

Aspen Group, Inc. ([NASDAQ: ASPU](#))

Q3 FY'2019 Results Earnings Conference Call

March 11, 2019 4:30 PM ET

Executives

Joseph Sevely - Chief Financial Officer

Michael Mathews - Chairman of the Board, Chief Executive Officer

Analysts

Darren Aftahi - ROTH Capital Partners

Eric Martinuzzi - Lake Street Capital

Mike Malouf - Craig-Hallum Capital

Operator

Good afternoon. Welcome to Aspen Group's Fiscal Year 2019 third quarter earnings call. Please note that the company's remarks made during this call, including answers to questions, include forward-looking statements which are subject to various risks and uncertainties.

These include statements relating to future growth including from USU's FNP program and the Aspen University hybrid pre-licensure BSN campus model, student enrollments, the core Aspen online nursing unit's expected Q4 results and marketing plans and our liquidity.

Actual results may differ materially from the results predicted, and reported results should not be considered as an indication of future performance.

A discussion of risks and uncertainties related to Aspen's business is contained in its filings with the Securities and Exchange Commission mentioned in the press release issued this afternoon.

Aspen Group disclaims any obligation to update any forward-looking statement as a result of future developments.

Also, I'd like to remind you that during the course of this conference call the company will discuss Adjusted EBITDA and EBITDA, which are non-GAAP financial measures, in talking about the Company's performance.

Reconciliation to the most directly comparable GAAP financial measures are provided in the tables in the press release issued by the Company today. There will be a transcript of this conference call available for one year at the Company's website.

Now I will turn the call over to Joseph Sevely, Aspen Group's Chief Financial Officer.
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Joseph Sevely

Good afternoon. I will begin today by reviewing our financial results for our fiscal 2019 third quarter, then will turn the call over to the Chairman & CEO of Aspen Group, Michael Mathews.

To open, quarterly revenue was approximately \$8.5 million, a 49% increase from the comparable prior year period, and a sequential increase of \$0.4 million or 5%.

In the third quarter we had solid growth at USU and our new pre-licensure campus program. In fact, these two relatively new business units accounted in aggregate for 25% of the Company's overall revenues, up from 21% the previous quarter.

Just as a reminder, one of the unique features of Aspen's online core business model is that our students can choose when and how many courses they take throughout the year, different from the vast majority of universities in America in which students pay for their education with federal financial aid and are required to be continuously enrolled to remain eligible. As a consequence of this flexible scheduling and payment policy, Aspen online core sees more seasonality than other universities.

As we mentioned on last quarter's call, fiscal Q1 is our slowest seasonal quarter given it falls during the summer months, but we also see a seasonal slowdown in Q3 given it falls during the holiday period between Thanksgiving and New Year.

As a result, AU online core revenue declined slightly from the second quarter by less than 1%. However, class starts before and after that were strong so we are confident that is a seasonal dip that we'll also expect to see in Q3 in future fiscal years.

The good news is fiscal Q4 is our seasonal high point as most of the great month of January flows into revenue in Q4. So while we saw Aspen online nursing core revenues decline sequentially by less than 1% this quarter, in Q4 we expect revenues in Aspen online nursing core to rise in the range of \$1 million sequentially.

So yes, Aspen online nursing core is a bit of a whipsaw in terms of seasonality, but as we continue to get larger we have developed expertise at really understanding it and predicting it.

Aspen Group's Gross Profit for the third quarter increased to approximately \$4.2 million or a 50% margin. This represents a 46% increase in gross profit compared to last year's third quarter. On a sequential basis, gross profit increased 3% and gross margin remained at 50%. Aspen University's gross profit represented 54% of Aspen University's revenue for the quarter, while USU's gross profit equaled 45% of USU'S revenue for the quarter.

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Total instructional costs and services for the quarter rose to approximately \$1.8 million or 21% of revenue. Aspen University's Instructional costs and services represented 18% of Aspen University revenue for the quarter, while USU'S Instructional costs and services equaled 30% of USU'S revenue for the quarter. Both of these were up slightly by 1% as compared to the second quarter. However, we do continue to expect USU's instructional costs as a percentage of revenue to decline as revenue grows.

Marketing and promotional costs for the Quarter were approximately \$2.3 million or 27% of revenue, declining from 28% as a percentage of revenue in the second quarter. Aspen University's marketing and promotional costs were 25% of Aspen University's revenue for the quarter, the same as the second quarter. USU's marketing and promotional costs equaled 25% of USU's revenue for the quarter, down from 27% last quarter.

G&A costs for the Quarter were approximately \$6.3 million compared to approximately \$4.7 million during the comparable prior year period, an increase of \$1.6 million or 34%, and a sequential increase of approximately \$0.1 million or 1%.

Containing G&A increases as we continue to aggressively grow revenues is the key to margin expansion so we are satisfied with the very modest sequential increase in this area of 1%.

Net loss applicable to shareholders was approximately \$2.35 million or Diluted Net Loss per share of 13 cents for the Quarter as compared to a net loss of \$2.15 million or 15 cents per share for the comparable prior year period, an increase in the loss of approximately \$0.2 million.

Aspen University generated approximately \$0.4 million of net income for the quarter, USU experienced a net loss of approximately \$0.9 million during the quarter, and AGI corporate incurred \$1.8 million of expenses in the quarter. USU's net loss declined by over \$200,000, with over half of that improvement attributable to operating income. Since USU's revenues increased by about \$250K sequentially, USU achieved about 46% operating leverage in the quarter.

With regard to our liquidity position, Aspen Group ended the quarter with approximately \$4.2 million in unrestricted cash, down \$3.5 million from the level at the end of the second quarter. Cash used in operations for the quarter was about \$1.9 million, compared to \$2.1 million last quarter. We are satisfied with that sequential improvement of approximately \$200,000 given revenues rose by approximately \$400,000, and also considering the third quarter included a \$160K annual interest expense payment that didn't occur in the second quarter.

Overall cash used in the quarter of \$3.5 million was up from \$2.7 million last quarter due primarily to the repayment of \$1 million in principal on a convertible note related to the USU acquisition, as well as the aforementioned \$160K interest payment on that note. If not for the repayment of the convertible note and associated interest on that note, we would have had an improvement of over \$300K in terms of overall cash used.

At the beginning of the third quarter we established a \$5 million revolving credit facility. Together with the \$4.2 million in unrestricted cash, that means we ended the third quarter with \$9.2 million of liquidity resources.

Last week we announced that we entered into a \$10 million funded term loan with an initial maturity of 18 months and the ability for the Company to extend that maturity for an additional 12 months by paying a 1% extension fee. We also announced that we repaid the remaining \$1 million on our convertible note related to the USU acquisition, thereby eliminating the conversion option.

This now gives the company approximately \$9 million of additional liquidity resources, clearly enough to execute on our short- and long-term growth plans. Mike Mathews will provide more color on our growth plans in a few moments.

But before I do, let me just say that it is no secret that our valuation has slid over the past few quarters. We were concerned that, if the stock price remained at these levels and absent new funding, we could find ourselves having to choose between artificially slowing growth or accessing capital on unattractive terms. We didn't like either of those alternatives. Instead we decided to increase debt financing in a sufficient amount that it takes these concerns off the table.

While this debt is more expensive than a traditional bank line-of-credit, it is however less expensive than mezzanine debt. It is of course much less dilutive than equity and will allow us to continue our growth trajectory without reliance on any additional external funding. We are confident that the returns to our shareholders from that growth will significantly outweigh the cost of the debt.

Now I'll turn the call over to Michael Mathews.

Michael Mathews

Thanks Joe. Good afternoon everyone.

Today I'll begin with our enrollment results followed by an operational update of our two newest business units, USU and our pre-licensure BSN program, then I'll end by recapping our recent accreditation announcements.

Enrollments in the third quarter rose 40% year-over-year to 1,363. Aspen University accounted for 1,112 new student enrollments which included 120 Doctoral enrollments and 97 pre-licensure BSN AZ campus enrollments, while United States University accounted for 251 new student enrollments which were primarily MSN Family Nurse Practitioner or 'FNP' enrollments.

These year-over-year enrollment increases were a result of how we grew the call center and where we directed our increases in marketing spending.

In terms of enrollment center staffing, on a year-over-year basis, the Aspen online nursing core unit remained flat at 49 Enrollment Advisors or 'EAs.' The year-over-year increase of 21 EAs were all allocated to the three new business units; Aspen Doctoral – 6 EAs, Aspen pre-licensure BSN – 4 EAs and USU – 11 EAs.

As we've indicated in recent quarterly calls, this shift was carefully planned as a result of these new programs delivering materially higher LTV's than our traditional Aspen nursing core unit.

Let's walk through the LTV differentials. First, our Aspen nursing online core unit has delivered a historical LTV of \$7,350 per enrollment. Aspen's Doctoral unit delivers an LTV of \$12,600 per enrollment or an ARPU increase of 71%.

Our USU FNP program, which today represents 84% of USU's total student body, delivers an LTV of \$17,820 per enrollment or an ARPU increase of 142% relative to our traditional Aspen online nursing core unit.

Finally, we launched the Aspen BSN pre-licensure hybrid campus business back in July last year and have been carefully watching the persistence of that initial cohort of 92 enrollments. Not only is this the most expensive degree program in the company at approximately \$47,000 including both tuition and fees earned over a 3-year period, but we're seeing materially better persistence rates relative to our traditional Aspen online nursing core student.

For example, we began our first BSN pre-licensure semester in July with 29 students starting the final 2-year core program with all first-year prerequisites already completed, and two semesters later we have 25 that remain in the program, meaning we've only seen attrition of 14% to date among the initial cohort of students that began the final 2-year core program.

The graduation rate for our traditional RN to BSN online program is 76% and based on the early results from the BSN Pre-Licensure program, we project the graduation rate for pre-licensure to be in the same range, if not even higher.

So we're comfortable giving guidance that our BSN pre-licensure business will deliver the highest LTV's among all degree programs in the Company, and that LTV will be at least \$30,000. As the cohort continues to progress, we'll refine the LTV guidance to a more exact number, but at \$30,000 per enrollment, that would deliver an ARPU increase over 300% relative to our traditional Aspen online nursing core unit.

Given the ARPU increases across our three newest lines of business, it should be clear now why we have focused our growth capital on these businesses.

Since we announced our \$10 million term loan last Thursday, a number of shareholders have asked why we decided to increase our liquidity position by approximately \$9 million. The short answer is, we want to ensure we have adequate liquidity to grow all four of our business units over the next few years, thereby not having to pick and choose which to grow based primarily on LTV's.

We have lots of runway to continue capturing market share in our Aspen online nursing core unit and plan to increase advertising spending and our enrollment team in that traditional business later this calendar year, in addition to executing on our growth plans in our other three business units.

With that, now I'll provide business updates on our two fastest growing and highest LTV businesses; USU's FNP program and Aspen's BSN pre-licensure hybrid campus program.

As we previously announced, USU has successfully enrolled to its target of at least 150 FNP students every other month over the past two enrollment cycles, the November 2018 and January 2019 starts, which represents a 100% increase from the previous target of enrolling 75 FNP students every other month. As a result, USU ended the quarter with 803 FNP students, representing 84% of USU's active student body. Assuming we continue enrolling at least 150 FNP students every other month, we're estimating by the end of next fiscal year, or April 30, 2020, we'll have approximately 1,400 FNP students at USU, after taking graduations and other attrition into account.

Another way of analyzing this growth is; should we continue enrolling 150 FNP students every other month or 900 annually, assuming an LTV of \$17,820 per enrollment, that means we've begun booking FNP student LTV at a rate of about \$16 million per year, which will be earned as additional revenue of \$8 million per year over a two-year period.

One final comment on our USU FNP program. We just enrolled 165 FNP students for our March start date, so we're clearly on track to continue our pace of at least 150 enrollments every other month.

Now I'll provide an operational update on our Aspen pre-licensure BSN program. As previously disclosed, Aspen University spent approximately \$42,000 marketing its new

pre-licensure BSN program in the Phoenix metro in the months preceding its July, 2018 launch.

Since that initial marketing spend, Aspen has delivered 247 enrollments and begun three semesters (July & November – Day program, and the January – Night/Weekend program) without having spent any additional marketing dollars over the past 6 months. Consequently, the cost per enrollment to date for the pre-licensure BSN program has been approximately \$170.

As of January when we began the night/weekend program, Aspen now will start a semester every other month on a go forward basis, meaning we will now have 3 day semesters per year and 3 night/weekend semesters per year.

As a result, Aspen has begun marketing again to maintain steady prospective student lead flow and to prepare for the launch of our second campus on the north side of Phoenix in partnership with HonorHealth.

The initial semester for HonorHealth is now currently targeted to begin this coming September. These two campuses in Phoenix are projected to have approximately 1,000 active students by the end of next fiscal year or by April 30, 2020.

In terms of future campuses, we've set an internal goal of launching two campuses per year versus our original plan of one per year, starting in calendar year 2020. We'll be providing more details on our 2020 campus expansion plans later this calendar year.

Finally, hopefully you all have seen our two accreditation announcements over the past few weeks. Last year I mentioned that as timing would have it, we had to undergo accreditation reviews at both our universities in back-to-back months last fall. The outcome of both reviews was a successful confirmation of each university's accreditation.

In the case of USU, the regional accreditor WASCUC commended us for the improvements we've made since the acquisition in the areas of advising, marketing, enrollment, data analytics, technology and early warning tools to increase student success. In addition, the Commission commended our commitment to creating an affordable pathway to higher education through our monthly payment plan.

I'd like to end today's remarks by again thanking everyone at Aspen and USU for their efforts and the great teamwork that led to these successful accreditation outcomes.

That ends our prepared comments for this afternoon, now we'd like to open the call to address any questions.

Question-and-Answer Session

Operator

[Operator Instructions]

Our first question comes from Darren Aftahi from ROTH Capital Partners. Please go ahead.

Darren Aftahi

Hello guys, good afternoon. Thanks for taking my questions. Mike, as you're speaking on accreditation, for USU you kind of talked about the March enrollment was 165. I'm somewhat curious how accreditation could potentially change so that 150 or so students every other month could perhaps be a bigger number. Could you indulge what accreditation actually means in terms of that 150 every other month essentially increasing?

Michael Mathews

OK, so first of all the accreditation review was from WSCUC which is the regional accreditor in the western region which accredits institutions in California and a few other states. So their accreditation is for all degree programs, not just the specific program of the Master-level Family Nurse Practitioner or FNP program. The FNP program is accredited by the state of California Board of Registered Nursing (CA BRN), and I want you to understand that the 150 enrollments that we are currently targeting every other month, that's an internal guideline.

There's no firm 'rules' that get put into place by any regulatory bodies. We plan to maintain that 150 enrollment range every other month for the next few quarters at a minimum. And we of course work closely with the CA BRN as it relates to our growth plans as well as all other support expenses involved in growing this program methodically and carefully.

Darren Aftahi

Great. Then on pre-licensure, so a couple of questions. You called out enrollment LTV and what you've spent on marketing. So you marketed ahead of the initial launch and you're sort of marketing again ahead of the launch of HonorHealth. So I'm somewhat curious, what's the marketing spend going to look like as it stands right now? I mean the LTV is about \$30,000 and is one side of the equation, and you've kind of given us \$170 as the other side. I'm just sort of curious of you have any kind of sense for what that marketing efficiency ratio could actually look like?

Michael Mathews

Yes, I'd have to work that out for you in terms of the marketing efficiency ratio. But we're currently spending around \$5,000 a week, so about \$20,000 a month currently. And we'll probably continue doing that pretty consistently up through the September launch of HonorHealth. So you can kind of run the math in what the likely cost of enrollment will be assuming that we bring in initially say 100 students into HonorHealth in that first semester -- it would be probably 70 pre-requisite students and another 30 in the final 2-year core.

Another thing Darren, that spend rate that I just mentioned, that would include the spend rate that would support leads and enrollments for both campuses, not just HonorHealth.

Darren Aftahi

Got it, thank you. And just to get back to FNP, so what would cause you to increase if it's internal? What would cause you to increase that number or potentially make it every month? Is there an internal rate of return you want to see? Do you want more stability of metrics? What's kind of the pivot point for you to kind of increase or broaden the proliferation of the USU platform?

Michael Mathews

Sure, that's a good question. So understand that the FNP program is a national licensure program and it's a two-year structured program and as soon as the student completes year one, they have to be placed into their clinical rotation for that second year. And if you don't place someone on a 'just-in-time' basis there's a lot of issues that would cause, student complaints and accreditors would be upset, et cetera.

So what's important to understand in developing this program is from a faculty point-of-view we have to increase faculty over time. We have to increase the student services side of the house to support that growth, and most importantly, we have to build the office of field experience as these people are the ones involved in placing these students into their clinicals on a 'just-in-time' basis. So we're going to look later this year at moving to enrollments on an every month basis rather than every other month. But I'd prefer to talk about that as the subsequent couple of quarters go by and we'll give updates at that point.

Darren Aftahi

Thank you.

Operator

Thank you. Our next question comes from Eric Martinuzzi from Lake Street. Please go ahead.

Eric Martinuzzi

Thanks. Congrats on the 49% revenue growth. We definitely don't want to take that for granted and it's a nice accomplishment. A question specifically speaking of revenue, you talked about \$1 million incremental lift sequentially expected in core in Q4. I know you're not specifically giving guidance for Q4 but the three consensus right now is for about \$9.9 million in Q4. Is that within the ballpark of what you think you can do in Q4?

Michael Mathews

I guess what I would say is that we're very comfortable with the current analyst consensus range. Just on a bottom line perspective, the only exception would be that of course our interest expense is going to increase given this new term loan.

Eric Martinuzzi

Okay, because that's nine points, I mean again the analyst consensus would have you at about 37% growth all in. OK, and then shifting over I wanted to ask a couple questions on the pre-licensure hybrid campus. Historically I think you've been talking about July for your first class starts there. And now you're talking about September. What was the deciding factor there as to why that moved a couple of months?

Michael Mathews

Yes, it's really just an issue of how long the build-out is going to take. I'll give you a little color on that. The building that we're actually going to launch in is actually owned by HonorHealth. It's on the north side of Phoenix right at the junction of interstate 101 and 17 for those of you that know the Phoenix area. The building up until recently was actually a day care center. So as a consequence, it took us a period of time to get the architectural plans completed and then subsequently of course we have to get that approved by the city of Phoenix. And finally, it's a pretty significantly build-out plan given the changes to the building itself in order to turn it into a world-class nursing campus. So at this time, we're looking right now at the completion of the building to be in the July timeframe and because we don't have a semester that begins in August, our next semester of course would then be September.

Eric Martinuzzi

OK, and you also talked about given the debt that you have now, you can continue to pursue growth in all vectors. I know you're talking about calendar year 2020 before you start now two per year. But will they be, are you envisioning, this being similar to HonorHealth where you go into the next hybrid campus with a partner like that or will it be kind of a standalone Aspen location?

Michael Mathews

Yes, as we look at other cities both inside the state of Arizona as well as other states outside of Arizona, the first thing that we have to accomplish is implementing a corporate partnership with a significant healthcare institution to lock up the clinical placements that are necessary to launch a new campus in a given metro. When we get into discussions, it can go either direction. If it makes sense for us to put a campus inside the healthcare organization's real estate location then that would be something we'd love to do. In some cases, it's not possible, in which case we would launch Aspen on its own like we did our inaugural campus. So I think over time, you'll see us do both of these implementations depending on the situation.

Eric Martinuzzi

Okay, then one last question. You kind of hinted as you touched on it a little bit, but your most recent announcement in which you talked about the new debt facility, you basically said we haven't drawn on the revolver, we haven't taken anything out of the debt but you aren't talking about interest expense in Q4. So how much are we talking about taking on here in the near term and then could you give us the interest expense, if not for Q4, then maybe for fiscal 2020 just for modeling sake?

Joseph Sevely

Sure, so the \$10 million term loan that we just did is a funded facility bearing interest at 12%. So that'll incur interest of \$100,000 per month. There were also warrants issued on that. So we will amortize warrant expense over the life of the facility. We also for the current quarter, the fourth quarter, we prepaid our \$1 million convertible term loan and we did pay interest on that. So we will be expensing that in the current quarter as well.

Eric Martinuzzi

Okay thanks for taking my questions.

Operator

Thank you. Our next question comes from Mike Malouf from Craig-Hallum Capital. Please go ahead.

Michael Malouf

Great, thanks guys for taking my questions. Michael, could we focus a little bit on the pre-licensure program for just a second. How can you give us confidence that the level of education and specifically with regards to testing coming out of the program can remain at such a high level that you feel confident sort of accelerating the program in the next year. I'd love to get some color on that.

Michael Mathews

Well, I mean frankly I feel like we have a world-class senior leadership team on the academic side. Dr. Cheri St. Arnauld, our Chief Academic Officer for Aspen Group, Inc. And in addition of course she came from the very strong university, Grand Canyon University. And subsequently we brought in Dr. Anne McNamara who is the former Dean of Nursing for Grand Canyon, to head up all our pre-licensure programs from campus to campus, city to city. Anne's history is she never had a year less than 90% NCLEX scores. So my confidence level and everyone's confidence level at Aspen is very high that we will achieve those similar type of metrics if not better.

Michael Malouf

And then when you take a look at some early indications from some of the students that joined you last year, how are they getting along with the more hybrid online/offline program versus what Anne was working at with Grand Canyon.

Michael Mathews

Yes, so I guess the best way to view this is to look at persistence rates. Persistence rates are, I think I indicated, that we've only lost 14%, so that is 86% persistence rate. The students have given us tremendous feedback in terms of how we approach the academics, the knowledge transfer happens online. In other words, the curriculum is online, then we bring the students in approximately three times a week to implement seminars or lectures with simulation activities immediately after the lecture. So then of course in year two of the core program, the final year, is when they go into their actual

onsite clinicals. So we believe that we are preparing these students at an extremely high level and that we're going to have very high NCLEX scores and we're going to do a great job of preparing the next generation of great nurses in the state of Arizona.

Michael Malouf

That's great. That's really helpful and then just a quick question as you look out over the next couple of years for your traditional Aspen online nursing students. What do you think, does that number stay steady or increase a little bit? Obviously you're taking some of those assets and pushing it towards these higher LTV programs but the LTV at \$7,350 even that was pretty attractive. Do you think that you can continue to grow slightly or do you think that will trend down over the next couple of years?

Michael Mathews

No, our plan has been to keep enrollments over the past two, three quarters relatively flat in that area. Again we spend approximately \$1.3 million per quarter in that nursing online core business and we've averaged in the last three quarters about 960 enrollments a quarter which backed into a very strong cost of enrollment of about \$1,350. So from our point of view, we don't see any reason why we can't increase spending again in the coming months. We're expecting similar KPI results. There's no question that the market share is available for us to continue to take and we plan to do so.

We've been straddling the fence a little bit where we haven't had a tremendous amount of capital and we wanted to make sure that we started to move down the path of getting to Adjusted EBITDA, getting back to Adjusted EBITDA positive results. And so that's why we focused our incremental spending the last two, three quarters into those high LTV businesses to accelerate that process.

Michael Malouf

OK great. Thanks, I appreciate it.

Operator

Thank you. I'm showing no further questions in the queue. At this time, I'd like to turn the call over to Michael Mathews, Chairman & CEO of Aspen Group for closing remarks. Please go ahead.

Michael Mathews

Great, thanks everyone for your questions. And I want to thank everyone for joining us this afternoon and the team here looks forward to talking to you again soon. Good afternoon.

Operator

Thank you, ladies and gentlemen for attending today's conference. This concludes the program. You may all disconnect. Good day.