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PRESENTATION

Operator

Good evening, and welcome to the 2U first-quarter 2014 earnings results conference call and webcast. This call is being recorded. I would now like to turn the call over to 2U's Senior Vice President of Communications. Mr. Chance Patterson for opening remarks and introductions. Mr. Patterson, please go ahead, sir.

Chance Patterson - 2U Inc. - SVP of Communications

Thank you, Marcus. Hello everyone, and welcome to 2U's first-quarter 2014 earnings call. Following my introduction, I'll turn the call over to our CEO, Chip Paucek, who along with our COO, Rob Cohen, and CFO, Cathy Graham, will walk you through the financial results and guidance found in the earnings release distributed this afternoon. You can find a copy of this earnings release in the Investor Relations Section of our website at investor.2u.com. The recorded webcast of this call will be available in the Investor Relations Section of our website for three months from today. Also, we routinely post analysis and information on our website, which we encourage you to access and make use of.

Before we begin, I'd like to point out that during the course of this call we will make forward-looking statements regarding future events and the future financial performance of the Company. These forward-looking statements are subject to material risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements. We caution you to consider the important risk factors that could cause actual results to differ materially from those in the forward-looking statements. In particular, we refer you to the risk factors described in the financial prospectus or our initial public offering, filed with the SEC on March 28, 2014, the quarterly report on Form 10-Q that we filed today, and other filings with the SEC. Any forward-looking statements that we make today are based on the assumptions that we believe to be reasonable as of this date. We undertake no obligation to update these statements as a result of new information or future events.

During this call, we will also present GAAP and non-GAAP financial measures. The non-GAAP measures are in addition to, not a substitute for or superior to, measures of financial performance prepared in accordance with GAAP. The non-GAAP results and the related reconciliations to GAAP can be found in our press release. And with that, let me turn the call over to Chip Paucek.

Chip Paucek - 2U Inc. - CEO

Thanks, Chance. I'd like to welcome all of you to our first earnings call as a public company. Before I get into our Q1 financial highlights, given that this is our first call as a public company, I want to take a moment to remind you who we are. 2U enables top colleges and universities to build what we believe are the world's best online degree programs. Our approach, we like to think of it as no-back row. We also know the back rows, the seats closest to the exit, a refuge for minds that wander, home of the unraised hand. What if we could eliminate that back row and move every student forward to realize his or her potential?



Our stats platform and bundled tech-enabled services allow our university partners to do exactly that, expanding their reach globally, delivering what we believe to be the highest quality online education experience. In doing so, we're brand stewards for some of the best universities in the world, including USC, UNC Chapel Hill, Georgetown, George Washington, and Berkeley. Our partners have made online students equal to their on-campus counterparts, something that typically doesn't happen.

This is the real thing on every level. It's the same degree, same faculty, same quality, and therefore the same price as on-campus. Because of the intimate experience enabled by our software, these students aren't just becoming graduates, they're becoming Trojans, Tar Heels, Hoyas, Colonials, Golden Bears, and so on. Segregation of online students has officially ended. Online students have gone from out of sight and out of mind to right smack-dab in the front row.

From a business model perspective, 2U shares tuition revenue with its university partners over a 10- to 15-year period for each program. 2U handles all technology, student and faculty support, in-program placement, job placement, content creation, and student acquisition, making it both profitable and mission-driven for our university partners. The partner handles all things you would want a university to do, including admissions, financial aid, accreditation, and most importantly, brilliant faculty instruction. While we work to acquire qualified students upfront, we received 60% to 70% of the lifetime value of the student as they study and take their courses. Outcomes matter to 2U.

I'll now make a few comments on our financial performance for the first quarter, which was very strong all around. We exceeded our internal estimates across the board, including top-line revenue and its primary driver, full-course equivalents. We also spent effectively, allowing us to come in nicely ahead of plan on our adjusted EBITDA levels and net income measures. I'm pleased to announce that we delivered \$26.3 million in revenue for the quarter with a \$3.8 million adjusted EBITDA loss. This strong performance and our increased expectations are now reflected in the full-year guidance we've given for both top and bottom line. Clearly we're focused on growth, but as CEO I think it's really important for me to say that we're not just committed to year-on-year revenue growth, but also to decreasing losses and moving this Company towards overall profitability.

Now I'd like to spend a minute on new programs and new program offerings. We've committed to launch a minimum four new programs a year on an ongoing basis. In addition, you'll see other announcements from us that are not new programs, but rather additional offerings within an existing program. To help you understand everything that we enable for our partners, we've provided a list of programs and program offerings as an attachment to the earnings release. Kathy will explain how to think about the financial impact of additional offerings within existing programs in just a moment.

We currently have 15 total programs signed, 11 which are already launched with 4 more scheduled to launch later this year and in 2015. A key part of our portfolio strategy is to build additional programs in most of the degree verticals where we operate. It's clear that not every student is right for every school. By launching more than one program in the same academic discipline, we not only further our mission but unlock substantial leverage in the business model by converting more of the leads we're already generating into students.

Let's discuss our pipeline. First, 2014. Our 2014 schedule is now filled. The four programs launched or scheduled to launch in 2014 are first, University of California Berkeley's Master of Information and Data Science. Launched in January, this program was a, quote, greenfield opportunity, which means it was a new degree program for Berkeley, and they're offering it exclusively online. We expect to see more of these greenfields in the future.

Number two, George Washington University's Executive Master of Health Administration. Launched in April, this is our second degree with GW, following the successful Master of Public Health we did with them last year. They happen to be my alma mater, so that makes me happy.

Number three, Simmons College Master of Social Work. Set to launch in July of 2014, this is our second degree program with Simmons, joining the Master of Science and Nursing launched in 2013. This program, importantly, is our second in the social work vertical, accompanying the MSW offered by our longtime partner, University of Southern California.

Number four, again with Simmons College. The RN-to-BSN with classes scheduled to start in October. This will be the first undergrad program we enable. Importantly, this program also includes an RN-to-MSN option, allowing students that do not currently have a bachelors to pursue an advanced practice nursing masters degree in a continuous program. This is a very significant opportunity for 2U. It's the Company's first undergraduate degree program. It's a large market for degree conferrals, in that most US nurses have a two-year degree. This program will allow them to finish the bachelors, and help them rise up in the ranks of their organizations. Also, it allows us to significantly expand our funnel for the MSN advanced practice degree. Finally it's our third offering with the fantastic Simmons College of Boston, a historic and great institution that has truly leaned in in every way possible under the leadership of President Helen Drinan.

In addition to these full programs, I'd also like to highlight a new notable new offering that are -- expands our existing program with the Washington University School of Law. 2U will be enabling its first degree with a non-US university and its first dual degree. Washington University in St. Louis and Tecnologico de Monterrey have partnered to offer a dual Master of Law's LL.M degree. This will give students in Latin America the ability to receive their international and US legal training together, resulting in degrees from both schools. We've always believed the Company would launch degrees with universities outside of the United States, and this step with one of the finest institutions in Latin America is a first for us.



Now on to 2015. We have two new programs and three new offerings in existing programs signed and targeted for a 2015 launch. As disclosed in our prospectus, we've signed with Syracuse University's SI Newhouse School of Public Communication to launch a Master in Communications degree later next year, pending university and state process. This is a new vertical for 2U.

I'm thrilled to announce today that we've signed with Syracuse University's Martin Jay Whitman School of Management to enable their Master of Business Administration. This is a great opportunity for us to partner with a great university brand and expand access to high-quality degrees in one of the largest academic disciplines. Notably, this is our second MBA program, and a very big opportunity for the Company. The chancellor and President of Syracuse, Kent Syverud, was the Dean at Washington University at St. Louis School of Law, where he launched our groundbreaking LL.M program, and he's been a strong supporter. We're very excited to work with Dean Ken Kavajatz and his team to announce -- to build a fantastic flexible MBA program.

For new operating and exiting programs, in April we announced our first doctorate degree, giving us presence across the full spectrum of higher education from undergraduate to doctorate. The Doctor of Education, or EDD, is with the USC Rossier School of Education, and will launch in January of 2015. Rossier was our first partner, so it's really particularly sweet for me to announce our first doctorate with our original partner. We really love what it says about our business that our partners are expanding with 2U. We believe it shows they're happy and are looking for additional growth opportunities.

On that note, in our prospectus we also disclosed that we'll be enabling a Doctor of Social Work with our second partner, the USC School of Social Work. This new offering in USC's highly successful MSW program should launch in late 2015. Dean Marilyn Flynn continues to innovate with the USC School of Social Work.

Now we're making some additional news today with a new offering in our MBA relationship with the University of North Carolina's Kenan-Flagler Business School. In 2015 we will launch a Master of Accounting with Kenan-Flagler. We are excited to expand our Kenan-Flagler relationship and expand the opportunities that students have there. New Dean Doug Shackelford was the Associate Dean of MBA UNC before taking over the role of Dean, and he's truly a digital pioneer. We're excited about the pipeline. You can expect additional announcements throughout the year. With that, I'll hand things over to our President and COO, Rob Cohen, for some first-quarter operating highlights.

Rob Cohen - 2U Inc. - COO

Thanks, Chip. I want to start off by talking about Net Promoter Score, or NPS for short, which is how we measure satisfaction across our program. Our blended student and faculty NPS during Q1 was 71.5, up from 68.5 in the fourth quarter. This rivals some absolute industry stalwarts, including Apple iPad, Netflix, and Amazon. Let's remember that NPS is a high bar. Anything above 0 is good, and anything above 50 is world-class. We believe the more satisfied students and professors are, the more likely student outcomes are excellent.

From an operations standpoint, our dedicated team is providing active ongoing support for 11 online graduate degree programs. Here are some quick stats to illustrate this undertaking. 83% of all students that start at one of our programs had graduated or were still enrolled as of March 31. We are enabling, on average, over 1,000 live classroom sessions a week. To remind you, these sessions are live interactions between faculty and students in intimate classes that average only 10.5 students. At the end of March, our partner program had enrolled 9,568 students inception to date. We expect to surpass 10,000 students inception to date during this second quarter. And we have successfully placed students nearly 17,000 times in over 10,000 placement sites.

Our team and Company have received numerous accolades over the past few months, and I'd like to highlight two. Last month, we were announced as the winner of the Partnerships Award for the second consecutive year at the GSC Education Innovation Summit. Also last month, all of us at 2U were thrilled that Glassdoor honored Chip as one of the five highest rated CEOs among small- to medium-sized companies. The ranking relies on the input of employees, who provide feedback on Chip's leadership versus Glassdoor's anonymous online review survey. Chip received a 97% approval rating from 2U employees, ranging from interns to upper management. Finally, I'm pleased to announce that inception-to-date tuition bookings for our university partners through March 31 was \$531 million, a true testament to the value this Company creates for our partners. Cathy?

Cathy Graham - 2U Inc. - CFO

Thanks Rob, and good afternoon everyone. For the first quarter we recognize revenue of \$26.3 million, a 38% increase over the same quarter of 2013. As expected, the majority of our revenue continues to come from our first launch cohort, consisting of the four programs launched before 2013, which made up 88.5% of revenue for the quarter. Our revenue growth was driven by increases in full-course equivalents enrollments, or FCEs, and to a lesser extent, in average revenue per FCE. In the first quarter, FCEs increased by 28% over the same quarter of 2013, due both to growth in existing programs and to the addition of new programs and program offerings in 2013 and this first quarter.

For additional detail on FCEs and FCE trends, we've provided eight quarters of FCE history as part of our earnings release. We've also provided our platform revenue retention rate for the first quarter to give you more insight into the performance of our most established programs. Full explanations of these metrics can be found in the MD&A section of today's 10-Q filing.



Average revenue per FCE increased by 7% compared to the prior year, due primarily to a 5% weighted average increase in our partners' tuition rates. The remaining increase was due to an increase in credits per course during the quarter. This measure will vary quarter to quarter, based on which specific courses within various programs are being taught in that quarter.

Net loss attributable to common stockholders was \$7.1 million compared to \$3.8 million for the first quarter of 2013. On a per-share basis, our loss for the first quarter was \$0.93 compared to \$0.52 for the same quarter of 2013. Considering the impact of shares we sold in and warrants we revalued with our IPO, pro forma net loss per share was \$0.20. I'd like to make clear that our pro forma per-share loss is simply net loss adjusted only for warrant expense divided by pro forma shares. It does not exclude equity compensation expense of approximately \$1.2 million during the quarter.

The year-over-year expansion in our net loss was expected, and resulted primarily from having twice as many programs in the early development stage as we did in the 2013 quarter. We make significant investments in new and prelaunch programs, with expenses significantly outpacing revenues during this phase. As expected, having more programs in early development increased our loss on a year-over-year basis, but set the stage for accelerated future revenue growth.

While early-stage investments were the key driver of net loss expansion, there were two non-cash items that contributed as well. First, we recognized \$688,000 in warrant expense related to revaluing preferred stock warrants held by our senior lender for conversion to common stock warrants. This amount is reflected in the interest expense line item on our P&L, along with interest expense related to a \$5 million borrowing we made on our credit line that was repaid within the quarter.

Second, equity compensation expense increased to \$1.2 million in the first quarter compared to \$436,000 in the same quarter of 2013. The increase was driven by two factors: grants made for new hires, promotions and retention as we expanded our management team to support new programs, and the increasing valuations attributed to our common shares as we approached our public offering.

Our adjusted EBITDA loss for the quarter was \$3.8 million compared to \$2.4 million for the same quarter of 2013. As with net loss, much of the expanded adjusted EBITDA loss was driven by increased expenses related to having a greater number of programs in the early development stage. However, as you'll see looking at full-year guidance, which shows an improvement in our year-over-year adjusted EBITDA loss, we expect this dynamic to be temporary as we move forward with a consistent launch schedule.

Quickly commenting on the balance sheet. Our cash position pro forma for the public offering was \$106.2 million. This included proceeds of partial exercise of the underwriters over-allotment option, in which they purchased approximately 626,000 shares from us and 435,000 from selling shareholders.

I'd like to remind you that we recognize revenue for each program from the first day of classes to the last, and receive payment from our partner universities after the start of their academic terms. Each partner program has a unique academic calendar, although they are predominantly offering four academic terms per year. Depending on where our partners are in their academic calendars, at the end of each calendar quarter, we could have wide variations in cash, accounts receivable, and deferred revenue from quarter to quarter. We suggest that you look at changes in these accounts as a group to better understand our balance sheet position.

As this is our first opportunity to speak directly to some of you, I want to make sure everyone has a basic understanding of the financial lifecycle of a program. This will help you understand how our announcement of new programs and additional offerings within existing programs play into our financial models. We start investing in new programs about nine months before they launch. Over the next three to four years, we will invest, on average, net negative cash of between \$4 million and \$9 million in a program. Primary programs, which are the first programs we launch in a degree vertical, are at the high end of this range and on the longer end of that three-to four-year to breakeven period. Additional programs in existing degree verticals are at the lower end of both the investment and time to breakeven ranges.

Although our of technology and content development is similar for both primary and additional programs, marketing spend becomes materially more efficient when we add a second program. As we own the lease we generate, we can match more interesting students with appropriate programs when we offer more than one program in a degree vertical. And, because we have already built a lead base for our first program, second programs can scale more quickly and at lower incremental costs. We expect the programs we enable to reach steady-state scale in an average of 6 years into our 10- to 15-year contract terms.

As Chip said earlier, we often have multiple offerings within a single program that leverage similar content, marketing channels, or both. These additional offerings are one of the ways we drive our partner programs towards reaching their full potential. When we launch a new program, we often anticipate additional offerings as a part of our financial model for that program. So unless we tell you otherwise, you should assume that these additional offerings are already built into the program's long-term financial expectations.

Now looking at guidance, we expect revenue for the second quarter to be between \$23.3 million and \$24.1 million. At the midpoint of this range, it represents 27% growth over the same quarter of 2013. On a sequential basis, the decline in expected revenue is seasonal and anticipated. Due to their academic calendars, our partner programs generally have more days out of session during the second quarter than any other, which impacts the timing of our revenue recognition.



For full year 2014, we expect revenue of between \$105 million and -- \$104.5 million and \$107.5 million, reflecting the seasonal step-up in quarterly revenue during the second half of the year. Of second-half revenue, we expect that 48% to 49% will be recognized in the third quarter and 51% to 52% will be recognized in the fourth quarter. Remember that while we will be launching additional new programs over the remainder of the year, they contribute very little to revenue in their early operating quarters. The vast majority of revenue from this point in the year forward will come from already launched programs. And I'd like to remind you that we have tremendous revenue visibility for the rest of the year. Most of our remaining 2014 revenue expectations will be generated by returning students in our partner programs, who have a very high and predictable retention rates.

On the bottom line, we expect a net loss of between \$11.9 million and \$11.2 million for the second quarter, or between \$0.30 and \$0.28 per share on both a basic and a pro forma basis. For the full year, we are guiding to a net loss of between \$33.3 million and \$31 million. Based on our current forecast for share counts, this equates to a basic per-share loss of between \$1.04 and \$0.97, and a pro forma per-share loss of between \$0.85 and \$0.79. As in the first quarter, our pro forma per-share loss guidance is simply our net loss divided by pro forma shares. To adjust to a pre-equity compensation loss, we have provided you with equity compensation estimates for both second quarter and the full year.

For both periods, losses are expected to be greater than in 2013, although as you hear you'll hear, our adjusted EBITDA results for the year are expected to be better. In large part, this is driven by increases in both depreciation and amortization, and equity compensation expense. In combination, we expect these non-cash costs to be approximately \$2 million and \$6.5 million over the prior-year periods for second quarter and full-year 2014, respectively. We expect our adjusted EBITDA loss for the second quarter to be between \$8.3 million and \$7.7 million, slightly more than the \$7.3 million we reported for the same quarter of 2013.

As in the first quarter, any year-over-year increase in our loss would be largely driven by increases related to having a greater number of new and prelaunch programs. However, when looking sequentially versus the just-reported first quarter, our year-over-year adjusted EBITDA comparison is clearly improving as we settle into a consistent launch schedule. Reflecting this trend, we now expect an adjusted EBITDA loss of between \$19.7 million and \$17.7 million for the full year 2014. At the midpoint of the range, this represents an improvement over 2013 of approximately 12%. With that perspective on what we believe are very positive expectations, I'll hand things back over to Chip for some closing comments.

Chip Paucek - 2U Inc. - CEO

Before we wrap up and take questions, I want to share a quick story to illustrate how our programs are changing the lives of students. In all of our programs, students can enroll who have never been able to without this flexibility. Let me tell you about Cory Broussard. Corey is a father of four. He lives in Gonzales, Louisiana. He's a successful engineer for Shell Oil. He's enrolled in the MBA at UNC to further his educational goals while maintaining his challenging job. Cory spends 14 days a month working on an oil rig in the middle of the Gulf of Mexico. As Cory told me personally, we make it possible for him to change his life and fulfill his goals, all while keeping the great job that supports his family.

The reality is because of 2U, students don't have to quit their jobs to attend a top 20 B-school, which would have ever been possible for Cory and many others like him. I mean, think about it. Live class from an oil rig? I'd like to thank Cory for allowing us to talk about his life, say hello to his beautiful wife, [Roxy], and congratulate him on his expected graduation in October.

From a business perspective, 2U is not just taking share of an existing market. We're also making market by allowing students like Cory to fulfill their dreams. That is why we get up in the morning. We believe there is a critical long-term correlation between our financial success and our partner students' outcomes. Outcomes matter more than anything else, and Cory's proof of that. Let's eliminate the back row together, hash tag, no back row. With that, Cathy, Rob, and I will be happy to take your questions.

QUESTION AND ANSWER

Operator

Thank you, Mr. Paucek.

(Operator Instructions)

Michael Nemeroff, Credit Suisse.

Michael Nemeroff - Credit Suisse - Analyst

Congratulations on a nice start to public life. Very well done.



Chip Paucek - 2U Inc. - CEO

Thank you, Michael.

Michael Nemeroff - Credit Suisse - Analyst

Chip, can give us a sense as to whether the conversations that you're having with some of the targeted schools and the schools that you targeted, are getting easier? And if you could maybe tell us about the durations of those conversations, and whether they're lengthening, shortening, both as a result of the public offering and as a result of the momentum the Company seems to have?

Chip Paucek - 2U Inc. - CEO

The answer is yes. I wouldn't say so much the results of the public offering, but more just based on the quality that we're delivering for our existing clients. So our Syracuse announcement today is actually the fastest negotiation we'd ever had, was very short in total duration. So from not just the contract negotiation, but both contract negotiation and time from contract to launch, are shorter now than they've ever been. So pretty excited about what's happening in the pipeline overall.

Michael Nemeroff - Credit Suisse - Analyst

And then also if you could maybe give us a sense of how the hiring has gone? I know that as you launch a lot of these programs, they take a substantial amount of pretty quick hiring, you get a lot of people onboard. Is that -- how is that progressing, and do you think that you've -- you'll be able to ramp up as quickly as you're adding these new programs and verticals?

Chip Paucek - 2U Inc. - CEO

Yes. Pretty interesting that also, when we launch second programs in an existing vertical, part of what actually happens is it ramps more quickly overall. And that actually requires that we ramp the hiring for that particular program. And we launched a second program in social work, and now were in the midst of launching a second program in business. And of course, a second program in nursing, which all require faster hiring. And we've been able to keep up the pace and haven't had any issues related to that whatsoever.

I could tell you, the Company didn't launch any programs in 2012, and that was very purposeful. We had three great universities, four programs at three great universities. So we wanted to, number one, make sure that we delivered in 2013 the same quality as we had done in those early programs. And then we built an infrastructure that allowed us to scale and prepared us pretty well for 2014. So we're right on track.

Michael Nemeroff - Credit Suisse - Analyst

If you could maybe talk about -- I know that you guys have a pretty proprietary algorithm selection tool that gives you a lot of insight into which schools to partner with. And I know that's something that you've been tracking for quite a while now since you developed it. Is that -- how has that been trending? Has it been accurate? Is the correlation still as strong as it has been over the last couple of quarters? And are you still using it intensely to pick the schools that you're targeting?

Chip Paucek - 2U Inc. - CEO

Yes. We actually think in the last quarter or so we've improved it quite a bit. So we've used the proprietary program selection algorithm to select programs, whether it be our second programs in the vertical or some of our newer relationships, including the Whitman School of Management at Syracuse. So the algorithm, if anything, is looking certainly more predictive as of late. So we feel very good about its it going forward. And we do think it is, from the standpoint of a competitive edge to 2U and our partners, pretty important.

Michael Nemeroff - Credit Suisse - Analyst



Cathy, one for you, if I may. I think some of the news services may have crossed, or just gotten some of the numbers incorrect in terms of your guidance. Just to clarify what you said in the prepared remarks. The \$79 million to \$85 million on the loss for the year, that's including your stock-based compensation? If you excluded that stock-based compensation, I think my number works out somewhere into the low \$60 millions at the midpoint. Is that the comparable number we should be looking at?

Cathy Graham - 2U Inc. - CFO

Yes, it is the comparable number to be looking at. So just to clarify again, our calculation is net income adjusted only for warrant expense and not excluding equity compensation expense. And we have provided you -- divided by pro forma shares. And we have provided you with estimates of equity compensation expense for both the second quarter and the year-end guidance so that you can make those adjustments.

Michael Nemeroff - Credit Suisse - Analyst

That's great. Thanks. I'll pass it along, get back in the queue. But congratulations on a really strong start. Thanks very much.

Cathy Graham - 2U Inc. - CFO

Thank you.

Operator

Andre Benjamin, Goldman Sachs.

Andre Benjamin - Goldman Sachs - Analyst

First, I was wondering if you could talk a little bit about the competitive environment for the programs that you announced today? Or those more competitive situations maybe comment on who you went up against and why you think those customer chose 2U over those competitors?

Chip Paucek - 2U Inc. - CEO

So in general - Andre, thanks for the question. In general, we actually -- we don't participate in RFPs or competitive bidding processes. We typically identify a school that we think is both in a vertical that is very attractive to the Company and has a series of attributes that come strongly out of the program selection algorithm, without getting into details of what they are, that make that a particularly attractive school. Now, that's half the battle.

The second half of the battle is that the school has the leadership to pull it off, which we've learned from our six years of operating experience, is incredibly important in building these programs to scale. Without question, the leadership has to be there and be willing to change their processes to reflect the fact that their students aren't all in the local area. So a much bigger deal than might seem obvious.

By putting those two together, we're able to identify a school that is the partner for 2U. We're certainly not right for everyone. We are definitively not trying to bring everyone online. That is not our model. There are others that will go down that path. We're trying to build the world's best online degree programs, period. So in the case of Syracuse, clearly we were looking for a second program in what could be one of the larger verticals the Company operates in, business administration is very big. Syracuse, incredibly well-known brand with a leadership team from Chancellor to Provost to Dean that are just totally ready for the challenge.

So it wasn't a comp case with a competitive bid whatsoever. There was really no one else involved in the conversation between us and Syracuse. They are ready for it, and we're excited to take them to the online modality, so.

Andre Benjamin - Goldman Sachs - Analyst

Thanks. And maybe a two-part question on the doctorate programs you've announced. First, how did the terms of some of those programs differ from the masters, both in terms of the economics for you and the contract duration? And then I know you've given some color previously on the math for the revenue potential for 2U, and I believe that mostly just masters program. So maybe a little insight into how you think that your increased number of doctorate programs impacts that math?



Chip Paucek - 2U Inc. - CEO

The short answer, Andre, is that the contract is the same. The same terms, in general, across our partner portfolio. It is -- they're 10 to 15 years deals at a 60% to 70% revenue share. I'll hand it over to Cathy to talk a little bit about how to think about the doctorate program specifically on a financial basis.

Cathy Graham - 2U Inc. - CFO

Andre, sort of what I said in the call is that we view these as extensions, particularly now with the doctorate programs, as we don't have the level of experience in those programs as we do with the masters programs. So we view them as being additional offerings within our existing programs because they leverage, in large part, the marketing funnels and the marketing activities that we are already doing. We do make some incremental investment in these but the investment is significantly less than we would make in launching the original program. And we do have those investments built into our existing models. So for the doctorate programs, for the time being you should assume that they are built into our existing expectations.

Andre Benjamin - Goldman Sachs - Analyst

Last question. In terms of the pre-2013 programs, any color on how those have scaled and how much of the course equivalents are from those programs versus your new ones?

Cathy Graham - 2U Inc. - CFO

Well, I think that, as we said here, that full course equivalent -- that the first four pre-2013 programs represented about 88.5% of our revenue for the quarter. We're -- saw overall an increase of about 28% in full course equivalents overall, and in general those were pretty relational between revenue growth and full course equivalents.

Andre Benjamin - Goldman Sachs - Analyst

Thank you.

Chip Paucek - 2U Inc. - CEO

The only thing I would add, Andre, is our model, obviously the way the model works, programs have history, you're building bookings over time. And we're pretty excited about what we're seeing out of not just our old programs, but some of our new 2013 program launches.

Andre Benjamin - Goldman Sachs - Analyst

Thank you.

Operator

Brian Schwartz, Oppenheimer.

Brian Schwartz - Oppenheimer & Co. - Analyst

My congratulations on a real strong start here as a public company.

Chip Paucek - 2U Inc. - CEO

Thanks, Brian.

Brian Schwartz - Oppenheimer & Co. - Analyst



Chip or Rob, wanted to ask you a question. Maybe it's a derivative of Andre's question on the pricing out there. Is it possible to talk about the current pricing environment, or the take rates that you're seeing on these newer degree programs that you're signing up compared to some of those earlier programs that you've started?

Chip Paucek - 2U Inc. - CEO

Sure. Thanks for the question. So in general when we say 60% to 70%, that's not because they move during the agreement itself. It's because our early programs, we had a lower rev share, and our later programs have had a higher rev share. So without getting into specifics across the board, we certainly (technical difficulties) contract negotiation standpoint.

Brian Schwartz - Oppenheimer & Co. - Analyst

Great. And then another question on the competitive environment. Again, Chip or Rob, is it -- when you think about what you're replacing here in terms of these new degree programs out there, what are these universities using right now for their online degree programs? Is it mostly greenfield? Are they not using anything, and you're just essentially replacing like a depository like a blackboard that's out there? Any color on what you're replacing out there would be great. Thanks.

Chip Paucek - 2U Inc. - CEO

In general, sort of just generalized comment is most of the schools don't have an online program. Very rarely do you see that. Obviously over time more and more will. When there is some online initiative, it might be something that is homegrown. What we're quite proud of is, as far as our competitive set, we really are the only provider of a true SaaS solution to the school, comprehensive for not just the student, the online campus that the students see, but also for the professor and for the administrator to fully operate a high-quality online program at scale in a quality manner that's requisite with a Berkeley or a USC.

So in general, you find that most schools don't have online programs. Now, over time we think that that obviously opens up a huge opportunity for us to continue doing what we just demonstrated with Syracuse in launching more programs. Syracuse is an interesting study in a launch of a brand-new vertical for 2U, communications, which has some real market potential. And then a second program in one of the largest verticals, MBA.

Brian Schwartz - Oppenheimer & Co. - Analyst

Great. And then last question for me and then I'll pass it along. You did announce on the call here in international school, a first program outside of the United States here. I think it sounds like maybe it's a sister school with one of your partners here in the United States. I had thought international was more of an intermediate strategy for your business, and just wondering if there's any change to that thought? Or maybe you could update us here on how you're thinking about the international strategy and timing on that opportunity over the lifecycle.

Chip Paucek - 2U Inc. - CEO

We've always felt that international was -- is clearly part of the long-term story here, without question. Today, as an example, the Washington University of St. Louis Law School, we're operating an LL.M program that is purely 100% for people outside of the United States borders. It's for attorneys. It's not a degree that many on the call might be as familiar with, but if you're a practicing attorney somewhere in the world and you need to work with US law, having an LL.M from the US is important to state that you understand the US law and can demonstrate it, and you can even sit for the bar in many states in the country if you get a US LL.M. So that program we launched really focused on the world, not focused on the US.

The relationship with Monterey Tech is an extension of that program. It's our first dual degree program. We've always believed international would be part of the story. This is a great step in that direction, given that they're one of the leading institutions in Latin America. And really, if you're an attorney in Latin America you can get both your domestic degree and your US degree at the same time, two different degrees. And this was an affiliation that 2U worked to drive between those two schools. So we were sort of the key cog between the two schools.

Brian Schwartz - Oppenheimer & Co. - Analyst

Thank you for that color. And thanks for taking my questions for that. Good job on the quarter.

Chip Paucek - 2U Inc. - CEO



Thanks, Brian.

Operator

Michael Tarkan, Compass Point.

Michael Tarkan - Compass Point - Analyst

Thanks for taking my questions. I appreciate the total tuition booking number you guys have discussed. I'm trying to get a sense for the pent-up earnings that you have in the system at this point from your established programs, and basically how the leverage in the model works. I know it's kind of hypothetical, but I'm wondering if you were to shut down investments in your new programs today, can you help us understand what revenues and associated expenses would look like for those core programs at this point?

Cathy Graham - 2U Inc. - CFO

So if we were sitting here looking forward at this point and looking at our tuition-adjusted backlog, this is probably the best way to explain it to you. Our tuition-adjusted backlog at this point, which would be attrition-adjusted future revenue from students who are currently enrolled in programs. At this point it somewhere in the \$110 million range. So you can think of that as if we were to stop marketing and putting students on our books today, bringing in new students, we would have about \$110 million of revenue that has a low 20s cost of service against it. So that's kind of the way to think about that piece of the revenue.

What happens, of course, when you consolidate all of these programs into a portfolio, is that what you're seeing on the loss line for the Company is driven by investments in new programs, getting them launched, and getting them scaled. If you think about the first launch cohort, which is the first four programs that we launched in 2009, 2010, and 2011, those became adjusted EBITDA positive in 2013. And if you looked at them as though they had all launched at the same time as our first program in 2009, they would have about a mid-20s adjusted EBITDA margin on them now. So fundamentally what we're seeing is that we have good, strong, pretty predictable revenue on our existing programs, and the ones that are hitting maturity are hitting profitability.

But on a combined basis, what you're seeing are continuing losses being driven by investments in future growth. Now, as Chip said, and I'll repeat, we do have a commitment to getting the Company on a path to profitability. And I think you see that demonstrated by the fact that our full-year guidance for adjusted EBITDA is an improvement of about 12% at the midpoint over what we reported for 2013.

Michael Tarkan - Compass Point - Analyst

That's great. Thank you for that color. Just one quick follow-up on that. The \$110 million, is that the -- what the timeframe of that revenue? How should I think about that?

Cathy Graham - 2U Inc. - CFO

When we think of backlog, you can expect to get that over probably the next two-plus years, majority of it over the rest of this year and next year, a little bit somewhat the year after that. And that comes from the fact that on average our students are going to be in their programs for about 2.5 years, some shorter, some longer. But that's the period over which we would recognize that revenue.

Michael Tarkan - Compass Point - Analyst

Great. That's helpful. And then one other follow-up. Do you expect any impact from Department of Education rulemaking sessions around state authorization for distance education? I know that that's an ongoing thing. We are approaching the final hearings there. I think you handle that process for the schools. I'm just wondering if you expect any kind of disruption from that? Thanks.

Chip Paucek - 2U Inc. - CEO

Thank you. Truly, we built our state authorization process in the early years based on the fact that, frankly, we thought everyone was doing this. And we've been doing it, registering all of our schools in every state since the very beginning. So while any additional regulatory burden is always challenging for a company, we're extremely



well prepared for it. We routinely launch programs and only marketed programs where we are officially allowed to operate by the state, so green and red states per se. And pretty religious about making sure we maintain that discipline across our programs. So from a portfolio standpoint, I guess the short way to say it is, while we'd always loved less regulation, we're doing it today. So we're completely prepared for it.

Michael Tarkan - *Compass Point - Analyst*

Thank you.

Operator

Michael Huang, Needham and Company.

Michael Huang - *Needham & Company - Analyst*

Just a few questions for you. First of all, was wondering, when you guys look at your pipeline, was wondering if you could share with us what percentage are programs and offerings in existing verticals and what percentage are outside of current verticals? And then maybe as a follow-up to that, how do you think about whether it makes sense to add an incremental one in a current vertical, or whether or not to go after new verticals like engineering, architecture and others? Thanks.

Chip Paucek - *2U Inc. - CEO*

Thanks, Michael. It's a balance. We're obviously focused on both plowing virgin snow in verticals that are large and that have big market potential. We're constantly looking at greenfields, like in the case of Berkeley which is off to a fantastic start. That was a degree that you certainly wouldn't get to an enrollment prediction based on current market share, because there really are no degrees in that particular field until very recently. But we thought it was a pretty obvious, I should give Dean Anna Saxenian a lot of credit for making us see the light there. But individual programs, it's a balance of wanting to plow that virgin snow while simultaneously bringing in second programs, and in some cases even third programs, in existing verticals where that vertical is worth doing that.

As far as new offerings in existing programs, the reason we created this chart for you was we were worried that in announcing what we do all the time, which if you go back in our history there are many examples of new offerings in existing programs that are on that chart. Just a couple of examples are Masters of Arts in Teaching was our first degree with USC. We followed up later with Masters of Arts in Teaching Students Where English is a Second Language, and that program expanded that particular vertical. And so we've done that since the beginning, and we expect to continue to. We just didn't want to confuse you between that and the difference with a new full program, like in the case of -- whether it be first program in a vertical like Syracuse Newhouse, or second program in a vertical like Syracuse Business.

So that's all about just continuing to expand the market, whether it be because we're sharing content, which we do in some cases like the MA TESOL degrees, or sharing marketing funnel, like we are in like in many of the verticals, like in our nursing vertical where we started with family nurse practitioner and now we have acute critical care and midwifery. So just to be clear, we are still committing, even though you're going to see us continue to announce things like the dual degree to be with Monterey Tech, the fact is we are fully committed to no fewer than four full programs a year, whether it be first program or second program. And that's really what that list was for, to make it clear so we don't confuse people on the street.

Michael Huang - *Needham & Company - Analyst*

Got you. Very helpful. Is there a way to think about it? I know that every program and every vertical will be different, but is there a way to think about how much an offering could help scale enrollment at scale? Is there -- if you were to think about one of your programs as a minimum threshold of 500, does an offering add another 100 to that, or how do we think about that?

Chip Paucek - *2U Inc. - CEO*

We're being careful to make sure that you understand that when we add an offering -- Cathy was pretty clear to say that it was built in -- a new offering in an existing program, you should presume, is built into the existing model for that program. So, and as I said, sometimes it's because you're sharing content, sometimes it's because you're sharing funnel. You want to add anything, Cathy?

Cathy Graham - *2U Inc. - CFO*



No, I think that's it. We may at times give you guidance that says, we're putting something in as an offering and you should think of it a different way. You should think of it as expanding either the revenue opportunity or temporarily expanding our cost base before we get back on track. But unless we tell you otherwise, we really -- we view these programs as having multiple components. So we will have gotten into FCE numbers and the like. We will have build those additional offerings into our expectations over the long run.

Michael Huang - Needham & Company - Analyst

Got you, okay. And then I know that you're not going to drill too much into a cohort, so not give us too much color around each one of the individual programs, but was wondering when you're looking at that pre-2012 cohort, are they all executing at the same level? Are there any that are executing better or worse than internal expectation?

Chip Paucek - 2U Inc. - CEO

The reality is, it is a portfolio. It's hard to say that there's an average program. Obviously there will be some programs that are higher than others, and that is why we do tend to think about it on a cohort basis. I can tell you we do believe that those original four programs are reasonably predictive of the future. In other words, we do feel like on a cohort basis we're excited about what we're seeing in our 2013 launches. And now we've got the algorithm helping us select the 2014 and beyond launches. So while we don't go into an individual program, we do believe that what we're seeing on the ground would give us confidence that the core four are predictive of what we see long term.

Michael Huang - Needham & Company - Analyst

Got you, okay. And last question for me, I think Cathy in your prepared remarks you talked about a component of the ARPU increase is coming from tuition pricing across the programs. I think you had mentioned that it was up 5% year on year. Now, is that, first of all, is that the right number and is that pretty consistent with what you've seen historically, and ultimately what number do you assume around that going forward?

Cathy Graham - 2U Inc. - CFO

It is the right number you are using, that 5%. It comes from various tuition increases across our programs, not all of them were at that rate. But when you look at increases in tuition, in change in mix between courses, the number of courses being offered, FCEs in the various programs, and some addition of new programs at different rates. Yes, it is 5%. I would not build in 5% tuition increases going forward for a couple -- and we do not in our own models. It is not necessarily what we would expect to see, since some of that does come from mix.

Additionally, in the current environment I think we would all be prudent to say that our schools are for -- are discussing what their future increases are going to be. And not that they have arrived at conclusions or all will make the same conclusions, but we certainly would not mode in ourselves a 5% price increase.

Michael Huang - Needham & Company - Analyst

Great. Thanks so much, guys.

Cathy Graham - 2U Inc. - CFO

Thank you.

Operator

Jesse Hulsing, Pacific Crest.

Jesse Hulsing - Pacific Crest Securities - Analyst



Thanks for taking my question. Simmons in the Bachelor of Nursing program, it's your second foray into undergrad after a Semester Online. It seems much more targeted, and I guess specialized. Can you talk about your strategy there and your plans for the undergrad market?

Chip Paucek - 2U Inc. - CEO

Sure. Semester Online was a pilot program that we ran to prove to ourselves what everybody said was impossible. People said you can't teach undergrad with this instructional method, and we're pretty excited about the fact that Semester Online not only proves that the pedagogy would work, but that it sort of directly lead to us being able to work with a great historic women's college to launch an RN-to-BSN in a market that is predominantly female.

So it is a good question, Jesse, because it is a much more targeted -- we all tend to think of undergrad, maybe based on our own bias of what we've done from our own history, the more classic four-year residential, and undergrad is a very, very big market. There are many people that are pursuing different types of undergrad education. And in some ways, from a purely business model perspective, we expect this program to look very similar to one of our graduate programs from an operations and marketing perspective, which is part of the reason that we launched it.

I also would tell you that what's really nice about this particular opportunity is that the MSN is the path to huge value for an individual nurse. You can replace the doctor in a managed care facility or in a minute clinic. That's a big deal in terms of quality of life. And so today we have many people coming to us for either of our MSN opportunities that just don't have the ability to enroll because they don't have a bachelors. So we love what it does, either on its own as an individual undergrad marketing initiative, or as shared funnel and long-term continuous program between RN and MSN. So it's pretty powerful for us from that perspective.

Jesse Hulsing - Pacific Crest Securities - Analyst

And as a follow-up to that, Chip, when you look at your pipeline of programs, are there other undergrad programs out there, or is this a unique situation because of the tight relationship that you have with Simmons and that opportunity within the nursing vertical?

Chip Paucek - 2U Inc. - CEO

Certainly while I won't, I can't get into individual components of the future pipelines, it is safe to say, just like it is with graduate -- sorry, with International or doctorate, that we do expect to continue to expand our undergrad portfolio. Truly, undergrad is a big market. We are the leading player, we're the premier player, and if you're a great school in the country right now thinking about going online, we're certainly your top choice. So we do expect to continue to play more in that space. I think that's it.

Jesse Hulsing - Pacific Crest Securities - Analyst

Cathy, a question about your newer programs. The contract length and the tails on those, can you provide any details? Are they similar to prior programs that you've signed?

Rob Cohen - 2U Inc. - COO

Yes Jesse, I can take that one. So contract length, as we've said across the board for 2U is between 10 and 15 years. So the answer is very similar. The same from that perspective. And that's really, in our opinion, a key component of our needs on the side of the partnership, and schools that work with us know that. We're investing quite a bit upfront. Not upfront, but over the first three to four years net negative cash, and so that long-term commitment is important to us, and as well as our university partner. They know that we are truly a partner for the long term, and these are much more like marriages.

Jesse Hulsing - Pacific Crest Securities - Analyst

Right, right. And last question for me. There was some news last week, Chip, around a \$10,000 degree, bachelor degree. I guess, what are your thoughts on pricing of education and online education over time? And maybe talk a little bit about how 2U views itself as able to maintain pricing power? Thanks.

Chip Paucek - 2U Inc. - CEO



Well, I think really the key is that outcomes fundamentally matter. And when you go to a great school in this country, you tend to have a pretty phenomenal outcome. So just to speak about me for a second, without playing the violin for myself, I went to GW, got a Pell Grant, first person in my family to go to college, and the fact is GW fundamentally changed my life in every possible way, and sort of paves the way for me to do what I'm doing today, without question.

And when you go to a great school in this country, you typically have a pretty phenomenal outcome. And we fully embody that mission in this Company every day. Outcomes matter to a point where last week we actually released something that may not be as exciting or notable for investors, but it's incredibly important to our partner organizations, incredibly important to policymakers, anyone else that would be looking at the Company. Our impact report we released, it has a really solid amount of data to show the world that we're not just talking about it, we're delivering it, and we expect to deliver that every year.

So from that standpoint, Jesse, the long-term correlation will be, we believe as long as we focus on outcomes and quality, it all works out in the end. So you attend Berkeley, get a Master of Data Science, you typically have a pretty phenomenal outcome. Now, I also don't want to make light of the fact that from a tuition standpoint, while we charge the same level of tuition, it is a material decrease in student debt burden when you don't have to pick up your life, fundamentally quit your job, and moved to attend a great school. No small thing. So you're talking about a major impact to an individual's opportunity cost and debt burden.

So we -- and we think that's pretty important. The reason ultimately it's the same price is you've got the same quality, no distinction between the two degrees. Same degree itself. Same exact degree. So long term, we really like where we sit, as long as we remember to focus on what matters, which is outcomes.

Jesse Hulsing - Pacific Crest Securities - Analyst

Thanks, Chip. Good color.

Operator

We have no further questions in the queue at this time. I would like to turn the call back over to Mr. Chip Paucek for closing remarks.

Chip Paucek - 2U Inc. - CEO

Thank you very much. We really appreciate everyone being with us today for our first call as a public company. And we look forward to talking to you at conferences and at events going forward. And I encourage you to get out of that back row and come forward. Join us in the front row. Look forward to talking to you guys downstream. Take care, everybody.

Operator

Ladies and gentlemen, thank you for attending today's conference. This does conclude today's program. You may all disconnect, and have a wonderful day.

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