

Thomson StreetEventsSM



Conference Call Transcript

APOL - Q1 2008 Apollo Group Earnings Conference Call

Event Date/Time: Jan. 08. 2008 / 3:00PM MT

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

CORPORATE PARTICIPANTS

John Sperling

Apollo Group - acting Executive Chairman

Greg Cappelli

Apollo Group - EVP, Global Strategy

Joe D'Amico

Apollo Group - CFO

Brian Mueller

Apollo Group - President

CONFERENCE CALL PARTICIPANTS

Jeff Silber

BMO Capital Markets - Analyst

Sarah Gubins

Merrill Lynch - Analyst

Amy Junker

Robert W. Baird - Analyst

Jerry Herman

Stifel Nicolaus - Analyst

Gary Bisbee

Lehman Brothers - Analyst

Kevin Doherty

Banc of America Securities - Analyst

Brandon Dobell

William Blair and Company - Analyst

Corey Greendale

First Analysis Securities - Analyst

Jeff Lee

Analyst

Scott Schneeberger

CIBC World Markets - Analyst

Mark Marostica

Piper Jaffray - Analyst

Susie Stein

Morgan Stanley - Analyst

Edward Yruma

JPMorgan - Analyst

PRESENTATION

Operator

Good afternoon ladies and gentlemen, and welcome to Apollo Group Inc. first quarter fiscal 2008 earnings conference call. At this time, all participants are in a listen only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. Please refrain from entering into the queue until those instructions are given. (OPERATOR INSTRUCTIONS) This conference call is scheduled for one hour and is being recorded today, January 8, 2008 and may not be reproduced in whole or in part without permission from the Company. There

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

will be a replay of this call available through January 18, 2008, beginning approximately two hours after we conclude today. The replay number is 800-642-1687 or 706-645-9291 internationally. The conference ID number for the number is 27318003. Additionally, this call will be broadcast over the Internet and can be accessed via the Company's website at www.apollogrp.edu.

I would also like to remind you that this conference call may contain forward-looking statements with respect to future performance of Apollo Group, that involve risk and uncertainties. Various factors could cause the actual results of the Company to be materially different from any future results expressed or implied by such forward-looking statements. These factors are discussed in the Company's 10-K report and subsequent 10-Q reports filed with the Securities and Exchange Commission. The Company does not undertake any obligations to update anyone with regard to forward-looking statements made during this conference call. I would now like to turn the call over to Dr. John Sperling, acting Executive Chairman of Apollo Group. Dr. Sperling, go ahead, please.

John Sperling - Apollo Group - acting Executive Chairman

Thank you. Good afternoon and thank you for joining us today to discuss Apollo Group's first quarter results. We're off to a strong start in fiscal 2008 as the momentum we experienced last year continues. Before we discuss the quarter, I would like to update you on a few of the recent Board changes that we've made as we continue to fine tune our leadership team.

First, Peter Sperling has been named Vice Chairman. Peter has been with Apollo since 1983 and served in operational role as a member of the Board of Directors. We believe his understanding of the business and his experience and interest in the Company will continue to serve shareholders well and we have confidence in his leadership role as Board Vice Chairman. Additionally, Dino DeConcini, has formally been named Lead Independent Director, a role he's been performing for some time. Dino has served as a Director of Apollo since 1981 and his guidance and leadership have been invaluable. Finally, Ann Kirshner who was appointed to the Board last October has become a member of the Compensation Committee. We believe we now have a top notch group of (inaudible) Board members to guide Apollo's management as we continue to grow domestically and expand internationally.

I would like to turn the call over to Greg Cappelli now, who will update you on Apollo Global; Joe D'Amico will then review the highlights of the first quarter; and Brian Mueller will update you on operational progress and long term strategy. And finally, we will open the call to your questions. Greg?

Greg Cappelli - Apollo Group - EVP, Global Strategy

Thanks, John and first just along with Brian, I would like to officially welcome Allyson Pooley as the Head of our Investor Relations to Apollo Group. Many of you have probably spoken or met her over the past couple months, but we're thrilled to have her on board.

Since announcing Apollo Global in late October, we've been busy building the necessary infrastructure for the JV as well as identifying and evaluating a wide range of opportunities. We are pleased with our decision to work with the Carlyle Group in creating Apollo Global and the relationship continues to build. Together we've implemented a disciplined evaluation and due diligence process as we've identified potential partners and acquisition targets. In addition to acquisitions, Apollo's existing international offerings continue to perform well and other organic growth initiatives in foreign markets are also well under way.

We also continue to assemble a strong global management team which now includes an interim President, CFO, and COO and we continue to build on our global team which comprises employees in Chia, India, Europe, and Canada. Our focus has resulted in a growing pipeline of opportunities that validate the factors which drove our decision to create Apollo Global including the attractive demographics and economic growth in certain targeted international markets. The strong foreign demand for quality educational services at all levels and the increasing use of technology to deliver such services, which we think provides us with a unique competitive advantage.

Before I turn the call to Joe, let me just touch on our capital structure for a moment. We've been stressing for the last several quarters that we continue to evaluate our capital structure to achieve our goals. Including the utilization of leverage as appropriate. To this end, we announced today a new \$500 million unsecured revolving credit facility which is available to us for acquisitions and other needs we may have going forward. The revolving facility provides a multi-currency, sublimit for borrowing in certain foreign currencies up to \$300 million. We also have the ability to increase the facility by another \$250 million. We think this facility gives us additional financial flexibility and deeper financial relationships to help us capitalize on the global opportunities that exist.

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

During the first quarter, we didn't purchase -- repurchase any of our Class A stock. As I just discussed, with the creation of Apollo Global our potentially deep pipeline has grown significantly and we are busy evaluating the best use of our capital to create long term value for our shareholders. That said, we will continue to evaluate all of our capital needs carefully going forward, including the potential for additional share repurchases. In summary, we're excited about the outlook for both Apollo Group and Apollo Global. We continue to be disciplined in our approach to investing in both areas and we'll keep you updated on our progress going forward. With that I'll turn the call over to Joe.

Joe D'Amico - Apollo Group - CFO

Thank you, Greg. Financially, we've had a strong start to the year, with total consolidated revenues for Apollo Group of \$781 million, a 16.9% increase over the first quarter of fiscal 2007. Additionally, we generated an operating margin of 28.1%, a full point improvement when compared to the first quarter a year ago. Excluding share based compensation expense of \$15 million and share based compensation expense and special items of \$12 million in the first quarters of fiscal 2008 and 2007, respectively, our adjusted operating margin was 30% versus 28.8% respectively.

Net income for the first quarter increased 22.8%, to \$140 million, or \$0.83 per diluted share as compared to net income of \$114 million or \$0.65 per diluted share a year ago. Excluding share based compensation, we earned \$0.88 per diluted share in the first quarter of fiscal 2008 as compared to \$0.69 in the prior year.

Turning to the balance sheet and our cash flow, our cash and marketable securities, excluding restricted cash, totaled \$590 million at November 30, 2007, as compared to \$393 million at August 31, 2007. During the quarter, we generated \$208 million of cash flow from operations, which was reduced by \$24 million of CapEx and \$47 million for the purchase of Aptimus. Of the capital expenditures, approximately \$5 million were one-time in nature, and represent the continued build-out of our new corporate headquarters building in Phoenix. As a reminder, we have an option to execute a sale and leaseback transaction to monetize our investment in this new building when it is completed in the second half of fiscal 2008. At that time we execute to exercise the sale and leaseback and will receive approximately \$170 million in proceeds.

Gross student receivables were \$276 million at November 30, 2007, compared to \$282 million at August 31, 2007. Net receivables were \$188 million at November 30, 2007, compared to \$191 million at August 31. Our allowance for doubtful accounts increased slightly to \$105 million at November 30, 2007, from \$100 million at August 31, 2007. Our days sales outstanding remained consistent with the prior year, at 35 days, and declined from 38 days as of August 31, 2007. The improvement in DSOs since year end is due to a reduction in the percentage of accounts receivable under 90 days which we attribute to the improvements in our front end collection process. Our total allowance continues to exceed all receivables greater than 90 days.

Bad debt expense for the first quarter of 2008 as a percentage of revenue was 4.2%, compared to 3.5% a year ago. During the quarter, we performed a review of the components of bad debt expense and identified certain items that should have been reported or should have been classified as discounts or refunds, that is, as a reduction of revenue, as opposed to a charge to bad debt expense in prior quarters. We have not adjusted the prior year's bad debt expense or revenues for such items since the reclassifications are not material and would have no effect on reported net income; however, since the bad debt trend is not comparable, we have disclosed the impacts on revenue and bad debt expense in our press release and Form 10-Q. Taking into account the effect of the reclassification on prior periods, bad debt expense as a percent of revenue would have been 2.9% a year ago, and 4.4% last quarter, versus 4.2% in the current quarter.

Bad debt expense as a percentage of revenue increased over the prior year comparable quarter, primarily due to the continuing shift in our enrollment mix to a higher percentage of associate degree students when compared to prior periods. As we have said previously, bad debt is a cost of our business due to the relatively open enrollment policy that we maintain at the associates level. Importantly, our bad debt expense as a percent of revenue declined from the fourth quarter on a comparable basis by 20 basis points. Which is the first time in several quarters that this percentage has declined. We are hopeful that our efforts to manage bad debt levels will continue to pay off as we execute our plan of improving student retention in our associate's degree programs.

Deferred revenue declined \$7 million from the year end, to \$160 million and student deposits were essentially flat at \$330 million as of November 30, 2007. When compared to November 30, 2006, deferred revenue increased by \$28 million, and student deposits increased by \$73 million. These changes are seasonal in nature and consistent with our enrollment growth. Finally, you should note that goodwill increased \$37 million and other assets increased \$7.4 million, versus August 31, 2007. These increases relate to our acquisition of Aptimus. We have one year from the acquisition date to finalize our allocation of the assets and liabilities acquired. With that, I'll turn the call over to Brian.

Brian Mueller - Apollo Group - President

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

Thanks, Joe. The first quarter was a strong one with double-digit revenue and enrollment growth. We continue to outperform our long-term goals of mid-to high single digit growth in annual domestic revenue and low double-digit annual growth in domestic operating profit and free cash flow. In fact, revenue grew almost 17% year-over-year. Excluding stock based compensation and special items, operating income growth was almost 22%, resulting in a 30% operating margin which validates the heavy investments we made over the last couple years. Before I drill down into the results I would like to step back and review the overall environment.

The demographic and economic trends contributing to the rise of adult education over the past three decades continue. One of the primary drivers is underemployment. By this I'm referring to the growing numbers of working people whose wages are not high enough to provide them with a comfortable middle class lifestyle. Many of these individuals will seek higher education as an answer. Statistically the U.S. Department of Education's National Center for education statistics estimated that based on its most recent data from 2005, more than \$6.8 million or 39% of higher education students 24 years old -- are over 24 years old, placing a large percentage outside the consideration of traditional universities and colleges. The number is expected to increase by 21% from 2005 through 2016. During the same period, the 18 to 24-year-old segment making up the generation of echo boomers is anticipated to increase 15%.

The students in both of these age groups are candidates for our associate's program at Axia College which provides solid preparation for completing a four year degree. These echo boomers also have a different attitude about education and work and provide an example of how Apollo Group organizations rapidly adapt to changing market forces.

University of Phoenix commissioned a market research study that provided some interesting insights about echo boomer students including the fact that 70% of them must work while attending college. A large majority of the echo boomers are single women, most dependent heavily on the Internet for socializing, entertainment, and education, and they believe education is about earning power. They are pragmatic about their futures and don't necessarily want to leave home to attend college. At the same time they are the most education focused generation in history. Most of them understand the value of and express the desire to achieve a bachelor's degree. These trends are important to our business and continue to drive our enrollment growth.

Now let me review our results, specifically focusing on revenue, enrollment, and margin growth and update you on some of the initiatives we have in place to achieve our long-term objectives. As I mentioned, our revenue for the quarter grew almost 17% to \$781 million compared to the first quarter of the prior year. We are very pleased with this number and the continued positive trend we have experienced over the last several quarters. Importantly, revenue growth surpassed enrollment growth. For the second consecutive quarter. This increase in revenue was driven by three factors which we'll discuss in more detail. Namely, tuition price increases, improved retention, and an overall increase in total enrollment.

Tuition increases were particularly a factor in our associate's programs as we continued to benefit from the increase which took place in May of 2007. We also benefited in the first quarter from selective tuition increases in our other programs which went into effect July of 2007. As we anticipated, these tuition increases along with the improvement in retention levels are offsetting the mix shift of the student body into lower tuition rate associate's programs. Also positively impacting revenue growth is improved retention. Retention continues to be the number one focus at Apollo as it impacts so many aspects of our results including enrollment, revenue, profit levels, bad debt, and student default rates. The third factor positively impacting revenue growth is total enrollment. Total enrollment in the first quarter increased 11.4% year-over-year reaching a total of 325,000 students. Associate student enrollment continues to be our fastest growing segment, increasing 37.7% year-over-year. Associate students now represent 35% of our student base. Enrollment in bachelor's degree programs remained relatively flat year-over-year, decreasing by only 1.5%.

Let me now discuss student starts. During the first quarter we started approximately 67,400 students, a 7.8% increase over the prior year. Like last quarter, we faced a difficult comparable in starts due to the high drop rates we experienced a year ago. I'm speaking mainly about high drop rates of new student starts. As we said last quarter, a year ago we started many students who dropped quickly. The start number -- thus the start numbers from a year ago are artificially high. As you know, a little over a year ago we hired hundreds of new enrollment counselors and we began training our campus-based counselors to recruit students into the online programs. As our counselors gain experience and training, the students they enroll, particularly in the online programs, are better prepared for their college experience and are persisting at higher rates. The flip side of this is that the growth in our revenue per student, particularly at the associate's level is off of an artificially low base and the growth rate is not expected to be maintained at the current level.

I would also like to address the continuing trend of greater start growth at the associate's level relative to the bachelor's level. During the first quarter, starts at the associate's level increased 23% year-over-year, while bachelor's degree starts declined at 8.4%. Together, associates and bachelor starts for undergraduate starts as a group grew approximately 9% year-over-year and we believe that had we not started Axia three years ago, this number would be lower.

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

As a reminder, we started Axia in 2004 due to the fact that more and more of our leads involved students with fewer credit hours and therefore they needed better preparation for the rigorous academic programs a college student experiences. Enrolling these students directly into our bachelor's degree programs wasn't the answer as they were dropping at high rates. Axia College addresses the needs of these less prepared students. Specifically, classes are longer, the cost per credit hour is less and tutoring and counseling services are more comprehensive.

The demand for education from students that have fewer credit hours continues to be very strong. As I mentioned earlier, this demographic is large and projected to grow rapidly. Additionally, as counselor training increases, particularly our cross training of campus counselors to recruit students into our online programs, the number of students being referred to and starting at Axia continues to increase. A year ago, students with less than 42 credits in certain parts of the country would have enrolled directly in our bachelor's program. Today, the vast majority are counseled to begin their programs at Axia College where they are more likely to succeed.

Another factor is the unavailability of our online programs in certain geographies. During October, Axia became authorized in the state of Florida for the first time, which contributed to the mix shift in student starts in the first quarter. We are not sure when the mix shift will level off. What we do know is that the pool of Axia students available to potentially transfer to our bachelor's programs continues to grow rapidly. Eventually we expect this trend to lead to improved growth within our bachelor's programs.

Before I move to operating costs, let me touch on Insight schools. As a reminder, we acquired Insight a little over a year ago, and at the time Insight was approved in one state. In the last year, we have expanded and are now approved in five states including Washington, Wisconsin, California, Oregon, and Minnesota. We are currently operating in three of these states and will be opening in Oregon this month and in Minnesota in the fall. We have several other target states and believe we are on track to have a total of 10 by the beginning of the next school year, namely this fall.

Now let me discuss our operating costs. In the first quarter, we received -- we achieved an operating margin excluding share based compensation and special items of 30%. Up about 120 basis points from a year ago. Several factors led to this improvement. First, instructional costs and services declined 140 basis points to 42.7% of revenues from 44.1 in the first quarter a year ago. The improvement was primarily due to centralizing much of our financial and academic counseling which provides further leverage as our enrollment and revenue continue to grow. Second, we continue to benefit from space utilization as our online student body grows. As we've said previously, we are not necessarily reducing space but we are able to grow our student body without adding space as more students choose to study online. These improvements were offset somewhat by an increase in bad debt, which Joe discussed earlier.

Selling and promotional expense as a percent of revenue declined 70 basis points to 22.6 from 23.3 in the first quarter a year ago. Effectiveness in advertising productivity continues to improve. In the quarter, advertising spend increased approximately 9%, resulting in a 70 basis points improvement as a percent of revenue versus the first quarter a year ago, despite incurring Aptimus expenses in the month of November. Additionally, we again hired incremental enrollment counselors in geographies where we continue to believe there is additional opportunity. Particularly the Midwest and the Northeast. Based on the positive returns we are seeing on our ad spend, we increased the amount of dollars spent starting in December and we expect this to continue throughout the quarter.

Although our advertising as a percent of revenue decreased in the first quarter, we did experience an increase in the cost per new start versus a year ago. This is also related to the high drop rate we experienced a year ago. We have significantly decreased the number of early drops from the prior year, which had an effect of spreading our marketing and sales expenses over a relatively larger number of new starts in the prior year. We continue to believe the persistence of the current new students will be improved over the prior year, which should positively impact our operating profit going forward.

As a reminder, we launched our national branding campaign in January of '07. We continued to invest in to support our image which will also adversely impact cost per start in the short term. But we are pleased with the progress we are making and believe the long-term effects will be very positive. G&A expenses increased this quarter to 6.6% of revenues versus 5.6% in the first quarter of fiscal '07. The increase is due to investments we made over the last year in our finance and legal teams as well as continued investment in IT areas to support our enrollment growth. Additionally, we experienced higher legal costs in connection with some of our outstanding legal matters.

Let me now update you on two of our most important strategic initiatives that contribute to the above results and which will continue to drive our success. The first is retention and the second is reducing student acquisition costs. As I mentioned earlier, retention continues to be the number one priority at Apollo Group. We continue to target four key areas for improving retention.

First, building new programs which relate specifically to drive growth areas in the country. Second, analyzing and improving curriculum in places where students have specific difficulties. Third, evaluating instructional best practices and providing training to instructors throughout the

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

system. In fact, we currently provide over 60 faculty development workshops such as grades and feedback, assisting the academically at risk student, and dissertation mentor training. Fourth, increasing support services which have included additional tutoring and student workshops. Additionally, we have instituted a pilot program to provide scholarships to Axia students who graduate to a University of Phoenix bachelor's program. We are evaluating the impact of this program on student transfers and retention -- and retention have been very pleased with the initial results. As a result, we expect our discounts to increase. However, we believe this will improve retention which will drive revenue and profitability growth.

The second key initiative is our focus on marketing, lead generation, and the costs associated with acquiring a student. At the end of October, we've closed the acquisition of Aptimus and our marketing teams have been working over the past couple months to transition to the new platform. We are pleased to report that as the transition begins in earnest, we have begun to successfully manage our online marketing investments in house. Over the next several weeks, we will complete the transition of all affiliates as well as management of all search and display advertising. Over time, we will be implementing innovative marketing plans to more effectively communicate with prospective students and other constituents online, ultimately with the goal of lowering our cost of acquiring and starting a student.

I would like to address just a few other items before we take your questions. First, the current situation with the credit markets continues to be front page news and we received many questions about it from you. Recent legislative changes made by the Federal Government have lowered the margins earned by student loan lenders for administering and managing the title 4 government loan programs. According to news reports, this has pushed many student lenders to look elsewhere for improved profitability and some of you would like to know whether this has affected or will impact Apollo. Let me try and put this in perspective.

A few years ago Apollo made some decisions with regard to pricing that in light of the current credit situation have turned out to be particularly important. These decisions have allowed us to run our business without a heavy dependence on private loans. As a result, approximately 4% of our revenues are derived from private loans. Second, other than a small pool of loans, primarily for international students, we do not have any material risk sharing agreements with private loan providers. In total, our exposure is very small and we don't expect this to change. Finally, we know there are concerns in the market regarding the availability and accessibility of Title IV loans. We have not seen any impact to date on our students obtaining financial aid. We have a strong and diverse selection of unaffiliated student loan providers that are reviewed quarterly to include lenders that offer competitive borrower benefits, have exceptional operating standards, possess technical wherewithal, and are committed to providing outstanding service and expedited processing by meeting or exceeding established performance standards. In our opinion the student loan market remains competitive and our students have quality choices to meet their educational financing needs. With that, I'll turn the call over to the operator so we can take your questions.

QUESTION AND ANSWER

Operator

Thank you. Ladies and gentlemen, at this time we will be opening up the call to the question-and-answer session. Each caller will be limited to one question. (OPERATOR INSTRUCTIONS) One moment, please, for the first question. Our first question is from the line of Jeff Silber. Please go ahead.

Jeff Silber - BMO Capital Markets - Analyst

Thanks so much. Appreciate all the color, Brian. I just wanted to delve a little bit further into this private lending issue. I think you said -- I don't -- the words you used were review the lender's agreements quarterly. I know you haven't seen any of this as of yet but as you do these reviews, are lenders coming to you, and asking for more risk sharing? Are you hearing that in the market at all?

Brian Mueller - Apollo Group - President

Joe, you had some meetings just recently. What are you hearing?

Joe D'Amico - Apollo Group - CFO

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

Right. Well, the lenders surely would like us to participate but we've declined. And we haven't seen any falloff in terms of our ability to enroll students or have any serious impact on our abilities to -- for our students to get loans. The level of private loans is down but they're still significant or at least to the 4% level for us.

Operator

Our next question is from the line of Sarah Gubins.

Sarah Gubins - Merrill Lynch - Analyst

Good afternoon. I'm hoping to understand a bit more about the pattern of Axia graduates transferring into University of Phoenix or finishing up their bachelor's degree program at Phoenix, particularly in light of the decline in bachelor's starts. Can you give us an update on what you're seeing for Axia graduation rates and the transfer rate for the bachelor's program and then maybe talk a bit about the level of discounts or scholarships that you're expecting for those people who are transferring in?

Brian Mueller - Apollo Group - President

Okay. Yes, there's number of points there. One, the -- we're not giving any color on the number of -- or the percent of students that are transferring from Axia to University of Phoenix and completing at University of Phoenix. We gave some initial information about that but it's -- we consider it proprietary and very competitive and we don't want to release that. Second point though is that it's easy for you to probably do some modeling around the number of students, the volume of students that are graduating -- that are going to Axia, therefore the volume of students that are graduating is getting bigger. That pool of people who can potentially transfer into our bachelor's program is growing month over month which is a very good thing from our standpoint.

The bachelor's growth or lack of it as compared to the associate's growth has to be understood from the standpoint of we now have more than half of our enrollment counselors out on the ground campuses. And if you look at a year ago, a student that would come with 42 credit hours or less, let's say 30 college credits, would likely have been put by one of those counselors into a bachelor's program. Today, those are -- those people are putting them into the associate's programs, into the Axia College program, and so it's that number is being artificially manipulated by what's going on from a new student standpoint.

And then the last question was about discounts. We don't know for sure what's going to happen to that discount line. It will probably go up some but it will only go up in relationship to our increased retention and therefore increased revenues. So anything that we invest from a scholarship standpoint into an Axia College graduate that would go to University of Phoenix baccalaureate program would only be done because what we know is we will benefit from the standpoint of increased student retention and therefore increased revenues. And that will result in increased profit. So those discounts are done very strategically in order to increase retention and revenues and we're experiencing that as part of our success this quarter.

Operator

Our next question is from the line of Amy Junker.

Amy Junker - Robert W. Baird - Analyst

If I could actually just follow-up on that question and I appreciate that you don't want to give us specifics on the numbers. But can you just at least tell us directionally if you're seeing improvement in the percentage of students that are continuing? I assume you're seeing better retention numbers, you talked about, but are you seeing a greater interest in those students wanting to go on to get a bachelor's or are most of them satisfied at this point with associates? And then as I think, again, a follow-up, when should -- should we expect the bachelor's to reaccelerate for all of this to come through before the end of fiscal '08 or is this going to be a fiscal '09 phenomenon where we should start to really see an acceleration in the bachelor's portion of it?

Brian Mueller - Apollo Group - President

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

We don't know for sure about that because the numbers are impacted by what new students are doing and at any given quarter, new students are 20% of our total student body. So it's a difficult question to answer. There's a lot of moving parts there. What I will tell you is that from a business model perspective, I'll say two things. Number one, as compared to what students are experiencing in community college programs, our graduation and transfer rates are very good. Very strong. So we think we're doing a very good job from the standpoint of servicing the needs of those students as they relate to what's going on in the rest of the industry.

Secondly, from a business model standpoint, it's very, very -- it's working very well. Our revenues are increasing. Our margins are increasing. And so what the result -- and we'll continue to work at it. We'll work at that as hard as anything that we're working at. But in terms of its impact on our business results, they're very good.

Operator

Our next question is from the line of Jerry Herman. Please go ahead.

Jerry Herman - Stifel Nicolaus - Analyst

Thanks, good afternoon, everybody. Hi, guys. Question with regard to new programs. You guys have talked about an expansion in the program offering and I'm wondering, Brian, if you can give some indication as to what sort of influence that's having at this stage of the game? Is it material or not? And how is it potentially changing the student acquisition process from a lead generation point of view and what sort of impact is it having on retention, especially in the more specialized programs?

Brian Mueller - Apollo Group - President

I think it's a very, very good question and it's something that we have a great deal of interest in understanding more thoroughly. We've have rolled out so many new programs in the last six to 12 months that we don't have contingent data yet on both the increased conversion rates, so its impact on student starting or its impact on retention rates. But what we do know is the Department of Education in recent survey to college students when they asked the college students to rank things that most were -- they were most -- that were most important to them as they considered a college choice, number one was program availability. And we know that the programs that we currently have as a percent of all programs that are available in higher education at all the four levels that we teach at are very small. And so we are monitoring the conversion rates. We continue to specialize with regards to our enrollment counselors, making them responsible for fewer and fewer programs, therefore, being able to be more expert at the programs they represent, and we'll watch closely the retention rates of students, especially in those niche programs. Initial evidence is that they're higher and we hope that they continue to go higher.

Operator

Our next question is from the line of Gary Bisbee. Please go ahead.

Gary Bisbee - Lehman Brothers - Analyst

Hi, guys. Congratulations on a nice quarter. I guess the question is two parts. But when do you expect you're going to lap this period of artificially high new student starts? Last year, that related to all the new reps you hired and as that's going to relate to starts performance? I guess over the last few quarters you said you're cautiously optimistic that in the near term you may be above that medium term guidance you've given. Is it realistic to assume that the starts growth can continue to do that once you've lapped this more difficult period? Thanks.

Brian Mueller - Apollo Group - President

Well, we were seeing high single digit revenue growth, low double-digit operating profit growth and we currently are exceeding those and so what we said was in the short run we would exceed those and we are. And the first question, though, the first question was -- oh, when is the lap. Let me -- I left a little bit out of that story. One of the -- a year ago, when all those enrollment counselors were trained to put students in online programs, they put a lot in that didn't stay and so that partially impacted that 25% increase number. That was doubly impacted by the fact if you

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

go back a year before that, it was the low point. Fourth quarter two years ago and first quarter two years ago we reached our low point with regards to our effectiveness as an organization and so there was a double impact there. I think what you'll see is gradually, over the next three quarters, things will level out and by first quarter of next year we will be comparing an apples and apples scenario.

Greg Cappelli - Apollo Group - EVP, Global Strategy

Gary, just one follow-up, when you think about -- I know you asked about the near term, but we remain comfortable with our long-term internal objective which we've given out quite a few times over the past couple quarters for mid to high single digit long term revenue growth and double digit operating profit growth. And to get there, you do have to make certain assumptions in terms of total enrollment growth and we have not changed our internal goals or view on that.

Operator

Our next question is from the line of Kevin Doherty. Please go ahead.

Kevin Doherty - Banc of America Securities - Analyst

Thank you. I just want to kind of follow-up on that last question. You talk about the strong demographic background kind of the lack of the credit crunch here. What scenario would really need to happen in your business to kind of level off to some of those longer term growth rates, particularly given how strong things have been recently?

Greg Cappelli - Apollo Group - EVP, Global Strategy

We evaluate those things all the time. I guess we -- we're like Intel and we're very, very paranoid so we're looking out for things that might impact us negatively. There's lots of things out there that could. But we -- we have a lot of confidence in what we're doing at each level of education that we service students at and we'll continue to work very hard at it and our progress in relationship to who our major competitor is, which are the traditional universities and the community colleges, we believe that our progress in providing increasing levels of quality is improving versus theirs. So -- we're confident about our future.

Operator

Our next question is from the line of Brandon Dobell. Please go ahead.

Brandon Dobell - William Blair and Company - Analyst

Hi, guys. Wonder if I could circle back from a different angle from the Axia matriculation question or idea here. Maybe it would be helpful to get a better sense, at least I know it would be helpful for me to get a better sense of what the Axia students actually look like relative to UOP students. Are they just the same students, less credit hours? Are they taking the same type of programs? Do they have the same kind of jobs, and same kind of positions? Trying to gain the likelihood of matriculation, the likelihood of going on to a higher degree, I guess would be helpful for us to understand if this is just really the same person with less credit hours or if there is even a decent difference in what those students might look like? Thanks.

Brian Mueller - Apollo Group - President

Okay. Yes, from a demographic standpoint, our University of Phoenix students are 33 to 34 years old, they're about 60% female and about 40% male. Our Axia College students are 28 to 29 years old, they're 70% -- 72% female, 28 to 30% male. Their average household income, the Axia College students is less. They are more entry level jobs in the economy than our University of Phoenix students. And so from an age perspective, there's not that great a difference. They have the same bent towards females versus males. They are at more entry level positions in the economy but we believe that their need for higher education is as great or greater than our traditional University of Phoenix students.

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

Anything else I can share? Ethnically and from a racial standpoint, it's pretty close in terms of how they break down between our University of Phoenix students and our Axia College students. I think one more thing it's important to note that we do very little Axia College advertising, we do very little advertising of our associate programs. The students that come to us and we put in Axia are students, 99% of them who have a goal of achieving a baccalaureate degree. We think this is just a good way to get them started and get them well-prepared for pursuing that.

Brandon Dobell - William Blair and Company - Analyst

Brian, would you say there's, in terms of the demographics, is there any reason why those Axia students would not at some point in time in their growth not want to get a bachelor's degree?

Brian Mueller - Apollo Group - President

No, I don't think so. Because if you look at -- if you look at the Axia College programs that we have, you will notice that there are a few where there is some direct benefit from having an associate's degree. There is some increased capability from an income standpoint. But there is still a much greater differentiator at the baccalaureate level and so there's not -- it's not a scenario where an associate's degree will give you an opportunity close to or equivalent to a baccalaureate degree so that people would be tempted to stop there. We are not seeing that happen.

Operator

(OPERATOR INSTRUCTIONS) Our next question is from the line of Corey Greendale. Please go ahead.

Corey Greendale - First Analysis Securities - Analyst

I have a question on the margins. Is there anything that you would highlight as being kind of unusual or unsustainable, positive or negative, that affected those or if the revenue picture looks similar to this over the next couple quarters, is this a pretty good indication of what the margins should do as well?

Brian Mueller - Apollo Group - President

Well, the -- the thing that will impact it is the seasonality. The second quarter, the revenue is going to be a little bit less, I mean, revenues are depressed a little bit because of the students taking off time in the holiday and so that's going to impact the margin. But other than that, there's not -- the gains that I think that we've made on the space side, we'll continue that. They won't continue to increase but we'll maintain that. From an instructional costs and services standpoint, those are gains we've made from an academic counselor and financial advisor standpoint, we expect to maintain those. Bad debt has come down a little bit from the previous quarter and so we gained a little bit there. And obviously the hope is that we'll maintain that.

So I don't think there's anything outstanding, other than we are going to spend -- I mentioned it in the script. We are going to spend a little bit more in December and January in advertising. We're gaining -- we continue to gain knowledge. We don't know what the upper limit is in terms of when we'll start to either decline in the return, positive return on that advertising dollar spend, so we'll spend a little bit more. If we get a good return, then we'll continue that. So that will go up a little bit as a percent of revenue. Other than that, there's nothing outstanding there that would say it's going to be significantly different, other than the seasonality, which I know you guys know about and take into account.

Operator

Our next question is from the line of [Jeff Lee]. Please go ahead.

Jeff Lee Analyst

Hi, good afternoon. What have you seen so far with integration of Aptimus and has it made any impact on the organization in the two months you've owned it so far?

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

Brian Mueller - Apollo Group - President

No. Well, I would say our goal is to make sure that we make this transition smoothly and we keep operating at our current level of effectiveness and I believe that we are doing that. We're watching that very carefully. Those guys are working really, really hard to make sure there's no steps backwards. Going forward, there's a lot of talent there. There's a lot of talent around some significant areas that impact Internet advertising that over time we hope to leverage and see improvements.

Operator

Our next question is from the line of Scott Schneeberger, please go ahead.

Scott Schneeberger - CIBC World Markets - Analyst

Hi, thank you. Apollo Global, could you speak to a little bit about where you're looking geographically? What types of business models you're reviewing? What the environment is out there? Just any color you can add since it appears that you're stockpiling cash there.

Greg Cappelli - Apollo Group - EVP, Global Strategy

Sure. As we said previously, we are initially focused on China and Asia in general, including India. Parts of Latin America, including Brazil and also Europe, where we've deployed resources now and have people on the ground. The environment is mixed. In certain parts of the world, because of successful IPOs, we've seen prices that have been bit up and in most cases we're scouring the landscape, we're trying to make sure we understand everything that's out there. We're going to be disciplined with our partner Carlyle in our valuation process to these businesses and we're in the stage right now of putting a nice pipeline together of opportunities that we want to follow-up on going forward. So I'd say overall, we've been working hard the past couple quarters to get the right people in place, to get the discipline in place, and we're -- we're pleased with where we are at this point.

Operator

Our next question is from the line of Mark Marostica. Please go ahead, sir.

Mark Marostica - Piper Jaffray - Analyst

Brian, I want to revisit a comment you made in your remarks concerning the federal loan environment. In particular, a few weeks ago Sallie Mae in a filing noted that it plans to be somewhat more selective in pursuing origination activity on the federal side and on the private side. But on the federal side, I wonder if you could help us understand your exposure to Sallie Mae? And secondly, what do you think this means, the statement in their filing means relative to your business? Does it slow down your enrollment process? Does it force you to look at other lenders? Can you give us a sense how you think that plays out over the next few quarters.

Joe D'Amico - Apollo Group - CFO

This is Joe D'Amico. With respect to Sallie Mae, they are one of our preferred lenders. We have four. And Sallie Mae continues to process new loans for us on the federal side without a hitch, been no cutbacks, no changes, no delays. So we haven't felt the effect on the federal side at all relating to Sallie Mae. And we continually look at our preferred lender list and go through a process of deciding whether to add or to change lenders who are participating with us. There is significant interest by a substantial number of lenders to become preferred lenders for the University of Phoenix.

Operator

Our next question is from the line of Susie Stein. Please go ahead, ma'am.

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

Susie Stein - Morgan Stanley - Analyst

Hi. Thank you. First, a follow-up to the last question. Can you just mention who the other three preferred lenders are? And also, is there any evidence in the market that prospective students are price shopping more than they have in the past because of the lack of available private loans? And are you directing your marketing efforts at that? I mean, can you envision a scenario maybe where you would actually benefit from what's happening in the private loan market?

Joe D'Amico - Apollo Group - CFO

Well, I'll answer the first question. With respect to who are the other preferred lenders, it's Citibank, Wachovia, and Wells Fargo.

Brian Mueller - Apollo Group - President

The answer to the second question is yes, we absolutely can envision a point in time when we will benefit from the fact that we've been able to build a business that is profitable at a level that is at a price that is quite a bit less than most of our competition. I think we're in the right place at the right time from that standpoint and as we expand out programmatically, I think that will put some pressure on people.

Operator

Our next question is from the line of Edward Yruma, please go ahead, sir.

Edward Yruma - JPMorgan - Analyst

More of a housekeeping question. I noticed that other receivables ticked up significantly sequentially. What goes into that and what drove that increase? Thank you.

Joe D'Amico - Apollo Group - CFO

Nothing unusual occurred there. It's just timing or.

Operator

We do have a follow-up question from the line of Gary Bisbee. Please go ahead.

Gary Bisbee - Lehman Brothers - Analyst

Just a question around this line of credit here. So -- and the decision not to buy back any stock this quarter. I think you've got \$600 million of cash, restricted cash and now you've got borrowing capacity for \$0.5 billion. Should we read anything into this in terms of how much you're thinking about potentially investing in international acquisitions and in terms of doing something quickly because of the stockpiling cash? How are you going to think about buybacks? It seems to me with your cash flow what what it is, your balance sheet what it is, and now that borrowing power, there still would be lots of room for buybacks as well? Thanks.

Greg Cappelli - Apollo Group - EVP, Global Strategy

Why did I know you were going to ask me that question, Gary. No, you shouldn't read anything into it. Let's step back for one second. A quarter ago we were able to get off over \$430 million in repurchases which we were pleased with. We did take a step back this quarter, just to take a look at all of our capital needs going forward and we've been evaluating those comprehensively. Think about our businesses now. It's not just the University of Phoenix and the capital needs two or three years ago of building that business. We've got Aptimus and there are opportunities to put capital to work in that industry.

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

Insight schools, there are opportunities there. And we're excited about the growth potential in that part of our business. There is the University of Phoenix and all the initiatives that Brian has talked about, from retention on to new programs. And now there's Apollo Global, where -- and I know I failed to mention this from the earlier question from the last caller, but we are looking at K-12, post secondary, vocational, and corporate training outside the U.S. So the good news is we've got no shortage of opportunities to actually deploy and put capital to work. What we're doing is we're trying to evaluate where we'll get the highest returns for all the projects that we're lining up in the pipeline and just to finish with your question, we are not adverse to opportunistically buying back stock as well. So that's something that we're continuously evaluating going forward. Hopefully that answers your question.

Operator

Our next question is from the line of Sarah Gubins.

Sarah Gubins - Merrill Lynch - Analyst

Thanks. Just a quick follow-up. Brian, you mentioned that a year ago reps were still putting students with less than a certain number of credit hours, in some cases into the University of Phoenix program as opposed to Axia. At what point were reps -- did reps really entirely start putting students with fewer credit hours into Axia?

Brian Mueller - Apollo Group - President

It varies. It really depends upon the comfort level of that person and so it varies. There's the -- the other thing that it varies around is the size of the campus. If you're in a very small campus, a very small marketplace where it's difficult to get class size and group size in the ground based programs, then you're going to have more people gravitating towards the online program where students can start every single week whenever it's most convenient for them. So I guess the answer is it varies. Thank you very much. Sorry, there is one more.

Operator

We have a question from the line of Jeff Silber. Please go ahead, sir.

Jeff Silber - BMO Capital Markets - Analyst

Thanks for letting me sneak in. Just looking quickly at the revenue per student, you had mentioned some selective price increases. Can you tell us what programs they were in? Was it bachelors? Master's? Et cetera. Do you have plans to continue that going forward. And can you also review, I know historically you talked about a national pricing model, what are your thoughts on that?

Brian Mueller - Apollo Group - President

The price increases were around both bachelors, masters, and doctoral programs. And going forward, as we talked about before, we have significant room for price increases at the doctoral level. We have significant room under Title IV loan limits at the master's level. We have some room at the associate's level. And at the baccalaureate level we have some students who are under Title IV loan limits. That varies at campuses in the Midwest. We have other students who are above Title IV loan limits. It's a mixed bag only at the bachelor's level. Right now we really like how the business is going. We like what we're getting in terms of conversion rates and retention rates and we like how the revenue per student is going at all levels and so we have no inclination to do anything currently. We'll just continue to watch it. We'll continue to evaluate and at some point if we do it, it would only be done because it would increase revenues, increase revenues per student because of its impact on retention. We would not do it if we weren't sure that it would do that. But again, thank you all for attending. We appreciate your attendance and have a good evening.

Operator

This concludes today's conference call. Thank you for your participation.

Jan. 08. 2008 / 3:00PM MT, APOL - Q1 2008 Apollo Group Earnings Conference Call

DISCLAIMER

Thomson Financial reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON FINANCIAL OR THE APPLICABLE COMPANY OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

© 2005, Thomson StreetEvents All Rights Reserved.