

RITTENHOUSE CAPITAL PARTNERS

**Education Industry Overview**

**October 1, 2005**

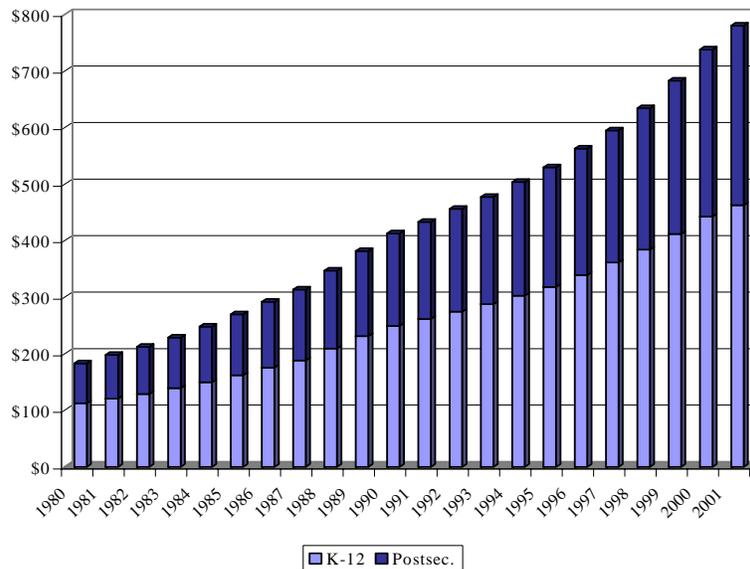
## INDUSTRY OVERVIEW

The education industry (exclusive of corporate training) in the U.S. is one of the largest industries as measured by expenditures, which totaled \$780 billion in 2001 or approximately 7.7% of GDP. Of the total expenditures, \$317 billion, or 41%, was spent in the postsecondary sector and \$463 billion, or 59%, in the K-12 sector. The following exhibit outlines education spending from 1980 to through 2001. During this period, both GDP and education spending had compound annual average growth rates in excess of 6%.

### Exhibit 1

#### U.S. Education Expenditures, 1980 – 2001

(\$ in billions)



Source: Digest of Education Statistics 2003 – NCES.

### Postsecondary Education

The value of a postsecondary education has never been higher. The Employment Policy Foundation estimates that, on average, a U.S. worker with a bachelor's degree will, over a lifetime, earn approximately \$900,000 more than a worker with only a high school diploma. This correlation between education and earnings is expected to increase over time, yet only 34% of U.S. adults have an associate's degree or higher. The traditional postsecondary education system was designed to serve 18- to 22-year-olds in a residential model, but today's student base is increasingly employed, part-time, older than 25, attending a 2-year college and seeking career-related education. This represents a significant shift in both the customer base and how postsecondary education is delivered. For-profit colleges and universities are addressing the changing demand by offering flexible and career-focused degree and diploma programs, both in campus-based and online models. In general, for-profit companies do not seek to compete with

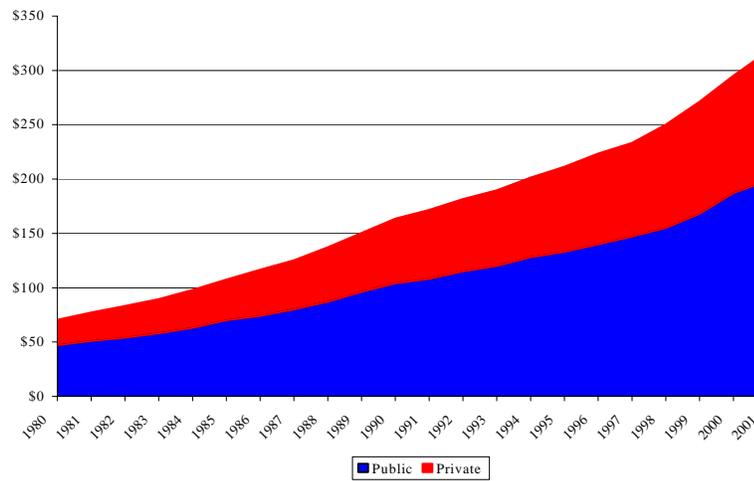
traditional providers but rather focus on serving market niches that are largely not addressed by the traditional model.

Postsecondary education is a large and growing segment of the U.S. economy, serving more than 16 million students and totaling approximately \$317 billion in annual expenditures. Since 1980, the industry has grown at a compound annual growth rate of 7.4%, outstripping GDP growth and thus becoming a larger portion of the economy over that period. The exhibit below shows total U.S. postsecondary expenditures for the years 1980 through 2001. Over this period, postsecondary expenditures increased from 2.5% of the GDP in 1980 to 3.1% in 2001.

**Exhibit 2**

**U.S. Postsecondary Expenditures, 1980 – 2001**

*(\$ in billions)*



Source: Digest of Education Statistics 2003 – NCES.

The breakdown of annual U.S. postsecondary education expenditures is outlined in the following exhibit.

**Exhibit 3**

**Breakdown of Total 2001 U.S. Postsecondary Expenditures (1)**

*(\$ in billions)*

|                      | <u>Expenditures</u> | <u>% of Total</u> |
|----------------------|---------------------|-------------------|
| Public Institutions  | \$198.6             | 63%               |
| Private Institutions | <u>118.8</u>        | <u>37%</u>        |
| Total Expenditures   | <u>\$317.4</u>      | <u>100%</u>       |

(1) Includes both current and capital expenditures

Source: *Digest of Education Statistics 2003 – NCES.*

Of the total industry expenditures, instruction, research and public service spending ranges from 31% for public schools to 46% for private schools. Student services and institution support range from 55% to 28%.

### **Institutions and Enrollments**

According to the U.S. Department of Education (“DOE”), there are 9,258 colleges and universities in the U.S. Of this total, 4,197 are degree granting, meaning that they are authorized to grant associate’s level degrees or higher and are eligible to participate in the federal student loan financing programs authorized by Title IV of the Higher Education Act known collectively as “Title IV.” The remaining 5,059 institutions are typically small, single-site and, in aggregate enroll less than 3% of all students.

In 2001, according to the DOE, 15.9 million students were enrolled in degree-granting programs and an additional 400,000 in other programs. Of the 15.9 million students enrolled in degree programs, 86% were enrolled in undergraduate and 14% in graduate programs. The DOE projects that by 2013 the total number of students in degree-granting institutions will increase 15% to 18.2 million, with the undergraduate/graduate blend remaining stable. The main factor contributing to this growth is an expected 10% increase in the number of new high school graduates over the period.

### **Exhibit 4**

#### **Degree Granting Institutions – Fall 2001**

|                            | <u>Institutions</u> | <u>Students<br/>(000's)</u> |
|----------------------------|---------------------|-----------------------------|
| <u>Two-Year Colleges:</u>  |                     |                             |
| Public                     | 1,101               | 5,997                       |
| Private - Non-profit       | 172                 | 48                          |
| Private - For-profit       | <u>560</u>          | <u>206</u>                  |
| Subtotal                   | 1,833               | 6,251                       |
| <u>Four-Year Colleges:</u> |                     |                             |
| Public                     | 612                 | 6,236                       |
| Private - Non- profit      | 1,504               | 3,120                       |
| Private - For-profit       | <u>248</u>          | <u>321</u>                  |
| Subtotal                   | <u>2,364</u>        | <u>9,677</u>                |
| Total                      | <u>4,197</u>        | <u>15,928</u>               |

Source: *Enrollment in Postsecondary Institutions, Fall 2001 – NCES.*

### **Undergraduate Enrollments and Trends**

Undergraduates represent the vast majority, 86%, of total enrollments. Over the past 30 years, several trends have emerged that have significantly altered the composition of the undergraduate market.

- A dramatic rise in the portion of the market served by 2-year institutions
- A marked increase in the number of part-time students
- An increase in the percentage of minority students
- An increase in the percentage of students who are 25 or older

Thus, one of the fastest growing components of the student population is that of non-traditional students entering the market. The non-traditional student is more likely to be seeking a career-focused education that is conveniently delivered, either part-time or online. This, in part, explains the reason that community colleges and for-profit schools have grown substantially in recent years.

Exhibit 5 depicts undergraduate enrollment trends from 1970 through 2001.

### Exhibit 5

#### Undergraduate Enrollments Trends

| <u>Demographic Characteristic</u> | <u>Percentage of Students</u> |             |                   |
|-----------------------------------|-------------------------------|-------------|-------------------|
|                                   | <u>1970</u>                   | <u>2001</u> | <u>% Increase</u> |
| Part-Time Students                | 28%                           | 39%         | 39%               |
| Enrolled in 2-Year Colleges       | 31%                           | 46%         | 48%               |
| Minority Representation (1976)    | 18%                           | 32%         | 78%               |
| Age 25 and Older                  | 20%                           | 29%         | 45%               |

*Source: Digest of Education Statistics 2003, General Partner Estimates, NCES.*

### **Tuition**

Tuition at all types of postsecondary institutions has risen considerably faster than the rate of inflation and consumes a greater portion of household income today than it has at any point in the past. On average, in the last decade inflation-adjusted (real) tuition and fees have risen approximately 90% at public colleges and 71% at private colleges. For the academic year 2004-2005 alone, tuition rose 6% at private four-year colleges and 10.5% at public four-year colleges. Postsecondary education is not generally an industry characterized by price competition, although public pressure to rein in college costs is increasing. Tuition of for-profit institutions is typically higher than that of public four-year colleges and lower than that of non-profit, private four-year colleges. Exhibit 6 shows enrollment-weighted average tuitions and their percentage increases.

**Exhibit 6****Enrollment-Weighted Average Undergraduate Tuition***(in constant 2004 \$)*

|                   | <u>Tuition and Fees</u> |                  |                 |
|-------------------|-------------------------|------------------|-----------------|
|                   | <u>2003-2004</u>        | <u>2004-2005</u> | <u>% Change</u> |
| Two-Year Public   | \$1,909                 | \$2,076          | 8.7%            |
| Four-Year Public  | \$4,645                 | \$5,132          | 10.5%           |
| Four-Year Private | \$18,950                | \$20,082         | 6.0%            |

*Source: Trends in College Pricing 2004, The College Board.*

**Total Cost of Education**

Tuition and fees do not represent the total cost of postsecondary education. Rather, tuition and fees only represent the portion of the cost that an institution passes onto a student. Vast state and federal subsidies, as well as tax-deductible gifts and endowments, subsidize a significant portion of the cost of educating students at public and private non-profit institutions. In fact, tuition and fees charged to students, at public four-year colleges cover on average less than 20% of the actual cost of the education. Apollo Group founder John Sperling, in his book "For-Profit Higher Education" (1997, Transaction Publishers), estimated that in 1995 taxpayers paid more than \$3 billion in subsidies to underwrite the education of the 161,000 students who attended the nation's 50 most expensive private colleges and universities, equaling more than \$18,000 per student for one year of education. Exhibit 7 shows the portion of the total cost of education that comes from tuition and fees and from other sources.

**Exhibit 7****Contribution to Total Revenues - 2002**

|                    | <u>Four-year Insitutions</u> |                | <u>Two-year Institutions</u> |                |
|--------------------|------------------------------|----------------|------------------------------|----------------|
|                    | <u>Tuition</u>               | <u>Other</u>   | <u>Tuition</u>               | <u>Other</u>   |
|                    | <u>and Fees</u>              | <u>Sources</u> | <u>and Fees</u>              | <u>Sources</u> |
| Public             | 15%                          | 85%            | 17%                          | 83%            |
| Private non-profit | 40%                          | 60%            | 57%                          | 43%            |
| Private for-profit | 90%                          | 10%            | 85%                          | 15%            |

*Source: Enrollment in Postsecondary institutions, Fall 2002, NCES.*

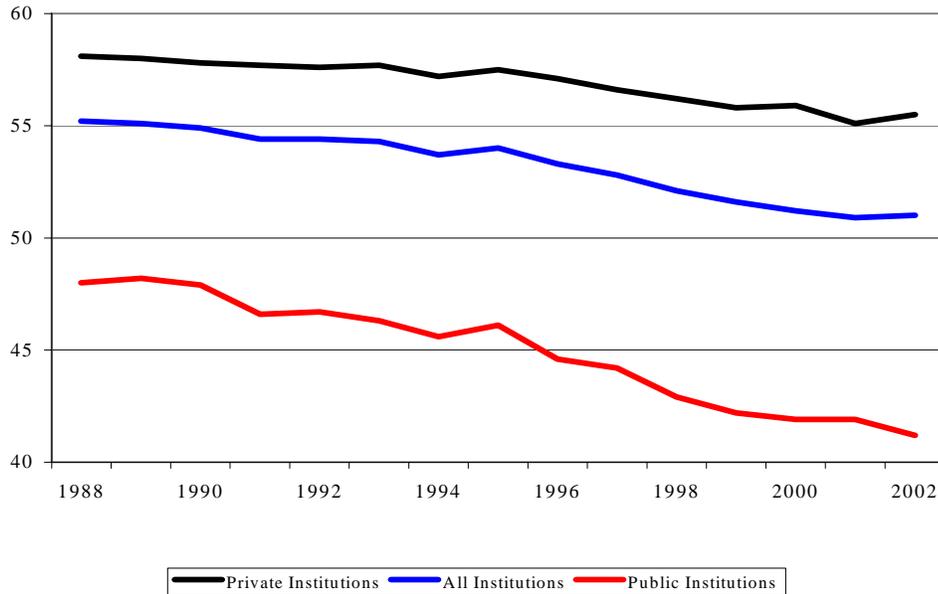
**Graduation Rates**

Graduation rates across all types of institutions have been decreasing steadily over time. They also vary geographically and across different types of institutions. Currently, approximately half of students enrolled at four-year colleges complete their degrees within five years, and less than a third of students at two-year colleges graduate within three years. In contrast, according to the

Career College Association (CCA), approximately 60% of students attending a for-profit, two-year college will graduate within three years.

**Exhibit 8**

**Percentage of Four-Year College Students Who Earn a Degree Within Five Years**



Source: ACT.

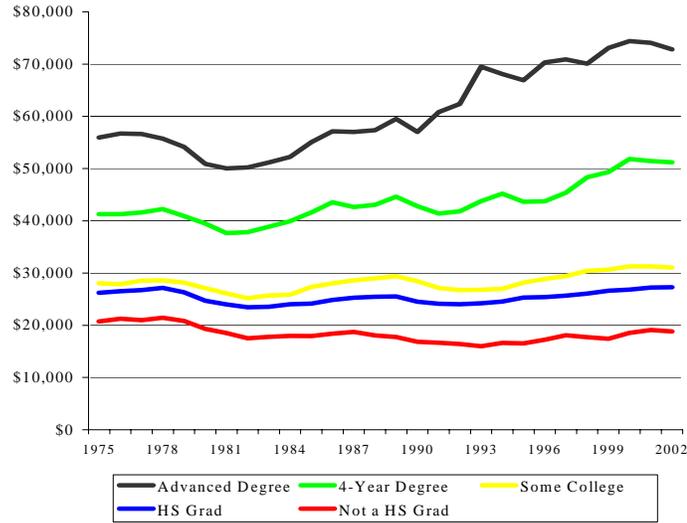
In many ways the variations in graduation rates shown in Exhibit 8 highlight the challenges facing the education system and the growing divide between different types of institutions and student populations. *Business Week*, in its January 10, 2005 issue, discussed the increasing stratification of the education system due to rising tuition costs and made the following observation: “Less than one-quarter of well-qualified low-income students earn a BA within six years, versus nearly two-thirds of higher-income students,” further perpetuating and widening socio-economic gaps in the U.S.

**Value of a Degree**

There is a significant correlation between education and earnings. This correlation has been increasing over time and is forecast to continue into the future as the percentage of jobs that require postsecondary education increases relative to the overall job market. The reasons for the wage/education correlation are varied. For one, technology has revolutionized the workplace and many types of formerly blue-collar jobs now require specialized training. In addition, globalization and outsourcing have put pressure on the wages of unskilled U.S. laborers. In its March 2003 review, the Employment Policy Foundation estimated that the lifetime earnings premium of a U.S. worker with a four-year degree versus a worker with only a high school diploma is approximately \$900,000. In 1975, according to the U.S. Bureau of Labor Statistics, a worker with a high school diploma would, on average, earn approximately 63% of what a worker with a bachelor’s degree would earn. By 2002, the same worker on average would only earn 53% of what the college graduate would earn, representing a 16% decline in relative earning power over the period.

**Exhibit 9**

**Median Earnings of Workers 19 Years and Older**  
(in constant 2002 \$)

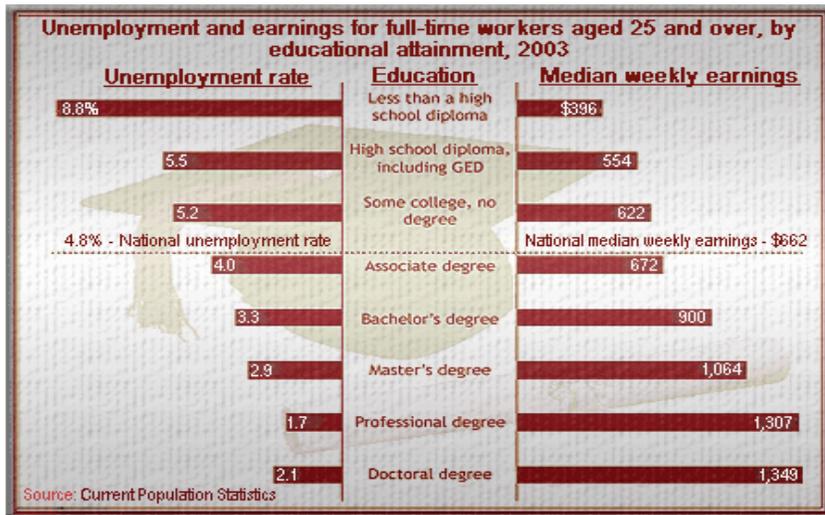


Source: U.S. Census Bureau, Current Population Survey 2002.

The same forces that drive down the wages of workers who lack postsecondary education also impact unemployment rates. In fact, unemployment rates are closely correlated with education attainment levels. The following exhibit shows this correlation.

**Exhibit 10**

**Unemployment and Earnings Levels**



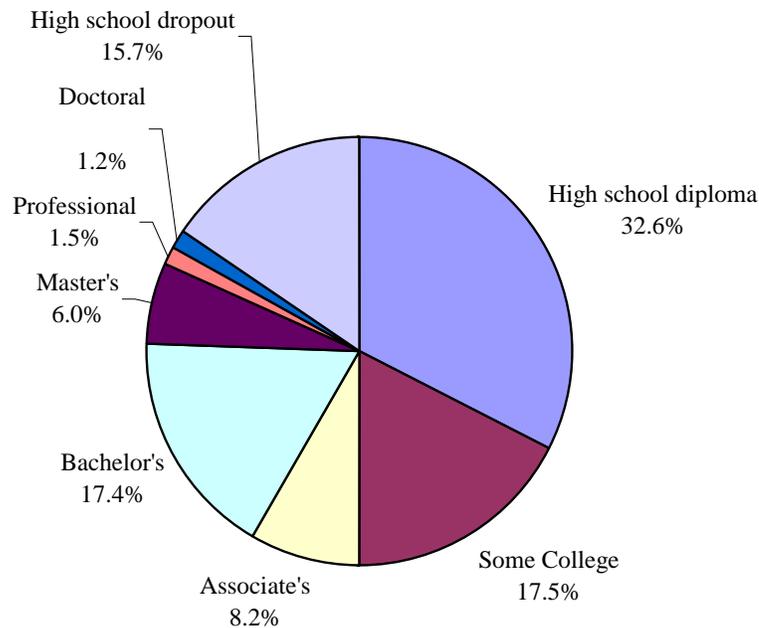
*Source: U.S. Census Bureau, Current Population Survey 2003.*

Total employment is projected to increase by 22.2 million jobs over the 2000–2010 period, rising to 167.8 million, according to the U.S. Bureau of Labor Statistics. The economy will continue generating jobs for workers at all levels of education and training, but growth rates are projected to be faster, on average, for occupations generally requiring a postsecondary award (a vocational certificate or other award or an associate's or higher degree).

The U.S. Bureau of Labor Statistics also projects that by 2010 jobs that require a bachelor's degree or higher will increase approximately 22%, an associate's degree approximately 32% and postsecondary vocational training approximately 18% versus 2000 levels. Over the same ten-year period the number of students in the postsecondary education system is expected to grow by approximately 15%, exposing a gap between the projected jobs available and the number of qualified workers in the U.S.

### **Adult Education Levels**

Despite the increasing earnings premium associated with postsecondary education, only 34% of U.S. adults have an associate's degree or higher. The remaining 66% are comprised of people who have completed some college (17.5%), are high school graduates (32.6%) or did not complete high school (15.7%).

**Exhibit 11****Highest Education Attainment Level of U.S. Adults – March 2001***(total population 25 and older of 177 million)*

*Source: U.S. Census Bureau, Current Population Survey 2001.*

**Distance Learning and Online Education**

Rapid advances in Internet technologies and access, coupled with demand for flexible learning models, have led to growing interest in distance learning, which is defined by the DOE as “education or training courses delivered to remote (off-campus) sites via audio, video (live or prerecorded), or computer technologies, including both synchronous (i.e., simultaneous) and asynchronous (i.e., not simultaneous) instruction.” In its July 2003 survey for the 2000-2001 school year, the NCES found that 56% of degree-granting institutions offered distance education courses and an additional 12% expected to do so by 2006, versus 33% and 25% for the 1995-1996 school year. In 2002, the NCES estimated that approximately 8% of all undergraduates had taken a distance learning course, with 59% of those taking the course over the Internet.

According to Eduventures, the revenue growth rate in online postsecondary education exceeded the revenue growth rate of the overall market from 2001 to 2003. In March 2004, Eduventures projected that online enrollments would be 915,000 as of December 31, 2004, and would grow to

approximately 1.6 million by December 31, 2007, representing a \$5.1 billion market in 2004 and a \$10.4 billion market in 2007.

#### **Title IV Financing of Postsecondary Tuition**

The loan and grant programs authorized by Title IV and administered by the DOE are the primary source of federal financial aid to students. According to the DOE, in 2002 Title IV programs totaled \$105 billion (of which \$49 billion were in the form of loans), a tripling from their level in 1992.

The Title IV programs include Pell Grants, Stafford loans, parent PLUS loans; and three campus-based programs: federal work-study, Perkins loans and Federal Supplemental Educational Opportunity Grants. Pell Grants are awarded on the basis of need and are intended to aid students in the lower income levels. The maximum Pell Grant amount in 2003-2004 was \$4,050.

There are two types of federal Stafford loans. Subsidized Stafford loans are need-based, and the federal government pays the interest for students while they are enrolled. Unsubsidized Stafford loans are not need-based, and students are charged interest on the loans while they are enrolled. Students who qualify may take out subsidized, unsubsidized; or a combination of both types of Stafford loans. Both types of Stafford loans have annual borrowing limits that vary by student class level and dependency status. For example, in 2003–2004, the combined (subsidized plus unsubsidized) annual Stafford loan limits ranged from \$2,625 for dependent first-year undergraduates to \$5,500 for dependent undergraduates in the third year or above; for independent undergraduates, the annual loan limits ranged from \$6,625 for first-year students to \$10,500 for independent students in the third year or above; and for graduate and first-professional students, the annual loan limit was \$18,500, but students at eligible medical schools could borrow up to \$38,500 annually.

PLUS loans are available to the parents of dependent undergraduates and are not need-based. There is no fixed annual PLUS loan limit. Parents may borrow any amount that does not exceed the student's total price of attendance at the institution minus any other financial aid received.

The Title IV campus-based program funds are allocated to institutions, and the financial aid officers at the institutions determine the allocation of awards to students within federal guidelines. Pell Grant recipients are given priority for Federal Supplemental Educational Opportunity Grants and Perkins loans.

#### **Regulation**

Postsecondary institutions participating in Title IV are regulated at the state and federal levels and must also be accredited by a private accrediting agency. All institutions must be registered in the states in which they operate. Regulatory burdens vary by state and are generally set by the state board of education. Federal oversight of postsecondary institutions is primarily tied to Title IV programs and is overseen by the DOE. National and regional accrediting bodies set and enforce educational standards. For-profit institutions are held to stricter Title IV standards than non-profit institutions and are also subject to additional regulations and restrictions.

#### **Accreditation**

Accreditation ensures that an institution's educational programs meet certain quality standards. In order to be eligible to participate in Title IV, institutions must be accredited by a regional or national body that is recognized by the DOE. Accreditation falls into two main categories, institutional and programmatic. Institutional accreditation, which can be regional or national,

designates the named institution as meeting the accrediting body's standards. Regional accreditation is governed by six geographically assigned bodies and is, in general, the most difficult accreditation to obtain. It is recognized by the DOE and is required in order to grant doctoral degrees. National accreditation is typically most appropriate for career-based education such as that offered by culinary or technical schools. Many national accreditors are recognized by the DOE. Finally, certain fields of study require or are enhanced by programmatic accreditation or must be approved by their relevant professional licensing boards. Most academic programs, however, do not require programmatic accreditation or professional board approval.

### **Federal Regulation**

There are areas of regulation that apply to for-profit institutions that participate in Title IV and certain of these may be impacted by the pending reauthorization of the Higher Education Act (see discussion below).

**90/10 Rule:** No more than 90% of a school's revenues in one fiscal year can originate from Title IV sources.

**Default rates:** If a school's student loan default rate is 25% or higher for three consecutive years or exceeds 40% in any one year it will lose Title IV eligibility.

**Financial responsibility:** Schools must meet or exceed certain financial ratios calculated using net worth, assets and earnings.

**Distance learning:** No more than 50% of students may be enrolled in distance learning programs. Exceptions are granted to institutions that are participating in the DOE's distance education demonstration project.

**Change of control review process and restrictions:** When a majority stake in a postsecondary company changes hands or certain other changes of control occur, the continuation of Title IV funding must be reauthorized and the transaction approved by the DOE. This review process can be lengthy as it analyzes whether the new owner has the capability to manage Title IV programs and the financial stability to keep the school in operation. This review process is presently more onerous for new entrants to the industry who lack prior experience in administering Title IV programs.

**Other areas of restriction:** The U.S. Department of Labor stipulates that for-profit institutions may only grant degrees in "occupational" areas. In practice, this is broadly accepted to include programs ranging from a culinary associate's degree to a Ph.D. in psychology. Still, for-profits are forbidden from offering certain academic degrees. Finally, students of for-profit schools face greater limitations on their ability to transfer credits than do students of traditional schools.

### **The Higher Education Act**

The Higher Education Act of 1965 (the "Act") was enacted to create a regulatory framework to provide oversight to the postsecondary education industry. In the 1980s, several "diploma mill" scandals emerged in which unscrupulous operators were granting postsecondary education that held little or no value to the student, who then often defaulted on his or her Title IV student loan. The reauthorization of the Act in 1992 included many new provisions intended to rein in unethical practices and established financial and operating standards to which institutions participating in Title IV must now adhere. The resulting post-1992 regulatory environment is more complex but designed to ensure the integrity of the industry. Congress is currently in the midst of another reauthorization process for the Higher Education Act. Industry participants

expect that the reauthorization could prove more favorable to the for-profit sector than prior reauthorizations and reflect changes that have impacted the industry since 1992, such as the dramatic growth of online learning.

### **Challenges Facing the U.S. Postsecondary Education System**

The U.S. postsecondary education system had long been viewed as the best and most sophisticated one in the world, one that is credited with being the backbone of the U.S. economy. But recent data from the Organization for Economic Cooperation and Development shows that, while the U.S. continues to be one of the biggest spenders on education worldwide, its level of achievement has been slowing down substantially and lags behind that of many other industrialized nations. The report analyzed 32 industrialized nations and found that in 2000 the U.S. was:

- Tied for 13<sup>th</sup> place in the percentage of the population entering postsecondary study
- Ranked 1<sup>st</sup> among nations in the percentage of 45 to 54 year-olds who have at least a high school diploma
- Ranked 9<sup>th</sup> among nations in the percentage of 25 to 34 year-olds who have at least a high school diploma

In its recent report, **The 21<sup>st</sup> Century at Work: Forces Shaping the Future Workforce and Workplace in the United States**, the RAND Corporation confirms such data:

*“The international comparisons suggest that the educational delivery by U.S. schools is, at best, about average among developed nations. This is consistent with Hanushek and Kimko (2000), who found that the quality of U.S. schools could not take credit for causing the high growth rate of U.S. GDP over the twentieth century. Instead, the openness and fluidity of U.S. markets and the low level of intrusion by the government in economic operation—through relatively little regulation, low taxes, and few government-owned industries—stimulated more innovation and investment in the U.S. than in most other developed countries. Presumably, though, growth could have been even more impressive had U.S. schools been of higher quality.”*

### **For-Profit Education Model**

A for-profit education industry has emerged to focus on serving the growing market of non-traditional students. The for-profit sector has 4,348 institutions serving more than 765,000 students. The for-profit sector is very diverse, offering a full complement of traditional two-year and four-year degree programs as well as shorter, career-specific diploma and certificate programs.

In general, the student who attends a for-profit institution is seeking a career-focused education. He or she might enroll in an associate’s degree program in culinary arts or a Ph.D. program in psychology. On average, such students are older than traditional students and often attend school part-time while they are working. The students are typically seeking to enter a new career or advance in their current one, often seeking a professional qualification that enhances earnings potential. For example, in most public school systems a teacher with a master’s degree earns more than a teacher with only a bachelor’s degree.

For-profit schools are student-centric versus faculty-centric. Classes are taught days, nights and weekends (leading to more efficient use of capacity than at traditional schools), and many for-profit schools offer online degree programs for convenience. While traditional universities also offer online education, it is rare that they offer a full degree program online due to faculty

objections and the universities' concern about broadening their enrollment base and potentially diluting their brand.

For-profit schools often have multiple geographic locations operating under the same brand. Facilities are usually located in areas that are convenient to automobile or public transportation. They typically do not have sports teams, campuses or elaborate facilities.

A common term for for-profit schools is "career colleges," which typically refers to the fact that for-profit schools offer education programs in occupational fields. CCA, in its 2005 Fact Book, reported that its 1,270 member organizations educate more than one million students each year for employment in more than 200 occupational fields, graduating approximately half of the technically trained workers who enter the U.S. workforce each year. It estimates that career colleges confer approximately 39% of all health degrees/certificates and 35% of all technology degrees/certificates awarded at two-year and less institutions in the U.S.

CCA estimates that approximately 7% of all college students attend a career college and that career colleges comprise approximately 38% of all institutions participating in the Title IV financing programs. Some key demographics of the student population of CCA's members are:

- Employed while in school – 79%
- First generation college students – 69%
- Minorities – 51%
- Single parents – 30%
- African American – 21%
- Hispanic – 19%

These statistics further support the observation that the for-profit colleges and universities have been able to capitalize on changing student demographics.

### **Publicly Traded Postsecondary Companies**

There are 11 publicly traded for-profit postsecondary schools, as listed in the first exhibit below, and together they have \$8.4 billion in combined trailing revenues. An additional company, Laureate Education, with approximately 159,000 students, focuses primarily on international markets and as such is not included in the exhibit. The 11 public companies enrolled more than 580,000 students as of the third quarter of 2004, representing approximately 3.5% of the projected 2004 total U.S. postsecondary student population. According to the 2004 Legg Mason Postsecondary Fact Book, total enrollment growth for these schools (exclusive of Lincoln Educational that went public in June) has averaged 24% per year since the end of 2001.

In the case of service providers to the industry, there are a limited number of companies primarily focused on serving the postsecondary education industry and very few of those are publicly traded companies.

**Exhibit 12****Public Company Information****Postsecondary Schools**

(\$ in millions, except per share amounts)

| Symbol  | Company               | Stock Price<br>9/30/2005 | <u>52 Week</u> |          | TTM<br>Sales | Market<br>Cap | Enterprise<br>Value | Enterprise<br>EBITDA | <u>Enterprise Value to</u> |        |
|---------|-----------------------|--------------------------|----------------|----------|--------------|---------------|---------------------|----------------------|----------------------------|--------|
|         |                       |                          | Hi             | Low      |              |               |                     |                      | Rev.                       | EBITDA |
| APOL    | Apollo Group          | \$ 66.39                 | \$ 87.45       | \$ 62.55 | \$ 2,150     | \$ 11,986     | \$ 11,672           | \$ 737               | 5.4 x                      | 15.8 x |
| CCDC    | Concorde Career       | 15.35                    | 20.35          | 13.38    | 82           | 92            | 72                  | 6                    | 0.9 x                      | 11.5 x |
| CECO    | Career Edu. Corp.     | 35.56                    | 43.09          | 26.22    | 1,940        | 3,661         | 3,220               | 422                  | 1.7 x                      | 7.6 x  |
| COCO    | Corinthian Colleges   | 13.27                    | 20.25          | 11.90    | 964          | 1,211         | 1,180               | 149                  | 1.2 x                      | 7.9 x  |
| DV      | Devry Inc.            | 19.05                    | 24.48          | 13.00    | 781          | 1,344         | 1,410               | 110                  | 1.8 x                      | 12.8 x |
| EDMC    | Education Mgmt.       | 32.24                    | 36.03          | 24.21    | 1,020        | 2,419         | 2,320               | 234                  | 2.3 x                      | 9.9 x  |
| ESI     | ITT Education         | 49.35                    | 54.32          | 34.26    | 654          | 2,282         | 1,930               | 176                  | 3.0 x                      | 11.0 x |
| EVCI    | EVCI Career College   | 6.38                     | 11.05          | 4.44     | 39           | 79            | 76                  | 6                    | 2.0 x                      | 13.5 x |
| LINC    | Lincoln Educational   | 11.79                    | 21.00          | 11.67    | 282          | 295           | 276                 | 35                   | 1.0 x                      | 7.9 x  |
| STRA    | Strayer Education     | 94.52                    | 118.52         | 77.24    | 202          | 1,360         | 1,250               | 77                   | 6.2 x                      | 16.3 x |
| UTI     | Universal Tech. Inst. | \$ 35.91                 | \$ 40.80       | \$ 29.21 | \$ 296       | \$ 996        | \$ 949              | \$ 62                | 3.2 x                      | 15.4 x |
| Total   |                       |                          |                |          | \$ 8,409     | \$ 25,726     | \$ 24,355           | \$ 2,012             | 2.9 x                      | 12.1 x |
| Average |                       |                          |                |          | \$ 764       | \$ 2,339      | \$ 2,214            | \$ 183               | 2.6 x                      | 11.8 x |

Source: Company filings.

**Service Providers**

(\$ in millions, except per share amounts)

| Symbol  | Company         | Stock Price<br>9/30/2005 | <u>52 Week</u> |         | TTM<br>Sales | Market<br>Cap | Enterprise<br>Value | Enterprise<br>EBITDA | <u>Enterprise Value to</u> |        |
|---------|-----------------|--------------------------|----------------|---------|--------------|---------------|---------------------|----------------------|----------------------------|--------|
|         |                 |                          | Hi             | Low     |              |               |                     |                      | Rev.                       | EBITDA |
| BLKB    | Blackbaud, Inc. | \$ 14.17                 | \$ 15.22       | \$ 9.46 | \$ 152       | \$ 593        | \$ 542              | \$ 46                | 3.6 x                      | 11.7 x |
| BBBB    | Blackboard, Inc | 25.01                    | 25.94          | 13.54   | 124          | 673           | 574                 | 27                   | 4.6 x                      | 21.3 x |
| ECLG    | eCollege.com    | \$ 14.86                 | \$ 15.24       | \$ 8.36 | \$ 96        | \$ 325        | \$ 332              | \$ 15                | 3.5 x                      | 22.0 x |
| Total   |                 |                          |                |         | \$ 371       | \$ 1,590      | \$ 1,448            | \$ 88                | 3.9 x                      | 16.4 x |
| Average |                 |                          |                |         | \$ 124       | \$ 530        | \$ 483              | \$ 29                | 3.9 x                      | 18.3 x |

Source: Company filings.

**In Registration to go Public**

(\$ in millions )

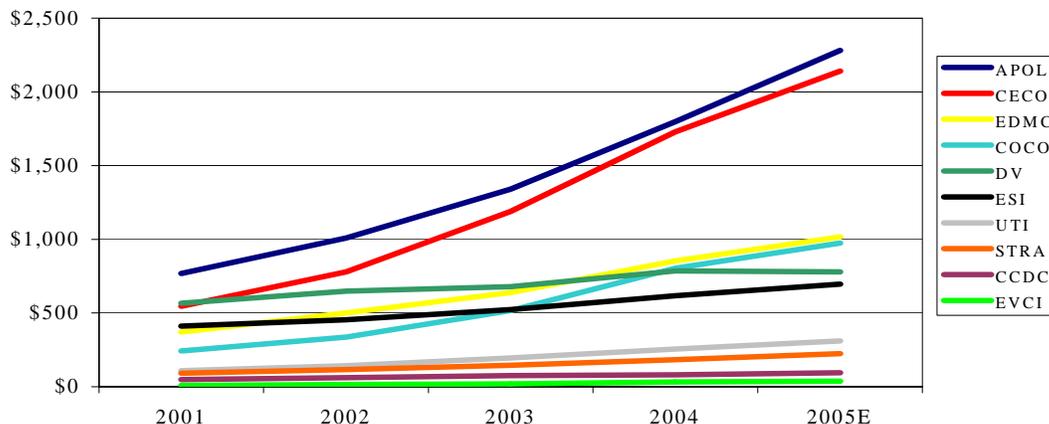
| Proposed<br>Symbol | Company                   | 2004<br>Sales | 2004<br>EBITDA |
|--------------------|---------------------------|---------------|----------------|
| CAPU               | Capella Education Company | \$118         | \$15           |

Source: Company filings.

The following exhibit depicts the annual revenues of the publicly traded postsecondary companies, excluding Laureate Education, which was formed in May 2004 and Lincoln Educational, which went public in June, 2005. As can be seen, the two largest companies in terms of market capitalization and sales, Apollo and Career Education, have experienced the most dramatic revenue growth rates over the period. This correlation of size to revenue growth also tracks with many of the other companies with smaller market capitalization.

**Exhibit 13****Revenue Growth of Publicly-Traded Postsecondary Schools**

(\$ in millions)



Source: Company filings and various research estimates.

**Postsecondary Industry Private Equity Market**

The level of transaction activity in the private equity market has accelerated substantially in the past few years. Until 2001, few deals were completed in the industry as investors gravitated toward K-12, corporate training and technology investment opportunities. As the dot-com boom subsided in 2001, investors became attracted to the economic characteristics of the postsecondary business model. In addition, by that time the success of the public companies in the industry and the active M&A market provided validation and positive exit potential.

Eduventures recently estimated that more than \$161 million was invested in higher education in 2004, up from \$83 million in 2003 and \$92 million in 2002. The majority of transactions in the industry have been recapitalizations or buy-outs and the largest transaction of 2004 was TA Associates' \$53 million purchase of Florida Career College. The General Partner believes the prevalence of control transactions is largely driven by the fact that the private equity firms active in the industry are seeking to invest at least \$10 million of capital and transactions of that size or larger non-control have been scarce. Several private equity firms are pursuing consolidation strategies, acquiring a "platform" company and then making complementary acquisitions. A notable characteristic of the transactions listed in Exhibit 14 is the quality of the outcomes, including several initial public offerings and successful sales.

### Exhibit 14

#### Selected Postsecondary Private Equity Investments

| <u>Investor</u>          | <u>Company</u>                 | <u>Year of</u>    |                                | <u>Amount</u> | <u>Outcome</u>  |
|--------------------------|--------------------------------|-------------------|--------------------------------|---------------|-----------------|
|                          |                                | <u>Investment</u> | <u>Transaction Description</u> |               |                 |
| Salix Ventures/HLM       | Prism Education Group          | 2005              | Private placement              | \$6.2         | Private         |
| Arlington Capital Ptr.   | Institute of Technology        | 2004              | Acquisition                    | N/A           | Private         |
| Frontenac                | Deltak Education               | 2004              | Acquisition                    | \$25.0        | Private         |
| Great Hill Partners      | Chubb Institute                | 2004              | Acquisition                    | N/A           | Private         |
| JLL Partners, Inc.       | The Marco Group                | 2004              | Acquisition                    | \$52.0        | Private         |
| Sterling Capital         | Florida Coastal School of Law  | 2004              | Acquisition                    | N/A           | Private         |
| TA Associates            | Florida Career College         | 2004              | Acquisition                    | \$53.0        | Private         |
| Generation Partners      | MedVance Institute             | 2003              | Private placement              | \$9.5         | Private         |
| Great Hill Partners      | Northface                      | 2003              | Private placement              | \$13.0        | Private         |
| Hanseatic Partners       | Higher One                     | 2003              | Private placement              | \$2.5         | Private         |
| ABS Capital Partners     | American Public University     | 2002              | Private placement              | \$10.0        | Private         |
| Emerald Investments      | MedVance Institute             | 2002              | Bridge financing               | \$1.5         | Private         |
| Putnam Investments       | Capella Education Company      | 2002              | Private placement              | \$7.5         | IPO in reg.     |
| William Blair/Clearlight | US Education                   | 2002              | Acquisition/Formation          | N/A           | Private         |
| Charlesbank Capital      | Universal Technical Institute  | 2001              | Follow-on capital raise        | N/A           | 2003 IPO        |
| Emerald Investments      | American Public University     | 2001              | Private placement              | \$0.5         | Private         |
| GTCR                     | ForeFront Education Group      | 2001              | Acquisition                    | N/A           | Private         |
| Huron                    | Delta Colleges                 | 2001              | Recapitalization               | N/A           | Private         |
| Leeds Weld               | Ross Education                 | 2001              | Acquisition                    | N/A           | Sold to DV      |
| Penske Capital           | Universal Technical Institute  | 2001              | Follow-on capital raise        | N/A           | 2003 IPO        |
| Forstmann Little         | Capella Education Company      | 2000              | Private placement              | \$35.0        | IPO in reg.     |
| Stonington Partners      | Lincoln Technical Institute    | 2000              | Acquisition                    | N/A           | 2005 IPO        |
| Great Hill Partners      | Hi Tech Institute              | 1999              | Recapitalization               | \$27.0        | Private         |
| BCI                      | Alta Colleges/Westwood schools | 1998              | Private placement              | \$8.0         | Private         |
| Novak Biddle, Carlyle    | Blackboard, Inc.               | 1998              | Private placement              | N/A           | 2004 IPO        |
| Olympus Partners         | Stratys/NTU                    | 1998              | Recapitalization               | \$22.0        | Sale to Sylvan  |
| SG Cowen                 | Stratys/NTU                    | 1998              | Recapitalization               | \$22.0        | Sale to Sylvan  |
| Weiss Peck & Greer       | Masters Institute              | 1998              | Private placement              | \$13.0        | 2001 bankruptcy |
| Jordan Company           | Universal Technical Institute  | 1997              | Recapitalization               | \$26.3        | 2003 IPO        |
| Heller Equity Capital    | Career Education Corp.         | 1994              | Purchase                       | N/A           | 1998 IPO        |
| Primus                   | Corinthian                     | 1994              | Purchase                       | N/A           | 1999 IPO        |
| Frontenac                | DeVry                          | 1987              | MBO                            | N/A           | 1991 IPO        |
| Primus                   | DeVry                          | 1987              | MBO                            | N/A           | 1991 IPO        |
| Camden Partners          | Concorde Career College        | NA                | PIPE                           | N/A           | Public company  |

## Postsecondary Merger and Acquisition Activity

The postsecondary industry has been consolidating over the past several years. The market is fragmented, with 4,348 for-profit schools serving 765,000 students as of 2001. The most active acquirors have been the publicly traded companies and private equity firms. Acquisitions have been a key growth driver for public companies such as Career Education Corporation, Corinthian Colleges, Inc. and Education Management Corporation. In fact, both Career Education and Corinthian were formed in the early 1990's through venture-backed buy-outs. The unique regulatory framework of the industry increases the appeal of acquisitions as a way to enter new program areas or geographic locations without going through lengthy accreditation processes.

### Exhibit 15

#### Recent Postsecondary M&A Transactions

| <u>Acquiror</u>                      | <u>Target</u>                                     | <u>Date Effective</u> | <u>Company Valuation</u> |
|--------------------------------------|---|-----------------------|--------------------------|
| EVC Career Colleges                  | Technical Career Institutes, Inc.                 | Pending               | \$16.0                   |
| Lincoln Technical Institute          | New England Technical Institute                   | 1/11/05               | \$20.0                   |
| Lincoln Technical Institute          | Southwestern College of Business                  | 1/23/04               | \$14.5                   |
| Deltak Education                     | Webster College                                   | 9/22/04               | NA                       |
| Corinthian Colleges, Inc.            | American Motorcycle Institute                     | 8/4/04                | NA                       |
| Kaplan, Inc.                         | Texas School of Business                          | 4/1/04                | \$36.3                   |
| SunGard Ddata Systems                | Collegis  | 3/1/04                | NA                       |
| Huron Capital Partners               | Miami-Jacobs Career College                       | 1/20/04               | NA                       |
| Career Education Corporation         | Western School of Health & Business Careers       | 8/5/03                | \$8.0                    |
| eCollege.com                         | Datamark  | 11/3/03               | \$72.0                   |
| Education Management Corporation     | Bradley Academy for the Visual Arts               | 10/8/03               | NA                       |
| SCT                                  | Newfront Software                                 | 9/18/03               | NA                       |
| Corinthian Colleges, Inc.            | CDI Education Corporation                         | 9/4/03                | NA                       |
| Education Management Corporation     | American Education Centers                        | 9/2/03                | \$109.0                  |
| Corinthian Colleges, Inc.            | East Coast Aerotech, LLC                          | 8/7/03                | \$2.9                    |
| Corinthian Colleges, Inc.            | Career Choices, Inc.                              | 8/4/03                | \$42.8                   |
| Education Management Corporation     | South University, Inc.                            | 7/14/03               | \$50.0                   |
| Career Education Corporation         | Whitman Education Group, Inc.                     | 7/1/03                | \$233.0                  |
| Devry, Inc.                          | Dominica Management, Inc. (Ross University)       | 5/19/03               | \$310.0                  |
| Kaplan, Inc.                         | FTC Holdings Limited (FTC)                        | 4/3/03                | \$87.4                   |
| U.S. Education Corporation           | Western Career College                            | 2/25/03               | NA                       |
| Career Education Corporation         | Formastrat S.A. and subsidiaries (INSEEC Group)   | 2/18/03               | NA                       |
| Wellspring Capital Management LLC    | Vatterott College                                 | 1/17/03               | \$105.0                  |
| Kaplan, Inc.                         | RETS Technical Center                             | 12/17/02              | NA                       |
| Sylvan Learning Systems, Inc.        | Stratys Learning Solutions / NTU                  | 11/6/02               | NA                       |
| Education Management Corporation     | California Design College                         | 10/15/02              | NA                       |
| Kaplan, Inc.                         | Concord School of Management                      | 10/10/02              | NA                       |
| Education Management Corporation     | Institute of Digital Arts (IDA)                   | 10/3/02               | \$25.8                   |
| Education Management Corporation     | Center for Digital Imaging and Sound (CDIS)       | 10/3/02               | NA                       |
| SCT                                  | Campus Pipeline                                   | 10/2/02               | \$42.0                   |
| Sylvan Learning Systems, Inc.        | Glion Group S.A.                                  | 9/4/02                | \$39.8                   |
| Career Education Corporation         | Missouri College                                  | 9/3/02                | \$6.1                    |
| Concorde Career Colleges, Inc.       | Extended Health Education                         | 8/27/02               | NA                       |
| Huron Capital Partners               | McCann Education Centers, Inc.                    | 8/1/02                | NA                       |
| Corinthian Colleges, Inc.            | Wyo-Tech Acquisition Corp.                        | 7/2/02                | \$84.4                   |
| U.S. Education Corporation           | Silicon Valley College                            | 6/27/02               | NA                       |
| Kaplan, Inc.                         | TESST College of Technology                       | 5/6/02                | NA                       |
| Charlesbank Capital / Penske Capital | Universal Technical Institute Inc.                | 4/8/02                | \$115.0                  |
| Logistics Management Resources, Inc. | Interstate University, Inc.                       | 4/1/02                | NA                       |
| Corinthian Colleges, Inc.            | National School of Technology, Inc. (NST)         | 4/1/02                | \$14.0                   |
| Sylvan Ventures                      | Walden University                                 | 2/21/02               | \$80.0                   |
| Corinthian Colleges, Inc.            | Learning Tree University, Inc. and LTU Extension, | 1/2/02                | \$5.3                    |

Throughout the late 1990's and into 2002, the public companies demonstrated a willingness to purchase small schools to acquire a strategic asset or platform. However, as the acquirors' own platforms have become broader they are less interested in small deals and instead are primarily

focusing on large transactions. The ramifications for small schools, which in many cases are family-operated, are significant. It deprives them of exit opportunities, which means that they will be increasingly forced to compete with large, well-capitalized companies for students. It is likely that in order to succeed, many small schools will have to raise capital in order to market effectively in a more crowded competitive arena or to increase their companies to a size that is more likely to attract acquiror interest.

### **International Postsecondary Education**

An area of growing interest to postsecondary schools and investors is the market opportunity outside of the U.S. The international postsecondary market is estimated by Harris Nesbitt to be larger than that of the U.S. and at the early stages of a dramatic growth curve. The following table shows the penetration (percentage of eligible school-age population taking some postsecondary coursework) levels and recent growth rates, as well as overall population sizes for selected countries.

#### **Exhibit 16**

#### **Select Postsecondary Penetration Rates**

|               | 2004<br>Population<br>(millions) | 1999 | 2000 | 2001 | 2002 | CAGR  |
|---------------|----------------------------------|------|------|------|------|-------|
| China         | 1,299                            | 7%   | 10%  | 13%  | 16%  | 31.7% |
| India         | 1,065                            | 11%  | 11%  | 11%  | 12%  | 2.9%  |
| Indonesia     | 239                              | 15%  | 15%  | 15%  | 16%  | 2.2%  |
| Brazil        | 184                              | 15%  | 16%  | 18%  | 21%  | 11.9% |
| Mexico        | 105                              | 20%  | 20%  | 21%  | 22%  | 3.2%  |
| United States | 293                              | 70%  | 71%  | 81%  | 83%  | 3.8%  |

Source: Harris Nesbitt, *Education and Training*, Sept 2005

According to the Organisation for Economic Co-operation and Development (“OECD”), an organization of 30 member countries formed in 1961 as the economic counterpart to NATO, education plays a key role in OECD countries. Below are excerpts from its annual **Education at a Glance** survey, which mirror the trends that have been experienced in the U.S.

*“Education is a gateway to employment, and in almost all OECD countries, educational attainment levels continue to rise. On average, three quarters of people born in the 1970s have gone all the way through secondary school, now the essential baseline qualification for successful entry into the labour market, compared with only half of those born in the 1940s.”*

*“The earnings premium for people with tertiary education, as opposed to those with only secondary education, grew further between 1997 and 2003 in all but four of the 22 OECD countries with available data, on average by one percentage point each year. (This earnings premium ranges from around 25% in Denmark and New Zealand to between 50% and 119% in the Czech Republic, Finland, France, Germany, Hungary, Ireland, Italy, Portugal, Switzerland, the United Kingdom and the United States.)”*

*“What is more, OECD studies show that the earnings gap between the better-educated and those with lower qualifications is growing rather than shrinking. In all OECD countries, people without upper secondary education face a significantly higher, and growing, risk of unemployment. On average, 15% of 20-to-24-year-olds in OECD countries without upper secondary qualifications are unemployed, double the rate of those who have completed secondary school.”*