the future.

Budgetary Pressure

Although the University has a balanced budget for 2016-17, it is presenting deficit forecasts for 2017-18 and 2018-19. The University is facing a number of risk factors, most notably funding uncertainty related to provincial operating funding. Without increases in provincial funding to offset inflationary costs, and combined with legislatively mandated ceilings on tuition increases, the University will continue to explore and implement process efficiencies and revenue generating opportunities. The University will continue to work in partnership with the government, to help bridge the gap between increasing costs and stagnant revenues. While prudent financial management has resulted in balanced results, budgetary pressures remain a significant strategic risk for the University of Calgary.