Investments
Industry Analysis
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I work for an online education company. While we are still a private company, we spend a lot of time examining and discussing our competitors in the education and edtech space. For this reason, examining the online education industry and our main competition seemed like a useful exercise both for this assignment and also to enhance my knowledge of the space for work. I will take their earnings data, my knowledge of the industry, and a few key calculations to determine which (if any) of the stocks would be wise to invest in.

Online Education Industry

This is a great time to be in the online education space. Because of the shift online and recent government aid becoming more open to alternative education, the space has been growing rapidly and with an eye towards the future. At my company, we spend time exploring where online education is going next, and the avenues to get there. A big focus for us is seeing where other companies are, and how to stay ahead of them. I have chosen three public companies with some overlapping customers or functionality to us, and will discuss them each in turn. All of these are companies I am familiar with from working in the same industry as them, and are ones where knowing more about where they stand financially is beneficial for my every day work.

Chegg, Grand Canyon Education, and Strayer all are in the education space. The reason I am familiar with them is that they all have a strong online presence and attract students that way. My company hosts and owns our own educational content, but we are familiar with schools like GCU and Strayer because they are competitive for accessing students who are looking for a college education in a more flexible manner. Sometimes this is because they are non-traditional students — maybe they are people who did some college but didn't finish, or who went straight into the workforce but regretted not ever taking the time to get their Bachelors. Often, they are less able to advance later in their careers because they lack degrees, so they turn to online or alternative credit providers to get there.

Chegg I am familiar with because we compete with them on the most direct level, because they target students who need help studying or access to materials to help them learn. Since my company hosts lessons and videos, they are similar in many areas to meeting the students' needs in a similar way to us. We also offer solutions to questions students need help with, whether that's through lesson pages or flashcard sets. Chegg is all online, unlike GCU and Strayer, and also has the most limited business model. This was evident once the financials were put side-by-side and it was a dramatic difference in their profits and growth verses the fully-fledged universities.

Assumptions for Calculations:

Rf = 2.89%

Interest rate = 4%

Er(m) = 10%

SWOT Analysis

Grand Canyon Education - LOPE

Strengths:

- High public awareness due to prominent ad campaigns.
- Christian university – appeals to specific audiences.
- Strong online offering (this is why we are familiar with them).
- Has both an online and brick-and-mortar location, broadening potential customer base.
- Better educational reputation than University of Phoenix, even with arguably similar online offerings.
- Unlike Strayer, is no longer for-profit.
- Has NCAA athletics, a big perk to many prospective students and adds to visibility of school.
- Highest ROE.

Weaknesses:

- As a formerly non-profit and now for-profit school, can be looked down on by others in education space for attempting to gain profit.
- Goes in and out of for-profit status.

Opportunities:

- Stock could pay dividend to attract more investors.
- Shift to online education could help them gain more students.

- Can potentially leverage in-person locations with online success to offer mixed program.

Threats:

- Stock had the highest beta of those I analyzed, showing risk.
- For-profit and then not-for-profit status shows wavering of profit model, unclear mission.

Chegg - CHGG

Strengths:

- Online homework help creates network of students who will use again.
- Textbook rental/purchase option follows students from high school to college and opens more revenue streams.
- Wide range of tutoring options.
- Membership fee is monthly, creating recurring revenue.

Weaknesses:

- Students aren't always willing or able to sign up for recurring fees, so they could utilize free trial for one-off answers and move on.
- Students will attempt to find answers for free before consulting Chegg at a cost.
- Lowest stock price by almost 25%.
- Lowest ROE, no dividend, low growth.

Opportunities:

- Expand textbook solutions to solutions to commonly searched problems online.
- Expand into offering full-fledged lessons, not just shorter pieces of content focusing on a specific question.
- Publish unique URLs for student-submitted questions to widen land-grab

Threats:

- Many students use Amazon to purchase textbooks, and Amazon has a wide market share.
- Many online education services (like mine!) offer similar things — tutoring, flashcards. Quizlet in particular has a strong SEO presence in online flashcards.

Strayer Education - STRA

Strengths:

- Strong online presence in terms of enrollment.
- Only analyzed stock that pays a dividend, which many investors like.
- Strong ROE.

Weaknesses:

- Has had rocky history of enrollment going up and down.

- No NCAA perk like Grand Canyon University, could be less attractive to potential students.
- More brand identity based in being online, unlike GCU which does much of its advertising focusing on the brick-and-mortar appeal to students, not just the online aspect.

Opportunities:

- Widen enrollment with increasing trust in online education and broader accpted use of financial aid.

Threats:

- Stigma of online education, in particular online for-profit education
- Balancing student needs and shareholder desires seems potentially tricky

Financial Comparison

Stock	Current Price	Dividend	ROE	Beta	P/E Ratio	EBITDA
Grand Canyon	107.45	-	23.11%	1.17	25.46	336.98
Chegg	22.23	-	-6.62%	.95	-	-2.33
Strayer	101.57	1%	19.98%	.91	29.09	77.52

Current as of 3/11/2018 per Yahoo! Finance. EBITDA in millions.

Clearly, Chegg is behind the other education companies. Likely since it is purely online, and has a much lower recurring revenue price (~$5.00/month verses several thousand in tuition) it has much lower earnings, and negative ROE. This isn't an indication that the stock is doing well, or that it will do better in the future. Compared to the strongest EBITDA (earnings before interest tax depreciation and amortization) of Grand Canyon, Chegg seems pretty weak.

Both Strayer and Grand Canyon show promising revenue and ROE. To have a return on equity around 20% is stronger than my market assumption rate and 5X my risk free rate of a current bond. While the idea of for-profit education may seem flawed to some, it certainly seems like their model is bringing them significant cash flows and making them a stronger stock to hold.

It is interesting that with so much income, Grand Canyon hasn't chosen to pay a dividend. Of course they don't have to, but since Strayer does and because they seem to have large cash flows, it seems like something that could be valuable for them to consider. Looking at the three stocks in this table really puts the much smaller Chegg into perspective.

Calculations

For Strayer, the only one with a dividend, I took the rf rate, beta, and Er(m):

.0295+.91[.1-.0295]=.094 as k

1/(.1-.095)= **156.25** as V0.

This is far higher than the current price, and could indicate that this is a underpriced stock with a high value. Based on their earnings and growth rate, perhaps those factors have added value to the stock and made it worth holding.

Chegg has never paid a dividend, so for them I took interest rate plus their beta times a k=10% and got a k=12.29, which is above the market return I had set of a required return of 10%. But when comparing that to their negative ROE and much lower EBITDA, it seems like perhaps here, k is misleading.

Grand Canyon has also never paid a dividend, so I did the same calculation with their beta and arrived at 14.59%, 2.3% higher than Chegg. This combined with their ROE and earnings seems to paint a picture for a solid stock offering with good growth and positive expected future returns. This makes me more confident that buying them would be a decent move for the future.

Conclusion

Based on the SWOT analysis, industry knowledge, competitor research, and the financials, I have decided to advise to:

Sell Chegg

Buy Grand Canyon

Hold Strayer

This worked out in an interesting way, with one fitting into each bucket. As education online becomes more profit-friendly and socially accepted, for-profit or at least publicly traded universities should be able to continue to grow their enrollment and continue the earnings success they have seen. Since Strayer pays a dividend, it's a good stock to hold for a while, since there is a recurring revenue element. Grand Canyon seems to be holding strong and poised for future success, as going back to non-profit may help them take some risks they didn't feel as comfortable doing as a for-profit university.

Since Chegg appears to be struggling, it doesn't seem like a good time to hold their stock. While it is the cheapest, it still has the lowest ROE, the weakest revenue model, and the lowest profits. With competitors like Quizlet offering similar online resources, and without the scope to offer actual education like Strayer and Grand Canyon, it seems likely that Chegg may fall further along the wayside as technology improves and companies with lots of cash turn to also creating online resources. Also, a company who has a main segment of their business competing directly with Amazon is never one I'd recommend taking on. The future of online education is bright, and it looks like at least 2 of these stocks are prepared to grow with it.

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