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## STRAYER EDUCATION, INCORPORATED: AN EQUITY VALUATION

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### CASE DESCRIPTION

*This case will require the student to value the equity of Strayer Education, Incorporated, (NYSE:STRA) and make a buy or sell recommendation as an independent analyst. The data given should be examined to determine whether or not the company's stock is valued above or below the market price in order for investors to make a buy or sell decision. The student must assess the real estate industry environment using Porter's five-force model of competitive strategy and the DuPont identity. Valuation techniques employed include the capital asset pricing model, the two-stage dividend-discount model, the P/E valuation approach, and the Gordon model.*

### CASE SYNOPSIS

*The student is placed in the role of an equity analyst and asked to prepare a buy or sell recommendation for Strayer Education, Incorporated(NYSE:STRA) stock. Strayer Education, Inc. through its subsidiary, Strayer University, offers graduate and undergraduate degree programs in business, information technology, education and public administration. The student must assess the competitive environment of Strayer using the DuPont identity and Porter's five force model of competitive strategy as well as estimate the value of the stock. All information in the case is publicly available.*

### STRAYER EDUCATION INCORPORATED

Strayer Education, Incorporated is an educational services holding company whose primary asset is Strayer University, a 115 year old institution of higher learning focused on educating working adults. Strayer University offers associate, bachelor's and master's level degree programs in Business Administration, Accounting, Computer Information Systems, Education and Public Administration. Strayer serves students at 39 physical campuses in Maryland, the District of Columbia, Virginia, North Carolina, South Carolina, Tennessee, Pennsylvania, Georgia, Florida and Delaware. Strayer serves students in all 50 states and 60 foreign countries on the Internet through Strayer University Online.

Strayer's revenue comes from tuition payments and fees paid by, or on behalf of, Strayer University students. The revenue comes in three forms. Roughly half is paid through federally

insured student loans by banks, approximately 20 percent is paid directly to Strayer by corporations or institutions on behalf of their employees who attend Strayer, and the remainder is paid by students through their own sources of credit.

Strayer's expenses include salaries paid to the faculty at the University who perform the teaching duties, salaries paid to the administrative and admissions staff who manage the campuses and recruit the students, and salaries paid to corporate staff who manage the company's affairs. Expenses also include lease payments for campus buildings which are leased and depreciation for campus buildings which are owned, as well as advertising and marketing costs for recruiting prospective students to Strayer. Finally, expenses also include educational equipment and supplies.

Item	2005	2004	2003
Total Assets	225,845	210,114	182,556
Total Revenue	220,507	183,194	93,909
Net Income	48,065	41,240	33,674
Stockholder's Equity	151,840	148,992	32,976

#### EDUCATIONAL SERVICES INDUSTRY

The educational services industry is currently being affected by both positive and negative trends. On the positive side, most educational service providers are expected to benefit greatly from strong online enrollment growth and positive demographic trends. Online education is becoming more widely accepted and respected while more and more people around the world are realizing the importance of a good education. Most firms in the industry are generating strong free cash flows and using the excess cash to repurchase shares, while some are making acquisitions with the free cash flows.

The most important negative trend facing the industry is a deceleration of campus based enrollment rates and a continuing rise in acquisition costs. The recent trend of slowing campus based enrollment rates is expected to continue in the short term. Among the factors affecting campus based enrollment growth rates is poor student-starts growth. A stronger job market has led some individuals to choose a better job rather than return to school. Higher marketing costs have also made it more expensive to recruit students.

Online enrollments are expected to remain a strong point for firms in the industry. Online enrollments are expected to continue to grow in excess of 20 percent for the majority of firms in the industry. Most of the firms realize the profitability of these operations and therefore are making

investments to upgrade their online offerings. Over the next several quarters, online operations are expected to become a greater proportion of firms' total operations. Strength in this area should help offset weakness in campus based enrollments.

Company	ROE	PROFIT MARGIN	ROA
STRA	31.7	21.8	31.7
APOL	71.23	18.45	40.4
COCO	8.50	3.56	6.92
DV	8.03	5.13	4.48
CECO	12.86	6.39	14.88
Industry	21.7	11.6	19.68

Source: Value Line Investment Survey

Based on the information in Table 3, firms in the educational services industry have been quite profitable recently, both in terms of profit margin and return on equity. Strayer has been particularly strong in light of its debt free balance sheet.

#### VALUATION DATA

Your analysis requires some information about the market in general as well as information on how the price of STRA stock behaves under certain conditions. While compiling the following information, you realize that your estimate of the value of STRA stock is quite sensitive to certain factors. In this regard, you decide to conduct a sensitivity analysis to determine how sensitive the value estimate is to various input variables.

The data collection begins with interest rates. Consulting a reliable source, you learn that the interest rate on a 90 day United States treasury bill is 4.5 percent while interest rates on a 6 month treasury bill are 4.9 percent. A long term government bond is trading to yield 5 percent. Recent rates on certificates of deposit at large banks are around 4.8 percent and large creditworthy corporations have issued commercial paper with a yield of 5 percent. During this same time period, the standard and Poor's 500 earned an average return of 10.2 percent.

In addition to the above information on market interest rates, Table 4 contains some information you compiled relating to Strayer Education and the market. Strayer's income statements for the past three years are also presented. The dividends and earnings of Strayer grew over the past 5 years rapidly. This growth rate of approximately 16 percent is expected to continue over the next 5 years due to market conditions and the economic outlook for the industry.

Strayer Education Inc., Balance Sheets			
<b>ASSETS</b>			
Current Assets	12/31/05	12/31/04	12/31/03
Cash And Cash Equivalents	74,212	97,004	82,089
Short Term Investments	45,594	25,753	25,951
Net Receivables	55,935	41,698	36,062
Inventory	-	-	-
Other Current Assets	2,581	3,679	1,656
Total Current Assets	178,322	168,134	145,758
Long Term Investments	-	-	-
Property Plant and Equipment	46,684	41,137	35,930
Other Assets	839	843	868
Total Assets	225,845	210,114	182,556
<b>LIABILITIES</b>			
Current Liabilities			
Accounts Payable	11,658	13,349	11,864
Short/Current Long Term Debt	-	-	-
Other Current Liabilities	55,778	42,059	39,134
Total Current Liabilities	67,436	55,408	50,998
Long Term Debt	-	-	-
Other Liabilities	6,364	4,707	2,666
Deferred Long Term Liability Charges	205	1,077	228
Minority Interest	-	-	-
Total Liabilities	74,005	61,192	53,892
<b>STOCKHOLDERS' EQUITY</b>			
Misc Stocks Options Warrants	-	-	-
Redeemable Preferred Stock	-	-	95,686
Preferred Stock	-	-	-
Common Stock	143	147	107
Retained Earnings	47,020	7,983	(26,918)
Treasury Stock	-	-	-
Capital Surplus	105,328	140,943	59,838
Other Stockholder Equity	(651)	(151)	(49)
Total Stockholder Equity	151,840	148,922	32,978
Net Tangible Assets	\$151,840	\$148,922	\$32,978

Strayer Education, Inc. Income Statements			
PERIOD ENDING	31-Dec-05	31-Dec-04	31-Dec-03
Total Revenue	220,507	183,194	147,025
Cost of Revenue	76,977	63,860	53,116
Gross Profit	143,530	119,334	93,909
Operating Expenses			
Research Development	-	-	-
Selling General and Administrative	68,666	53,851	42,781
Non Recurring	-	-	(1,772)
Others	-	-	-
Total Operating Expenses	-	-	-
Operating Income or Loss	74,864	65,483	52,900
Income from Continuing Operations			
Total Other Income/Expenses Net	2,982	1,595	2,420
Earnings Before Interest And Taxes	77,846	67,078	55,320
Interest Expense	-	-	-
Income Before Tax	77,846	67,078	55,320
Income Tax Expense	29,781	25,838	21,646
Minority Interest	-	-	-
Net Income From Continuing Ops	48,065	41,240	33,674
Non-recurring Events			
Discontinued Operations	-	-	-
Extraordinary Items	-	-	-
Effect Of Accounting Changes	-	-	-
Other Items	-	-	-
Net Income	48,065	41,240	33,674
Preferred Stock And Other Adjustments	-	(1,389)	(5,136)
Net Income Applicable To Common Shares	\$48,065	\$39,851	\$28,538

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Beta Coefficient for STRA	.85
Price/Earnings Ratio For STRA	30
Return on S&P 500	.10
Recent Price for STRA	106
Dividend declared for next year	1.00
Earnings per share estimate	3.55

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