



**CAPITOL  
SECURITIES**  
MANAGEMENT, INC.

**EQUITY  
RESEARCH**

**December 4, 2014**

**CURRENT PRICE:** \$10.86  
**RATING:** HOLD  
**PRICE TARGET:** N/A  
**CURRENT YIELD:** N/A

**EPS Estimates - Non-GAAP**

	DEC 13A	DEC 14E
1Q	\$0.44	(\$0.10)A
2Q	\$0.22	\$0.28A
3Q	\$0.18	\$0.14A
4Q	(\$0.12)	\$0.17
	<b>\$0.74</b>	<b>\$0.49</b>

**Trading Data**

52-WEEK PRICE RANGE: **\$20.15 - \$10.56**  
SHARES OUTSTANDING: **46.5(M)**  
MARKET CAP: **\$505(M)**  
AVG. DAILY TRADING VOLUME: **0.14(M)**  
S&P 500: **2,071**

**Valuation Data**

BOOK VALUE: **\$7.97**  
PRICE TO BOOK: **1.36x**  
DIVIDEND: **N/A**

**BRIDGEPOINT EDUCATION, INC (NYSE: BPI)**

*Approaching the Moment of Truth*

**Highlights**

- 3Q14 earnings of \$0.14/share vs. \$0.25/share during 3Q13
- Sequential quarterly improvement in new admissions
- Lower costs unable to offset lower revenues
- Potential turnaround in 2015
- Maintain HOLD rating

**Investment Thesis**

BPI is in the for-profit education sector. The company primarily offers online classes for students, working professionals, and military personnel lacking time to attend regular college/university campuses. This stock recently declined due to regulatory issues and falling revenues. Given the potential for an earnings recovery, and small levels of debt, this stock may be attractive to speculative growth investors, given its low valuation. However, in light of recent for-profit industry concerns, investors should wait for evidence of an earnings turnaround.

**Company Summary**

Bridgepoint Education, Inc. (BPI-\$10.86), headquartered in the San Diego CA metropolitan area, is a for-profit education provider. The company offers postsecondary education services both online and through 2 college campuses. BPI's regionally accredited academic institutions provide associates, bachelors, masters, and doctoral programs in business, education, health sciences, psychology, and social sciences. These are provided through approximately 1,145 courses with 73 degree programs and 107 specializations. As of 12/31/13, BPI had a total of 63,624 students enrolled both online and through its campuses at Clinton, IA (Ashford University) and Colorado Springs, CO (University of the Rockies). 1,800-1,900 students attend BPI's Ashford University and University of the Rockies. BPI has approximately 4,500 full time and adjunct faculty members and 2,400 non-faculty staff in university services/administration, academic advising/support, enrollment services, financial aid, information technology, human resources, corporate accounting/finance, and other administrative duties.

*For Important Disclosure information regarding the Firm's rating system, valuation methods and potential conflicts of interest, please refer to the last two pages of this report.*

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The company was started in 1999 by the Warburg Pincus Private Equity VIII, L.P. In 2004, current president Andrew Clark, and other current members of the executive management team joined BPI. The company went public in 2009. In 2005 BPI purchased the Franciscan University of the Prairies and renamed it Ashford University. The Colorado School of Professional Psychology was bought in 2007 and renamed the University of the Rockies

## Recent Earnings

BPI reported fully diluted 3Q14 earnings of \$0.14/share vs. \$0.25/share during 3Q13. The decline was due to lower student admissions, as the for-profit industry adjusts to new operating guidelines created by regulators. When comparing the two quarters, revenues decreased 11% to \$162.7 million, from \$182.8 million, as total student enrollment fell to 59,552 from 68,566. New student enrollments rose mid-single digits during 3Q14 vs. 3Q13, and slightly exceeded the rate of new enrollments during 2Q14.

Instructional cost/service expense decreased 4.6% to \$79.7 million, from \$83.6 million, due to lower instructional expense/academic support labor costs. This was partly offset by higher bad debt expense, totaling \$9 million during 3Q14. Admissions advisory/marketing expense declined 12% to \$56.8 million, from \$64.5 million, attributable to lower tv advertising expense and lower compensation resulting from fewer admissions personnel. These were partially offset by an increase in direct advertising channels expense. General/administrative expense rose 2.4% to \$15.6 million, from \$15.2 million, because of higher administrative compensation, other administration expenses, corporate support services, and IT costs.

Operating income decreased 45.8% to \$10.6 million, from \$19.5 million, as the 6.8% decline in total costs/expenses were unable to offset the 11% decrease in operating revenues. Net income fell to \$6.3 million, from \$14.2 million. The effective tax rate for 3Q14 was 46.1%, vs. 30% during 3Q13, due to the effect of a lower pre-tax income on relatively constant non-deductible expenses and a \$1.9 million tax reserve release resulting from the expiration of a statute of limitations in 3Q13. Fully diluted EPS calculations were based on 46.5 million outstanding shares compared to 56.4 million shares outstanding

### EARNINGS CONFERENCE CALL:

During the 3Q14 conference call management discussed several topics. The company noted student enrollments rose mid-single digits during the just completed quarter (vs. 2Q14) and expects the same during 4Q14. Also, its Ashford Forbes School of Business saw new student enrollments rise by double digits. BPI stated it believes Ashford is positioned favorably for future student growth. Expectations are new student enrollments will be positive throughout next year with total enrollments turning higher during 2H15. Management anticipates giving further clarity on BPI's turnaround progress during the 4Q14 earnings conference call.

Management noted BPI has experienced recent improvement in its student retention rates. The company recently began reporting 12 month retention rates for active students every quarter. This number is compared to the prior



year's 12 month period ending in a comparable quarter. BPI reported its retention rate for the 12 month period ending on the conclusion of 3Q14 rose to 65.8% from 60.8% when compared to the same period ending on 3Q13. Regarding regulatory guidelines, management said it was too soon to comment on the impact of the new "Gainful Employment" rules impact on its student enrollment and stated new "regs" could be complicated and expensive.

## Our Thoughts

Losing two-thirds of its stock value, since 2011, management has taken actions to adjust to changing operating fundamentals and increased regulations in the for-profit education industry. The question now being asked by Wall Street is,... "Has BPI positioned itself for an earnings turnaround?" Management believes it has by cutting costs, reducing staff, and shifting its business strategy. Based on increased student admissions, higher retention rates, and lower operating costs, BPI feels 2014 could be the nadir for its earnings decline and 2015 could mark the resumption of earnings growth. If so, this stock offers substantial appreciation potential. We expect further clarity on BPI's turnaround progress, during the 4Q14 earnings conference call scheduled for February 2015. Thus, the upcoming conference call could mark "the moment of truth" for BPI in terms of whether a turnaround is materializing, or not. BPI has very little debt and approximately \$4.06/share in cash on its balance sheet. We continue to rate these shares a HOLD.

## Risks

There are no guarantees BPI will be able to grow future earnings. Declining student enrollment, inability of students to access Federal loans, industry competition, and rising operating costs could negatively affect the company's profits. Additionally, new and future regulations could adversely impact the ability of the for-profit education industry's ability to grow earnings. Negative equity markets, rising interest rates, terrorist attacks, and failure to comply with the Sarbanes Oxley Act could cause a decline in BPI's share price. Another risk for BPI's shares is the volatility created by the wide swings of stock held in short positions.

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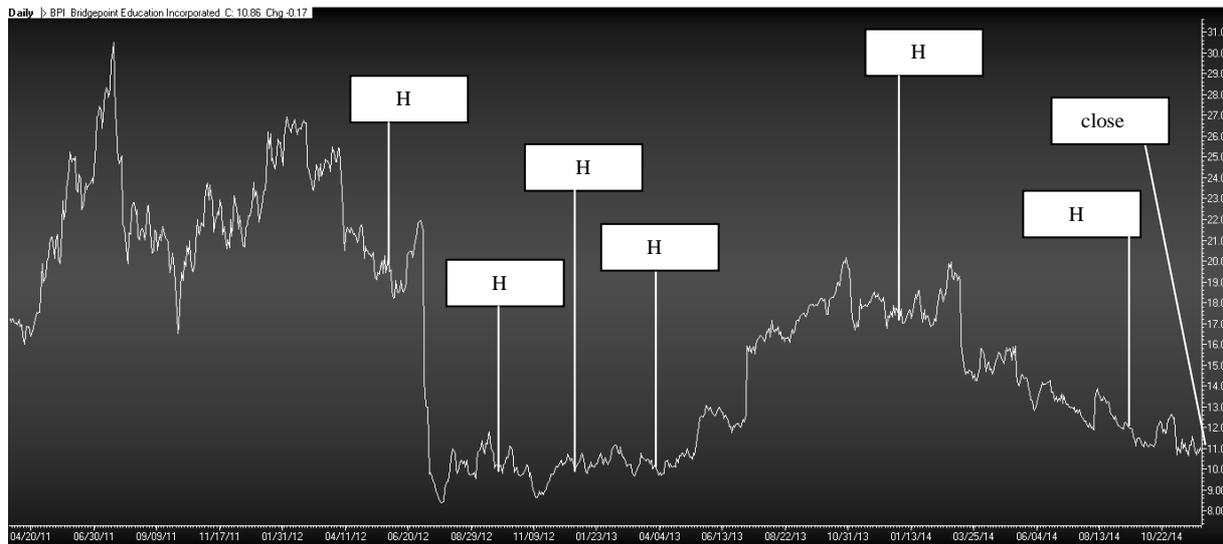


# EQUITY RESEARCH

BRIDGEPOINT EDUCATION, INC.  
(in millions, except per share data)

	1Q13	2Q13	3Q13	4Q13	2013	1Q14	2Q14	3Q14	4Q14e	2014e
Revenue	\$212,986	\$193,470	\$198,714	\$163,463	\$768,623	\$160,523	\$171,522	\$162,654	\$166,476	\$661,175
Instructional Cost & Services	97,028	99,603	105,542	93,755	395,928	86,454	76,853	79,707	79,725	322,739
Gross Profit	115,958	93,867	93,712	69,698	372,694	74,069	94,669	82,947	86,751	338,436
Marketing & Admissions Advisory	57,543	57,582	64,967	55,276	235,358	65,778	55,518	56,783	56,781	234,860
General & Administrative	18,739	17,152	15,175	25,828	76,894	16,269	16,737	15,583	15,598	64,187
Total Costs/Expenses	173,310	174,337	185,224	175,309	708,180	168,501	149,108	152,073	152,104	621,786
Operating Income	39,676	19,133	13,490	-11,856	60,443	-7,978	22,414	10,581	14,372	39,389
Other Income, net	837	748	1,051	710	3,346	367	712	1,080	822	2,981
Income Before Taxes	40,513	19,881	14,541	-11,146	63,789	-7,611	23,126	11,661	15,194	42,370
Income Taxes	15,846	7,767	5,520	4,686	22,779	3,212	10,171	5,370	7,445	26,198
Net Income	24,664	12,114	10,692	-6,460	41,010	-4,399	12,955	6,291	7,749	\$22,596
Net Earnings Attributable to Bridgepoint	\$24,664	\$12,114	\$10,692	(\$6,460)	\$41,010	(\$4,399)	\$12,955	\$6,291	\$7,749	\$22,596
Earnings Per Share	\$0.44	\$0.22	\$0.18	(\$0.12)	\$0.74	(\$0.10)	\$0.28	\$0.14	\$0.17	\$0.49
Diluted Shares Outstanding	55,001	55,634	56,431	53,098	55,487	44,987	46,503	46,503	46,503	46,503

## Important Disclosures



Ratings:  
Buy: B  
Hold: H  
Sell: S

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- (1) Buy – The stock's total return including dividends is expected to exceed the industry or market average by at least 10% over the next twelve months.
- (2) Hold – The stock's total return including dividends is expected to be in line with the industry or market average of +/- 10% over the next twelve months.
- (3) Sell – The Stock's total return including dividends is expected to be below the industry or market average by 10% or more over the next twelve months.

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