

# FINAL TRANSCRIPT

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## **BPI - Q3 2011 Bridgepoint Education Inc Earnings Conference Call**

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*Bridgepoint Education, Inc. - CEO*

**Jane McAuliffe**

*Bridgepoint Education, Inc. - EVP, Chief Academic Officer*

**Dan Devine**

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## PRESENTATION

**Operator**

Good morning and welcome to the Bridgepoint Education's third-quarter 2011 earnings conference call. Today's call is being recorded.

At this time I would like to turn the conference over to Mr. Paul Goodson, Associate Vice President of Investor Relations for Bridgepoint Education.

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**Paul Goodson** - *Bridgepoint Education, Inc. - Associate VP IR*

Thank you, Ann, and good morning, everyone. Bridgepoint Education's third-quarter earnings release was issued earlier this morning and is posted on the Company's website at [www.BridgepointEducation.com](http://www.BridgepointEducation.com).

Speaking on the call today are Andrew Clark, Chief Executive Officer; Dr. Jane McAuliffe, Chief Academic Officer; and Dan Devine, Chief Financial Officer.

Before we begin we would like to remind you that some of the statements we make today may be considered forward-looking, including statements regarding financial results and related guidance. These forward-looking statements are subject to a number of risks and uncertainties that could cause actual performance or results to differ materially.

Please note that these forward-looking statements speak only as of the date of this presentation, and we undertake no obligation to update these forward-looking statements in light of new information or future events, except to the extent required by applicable securities laws.

Please refer to our SEC filings, including our quarterly report on Form 10-Q for the period ended September 30, 2011, as well as our earnings press release posted this morning for a more detailed description of the risk factors that may affect our results. Copies may be obtained from the SEC or by visiting the Investor Relations section of our website.

This call is the property of Bridgepoint Education. Any distribution, transmission, broadcast, or rebroadcast of this call in any form without the express written consent of the Company is prohibited. A replay of the call will be available via telephone through November 8, 2011. To access the replay, dial 888-203-1112 in the United States and Canada, and 719-457-0820 outside the US; then enter the conference confirmation code 436-7480. The webcast will be archived on the Company's website for one year.

At this time it's my pleasure to introduce Bridgepoint Education's CEO, Andrew Clark.

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**Andrew Clark** - *Bridgepoint Education, Inc. - CEO*

Thank you, Paul, and welcome to Bridgepoint Education's third-quarter earnings call. On the call today I will review our operation results and business initiatives for the third quarter. Then Dr. Jane McAuliffe, our Chief Academic Officer, will update you on our academic programs and quality initiatives.

She will be followed by our Chief Financial Officer, Dan Devine, who will review our third-quarter financial results and key operating metrics. Following his remarks I will discuss our 2011 guidance in my closing comments.

For those of you on the call who may be new to our story, I would like to provide a brief introduction to the Company. Bridgepoint is an innovative educational services company that is using the power of both innovation and technology leadership to advance higher learning. Our institutions, Ashford University and the University of the Rockies, offer a practical and dynamic educational model to students seeking associate, bachelors, and graduate degrees online or on campus.

Our universities offer an especially enriching and engaging learning experience through a growing number of proprietary technology platforms including Constellation, which is our proprietary cloud-based digital learning platform that adapts educational resources to each student's learning style and needs; Ashford and Rockies Mobile, our mobile learning environments; and Waypoint technology, our proprietary assessment and (technical difficulty) platform.

These new innovations expand and enhance our efforts to offer students a broad selection of rigorous, engaging, and practical courses. As our enrollment and financial metrics indicate and Dr. McAuliffe's comments will demonstrate, we continue to serve the academic needs of our students at both Ashford University and University of the Rockies.

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Trends at both academic institutions reflect continued demand among a broad cross-section of working adults for our programs. As of September 30, 2011, total student enrollment was 90,597 students, an increase of 17.4% over the same period in the prior year.

New student enrollments for the third quarter of 2011 were approximately 22,000, reflecting a decrease of 8.3% over the same period in the prior year. As expected, new enrollments in the second half of 2011 are being affected by several factors including reduced admissions counselor productivity, resulting from the regulatory changes that were implemented on July 1.

As we noted in September, we experienced better enrollment trends during the third quarter than we assumed in the full-year guidance provided during our second-quarter earnings call in August. The third-quarter results we are reporting today and our outlook for the remainder of 2011 are in line with those improved expectations.

In September, we also stated that we expect to see new enrollments turn positive sometime during the second quarter of 2012, with full-year new enrollments, total enrollment, and revenues showing positive growth for 2012. We are reaffirming that view today.

We believe one of the reasons our institutions continue to attract students is that we have successfully used technology to drive learning outcomes and improve the student experience. A cornerstone of our success in this area is our proprietary Constellation platform.

Far more than an e-reader, Constellation is a cloud-based digital learning platform that enables our universities to deliver dynamic and individualized learning experiences based on each student's needs. As such, we believe it represents an important first step toward the development of a personalized learning experience for every student.

We continue to expand the number of courses being offered on Constellation, and I am pleased to report that as of September more than 65,000 of our current students have used Constellation. Most importantly, students like it and often ask for it when they take a course with a traditional textbook.

We have invested heavily in our predictive analytics capabilities using data from internal and external sources to assess learning styles and predict student outcomes. This allows us to suggest courses of action to improve learning, help potentially struggling students early in their classes, and overall provide the opportunity for improved student success. We expect these tools will be effective at helping ensure that the right students are admitted to our programs and receive the help they need to succeed.

Another area of focus is on making the college experience available to our students anytime and anywhere through mobile technology. In addition to Constellation, Ashford students can now access their classrooms, fellow students, instructors, and other advisers and administrative data on Apple and Android tablets and smartphones. We are proud of the enthusiastic reception our students have given Constellation and our mobile technologies, and I encourage you to read and compare their reviews on Apple's App Store.

Constellation, predictive analytics, and mobile learning technologies are only a few examples of how we are enhancing education through innovation. As a foundation for the future, we are instilling a culture of innovation on our campuses with our faculty and throughout our entire organization. This initiative, called [Innovation U], enables everyone to showcase their creativity and contribute to our progress in an online forum on everything from product updates and ideas to internal productivity enhancements.

Our commitment to innovation is already providing important benefits to our students and institutions, and this focus is a significant differentiator in providing a highly engaging and quality learning experience to students. We are beginning to incorporate these messages into more relevant and focused branding for Bridgepoint, Ashford, and University of the Rockies.



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By early December you will begin to see new visuals, logos, and messaging in many different venues. Our branding initiatives will support and inform our marketing communications and outreach channels and more effectively differentiate and position our institutions in their respective markets.

As one example of how we will deliver these messages, in January Bridgepoint will present Constellation to the higher education track at the Consumer Electronics Show. There, we will introduce Constellation and further engage with educators, publishers, and the technology community on the critical role technology and innovation can and must play, by enhancing academic quality and helping ensure positive student outcomes.

Taking a broader view of our accomplishments to date in 2011, our institutions have successfully managed through a major transition in how our industry operates. We have made significant progress on key initiatives. We have strengthened our support for students and faculty through innovative technologies. And we have enhanced transparency for prospective students.

We are pleased with this progress, and we believe we are increasingly well positioned to meet the educational needs of students. Now I would like to turn the call over to our Chief Academic Officer, Dr. Jane McAuliffe, to update you on several key academic areas.

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**Jane McAuliffe** - Bridgepoint Education, Inc. - EVP, Chief Academic Officer

Thank you, Andrew. Today I would like to comment on our improved third-quarter persistence; review the status of Ashford's move to WASC accreditation; and provide you with a few details about our efforts to ensure instructional quality through Quality Matters.

As Andrew said, we believe our enhancements to quality are visible to students through a better educational experience. And our success at leveraging technology to deliver stronger educational outcomes is increasingly differentiating our institutions' offerings.

We are pleased to report that we are continuing to see improving student persistence levels. Newly implemented programs and procedures are improving the academic readiness and persistence of our student body, enhancing the quality and value of our academic programs, and driving favorable performance outcomes we track. One such outcome is the large number of graduates we will have in 2011, more than 15,000, which is greater than the last two years combined. The leadership team had the wonderful opportunity twice this year to visit the Ashford campus for two graduation ceremonies, each of which was attended by over 5,000 students, friends, and family.

Our success with persistence and graduation is also due in part to our long-standing practice of seeking the highest quality prospective students, which is a practice that remains central to our recruitment focus. Having well-prepared students and maintaining high persistence levels are important goals for both of our institutions.

I want to provide you an update on accreditation for Ashford University. Having already established eligibility to move forward with an application for initial accreditation with the Western Association of Schools and Colleges, Ashford University continues its focused preparations for the submission of the WASC self-study in December 2011.

The self-study effort has brought university faculty, staff, and administrators together in positive, well-coordinated, and collaborative discussions to develop appropriate documentation on how the University demonstrates compliance with the current WASC standards for accreditation. This self-study process is a worthy process, as it allows University faculty and leadership to reflect on current practices and build towards the future.

As we have reported previously, Ashford University plans to host a visiting team from WASC in March 2012. Ashford's materials and the report of the visiting team will be considered by the WASC commission at a meeting following the on-site team visit

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and completion of the team's reports. A decision relative to Ashford's application for accreditation is expected to be made at that time.

The University leadership values its collegial relationship with the WASC staff as we work through each stage of this process. The President of the University also continues to keep the Higher Learning Commission informed of progress, in the University continues to be accredited by the Higher Learning Commission.

I am very pleased with how the University leadership has continued to move forward and commend them on their focus and dedication to this project.

As part of our many efforts to ensure quality, both Universities continue to expand their presence with Quality Matters, a nationally recognized, faculty-centered peer review process designed to certify the quality of online courses and components. Ashford now has a total of 329 courses approved. They also have 67 Quality Matters Certified peer reviewers among its faculty and staff; and of those, 10 are Master Reviewers.

The University of the Rockies has 61 courses approved. They have 55 faculty QM Certified peer reviewers, with three certified as Master Reviewers. With this number of certified faculty at both institutions, not only does this provide a better quality experience for our students, but this allows the faculty to share knowledge and review courses from other universities, which ultimately impacts students external to our universities.

Now I will turn the call over to our CFO Dan Devine, to discuss our third-quarter financial results.

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**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

Thank you, Jane. For the third quarter, revenue increased to \$242.8 million compared with \$190.9 million for the same period last year. The increase in revenue was primarily the result of an increase in student enrollment and a 5% tuition increase effective April 1 of this year.

As of September 30, 2011, total student enrollment was 90,597, an increase of 17.4% from the same period last year. New enrollments for the period, 22,000, as compared to 24,000 for the third quarter of 2010, which represents a decrease of 8.3% over the same period last year.

For the third quarter of 2011, instructional costs and services were \$69.6 million or 28.7% of revenue, compared with \$50.2 million or 26.3% of revenue in the same period last year. The increase as a percentage of revenue included increases for direct compensation for academic management and an increase in bad debt.

As a percentage of revenue, bad debt expense for the quarter was 7.1% versus 5.5% for the same period last year. The increase was primarily due to timeliness of financial aid processing and collection efforts as well as weak general economic conditions. We are enhancing our processes both internally and with our business partners to improve this metric.

Marketing and promotional expenses for the third quarter of 2011 were \$68.8 million or 28.4% of revenue, compared with \$55 million or 28.8% of revenue in the same period last year. The decrease as a percentage of revenue for the quarter was primarily due to decreases in advertising and allocated selling costs when compared to the same period in the prior year.

General and administrative expenses for the third quarter of 2011 were \$34.5 million or 14.2% of revenue, compared with \$23.3 million or 12.2% of revenue for the same period last year. The increase as a percentage of revenue for the quarter was primarily due to increases in administrative headcount in the areas of information technology and regulatory compliance when compared to the same period in the prior year.

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Included in our three main expense categories for the third quarter of 2011 is approximately \$3 million related to stock-based compensation expense in the aggregate, compared with \$2 million for the same period last year. For the third quarter of 2011, operating income increased to \$69.8 million from \$62.4 million in the same period last year.

Our effective tax rate for the quarter ended September 30, 2011, was 37.8% which is lower when compared to the 42.4% for the same period last year. The decrease is primarily due to the impact of California and other state tax law changes that took effect in 2011.

Net income for the third quarter of 2011 was \$43.8 million or \$0.78 per diluted share, compared with net income of \$36.1 million or \$0.61 per diluted share for the same period last year. Fully diluted EPS is calculated based on a diluted share count of 56.4 million shares for the third quarter of 2011 compared with 59.3 million shares for the same period in 2010.

During the third quarter of 2011, we repurchased approximately 1.7 million shares of common stock at a weighted average purchase price of \$21.82 per share, for a total cost of \$36.4 million, which effectively concludes the stock repurchase program authorized by our Board of Directors. The impact of the third-quarter repurchases on fully diluted EPS for the quarter was \$0.01 per share. As of the end of the third quarter, we have repurchased a total of 7.3 million shares at a weighted average share price of \$18.62 per share.

As of September 30, 2011, we had a total cash, cash equivalents, short- and long-term marketable securities of \$344.7 million compared with \$299.1 million as of December 31, 2010. The Company generated \$148.7 million of cash from operations for the nine-month period ended September 30, 2011, compared with \$115.2 million for the same period in 2010.

As of September 30, 2011, our accounts receivable, net of allowance for doubtful accounts, was \$87.7 million which represented 33 days sales outstanding on a quarter-to-date basis compared with a 36 days sales outstanding for the same period last year. Capital expenditures for the nine-month period ended September 30, 2011, were \$24.4 million compared with \$18.5 million for the same period last year.

Now I'll turn the call back over to Andrew for our 2011 guidance.

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**Andrew Clark** - *Bridgepoint Education, Inc. - CEO*

Thank you, Dan. As I mentioned previously, we are pleased with our performance through the first three quarters in 2011. As we look toward the remainder of the year we are updating our annual guidance for the year ending December 31, 2011, as follows.

Total student enrollment at year-end is expected to be between 83,000 and 85,000. Revenue is expected to be between \$920 million and \$926 million. Net income is expected to be between \$168.5 million and \$170.3 million.

Fully diluted earnings per common share is expected to be between \$2.95 and \$2.98, based on an estimated fully diluted weighted average share count of 57.1 million for the year ending December 31, 2011. Bad debt as a percentage of revenues for 2011 is expected to be 6.1%. Capital expenditures for 2011 are expected to be approximately 4% of revenue.

The Company's effective tax rate for 2011 is estimated to be 37.7%. This guidance assumes no further share repurchases in 2011.

Our conference call today once again demonstrates our commitment to the long-term success of our students, our academic institutions, and our investors. We believe it also demonstrates our success in using innovation and technology to enhance the student educational experience and differentiate our offerings.

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Throughout this period we have continued to deliver the outcomes that matter to students, and we have expanded our commitment to the enhancement of learning through innovation. We believe that these things above all else underpin our position in the industry as an important provider of quality postsecondary education.

At this time I will ask our operator to open the phone lines for your questions.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Jeff Silber, BMO Capital Markets.

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### Jeff Silber - BMO Capital Markets - Analyst

Thanks so much. I wanted to talk about your enrollment and revenue guidance. I guess looking at the implied guidance for the fourth quarter, it looks like we are going to see a pretty sizable sequential drop in revenues. I am just wondering what is causing that.

Is it enrollments? Are you seeing starts declining, getting worse? Is revenue per student going down? Any color you could provide would be great.

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### Dan Devine - Bridgepoint Education, Inc. - EVP, CFO

Jeff, this is Dan. Sure. So there's a couple components in the fourth quarter. One, and if we are talking sequentially --

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### Jeff Silber - BMO Capital Markets - Analyst

Yes.

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### Dan Devine - Bridgepoint Education, Inc. - EVP, CFO

You see a decline of I think \$26 million sequentially, you kind of roll it into the end of the year. Two components. Fourth-quarter revenue per student is always lower. There's less revenue days in the fourth quarter; you can see that prior year.

We also sequentially are expecting lower new enrollments in the fourth quarter. That is because we stopped enrolling people for 2011 beginning in early November, and we move those students after the holidays -- so that they're not distracted by the holidays -- into January.

So the new enrollment number will be down. It will be down year-over-year from the prior year. Prior year was 15,600. We expect that the decline will be greater than the decline we incurred in Q3. So there is a piece of information for you.

And then they are basically the components. Now, also we had a high retention for Q4 of 2010, or a high persistence rate; and I think we are taking a conservative view on that. So that would also contribute a little bit to lower revenue in the quarter.

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**Jeff Silber** - BMO Capital Markets - Analyst

All right. That's very helpful. And as a follow-up, there has been a lot of noise in the market and the media about what is going on, on the military side, in terms of potential cuts in tuition assistance. I know military is a relatively small component of what you do.

But I am wondering what you are hearing. Have you seen any impact on your military enrollment because of all this? Thanks.

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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, sure, Jeff. This is Andrew. That's a great question.

The news in the military has bounced around a little bit over the past three or four weeks as you know, and we did see an impact a little bit early on. And then we saw -- in terms of fewer Marines enrolling into our program.

But then we saw that come back pretty significantly when they reversed course. So it kind of bounced around a little bit.

I think your point that you made is an important one for us to emphasize, which is that it is a relatively small percentage of our revenue. So we don't view Bridgepoint to have a lot of exposure in that regard.

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**Jeff Silber** - BMO Capital Markets - Analyst

All right, great. Thanks so much.

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**Operator**

Trace Urdan, Wunderlich Securities.

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**Trace Urdan** - Wunderlich Securities - Analyst

Hey, good morning. Wondered if you guys could speak to the disruptive impact of changing the enrollment counts or compensation, where you feel you are in that transition in terms of the scale of the impact, and whether you feel like any of the testing that you did early on there may have made a difference.

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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, sure, Trace. It's a great question. I think that the piloting that we did early on was very beneficial and helped give us a lot of insight. But there is no substitute for getting 100% of your admissions counselors on to the plan.

The biggest -- and the challenge is really a management challenge in terms of managing the admissions counselors under a new plan. As you know, our plan is very straightforward. They get an increased cost of living increase; an increase for tenure; and then if the admissions counselor improves their own education -- they get a bachelor's degree or a master's degree -- they get a one-time increase for that.

So I would say we are pleasantly pleased with how that transition has occurred through the third quarter, and how management has learned and adapted to the changes in managing the admissions counselors. Really what we are looking for in our admissions counselors is a group that is intrinsically motivated by the opportunity to improve the lives of the students that they work with. So we focus on that from a hiring perspective, and we certainly focus on that from a management perspective.

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We are pleased with how the quarter has gone. And we have a pretty, I think, positive view about how that will continue to look in the fourth quarter. As we mentioned, in 2012 we expect our new enrollments to turn positive during the second quarter, and then certainly positive for the back half of 2012 and ultimately for the full year.

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**Trace Urdan** - *Wunderlich Securities - Analyst*

Okay. Then if I could ask one more, I just also was wondering if you could speak to what sort of an impact you believe Constellation has had on revenue per student on a year-over-year basis. And then maybe if it is possible, over the last couple of years.

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**Dan Devine** - *Bridgepoint Education, Inc. - EVP, CFO*

Well, over the last couple of years it has had an impact. It continues to -- the impact, obviously more and more students are using Constellation.

The specific dollar impact? I think if you were to do it -- the way I have explained it before is, okay, your average student takes about six courses per year, for example. If you had 100% of your population using Constellation you would have \$75 for six courses during the year. We are currently expecting that we're exiting this year at I think 50%. Right? 50%-ish?

And then, so it would be -- your total population midpoint times 50%, times \$75 would give you kind of a top-line impact. We expect that impact to grow to about 80% in 2012 as we complete the rollout of courses using Constellation.

So it has had an impact. I don't think it has had a huge, material impact in the revenue per student per month.

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**Trace Urdan** - *Wunderlich Securities - Analyst*

Okay. Thanks, Dan.

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**Operator**

Brandon Dobell, William Blair.

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**Brandon Dobell** - *William Blair & Company - Analyst*

Thanks. Looking for a little more color or commentary on what seems to be a pretty good persistence or retention quarter, I guess from a couple points of view. One, are you seeing outsize improvements on the front end? So students that are there one, two, three courses.

Or is it more apparent on students that have been there a year or between a year and two years? Thanks.

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**Andrew Clark** - *Bridgepoint Education, Inc. - CEO*

Sure, Brandon. I am going to let Jane start with her observations on what has contributed to the great persistence we had during the quarter, and then I will expand after she makes her comments.

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**Jane McAuliffe** - Bridgepoint Education, Inc. - EVP, Chief Academic Officer

Hi, Brandon. I think we are starting to see the effects of all the work that we are doing upfront. If you think about the quality initiatives we put into place with the orientation; with required attendance in the beginning courses; how we walk our students to class and make sure they are prepared and are comfortable in that learning environment.

So by the time they get there, all that upfront preparation has really given them a sense of confidence that they can succeed and they can achieve and they know what to expect. So we think that is having a good impact for us.

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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, and I would just emphasize, Brandon, that as I said in my opening remarks, we made a tremendous investment into data analytics and into that group internally within the organization, and predictive modeling, and really understanding the characteristics and the behaviors of students that ultimately are successful academically and end up graduating from our institutions.

While we have been at it for some time I think we still have more opportunity there. But I think that that investment that we have made already in that area has benefited us.

You have seen all of the things that Jane has done from a quality perspective, and how that has enhanced our persistence for I believe it is five out of six quarters, of the last six quarters. And we believe that there is still more opportunity for improved persistence.

And this is coming off of more difficult comps, effectively. Last year, our persistence increased all the way through to the first quarter of this year. Our second quarter was down 70 basis points; and then you saw this quarter and how well we did.

So I think that even with increased students graduating, even with difficult comps, all the quality initiatives and data analytics, predictive modeling we are doing are going to lead to an opportunity to see improved persistence in 2012.

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**Brandon Dobell** - William Blair & Company - Analyst

Fair enough. Then on the last couple of calls from some of your peers there has been a healthy amount of commentary about the delta between inquiries or applications and show rates, regardless of platform, age group, what have you.

Any commentary there just comparing how the application flow has been relative to what your show rates or start rates have been? Thanks.

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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, I would say that the applications and interest in our institutions has been relatively the same, pretty consistent. Certainly consistent with our expectations.

The show rate has declined slightly as you would expect. It's absolutely correlated to the admissions counselor decline in productivity. So that is an area that I know that our management team is continuing to focus on and looking for ways to improve that show rate and have it be more in line with what it has been historically.

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**Brandon Dobell** - William Blair & Company - Analyst

Okay. Thanks a lot.

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**Operator**

Andrew Steiner, JPMorgan.

**Andrew Steiner** - JPMorgan - Analyst

Hi, there. In the implied fourth-quarter guidance, I think the operating margin comes out somewhere between 14% and 15%. That is pretty much down significantly sequentially.

Is that mostly driven by the revenue decline that you already spoke about? Or are there any expenses, particularly in the fourth quarter, which ramp relative to the third?

**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

It is primarily driven -- the majority of that results from the sequential decline in revenues. If you look at the growth in expense quarter over quarter is consistent with what the growth in expense was in Q3 over Q2, with the exception of the growth in instructional cost spend is flatter in Q4 than it was in Q3. So it's primarily driven by the change in the revenue.

**Andrew Steiner** - JPMorgan - Analyst

And aside from the branding initiatives, are there any larger marketing investments on the near-term horizon?

**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, Andrew, this is Andrew. Great question. We would absolutely have some larger expenditures in that regard during the fourth quarter. So I think you could expect that during the fourth quarter.

Then certainly Dan and I's view is that we will continue to make an investment in that area throughout 2012 and beyond. I would expect that we would see that show up within sales and promotion as a percent of revenue in 2012. I would expect that between admissions counselor productivity and our branding initiatives, that you would see that be higher than it has been in 2012 and than it was in 2011.

**Andrew Steiner** - JPMorgan - Analyst

Okay. Thanks so much. Appreciate it.

**Operator**

Peter Appert, Piper Jaffray.

**Peter Appert** - Piper Jaffray - Analyst

Thanks. So, Andrew, I was hoping you might be able to give us just a little more color on the productivity issue around enrollment counselors, in terms of just how you see this playing out over the next couple of quarters. In particular I guess the question comes from the fact that you indicated that you think, I think, productivity maybe is turning out to be a little better than you had initially anticipated; yet the start impact is still pretty negative near-term.



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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, well, sure, Peter. Be happy to provide a little bit more color on that. The start impact in the near-term is actually more favorable, certainly in the third quarter and then for the remainder of the year, than what we had initially modeled, back in the end of the second quarter. And even going to back to the beginning of this year when we were putting our thoughts together for the full year.

So I think we are very pleased with how it is looking. Certainly our negative new enrollment declines are, I think for the most part, less than what others in the sector have experienced. So I think that has a lot to do with the preparation that we did in piloting, as well as just the overall value proposition that we bring to prospective students.

With that said, it is definitely as I've characterized in conversations throughout the last 90 days, it is definitely a transition period. Our management team in the admissions area has I think done a very effective job in working through that transition with admissions counselors. We have a lot of confidence in the management of those admissions counselors and that we will see improvement beyond what we are just talking about towards the end of the year.

For example as I commented, we expect new enrollments to turn positive during the second quarter, sometime during that quarter. What gives us that confidence is what we have seen throughout the third quarter and what we see going into the fourth.

**Peter Appert** - Piper Jaffray - Analyst

So safe to assume that the December quarter would be the trough in terms of the largest year-to-year decline in terms of starts?

**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, that would be safe to assume. It's important to remember that our fourth quarter has obviously a tremendous amount of seasonality to it. What our fourth quarter looks like is not unlike what it looked like in previous fourth quarters in previous years.

So I wouldn't view our fourth quarter this year in 2011 as being really much different in terms -- at a high level -- from 2009's fourth quarter, 2010's fourth quarter.

**Peter Appert** - Piper Jaffray - Analyst

Got it. Thank you.

**Operator**

James Samford, Citi.

**James Samford** - Citigroup - Analyst

Sure, just a quick question. I hate to go back on this again, but as far as persistence goes and some new start trends in Q4, it looks like it's going to be significantly more than the 80% decline that you saw this quarter. That just sort of is depending on what the persistence rates are.

You could have down 25% to down 35%, I guess. Is my math wrong there? Or how should I be thinking about that?

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**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

Your math is -- I don't want to say it's wrong, but it is inconsistent with what we are viewing it. We would expect that the decline in the quarter -- I am sure you -- it sounds like you are using a flat favorable persistence in Q4.

**James Samford** - Citigroup - Analyst

Yes, if I do plus or minus 1% --

**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

That's your -- you have to be conservative on your persistence.

**James Samford** - Citigroup - Analyst

Okay.

**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

And it's not -- I will say the decline will not be 25% in new enrollments in Q4.

**James Samford** - Citigroup - Analyst

Great. That's really helpful. I guess a quick question for Jane. It sounds like the -- just wondering how you are leveraging predictive analytics.

Is that relatively new? ARE you seeing any sort of -- anything you can comment on as far as whether it is persistence or just quality of learning experience right now?

**Jane McAuliffe** - Bridgepoint Education, Inc. - EVP, Chief Academic Officer

It is new. We are excited to be looking at some of that initial data, and the teams are really going to use that to make some quality decisions within the classroom, within their instructional practices, within the day-to-day support for students from an academic perspective, and where we might be able to jump in and coach them as far as what we are seeing and what behaviors we can tend to see across-the-board with all students, and how those trends can help better inform how that student can be successful himself in the classroom.

So it is new for us, and we are just excited to get it rolling and to start using some of that data.

**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, I mean I would just add to Jane's comments that there is a tremendous amount of insight that we have gained from that investment, and we are just at the beginning. So we expect that we are going to have even further insight that is going to lead to even more improvements, as Jane mentioned.



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It's very exciting for us as an organization and for our institutions to be able to have that predictive capability and to proactively reach a student before they start having some significant type of issues that might lead them to dropping out of the institution.

**James Samford** - Citigroup - Analyst

Are those internally generated tools, or are you using somebody from outside for that?

**Andrew Clark** - Bridgepoint Education, Inc. - CEO

It is all internally generated. As I mentioned, we have spent quite an investment in terms of investing in people and a department as well as the tools to measure student behavior and characteristics and do that predictive modeling.

**James Samford** - Citigroup - Analyst

Great, thanks.

**Operator**

[Gerald Price], [High Analytics].

**Gerald Price** - High Analytics - Analyst

Hey, good morning, guys. I just have a quick follow-up question to Jeff's question at the beginning of the call on military funding. Could you provide just some additional color on how easy it would be for Bridgepoint to fill a funding gap if TA is cut?

**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Well, there are other options out there available to military students, obviously. The fact many of the -- not many, but some of our military students currently use some of those other options including Title IV. So there are other funding options that are available. I -- we have seen military students take advantage of those in the past, and I think they would continue to do that in the future.

**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

Are you --?

**Gerald Price** - High Analytics - Analyst

Thank you.

**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

Was your --? Okay.

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**Operator**

Mike Malouf, Craig-Hallum.

**Mike Malouf** - *Craig-Hallum Capital - Analyst*

Great. Thanks for taking my call. The cash continues to build even after the successful buyback in the third quarter. Can you just give us a sense on the uses of cash going forward, and whether or not buyback is on the horizon? Thanks.

**Andrew Clark** - *Bridgepoint Education, Inc. - CEO*

Yes, sure. This is Andrew. We continue to evaluate every single quarter our use of cash and the appropriate use that will provide the best return to our shareholders. So really when we do that evaluation we look at all options.

I can't really comment beyond that. Obviously, we have historically felt that the Company has been undervalued and there is tremendous value for the Company in purchasing back our stock.

**Mike Malouf** - *Craig-Hallum Capital - Analyst*

Then just a quick follow-up question on bad debt. That obviously moved up a little bit in the quarter.

Do you expect that to keep going? How high do you expect that bad debt could get? And are there any initiatives that you are doing to sort of cross that back down?

**Dan Devine** - *Bridgepoint Education, Inc. - EVP, CFO*

Sure. You know, we expect -- we feel that the bad debt issue is primarily an internal process issue. We are addressing those processes, enhancing them, improving staffing or product procedures where they need to be improved.

The expectation for the fourth quarter is that bad debt will be in aggregate dollars less than it was in the third quarter. So, we are making -- we intend to make progress on that metric going forward.

**Mike Malouf** - *Craig-Hallum Capital - Analyst*

Great. Thanks a lot.

**Operator**

Gary Bisbee, Barclays Capital.

**Zach Fadem** - *Barclays Capital - Analyst*

Hi, it's Zach Fadem for Gary. Question on Constellation. What is your target for having it rolled out 100% across all of Ashford? Do you see it improving your profitability over the near term and over the long term? Thanks.

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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, sure, Zack. I will talk to the first part of and let Dan answer the second part. Our view and focus is that we get Constellation rolled out to 80% of our students by the end of 2012.

Really the way that it works, we do have a some courses that are in a major that have a very small number of students in them, and it doesn't financially make sense in those particular courses for us to go to the expense of building a textbook for just those courses. That is kind of how we get to the 80% and we don't get up to 100%.

For that last 20% in those much smaller courses, our view would be to try and use publisher content that is digital and provide that to our students -- but through Constellation. But it wouldn't be our own content that we develop, as all the other content is. Dan?

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**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

Yes, sure. As far as the profitability of Constellation, we have said this before. It is more profitable than our overall margin for the Company, but not significantly. There is a fair amount of investment internally related to that product. We have a big development staff, some IT personnel assigned to that.

As we roll all of these classes out, what you do is you start over and you update all the classes. So there is an ongoing expense related to that product as well.

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**Zach Fadem** - Barclays Capital - Analyst

Okay. Thanks a lot. One other question. Just can you give me an update on what your current marketing mix is, and whether you are shifting that or whether you look to shift it over the next year?

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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Well, I mean our current marketing strategy is primarily a digital interactive media strategy. We have other channels by which we have prospective students, whether it's through companies that we work with, through community college articulation agreements, through the military, through referrals that we get from students that are really pleased with their experience at our institutions.

I think the way that the mix would change in 2012 and beyond is just again a strategy all around branding for those institutions. That strategy would be comprehensive, so it would include both traditional media as well as social media, or new media, so to speak. So you would see a broadening of the mix throughout 2012.

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**Zach Fadem** - Barclays Capital - Analyst

Great. Thanks a lot.

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**Operator**

(Operator Instructions) James Samford, Citi.

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**James Samford** - Citigroup - Analyst

Sure, just a quick question on any kind of color between new start trends among bachelors and graduate.

Also any comment on trends you're seeing in the online fraud ring issue that was raised during the quarter? I know that's been around for a while, but just wondering what you can and have been doing to combat that. Thanks.

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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, sure. Starting with our trends in bachelors and graduate students, we have seen that to be pretty consistent throughout 2011. I think you have seen our graduate student population increase from 9% to about 11% of our total enrollment from 2010 to 2011. So you do see that mix changing a little bit for us as an institution.

In terms of your question about fraud rings, I guess I would first describe that we have a practice that has been in place for some time now internally where we identify any student who we think might be participating in such a ring. We are very pleased with the process we have. It has yielded some students -- I wouldn't say it's a material amount by any means -- but some students that are participating in that.

We make sure if the group is large enough to refer those cases directly to the OIG for the Department of Education. So I would say that we are very vigilant about monitoring our student body for anything in those regards.

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**James Samford** - Citigroup - Analyst

Perfect. Thanks.

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**Operator**

Kelly Flynn, Credit Suisse.

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**Kelly Flynn** - Credit Suisse - Analyst

Thanks. My question is for Dan about cash flow. As cash flow lags net income significantly this quarter, I think there are a lot of moving parts there. But could you just give us some guidance on how you expect cash flow will track earnings.

And then particularly maybe touch on accounts receivable and deferred revenue and some reasons why that might improve from here. Thanks.

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**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

I read your note this morning, so I am prepared for your question.

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**Kelly Flynn** - Credit Suisse - Analyst

Thank you.

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**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

The issue in the third quarter compared to the third quarter of 2010, the timing between Q2 '10 and Q3 '10, and Q2 '11 and Q3, it was kind of flip-flopped. So we actually did better in Q2 '11 than Q2 '10; and we did worse I guess in Q3.

Year to date, our free cash flow is up 28% year-over-year, and our earnings are up 30%. So we are still tracking to a fairly decent match of earnings increase and free cash flow.

But we had some timing issues backing Q2 of 2010. There were some transitional issues related to how we were receiving our Title IV funds, and we took a tremendous amount of Title IV funds in, in July of 2010. I don't know if that helps you.

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**Kelly Flynn** - Credit Suisse - Analyst

Yes, but what about going forward? Should we think about it as tracking net income growth? Or I imagine deferred might be more of a drag in the near term. How should -- I guess the question is just, yes, how should we think about cash flow versus earnings in the next year?

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**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

I would expect that it would trend as it has in the past. It does -- which is, it tracks -- so this year I would say where it is this year, which is pretty flat to earnings, same level of growth. Whatever last year's --

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**Kelly Flynn** - Credit Suisse - Analyst

Okay, great. Then, I know we're running out of time but just quickly on military, I know you have gotten a number of questions on it. Andrew, you said the exposure is modest. But I think you have significant exposure to military.

So can you just, I guess for the record, quantify I guess as a percentage of enrollment and revenue military exposure, both TA and veterans, and how you think about that exposure moving forward? Thanks.

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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, sure. Well, first of all, Kelly, from an enrollment perspective, the military enrollment makes up about 18% of our total enrollment. And that has been fairly consistent. In fact if you look at 2010 and then 2011, that percentage has remained pretty much flat year-over-year.

In terms of percentage of revenue, I will let Dan take that.

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**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

Yes, the other two components of your question were percentage of revenue. We don't give out the percentage of exact revenue that the military components contribute.

Then your third part of that question was, what is the mix between VA, TA? In our 18% we include, obviously, TA individuals; we include VA individuals; and we include spouses and DOD employees, which effectively are partially reimbursed depending on what plans they use. So that is what makes up the 18% of total enrollment.

I can tell you -- I think we have given this kind of figure out before. It is probably 40% TA; 30% VA; 30% spouse/DOD.



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**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Yes, and so just following up on that, Kelly, I wouldn't agree with your characterization that we have significant exposure there to the military. I think our view is that our exposure there is pretty equivalent to most every other public education company that we are aware of.

**Kelly Flynn** - Credit Suisse - Analyst

Okay. I just meant significant as a percentage of enrollment. But regardless, thank you very much for that color. It's very helpful. I appreciate that.

**Andrew Clark** - Bridgepoint Education, Inc. - CEO

Thank you.

**Dan Devine** - Bridgepoint Education, Inc. - EVP, CFO

Thank you.

**Operator**

And at this time we have no further questions in the queue.

**Andrew Clark** - Bridgepoint Education, Inc. - CEO

All right. Well, I want to thank everybody for joining our earnings call. We will look forward to speaking with all of you next quarter.

**Operator**

This does conclude today's conference. We thank you for your participation.

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