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Grand Canyon Education, Inc. (LOPE)

Q2 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon and thank you for standing by. Welcome to the Second Quarter 2022 Grand Canyon Education Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speakers' presentations, there will be a question-and-answer session. [Operator Instructions] Please note that today's conference is being recorded.

I would now like to hand the conference over to your first speaker today, Dan Bachus, Chief Financial Officer. Please go ahead.

Daniel E. Bachus
Chief Financial Officer, Grand Canyon Education, Inc.

Joining me on today's call is our Chairman and CEO, Brian Mueller. Please note that many of our comments today will contain forward-looking statements that involve risks and uncertainties. Various factors could cause our actual results to be materially different from any future results expressed or implied by such statements. These factors are discussed in our SEC filings, including our annual report on Form 10-K, quarterly reports on Form 10-Q, and current reports on Form 8-K. We undertake no obligation to provide updates with regard to the forward-looking statements made during this call, and we recommend that all investors review these reports thoroughly before taking any position in GCE.

In addition, during today's call, we will discuss non-GAAP financial measures which we believe are useful as supplemental measures. These non-GAAP measures should be considered in addition to and not as a substitute for or an isolation from GAAP results. You can find additional disclosures regarding these non-GAAP measures, including reconciliations with comparable GAAP results in our Form 8-K filed today.

And with that, I will turn the call over to Brian.

Brian E. Mueller

Chairman & Chief Executive Officer, Grand Canyon Education, Inc.

Good afternoon and thank you for joining Grand Canyon Education second quarter fiscal year 2022 conference call. Service revenue was $199.8 million for the second quarter of 2022, a decrease of $1.7 million or 0.9% as compared to the $201.5 million for the second quarter of 2021. The decrease year-over-year in service revenue was primarily due to a decrease in online enrollments at GCU and to a lesser extent, students in a university partner's Occupational Therapy Assistants program of 34%, partially offset by increases in GCU's traditional campus enrollments, university partner enrollments in the Accelerated Bachelor of Science in Nursing programs and revenue per student year-over-year.

Operating income for the three months ended June 30, 2022 was $33.8 million, a decrease of $16.4 million as compared to $50.2 million for the same period in 2021. The operating margin for the three months ended June 30, 2022 was 16.9%, compared to 24.9% for the same period in 2021. The operating margin was negatively impacted by the investments that are being made to grow our partner enrollments. Net income decreased 48.3% to $25.6 million for the second quarter of 2022, compared to $49.5 million for the same period in 2021. The decline in net income was partially due to a significant reduction in interest income between years due to GCU paying off the secured note in the fourth quarter of 2021. GAAP diluted income per share for the three months ended June 30, 2022, is $0.80. As adjusted non-GAAP diluted income per share for the three months ended in June 30, 2022 is $0.85 or $0.01 over consensus estimate.

I want to start by putting our current performance within the context of the overall trends that exist in higher education today. While the trends I'm about to discuss are not positive, Grand Canyon Education strategy places itself and its partners in a differentiated and very strong position going forward. One, according to the National Student Clearinghouse Research Center, the percentage of 2020 high school graduates who immediately enrolled in college dropped by 6.8% last fall during the height of the COVID-19 pandemic, a decrease that was four times greater than the pre-pandemic, negative 1.5% for graduates in the fall of 2019. The pandemic disproportionately affected graduates of low income, high-poverty and high minority high schools, with their enrollments dropping more steeply than the more affluent counterparts. For instance, the decline in immediate college enrollments by graduates from high-poverty high schools minus 11.4% was four times larger than compared to graduates from low-poverty schools at negative 2.9%. And among graduates from high minority high schools, college enrollees in 2020 decreased 9.4%, compared to a 4.8% decline from low minority school graduates.

Three, enrollment at private, non-profit four-year institutions saw a decrease of 5.2% in 2020, compared – higher than the 3% drop at public four-year colleges. Four, according to Inside Higher Ed, as in so many spheres of life, COVID is having an accelerated impact on already concerning trends. For higher education, these sober statistics are acute signals of decades long enrollment decline of 13%, and with the number of high school graduates projected to decrease from 2017 through 2037, college enrollment challenges have just begun.

Five, according to the Wall Street Journal, the number of colleges closing in the past 10 years, around 200 has quadrupled compared with the previous decade. Six, in the past four years, there have been 95 college mergers, compared with 78 over the past 18 years. Seven, in 2019, 51% of American adults considered a college degree to be very important, down from 70% in 2013, according to a Gallup poll. Positive perceptions of college among adults 18 to 29 fell the fastest of any group to 41% from 74%.

Eight, lower demand has pushed some to handout more scholarships and grants in the 2021-2022 academic year. Students paid just 45.5% of the sticker price on average, the lowest ever, according to the National Association of College and University Business Offers (sic) [National Association of College and University

Business Officers] (00:07:07). And finally, the US government gave $76 billion in aid to colleges and universities to shore up their balance sheet as COVID-19 swept the country. That money delayed some hard decisions, said Robert Zemsky, a professor of higher education at the University of Pennsylvania. He predicts that 500 four year colleges and universities will close in the next year. There's obviously widespread dissatisfaction with higher education as an institution and the perceived value of the investment. Since GCE became a service provider, we have been saying consistently college is too expensive, students are taking on too much debt as tuition levels go up, diversity especially socioeconomic diversity goes down and academic programs take too long to complete adding to student debt levels.

In addition, academic programs are not tied directly enough to where the economy is going and where the jobs and careers of the future are going to be. Consolidation within higher education industry that many have predicted for at least 10 years is now taking place at accelerated rates. In the past, small and elite has dominated in places like U.S. News and World Report Rankings. In the future, large, affordable, extremely flexible in terms of delivery models and very workplace relevant will dominate in the new world of higher education. GCE and its partners have weathered the challenging times well, have made significant investments, and will continue to invest in programs, technology and people, and look forward to a very promising next 10 years.

In this context, I want to review the four pillars of Grand Canyon Education. First, GCU's traditional campus saw an increase of 5.7% in new students in the fall of 2021 over prior year, an increase of 9.5% in total enrollment and an increase of 36.1% in residential enrollment. The momentum continued in the spring of 2022 as new enrollments were up 39.6% over the prior year. Approximately, 70.3% of ground traditional students now live on GCU's residential campus. The average incoming GPAs at the 2021-2022 class rose to 3.6%, and the prestigious Honors grew 8.4% with average incoming GPAs of 4.1%.

We anticipate approximately 9,700 new students this fall with an average incoming GPA of 3.6% and an increase in the Honors College to 3,100 students with an average incoming GPA of 4.1%. The retention of returning students this fall will be even better than expected bringing the total on ground student enrollment body to just at about 25,000. With the larger percentage of those students choosing to remain on campus, resulting in university having to turn away some new students due to lack of beds. This, in spite of the fact that university built two new residence halls and repurposed a residence hall that was used to house prospective students. So, in essence, added three residence halls. These are remarkable results given the overall trends. The quality and the relevancy of GCU's academic programs, the low class sizes and support of its faculty that has less than a 5% turnover rate. The quality of counseling services. A new, very modern campus is ranked 18th in the country by Niche.com. The 20 advisory board with over 500 companies represented who are creating internships and employment opportunities for GCU students. And the very affordable tuition which hasn't been raised in 15 years, results in these students taking out less debt than the average state university students. These are all important contributing factors.

I also want to mention, unlike the national trend that is going on across the country, GCU expects over 3,000 of the 9,700 new students this year will be first-gen college students. These students are largely from the lower socioeconomic strata, but their enrollment at university because of the very affordable tuition rate is going directly against the national trend and is a very positive part of the GCU GCE story.

Pillar two, working adult students attending GCU online. As with traditional students attending universities across the country, 2021 saw a downturn in working adult students attending online. Unlike with traditional students attending GCU's campus, we experienced the downturn in online students as well. GCE has worked with GCU on two main strategies to combat the downturn and we are now seeing signs pointing towards positive growth again. Number one, we have invested in B2B strategies that are well-timed for this post-COVID period. The supply and demand at least in the short run educated labor has flipped. Since the country has reopened, we are working with over 23,100 industry partners in K-12 education, healthcare, financial services, social service agencies, technology and engineering companies, military bases, et cetera, developing custom strategic initiatives that are helping organizations grow their talent from inside. The number of information meetings scheduled and the attendance at the meetings now exceed where we were prior to the pandemic.

Number two, GCE continues to work with GCU to roll out new and relevant programs. Since the transition four years ago, GCU has rolled out 66 new programs, emphases and certificates. This is a remarkable accomplishment. These new programs have enrolled 19,843 new students. We are still running behind the number of counselors we have budgeted. But despite that, we are currently projecting new enrollment growth, in the mid-single-digits, in the second half of the year. It is important to note that this return to positive growth will be accomplished with no loss of strength in the quality of GCU's online student body. And as a result, no degradation of the quality metrics, including good graduation rates, cohort default rates reaching 5%, well below the national average and continued low student debt levels.

Next, I would like to discuss GCE's third pillar, its healthcare partnerships. Short-term, COVID has had a negative impact. Hospitals were extremely busy, preoccupied with COVID patients and many clinical placement opportunities were cancelled. Despite these very significant challenges, many instructional assignments requiring one-on-one clinical interaction in the hospital were replaced by simulations. Some of our university partners requested that we reduce the cohort sizes for 2022 due to concerns about the lack of clinical capacity, and some of the new sites that we hoped to open, especially in large markets have been pushed back to 2023.

We are disappointed in the second quarter enrollment number, but positive signs are emerging. We were only able to open four new locations between January 2021 and May 2022. We are currently planning to open 14 new locations between May 2022 and September 2023. Six in the second half of 2022 and eight in 2023. As a recent example, the State of Washington approved the university partner to open its first location in Seattle just a few months ago, and with very limited marketing, we were able to fill the entire cohort for this fall and the spring cohort is almost full. The other new locations that are scheduled to open this summer or fall of 2022, including GCU's locations in Las Vegas and Salt Lake City are off to a good start. We are optimistic that our partner in Southern California will be able to start its first cohort in the fall of 2023, and there are mature locations that had declines in total enrollment year-over-year will be back to full capacity by the end of 2023. I'm also very pleased to announce that the GCU locations grew 84% year-over-year from 176 students to 324 and that their first 71 graduates passed the NCLEX examination with a 100% first time pass rate. This is extremely important because GCU would ultimately like 40 of our 80 locations to be GCU locations. This relationship is good financially for GCU, but is also good for GCE given GCU's national footprint and brand recognition, the excellence of its nursing program, and its proven ability to scale.

As with GCU's traditional campus, the long-term environment is very positive for these GCE healthcare partnerships for the following reasons. Number one, the country needs 1.3 million additional nurses for the next five years alone. Nursing programs are very expensive to operate, and given the financial pressures facing many universities, they will be unable to invest the dollars it will take to scale the programs.

Number two, GCE has the capital to invest in the continued build out to eventually 80 locations. Three, in addition to the runway of 80 locations, up from 30 (sic) [32] locations currently, our enrollment budget for this coming year is only 50% of the actual spots that exist today. The 50% shortfalls due to the lack of efficient and highly supported prerequisite course environments. Regulatory issues creating slowdowns in opening plan locations and the lack of clinical placements due to COVID issues. GCE is working hard, investing in new enrollment simulation, virtual reality and prerequisite strategies to in the future fill all the spots that are available. This is a transitional year coming out of COVID-19 for the healthcare partnerships. However, there is a 10-year runway that is very promising that creates a winning scenario for students, that want into a promising career, healthcare providers desperately needing professional nurses and universities who want a low risk way to help solve the nursing shortage while at the same time creating additional revenue streams.

Last, as we discussed on last quarter's call, we continue to work on a new pillar. We're extremely excited because it's desperately needed in higher education today. In collaboration with our largest partner, GCU, we are developing accelerated certificate programs and the first three have or will roll out in the next couple of months. Two of the certificate programs are for students who want an efficient way to get into nursing school. We believe there's a big opportunity here. Getting prepared academically to apply to nursing school can be a daunting and confusing process. First, a pre-nursing certificate program allows recent high school grads to stay home and take the first 60 credits of your bachelor's degree completely online. GCU has worked with GCE to design state-of-the-art science courses that will prepare students to apply for a spot in eventually one of GCE's 80 locations. These courses will be taught mainly by full-time faculty with a tremendous amount of academic support for the students.

The second certificate program is designed for students who've completed a college degree in another academic area or who have a partially completed degree. The students will take mainly the science courses necessary to apply to one of our partners in one of our 80 locations. The first certificate has a synchronous component, while the second certificate is being taught completely asynchronously. Given that eventually GCE will have approximately 24,000 ABSN slots to our partners across 80 locations, we will need more than 24,000 students in certificate programs preparing for those opportunities. The third certificate program which will begin in September comes out of GCU's newly formed Institute for Workforce Development. The certificate will prepare students for a professional electricians apprenticeship program. This is a 16-credit hour, one semester program heavily focused on the mathematical concepts necessary to prepare for a career as an electrician. This program has been designed with a major industry partner who will offer apprenticeships to the students successfully completing this program. This partner needs 1,000 electricians for their business in Arizona alone. This partner also indicates the country is short a minimum of 100,000 electricians necessary to complete the building projects currently underway. GCU has 278 applications for the September start and is currently interviewing candidates and will accept 40 of them for the fall semester. Once the concept is proven, there is a potential to scale this program in a very significant way.

With that, I would like to turn it over to Dan Bachus, our CFO, to give a little more color on our 2022 second quarter, talk about changes in the income statement, balance sheet and other items, as well as to discuss the updated 2022 guidance.

Daniel E. Bachus

Chief Financial Officer, Grand Canyon Education, Inc.

Thanks, Brian. Included in our Form 8-K filed with the SEC, we have included non-GAAP net income and non-GAAP diluted income per share for the three months ended June 30, 2022 and 2021. Non-GAAP amounts exclude the tax effected amount of the amortization of intangible assets of $2.1 million in the second quarters of both 2022 and 2021. We believe the non-GAAP financial information allows investors to develop a more meaningful understanding of the company's performance over time. As adjusted non-GAAP diluted income per share for the three months ended June 30, 2022 and 2021 is $0.85 and a $1.12 respectively.

Service revenue was generally in line with our expectations in the second quarter of 2022. Revenue from traditional campus students slightly exceeded expectations due to higher summer school enrollment. Whereas revenue from online students were slightly lower than we expected, primarily due to slightly higher-than-expected graduations and students taking more time off from class during the quarter. Hybrid revenues were in line with our expectations. The hybrid enrollment growth rate is being impacted on a year-over-year basis due the timing of site openings. A 34% year-over-year decline in OTA enrollment and the closing of sites. Excluding enrollments from closed sites, ABSN enrollments grew 6.6% year-over-year, which was slightly below our expectations as a few sites had lower-than-expected summer enrollments due to the challenges Brian has discussed previously.

The revenue impact of this had little impact on second quarter revenues, but will have an impact on revenues in the second half, which I will discuss further in a minute. Revenue per student continues to grow on a year-over-year basis, primarily due to increased room, board, and other ancillary revenues from GCU students as compared to the prior year period and the growth in the enrollment of ABSN students. Service revenue per student for ABSN students generates a significantly higher revenue per student than we earn on the other students. As these agreements generally provide us with a higher revenue share percentage, the partners have higher tuition rates and the majority of their students take more credits on average per semester as they are in accelerated programs.

Our operating margin was slightly higher than our expectations. As I discussed on prior quarter's earnings calls, we have restarted hiring in which head count has mostly been flat since March of 2020 for our expected future growth, which is driving increased compensation costs in technology and academic services and counseling services and support costs. But as Brian mentioned, we remain below our head count plan, which is the primary reason that expenses were below expectations. We also plan for a significant increase year-over-year in travel and employee benefits as those amounts were significantly lower than pre-COVID levels in the prior year. We also plan for increased clinical costs at off-campus classroom and laboratory sites due to the nursing shortage. This spending has been in line with our expectations and the year-over-year difference in the timing of new site openings, all new sites in 2021, were opened in the first half of the year, whereas nearly all new sites opened in 2022 will be in the second half. It's having a negative impact on both revenue and expense.

Including both our 8-K and 10-Q filed today is a detailed explanation of the actual and anticipated impact of COVID-19 on all our university partners. Our effective tax rate for the second quarter of 2022 was 25.2%, compared to 23.3% in the second quarter of 2021, and our guidance of 24.9%. Our effective tax rate continues to be unfavorably impacted by an increase in the state income tax rate, primarily due to the fact that revenues continue to grow at the off-campus classroom and laboratory sites outside of Arizona. And the majority of these states have higher state income tax rates than Arizona. We repurchased 1,319,289 shares of our common stock in the second quarter of 2022, at a cost of approximately $128.5 million. The board is committed to spending at least $24 million during the rest of 2022, based on its previous commitments.

Turning to the balance sheet and cash flows. Total unrestricted cash and short-term investments on June 30, 2022 were $203.3 million. GCE CapEx in the second quarter of 2022, including CapEx for new off-campus classroom and laboratory sites was approximately $8.4 million or 4.2% of service revenue. We continue to expect CapEx for 2022 will be between $30 million and $35 million. Lastly, I would like to provide color on the updated guidance that we have provided in our 8-K filed today. Guidance that we have provided continues to be non-GAAP as adjusted net income and as adjusted diluted income per share as we have excluded amortization of acquired intangible assets. We continue to provide ranges for revenue, operating margin and earnings per share for each of these quarters. We do this because our financial results are seasonal.

As you will recall, the difference between the high and low-end of the previously provided ranges were primarily due to differing enrollment assumptions for GCU online and hybrid enrollments. The high end of our originally provided revenue guidance assume GCU online will return to new enrollment growth in the second quarter of 2022, whereas the low end assume new starts would remain down on a year-over-year basis in the second quarter, but would turn slightly positive in the second half of 2022. As Brian mentioned earlier, the B2B activity continues to improve, which gives us confidence that new online enrollments will return to year-over-year growth in the second half of the year. However, our head count continues to be approximately 10% lower than planned.

As mentioned earlier, our summer school hybrid enrollments were slightly less than we expected. Demand generally remained strong for our hybrid locations, but the clinical capacity issues and the prerequisite challenges that Brian has discussed previously continues to pressure cohort sizes at these locations. These challenges have impacted some locations greater than others, which has resulted in lower-than-expected summer school enrollments at a few of the hybrid locations. One recent example of the challenges currently being faced is a university partner that has historically had 100 student cohorts informed us that they would cap their cohorts in the summer and fall at 80 students each due to concerns around the availability of clinical faculty. Even though there were qualified students to fill the cohorts. We are working on solutions to ensure them that there is sufficient clinical faculty for the higher cohort amount, but at this time is more likely that the cohort sizes through the end of 2022 will be 80.

It is important to note that most of the locations met or exceeded their enrollment goals for the summer term and anticipate the same in the fall. But due to clinical capacities, we are not able to make up for the locations that had shortfalls with increases in future terms or at the other locations. As a result, we have adjusted our guidance for the second half of the year. The midpoint of the revenue guidance is in line with our previous low-end of a guidance. The midpoint of the EPS guidance falls between the midpoint and the low-end of our previous guidance. The adjustments are primarily due to the lower expected hybrid revenues and expenses. The difference between the high-end and the low-end of the range of the updated guidance is primarily due to differing online head count assumptions, with the high-end being if we can increase head count over the next couple of months to what we had originally planned, whereas the low-end assumes that net head count remains where it is today.

Traditional campus and hybrid revenues and expenses are generally the same in the guidance provided. The effective tax rate for the second quarters of 2022 have been lowered to 18.4% and 22.9% in the third and fourth quarters respectively, and operating margin has been adjusted down slightly as well to reflect contributions in lieu of state income taxes that were made last month. As in prior years, the impact of these contributions are to increase G&A expense for the $5 million in contributions in the third quarter and decrease the effective tax rate in the second half of the year $3.6 million or approximately three-quarters of which is recognized in the third quarter, and $1.4 million or approximately one quarter in the fourth quarter. The impact of this is $0.05 lower EPS in the third quarter and $0.05 higher EPS in the fourth quarter. Our weighted average share count takes into account the number of shares that have been purchased and what we intend to purchase the rest of the year.

As was discussed last quarter, the primary reason the board has been so aggressive in its stock buyback activity is that it believes the stock is considerably undervalued. A couple of the key metrics the board looks to make this determination is the ratio of enterprise value to adjusted EBITDA and the free cash flow yield rather than multiples of other education companies as although we can be viewed as being in the same sector, there are few if any appropriate comps. On an enterprise value to adjusted EBITDA basis, the stock is currently trading at roughly 10.7%, which is significantly less than the recent S&P average of approximately 17%. The average free cash flow yield for the S&P 500 remains at or about 2%, whereas the company's free cash flow yield is approximately 7.8%.

I will now turn the call over to the moderator so that we can answer questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. At this point, we'll conduct a question-and-answer session. [Operator Instructions] Our first quarter comes from Ryan Griffin with BMO Capital Markets. Your line is open.

Ryan Griffin
Analyst, BMO Capital Markets Corp.
Q

Hey. Good afternoon. This is Ryan on for Jeff. I was just wondering if you can provide any additional details on the ABSN closures. It seems like those classrooms and labs were quite large. Thank you.

Daniel E. Bachus
Chief Financial Officer, Grand Canyon Education, Inc.
A

Did you ask the closures?

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.
A

Yeah. Florida.

Daniel E. Bachus
Chief Financial Officer, Grand Canyon Education, Inc.
A

Yeah. Yeah.

Ryan Griffin
Analyst, BMO Capital Markets Corp.
Q

Yes. Yes.

Daniel E. Bachus
Chief Financial Officer, Grand Canyon Education, Inc.
A

Yes. There were two locations, one in, one, both of them in Florida. And as we've talked about in previous quarters, it was a joint decision between GCE and that university partner. That university partner wanted to refocus their efforts on locations closer to their campus. And so this fall, they're actually opening a second location in Albany, New York. So, we exited the Florida market. We will be reentering the Florida market, hopefully, in the next 12 months to 24 months, most likely with Grand Canyon University as our partner. So, we will be back in Florida. We think it is a good market and so that will happen. But yes, it did have an impact on our year-over-year enrollment growth, although, one of the reasons that we were happy closing those locations is that those locations, even though they had been open for multiple years, we're still losing money and so from a profitability standpoint that was a good decision for both partners.

Ryan Griffin
Analyst, BMO Capital Markets Corp.
Q

Got it. And then how would you expect your business to perform in a recessionary environment?

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.
A

I think it's going to – I think we're going to do really well. The ground campus is just going better than we could have even expected. We become a national institution and even though the number of students graduated from high school is going down in the percent of those going to college is going down. Increasingly, people are looking for affordable, high quality options and we represent that in a destination city and state. So, whether there is a recession or not? We won't be impacted from a ground perspective. I think that's just going to keep going really, really strong.

Online, we have turned the corner and we've turned the corner mainly because we've put such a great focus on licensure programs. The fastest growing programs now are in teacher education, people preparing to be teachers for the first time where there's a huge shortage of teachers in the country. Social work, there's a huge shortage of social workers in the country, counseling, et cetera. And so, even if there is a recession and the job market gets tighter, the people wanting to get in those occupational areas, there doesn't seem to be a decline in that. And you have to have licenses to operate, which means you have to earn degrees. And so, we think we positioned ourselves in a very strong place. The same is true with regards to the makeup of our online student body with regards to graduate students. Most of our graduate students are studying in licensure areas or areas that require licensure, and those people are currently operating in area where they want to get promoted, they want to move up. And so, we don't anticipate a downturn there. And I think from a healthcare perspective, if there's a recession and the job market gets tighter, the likelihood that people will want to go spend 16 months re-careering into a nursing program to earn a nursing degree as well as it pays and as good as the benefits are, I think that will increase the number of potential candidates for that program. So, we think we're really – we're very well positioned if there is a recession, if the job market gets tighter, we think we're really well positioned if that happens.

Operator: Hey. Thank you, Ryan. [Operator Instructions]

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.

A

I think we have a question from Alex.

Operator: Yes. Our next question does come from Alex Paris with Barrington Research. Go ahead, Alex.

Alexander Paris
Analyst, Barrington Research Associates, Inc.

Q

Hi. Thank you. And thanks for taking my questions. I just had a couple questions about the new certificate programs within the fourth pillar. Brian, I think you said that you have rolled out or will roll out soon. What has been rolled out? How is it being rolled out? Is it across the online and how do you charge for these things? Is it the same cost per credit hour or is there a difference?

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.

A

Well, I'll talk about three other certificates. The first one will be rolled out through what our ground campus enrollment counselors, mainly the people that work within high schools throughout the country that send students to GCU. They're identifying students who would like to stay home and save money, earn the first 60 credit hours of their undergraduate degree to prepare for a nursing program, are in those online for approximately the same tuition rate as you would pay if you are another online student. And so, that's being rolled out in September.

The second one is also being rolled out in September, and that's for students who have a partially completed degree or a completely completed degree, and want to take the science courses necessary as pre-reqs to get into one of our Accelerated Bachelor of Science in Nursing programs. That – those courses are all completed, the faculty have been hired, and we will roll out that opportunity to people starting into September. We are informing all of our partners and the people that represent those programs about that program, and they will have that as an option to send students to.

Right now, most people that express an interest in, they have a partially completed degree or a complete degree, they will be referred to a community college that can be a very long process. If they refer them to GCU's program starting in September, we have eight week courses. If you need to take five or six of those courses, you can take them within two or three weeks saying that you're interested and then each course is eight weeks, you can take them consecutively. And so, [indiscernible] (00:36:55), you can be through your prerequisite programs and eligible to start in one of the programs. So, we think that's going to streamline the process for people to get the pre-reqs done and get into one of our nursing programs. There will be a discount for that tuition as opposed to our normal tuition rates because we're very focused on preparing as many students as possible to get into the ABSN program scattered throughout the country.

And then the third program will be a slightly different kind of tuition rate as well that's the electricians program on our campus. Although we're receiving huge grant money for that program. We received an almost $700,000 grant from the State of Arizona, they are so excited about our workforce development center because of the construction explosion that's going on in Arizona, [indiscernible] (00:37:52) are an area where we are really scoring. We have a conservative partner who wants to make sure we get this thing right to start with and so we're only accepting 40 students in the first semester, somewhere between 40 and 80 the second semester. But once we've proven the concept, the amount of interest in this is tremendous. We've already had 278 people apply and we're just getting started. And so all three of those programs are shorter programs that lead to certificate that lead to tremendous workforce, workplace jobs and careers. And so, the universities, I think that in the future can work with students across the lifespan, all the way from [indiscernible] (00:38:41) down to even certificate programs that help build the workforce. I think we're preparing ourselves to be the premier supplier of that.

Alexander Paris
Analyst, Barrington Research Associates, Inc.
Q

It sounds very exciting. And I presume then by your comments that the first three are successful could lead to other certification programs offered by GCU?

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.
A

Yes, there are already people who are hearing about the electricians program that are approaching us the central partners they want to talk about [indiscernible] (00:39:11).

Alexander Paris
Analyst, Barrington Research Associates, Inc.
Q

All right. Then last one for me, just kind of big picture, Grand Canyon has historically grown organically. What are your thoughts with regard to M&A? Are there any capabilities out there that might make sense to buy rather than grow organically, particularly given what's happened with Edtech valuations and valuations in general over the last six months or so to say.

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.
A

You know, there's a lot of stuff out there and we have people call us all the time. We'll take a look at things. But the likelihood that we're going to do something in the next 12 to 24 months is not very great. We are so enthusiastic about this ground campus and our ability to grow it from the current 25,000 students to 50,000. Now that online appears to be [indiscernible] (00:40:00). We've got that moving again in a positive direction. We want to really focus on continuing to build out programs in that area. And then, it's expensive to grow to 80 locations with our hybrid campus partners. That is a lot of work. And the return on the investment there is so significant, especially in light of the fact that we've really stayed focused on where the gaps in the workforce development are. And that nursing thing has been historically so difficult for people to scale and the shortage is putting this country at such a – in a significant risk area that if we can build out all 80 locations and we producing 24,000 nurses on an annual basis. There's not a whole lot more that we can do. That would be – that would meet those specific need better than that.

It would very much be like what we're doing in teacher education. There's a huge shortage. We – most people don't know this. But we have 25,000 students in our Teacher Ed program, the majority of whom are studying to become first time teachers. Because we've put in place the infrastructure that they can do that at a distance, not only do the studying at a distance, but we can help them with their internship hours, their observation hours. We can schedule their student teaching. So, we are really excited about the areas that we currently have in place and the potential growth of those over the next 10 years. So, the likelihood that we would do something else right now is not great.

Alexander Paris
Analyst, Barrington Research Associates, Inc.
Q

Good. Thank you. I appreciate that color. Last one that just occurs to me. Just to clarify GCU online, did you mention new student enrollment for the second quarter? I realize you're projecting mid-single digits growth in the second half. How did it turn out in the second quarter?

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.
A

Yeah, it was down in the mid-single digits, which is what we kind of expected at going into the quarter given where the head count was. The momentum is good. But also, historically that the comps become different now. And it's those – the combination of those two things that now put us in a very favorable position going forward.

Alexander Paris
Analyst, Barrington Research Associates, Inc.
Q

Great. Thanks for that. That's all I have for now.

Operator: Thank you, Alex. Okay. Our next question will be coming from Jeff Meuler with Baird. Your line is open now.

Jeffrey P. Meuler
Analyst, Robert W. Baird & Co., Inc.
Q

Hi. Thank you. So, I heard that enrollment advisor head count is 10% behind plan. Can you help us understand how much you grew it during the quarter? And then just anything else you can say to give us confidence in going from down mid-single digits to up mid-single-digits on GCU online new enrollment beyond just kind of the easier comps. And I know you referenced kind of better partner channel. I don't know if there's any additional color you can give us there?

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.

A

No. The big thing there is, over almost 35% of our counseling staff is working on B2B strategies out in the marketplace. We're working with school districts, we've had some big school districts visit just recently Boston, Chicago and they're really asking us to help put together programs for their paraprofessionals to become licensed teachers. Military bases are asking us to prepare undergraduate students for cybersecurity careers because they can't compete with the outside world to get cybersecurity specialists. Those are just a couple examples. But that productivity, which during the pandemic was completely shut off, that comes back slowly because you have to get back out there and you have to meet with people you have to understand what it is they're trying to accomplish and you have to put together programs to help them accomplish that. But that's the main reason we're regaining momentum, those people are out again and they are – we've now gone through a period of about six months where they're reestablishing, rebuilding relationships, and now they're starting to start students. They're starting to the students legs behind, but that's now starting to happen. Our insight counselors, our advertising is for those people is still productive at about the same level that it has been. But we had to split those leads amongst everybody for a period of time. And so, they're coming back now to historical rates, the outside people are getting back to their historical productivity rates. And if that continues to happen, combined with the comps becoming easier, those are the things that are putting us in a strong position.

The other thing that is important to note is that, we are into BSN program and the Master of nursing programs almost throughout the industry has taken a hit because nurses have been extremely busy and reluctant to go back to school, even though the requirements inside hospitals haven't changed. They still have the requirements around a certain percentage of their nurses should be baccalaureate prepared. So that stuff hasn't changed. But the nurses have been reluctant to go back. And so, throughout the country those numbers are down. Fortunately, we have been developing some new programs that are in huge demand, especially the social work program. We're gaining major momentum with that program. And so, as those programs were declining in enrollment and a lot of people were hurting as a result or should we had replaced those with a lot of programs that are newly developed, and so those programs plus the outside people and return to normalcy of the inside people, all of those contribute to the momentum coming back. We are – we gained a few in the last quarter, but it was pretty flat. But interestingly enough, I think everybody is starting to see another flip again. And we have very good jobs and we've got good benefits and good advancement opportunities. And so, if the job market does tighten up, which I think a lot of people think it's going to, that would be to our advantage in a way, because it'll be easier to get that 10% deficit back to where it should be.

Jeffrey P. Meuler
Analyst, Robert W. Baird & Co., Inc.

Q

Got it. And then, is the clinical instructor [indiscernible] (00:47:20-00:47:29) was there regulatory changes that were temporary during COVID in terms of how much simulation could be used for clinical experience that is now normalizing or just is there partner pushback on simulations? Just help me understand the clinical instructors and the ability. Was there regulatory changes that were temporary during COVID in terms of how much simulation could be used for clinical experience that is now normalizing or just is there partner pushback on simulations? Just help me understand the clinical instructors and the ability to use simulations in lieu of live in-person experiences?

Brian E. Mueller

Chairman & Chief Executive Officer, Grand Canyon Education, Inc.

A

Well, there's definitely a trend in many places, not all. With the boards loosening – not loosening requirements, but being more open to get this work done without a one-on-one nurse, professors involvement. And so, in some states, for example, as much as 40% of the work that used to get done in a one-on-one is now being done through simulations or other virtual reality exercises. So, that's part of it. A bigger part of it is, is just faculty availability. And if the Master's preferred nurses were reluctant to take one-on-one clinical opportunities because they were getting paid so much in overtime to work on the floor. And so, we've had to increase what we pay to make it attractive and increasingly now as nurses have been paid to be traveling nurses. We will start paying traveling professors, people that are willing to move, to travel, and take over – take these assignments. And so, the thing is evolving, but hospitals are also being a lot more cooperative in terms of wanting to work with us to create clinical spots and to induce faculty members to want to do that work.

In Arizona, for example, with the explosion of population on the West Side, we've already got a West Side location, but we've got new cities coming to us and saying, would you put another location in our city? Because we got a growing healthcare area and we want to hire our local, we want our local high school graduates to go, be nurses in our local hospitals. And so, we've been, I think through the toughest part of this. And going forward, I think there's going to be a great deal, more cooperation with the nursing boards, with the hospitals, with clinical faculty. I think there'll be greater levels of cooperation going forward, and we think we'll be in a strong position to take advantage of that, especially because we've got 14 new locations we're going to open in the next 18 months. So, one thing I'd add is, with 27 partners and 32 locations, it's just – it's very low partner and location specific. As we've talked about before, some of these challenges that took us by surprise a little bit recently had popped up in other locations a year ago, where they had already requested that we bring down their cohort size.

The example that I gave today on the call, they had not done that until recently. And so, it's just – I wouldn't say it's necessarily worse or better to answer your direct question, but more that it's just – it's location by location and university partner by university partner specific. But that's why, I really am emphasizing the work that's getting done through the GCU program. I am extremely excited about what's happened at our West Valley location, our Tucson location. Those are Accelerated Bachelor of Science in Nursing locations. They're fairly new. We had 71 students. We fill them to capacity. We had 71 students graduate in the first and second quarter. And in spite of the challenges, we had a 100% first time pass rate on the NCLEX examination.

So, this can be done. It can be done in extremely high quality way. But we've got to give some of our partner institutions the confidence to make it happen. And I think as we get more GCE locations open and we have that level of success, I mean the GCU locations are up 80%. And there's been absolutely no reduction in quality because like I said, we had a 100% first time pass rate on the NCLEX examination. So, this can happen. It can happen in a high quality way. But GCU's going to have to take a leadership role in convincing others that, that it can happen.

Jeffrey P. Meuler

Analyst, Robert W. Baird & Co., Inc.

Q

Got it. And then the last one for me, the 14 planned locations, where are you in terms of regulatory approval process on those 14?

Brian E. Mueller

Chairman & Chief Executive Officer, Grand Canyon Education, Inc.

A

Most of them have already been approved. There are some, especially the – fall 2023 ones, and that we mentioned one which is Southern California that are going through the regulatory process. But I think we're more optimistic today than we were even three months ago that, that will get approved and be able to get opened. There's no guarantees on a few of them, but we're feeling that things are moving in the right direction.

Jeffrey P. Meuler
Analyst, Robert W. Baird & Co., Inc.

Q

Okay. Thank you.

Brian E. Mueller
Chairman & Chief Executive Officer, Grand Canyon Education, Inc.

We have reached the end of our second quarter conference call. We appreciate your time and interest in Grand Canyon Education. If you still have questions, please contact myself, Dan Bachus. Thank you very much.

Operator: Thank you for your participation in today's conference. This concludes the program, and you may now disconnect.