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Stride, Inc. (LRN)

Q1 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Stride, Inc. First Quarter Fiscal 2023 Earnings Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

Tim Casey, Vice President of Investor Relations, you may begin your conference.

Tim Casey

Vice President-Investor Relations, Stride, Inc.

Thank you and good afternoon. Welcome to Stride's first quarter earnings call for fiscal year 2023. With me on today's call are James Rhyu, Chief Executive Officer; and Donna Blackman, Chief Financial Officer.

As a reminder, today's conference call and webcast are accompanied by a presentation that can be found on the Stride Investor Relations website.

Please be advised that today's discussion of our financial results may include certain non-GAAP financial measures. A reconciliation of these measures is provided in the earnings release issued this afternoon and can also be found on our Investor Relations website. In addition to historical information, this call may also involve forward-looking statements. The company's actual results could differ materially from any forward-looking statements due to several important factors as described in the company's latest SEC filings. These statements are made on the basis of our views and assumptions regarding future events and business performance at the time we make them and the company assumes no obligation to update any forward-looking statements made during this call. Following our prepared remarks, we'll answer any questions you may have.

I'll now turn the call over to James. James?

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James Jeaho Rhyu

Chief Executive Officer & Director, Stride, Inc.

Thank you, Tim, and good afternoon, everyone. The world has been volatile, to say the least, these past few years, with many companies reeling from the impact of that volatility. When the COVID pandemic first hit, we were coming off a decade of strong economic growth, a long bull market and historically low inflation, interest rates and unemployment in a relatively peaceful global environment. Fast-forward a couple of years and we've experienced not one but two stock market corrections, almost double-digit inflation, interest rates that have tripled and heightened global tensions.

Amid all this turmoil, there is one constant that gives me optimism, the resilience, ingenuity and resolve of America, and in particular, its younger generations. In this environment, for us to continue to provide opportunities for this country to prosper, we need to ensure we are adapting to an increasingly diverse and evolving world. I believe part of that evolution is changing how we think about education. We need to focus our younger generations on skills and tools that will help them succeed in the digital world and this requires rethinking some of the norms that we've held here for generations.

The model Stride has built in online and career learning has taught us a lot about some of the vulnerabilities in our education system. First and foremost, we need to begin treating our customers like customers. We should be listening to them and innovating to meet them at their point of need and those customers extend beyond the students to include the families, teachers, and employers who will empower the next generation and build on America's legacy.

And as we have listened to our customers, a few key themes emerge. Students and parents need more options, not just online and brick-and-mortar programs, but options around what our children learn, how they learn, and even when they learn. Teachers continue to be the backbone of each child's education even as the role of a teacher is evolving and that many teachers are reeling from the stresses of the pandemic and questioning their role in education. So, we need to find ways to further support and enable them.

Students are also telling us that they learn in different ways than their parents did. They want more say in what they learn, and they want their education to be practical and digital. They want technology infused throughout the experience, and they want that technology to be on par with the technology they use in their everyday lives.

Over the past several years, the rollout of our Career Learning programs has tried to address some of this feedback. Our programs deliver in-demand career certifications for students in middle and high school. We saw that employers were struggling to hire talent with the right hard and soft skills, and we knew we could help.

In 2018, we enrolled less than 2,000 students in these nascent programs. This year, we have over 60,000 students in these programs, and we're just now starting to get enough scale to really have an impact on the talent gap. While it is still only a small fraction of our 2030 goal to have more than 100,000 graduates from our Career Learning programs, we are making good progress.

Additionally, the pandemic has exacerbated both the need we see in the marketplace and our resolve to deliver on our programs. Employers still struggling to identify, recruit, and hire skilled workers. Numerous studies have confirmed these challenges and demonstrate the importance of our Career Learning programs.

We offer programs that teach real skills that are in high demand in the current environment and will be in high demand for years to come. Computer and IT-related jobs will continue to drive a digital economy. Healthcare physicians are expected to add 26 million jobs by 2030. We will be part of training these future employees.

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An investment in our career programs achieved a significant step forward this fall. We launched the pilot of our new career platform that provides what our customers have been asking for, an all-inclusive solution for career education. The platform leads students through personalized career exploration to help them decide which career paths may be right for them. They are directed to self-paced training to develop the skills they need to be successful and they are able to obtain industry-recognized certifications and use these skills and certifications to access internship and job opportunities. That seamless customer journey from exploration to job provides a new paradigm for students to succeed and the best part is that we intend to make this free to all students, no more college debt.

The platform also helps schools and districts solve their own set of challenges. Schools believe that preparation for the workforce is the number one measure of success for their programs and 90% of school districts say that career learning is their top priority. 75% of school districts are considering outsourcing their career learning options. Without platform, schools don't have to increase spending as we are offering this to school districts at no cost.

Given the current staffing challenges and desire to recruit skilled staff, we can monetize the platform through placement and recruiting fees that employers are already conditioned to pay. This means that schools can address their challenges without budget impact, students can get the training and certifications they need at no cost to them, and employers can access highly skilled and certified employees without increasing HR budgets. It's a win for everyone involved.

We've already received some extremely positive feedback from our pilots which span major metro areas to rural school districts. In addition to our fast-growing middle and high school business, our Adult Learning business is growing at over 25% a year. We are now on a run rate of over $100 million and on pace to hit $200 million over the next several years. And each of our product lines will grow this year for the first time.

We are also investing in both our professional development and tutoring platforms. That tutoring platform will match students with certified US-based teachers to now tutors on the other side of the world. We want to enable the teachers right here in the US to earn more. And speaking of teachers, we realized that we can also help with the teacher shortage problem plaguing many school districts in our country. Over the summer, we rolled out a teacher shortage hybrid solution that can supplement district's local teachers. We continue to provide more and more tools for teachers to help them be more efficient and effective.

We just completed our first gaming series using the Minecraft game and provide lessons in history, geography, and science. This and other co-curricular offerings are growing at exponential pace. Our art and photography contests are drawing interest from tens of thousands of entrants versus just a few thousand last year. Our Esports leagues and programs just completed a summer school program that was oversubscribed many times over and now counts tens of thousands of users. By listening to our customers, we've delivered these programs and shown the ability to dramatically improve retention compared to pre-pandemic levels.

Our new enrollment withdrawals are at all-time lows, and we welcomed our largest cohort of re-registrations this fall. It's all about focusing on our customers and their outcomes. That includes more job placements than ever and stronger academic outcomes as well. We all know about the learning loss that most schools experienced during the pandemic that has been written about extensively this week. Well, over the past two years, the programs we manage have seen improving graduation rates, improved course pass rates, increasing retention rates, and positive increases in ELA, reading, math, science, and social studies.

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So our model has proven itself in the face of the pandemic and parents and students continue to demand more choice in their education. 70% of parents want schools to offer multiple learning modes, including in-person, online, and hybrid options. Our school districts are starting to move away from offering more choice that they offered during the pandemic. In January 2022, 40% of public schools offered full-time remote instruction but by June of this year, that number had dropped to 33%. And meanwhile, only 10% of public schools offer a hybrid option.

Stride will continue to offer parents and students multiple options for their education, and the landscape appears to be supporting us. Over just the past two years, 20 states have started to expand voucher-type programs. This is a great start, but we believe more can be done to allow families to attend their preferred school. While our General Education enrollment have fallen more than we hoped, much of that is because families are embracing our career programs. But we can still do a better job in attracting a broader range of new families to our programs in both career education and general education. And while overall enrollments are up around 40% from pre-pandemic levels, our revenue is up over 70% and operating income is up over 500%. So we have demonstrated an ability to scale extremely profitably while also investing in innovation at the same time.

Now, for this fiscal year, just like last year, we said our intent is to grow and our first quarter results and full year guidance indicates we will. While enrollments overall are lower, we are finding ways to make up for that shortfall with other products and growth vectors. And we think General Education enrollments have probably bottomed out at these levels and the other growth areas will continue, which sets us up for longer term trajectory of growth.

In addition, in spite of the tremendous pressures we are feeling from inflation, we are finding ways to be more efficient and find more leverage in our business. On both the top and bottom lines, our guidance range this year is a little larger than most because we see opportunity in-year to find ways to improve our results. So, we believe you will see that improvement as the year progresses and we will narrow in our guidance range accordingly.

One early example is that our enrollment numbers since September 30, pre-pandemic, October is a month that see the deterioration in enrollments. That trend returned last fall but so far this October, we have seen net increases in enrollments. As you may remember, last year, we saw in-year demand as measured by application volumes be 20% to 30% higher than the previous year. Well, so far this year, we are seeing application volumes several percentage points higher than even last year and in-year, new enrollment volumes for the first few weeks of October are more than 20% higher than last year and well over 50% higher than pre-pandemic levels.

So ultimately, our goal for the year will be to continue to expand on the top line growth and aim to achieve a basically flat year-over-year adjusted operating income plus or minus 50%. And longer term, we remain committed to the 2025 targets we previously communicated. Given the range of products and services we're putting in the market that we were not aware of when we set our original 2025 targets, I see the opportunity to create even greater value for our customers and stakeholders than when we issued them.

It's the incredible people in the Stride community that make all this possible. From educators to administrators, there isn't a more passionate and dedicated team in the industry, and we are still at just the beginning of our journey to disrupt the education system. More to come. Thank you so much for your time today and now, I'll pass the call over to our CFO ,Donna Blackman. Donna?

Donna Meacham Blackman

Chief Financial Officer, Stride, Inc.

Thank you, James, and good afternoon, everyone. I want to start by thanking all of Stride's employees for another successful school launch and enrollment season. It always impresses me that we can enroll and onboard

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hundreds of thousands of students onto our platform. We know how important it is for students and families to have a smooth start to the school year. So, I thank all of the Stride teachers, administrators, and support staff for their hard work.

Now, turning to our reported results, revenue for the quarter was $425.2 million, an increase of 6% over the same period last year. Adjusted operating loss of $19.9 million was down compared to last year and capital expenditures were $16.8 million, an increase of $1.4 million over last year.

Career Learning's strong enrollment growth coupled with increases in revenue per enrollment delivered another quarter of revenue growth for Stride. General Education enrollment and revenue declined but remained above pre-pandemic levels. These results demonstrate what we have been saying for the past two years. Stride will emerge from the pandemic as a stronger company with a fast-growing Career and Adult Learning business and a solid core General Education business.

Overall, Career Learning revenue for the first quarter increased 63% to $153.5 million, driven by strength in middle and high school career enrollment and adult learning growth. Career Learning middle and high school revenues were $125.5 million. Enrollment for middle and high school reached 61,600, a 47% increase from last year. We are incredibly impressed with the continued enrollment growth in this business and believe they will be a growth driver for many years to come. Revenue per enrollment for the quarter was $2,029, up 20.2%. Some of this strength is timing-related and we anticipate finishing the year up 7% to 10%.

Adult Learning also continued to show strong gains, with $28 million in revenue, up 24% from last year. This business is on track to achieve over 30% growth year-over-year for the full year.

General Education revenue decreased to $271.7 million or 11%. This was due to a decline in enrollment from our pandemic high. Gen Ed enrollment decreased to 112,300, still up almost 2,000 enrollment from pre-pandemic levels. It's important to note that even with the Gen Ed declines, our overall enrollment, including Career Learning, are up significantly from before the pandemic. We believe that as we've expanded our Career Learning options, some of the students and families who would otherwise have chosen Gen Ed have opted for Career Learning offerings.

The decline in Gen Ed enrollment is somewhat offset by an increase in revenue per enrollment of $2,216, up 18% from last year. Similar to Career Learning, the strength in revenue per enrollment was partially timing, and we would expect to finish the year up 7% to 10%.

Gross margin for the quarter was 30.5%, down 110 basis points compared to the first quarter of 2022. As with last year, we expect a normal seasonal pattern in our spending and profitability this year. However, as we mentioned last quarter, we do think there will be some tightening of our gross margins for the full year.

Given inflationary pressures which I'll discuss more shortly, we believe we could see a reduction of up to 200 basis points for our full year gross margin. Selling, general and administrative expenses for the quarter were $158.4 million, up $25 million from last year. The increase in SG&A is primarily driven by higher costs associated with the marketing in enrollment, as well as increases in our Adult businesses as they continue to scale.

Stock-based compensation expense for the quarter was $5.5 million, down from last year due to the timing of stock-based grants tied to our Career Learning business. We expect fiscal year 2023 stock-based compensation expense to increase marginally from last year in the range of $20 million to $25 million.

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Adjusted operating loss for the quarter was $19.9 million. Adjusted EBITDA was $3 million. Profitability for the quarter was impacted by increased marketing expenses as well as earlier teacher hiring. As we anticipated, inflation has driven up our costs faster than revenue per enrollment funding increases. Inflation has impacted all companies and we are not immune. As we said last quarter, we are fully funding teacher and staff salary increases because it is important for students to have instructional consistency. We made these decisions even in the face of increasing materials and marketing expenses because we believe it is the right thing for the company in the long-term.

But we're not just standing idly by. We are continuing to drive efficiencies throughout the company by finding scale across our nationwide footprint and increasing materials-free courses. Moreover, we are still in a strong financial position and we remain committed to investing in our new products. These initial investments will ensure market fit through pilot programs and drive early awareness and we believe the investment will deliver long-term growth opportunities.

So while we expect to see a decline in both growth and operating margins this year, we believe we will be able to offset these declines during the year through ongoing efficiency efforts. However, there is still work to be done and we will need to execute on these efficiency efforts to continue to drive margin improvement in the year.

I want to emphasize that we still believe we can achieve our 2025 targets. Inflationary pressures and a looming potential recession will make it a challenge but we strongly believe we are up for the task. An improving funding environment, strength in Career and Adult Learning, new products, and a return to moderate growth in Gen Ed enrollment position us for success in the years ahead. So, while we may achieve the targets in a slightly different way than we originally anticipated, we believe there are ample opportunities for us to meet and exceed our original targets.

Interest expense for the first quarter totaled $2 million. We expect full year interest expense to be between $7 million and $9 million. Our effective tax rate for the quarter was 25%. For the full year, we believe we will finish with a tax rate in the 27% to 29% range, similar to prior years. Diluted loss per share was $0.54.

Capital expenditures in the quarter totaled $16.8 million, up $1.4 million from last year. As you can see from our guidance, we will continue to invest behind our new, more mainstream products this year. We believe these products will expand our addressable market and expect them to impact growth in the coming year.

Free cash flow in the first quarter, defined as cash from operations less CapEx, was negative $160 million as compared to negative $146.9 million in the prior year period. This is our normal seasonality of cash flows and relates to school launch enrollment and onboarding of new students. As is typical, we expect to see positive cash flow for the next three quarters. We ended the quarter with cash and cash equivalents of $194.5 million. Our strong cash position allows us to continue to invest in organic growth opportunities.

Turning to our guidance, for the second quarter of the fiscal year 2023, we are forecasting revenue in the range of $435 million to $465 million, adjusted operating income between $70 million and $80 million, and capital expenditures between $17 million and $20 million.

For the full year, we forecast revenue in the range of $1.71 billion to $1.79 billion, adjusted operating income between $160 million and $190 million, capital expenditures between $70 million and $80 million, and an effective tax rate between 27% and 29%.

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To summarize, we anticipate another year of growth for Stride, driven by strong Career and Adult Learning results. While short-term margins have been pressured by inflation and investments in new products, we are still in a strong financial position with an excellent balance sheet. We believe our shift towards Career Learning six years ago has set us up for long-term success. We are also excited about the next few years as we begin to see how our new products succeed in the market.

Thank you for your time. Now, I'll turn it over to the operator for Q&A. Operator?

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Jeff Silber with BMO Capital Markets. Your line is open.

Jeffrey M. Silber
Analyst, BMO Capital Markets Corp.

Q

Thank you so much. I know the focus of the call was mostly on Career Learning. I completely understand it, but I'm going to start with General Education. Obviously, the enrollment decline was pretty surprising, at least to us. Can we get into a little bit more color there? I mean, did you lose any contracts? Is it more of a competitive issue? Any color on that would be great.

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah. I think – so, first of all, I think that the Gen Ed enrollment sort of have bottomed out and if you look pre-pandemic where our General Education business is at, sort of around those pre-pandemic numbers. So we feel pretty good that it's bottomed out at this level. We certainly see the return to school post-pandemic having an impact. I think we see some fatigue in the marketplace around online learning and we see some sort of increased competition from local brick- and-mortar schools.

Having said all that, I also think that our execution this summer could have been better. And so I think it's a combination of factors but overall, I think we see overall demand in the market for online education continuing to increase post-pandemic. And I think that we probably did lose a little bit of market share, and I think that's on us to improve. But I think the overall market for us continues to improve and I think the overall market opportunity in both General Education and Career Learning is going to continue to improve. So, I think that we've got some work to do to improve our execution but I think the market's there for us. And I think that we got to execute better.

Jeffrey M. Silber
Analyst, BMO Capital Markets Corp.

Q

So, let me just dig into those comments just a little bit. Maybe we can talk about some of the execution. Can you give us some examples of things that you might need to improve?

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah. And I think, for example, we went into this year, I think, less clear about the messaging we were putting into the market post-pandemic. I think we also had a number of situations throughout the country that either a teacher strike or uncertainty around school situations where we could have been more localized in how we communicated

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with a certain market. So, I think part of it is really just adapting better to being a national footprint player, but having more localized messaging because the reality is, particularly with the pandemic, the sensitivities around school options and school choice have become very localized. And I think that a lot of what our messaging needs to do is to actually drive into that local residents as opposed to sort of the national cookie-cutter, if you will, approach.

Jeffrey M. Silber
Analyst, BMO Capital Markets Corp.

Q

And are comments like that some of the reasons why you think enrollments may have bottomed out? You think there could be room for some improvement if you do improve the execution next year?

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah. And I'll give you even a couple of examples very recently, which I sort of refer to in my remarks. But just in the past – it's been 24 days, I guess, of information that we've got since the quarter end, we see – we actually see improvement in the numbers. Excluding sort of the pandemic year, October is generally a time where we bring on a lot of enrollments for the fall and then we do see some attrition through October into November, and we actually have gained enrollments in October.

So I think little by little, our execution is starting to improve but I think that just the circumstances around education continue to work in our favor in that I think parents and customers, they continue to look for options and they continue to be, I think, be disappointed with the options that they're getting in some of their brick-and-mortar districts. And I think we continue to be a good, viable option. So, I do think that there's evidence that suggests that even in the past few weeks that we've got some room – some upside here in-year and going into next year.

Jeffrey M. Silber
Analyst, BMO Capital Markets Corp.

Q

Okay. Great. Thanks for the color. I'll jump back in the queue.

Operator: Your next question comes from the line of Greg Parrish with Morgan Stanley. Your line is open.

Greg Parrish
Analyst, Morgan Stanley & Co. LLC

Q

Hey, thanks for taking my question. I mean, [ph] sorry I'd (29:29) kind of double down on this but why is this the new baseline in Gen Ed? Because I mean you mentioned a couple things that there's competition from brick-and-mortar and brick-and-mortar knows how to do this now. There's also – and you mentioned this in your remarks as well there's some cannibalization. It's in middle and high school. So, I mean, I guess what gives you such confidence that like this is the new baseline going forward?

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Well, I guess the first thing I would say is that I think the general public and most customers would disagree with you that brick-and-mortar has figured this out. I think at least from all the information research studies that we can see and find, in fact, most brick-and-mortar schools have not figured it out and there's not a lot of satisfaction with the programs for brick-and-mortar schools that are out there.

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So I think that's the first data point and I think you see brick-and-mortar schools somewhat retreating from even putting an emphasis on their ability to do virtual programs. So some of them still have programs but you see, I think, some of them retreating the emphasis on those programs. I think you also are going to start seeing a little bit more emphasis on outsourcing some of those programs because I think they realize that they're just not – they're not going to be good at it.

So the other – I think the other piece of the comments there, I think we are seeing some cannibalization. So, I think that while there is cannibalization, I think just the strength in what we're seeing this fall in terms of the pipeline does tell us, I think, that there is probably bottoming out here. And I think uncertainty in the marketplace tends to work in our favor and I think that the ongoing – continued uncertainty in the marketplace, there are some new variants of the virus. We're seeing spikes because of that. So I just think that the uncertainty that's happening in the marketplace works in our favor and I'm just not sure that – we've been saying now for two years that that's going to go away and we really haven't seen that go away. So we think that this is probably a point of which we've got a floor underneath us but I think it's a fair question and I think we'll see.

Greg Parrish
Analyst, Morgan Stanley & Co. LLC

Q

Okay. That's very helpful. Thanks. I want to talk about the operating income margin guidance because, I mean, it sounds like you need a couple things to happen to get that. And maybe that's wrong and correct me, but you talked about a couple things. You just talk about in-year revenue acceleration. You talked about gaining efficiencies on the expense line throughout the year. I guess – I mean, do those have to happen to meet your guidance or is that just upside?

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah. No, I do think it actually has to – we have work to do. And I don't think it's a slam dunk but here's what I would say. And this is just historical framing, is that I think in the 10 years that I've been with the company, we have yet to miss guidance. And so I think we tend to put guidance out that we feel even if we have still work to do, we feel comfortable in our ability to execute against that.

And so I think we feel pretty good. And I mentioned in my comments, our goal, which is also within the range of our guidance, is to be flat plus or minus couple percent on adjusted operating income. So – and that's above the midpoint. So I think we're shooting for above the midpoint and we're working hard every day to make sure that we drive the cost structure to achieve that.

Greg Parrish
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Great. And then help me, maybe this is a sort of an ignorant question. But I mean you have a pretty big step-down in kind of overall enrollments, but you have a pretty big step-up in some of your teacher costs and you had a pretty big teacher base last year. So I mean, I guess – I mean, was there no kind of mark-to-market in teachers? I mean, how do you kind of assess that internally? Are you sort of overstaffed in Gen Ed or are they allocated somewhere else? I know you have some sort of other areas where you want to sort of monetize those teachers with school districts. Maybe that's the answer, but maybe kind of help me kind of fill the gaps there.

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

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Yeah. I think it's a little bit of a mix. We certainly are investing in certain places but also which is a little bit of a nuance that maybe not everybody is aware of, but oftentimes, when we get funding increases, those funding increases come with pre-prescribed costs associated with them, often at zero margin to us. And so there's some of that that's at play here that were sort of forced is the wrong way [ph] but say but then (34:13). The way that the funding works is, is that we have to spend against it.

And so there's a mix of that in there as well as I think just we are investing in certain things. I do think that we were fully staffed in most years. We're actually – we go into the year a little bit understaffed. This year, we wanted to make sure we were fully staffed. So, I think there's a number of things at play there.

Greg Parrish
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Great. Thanks.

Operator: [Operator Instructions] Your next question comes from Tom Singlehurst with Citi. Your line is open.

Thomas A. Singlehurst
Analyst, Citigroup Global Markets Ltd.

Q

Yeah. Good evening. It's Tom here from Citi. Thanks for taking the question. Apologies, I missed this at the beginning, so I'm sorry if I'm covering old ground. I just wanted to understand, firstly, just sort of tracking the development, the General Ed enrollment trend, I recall, I think, at the full year, you talked about relatively robust sort of survey work in terms of sort of indicating that enrollment would be fairly resilient. I suppose the question there is, A, was that – did that just turn out not to be the case and the survey work didn't work or you'll come back to a point to that execution? Do you think that was enough to sort of take the [ph] showing (35:44) off there? Just interested in sort of exactly whether it was a function of you guys not, could I say, executing 100% or whether there's generally been a pullback in sort of industry level demand.

And in that context, I was interested in something that Pearson said that links to revenue per enrollment because they indicated that there had been a sort of revenue mix effect in the quarter for their virtual school business whereby enrollment were relatively weak, that the average revenue per student was very favorable. I was wondering whether there was anything sort of underlying that explained that sort of [ph] jaws (36:30) effect in aggregate. But those are the two questions for the moment. Thank you.

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah. I mean, I think for sure we have also much like Pearson. I think our business is probably mixed similarly to them that we've got some revenue per enrollment strength that's due both to the overall funding environment but also to the mix. So I think there's sort of both components there. And so, yeah, I think it's probably fairly similar.

I think to your earlier – your first part of the question, last year, we saw in-year demand be very strong relative to the prior year. And I think we continue to tell people that on our earnings calls when we got into the summer season, we didn't see that in-year strength translate as much in the summer season. And I do think that some of that was execution. Some of that was a little bit of sort of – I keep calling this fatigue that people have had around enrolling for some of these programs, but I think the overall market continues to grow while the overall market continues to grow.

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And so I think what we saw is a little bit of a softness, I think, in our execution and we're talking several thousand enrollments can push us down a few percent to down 8%, right? So it's not a huge swing we have to have for us to be down the 8%. So, I think that it's a combination of factors, but I definitely think that some of the execution played into it and I think that the market continues to be robust for these programs.

And I think the behaviors we're seeing where historically a lot of the behaviors of families we saw were – happened sort of between 4th of July and Labor Day. And we're seeing now some of the behavior shift to more in-year behaviors, and I think what the early indications are is that families, I think, want to believe that sort of the default should be to go back into their brick-and-mortar school district. And I think when they go back in, sometimes they realize that, oh, things haven't changed. Things haven't improved. They're not meeting the needs that I have as a customer and so therefore, they look for new options in September into October. And I think again, for the, at least small sample size of the first several weeks of this sort of post-count day season, post-Q1 season, we're seeing some relative strength even above and beyond last year where we saw some strength and well above pre-pandemic levels. And that's why I think we might see consumer behavior shift a little bit into season from – relative to pre-pandemic levels, we're seeing a much higher level of demand than we did pre-pandemic so...

Thomas A. Singlehurst
Analyst, Citigroup Global Markets Ltd.

Q

Perfect. One follow-up, if it's okay, on I suppose the cyclicality of the – I was going to say the Career Learning business. But I'm really talking about the Adult Learning business and in particular, the sort of institutional sort of offering, I presume, within Galvanize. Should we be worried at all about organizations and enterprise becoming more circumspect about sort of procuring sort of enterprise L&D resources...

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah.

Thomas A. Singlehurst
Analyst, Citigroup Global Markets Ltd.

Q

...and tools in this environment or do you think that will remain robust [indiscernible] (40:17)?

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Well, I think the good – yes, I'm sorry. I'm sorry. I thought you were finished. Go ahead.

Thomas A. Singlehurst
Analyst, Citigroup Global Markets Ltd.

Q

I was going to say do you think it will remain robust despite the macro challenges?

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah. I think the good news/bad news for us is that within the context of our Adult businesses, we didn't have a material amount of that enterprise side business. When we did some of these acquisitions, we were actually pretty bullish that that would materialize. They didn't and so therefore, I think the risk of the macro trends working against us there is just mitigated by the fact that we just didn't have material amount of business there.

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As it turns out, what we are seeing is still some healthy opportunity on the enterprise side for those businesses. I think as companies try to figure out what their staffing and hiring needs are, particularly in the technology space, technology tends to be prioritized. And there still, I think, is a lot of demand that employers don't know how to fill appropriately. And so I think there still is a lot of opportunity therefore, but it's just not material enough one way or the other to impact us too much at this stage.

Thomas A. Singlehurst
Analyst, Citigroup Global Markets Ltd.

Q

Very clear. Thank you.

Operator: [Operator Instructions] Your next question comes from the line of Stephen Sheldon with William Blair. Your line is open.

Matthew Filek
Analyst, William Blair & Co. LLC

Q

Hi, Jim. This is actually Matt Filek on for Stephen Sheldon. To start, was wondering if you can talk about what drove the increase in SG&A expense relative to the prior year. Sounds like higher marketing costs is driving some of that, but any additional detail would be helpful. And as a second part, how should we think about SG&A looking ahead over the next several quarters?

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah. I think the higher SG&A, it's really a function of two things. I think you captured one piece of it, which is I think the marketing expense did tick up a little bit for us. But I think there's inflation. I think that's – the big story right now is you've got inflation across the board on almost every cost item that we've got. And I think that – I don't know, Donna, if you had any of it, but I think that's really the two big drivers there.

Donna Meacham Blackman
Chief Financial Officer, Stride, Inc.

A

I think I would sort of add the timing of hiring had some impact on our [indiscernible] (42:44) with respect to SG&A. I think the inflation on not only the marketing, but also on the salary and wages. And as you sort of think about the rest of the year, I would think a lot of that increase being more in line with inflation.

Matthew Filek
Analyst, William Blair & Co. LLC

Q

Got it. That's helpful. Thank you. And then switching gears here. How have application to enrollment conversion rates been trending relative to your expectation and if you could, what are some of the underlying forces driving those trends?

James Jeaho Rhyu
Chief Executive Officer & Director, Stride, Inc.

A

Yeah. I think what we see from – I'll actually start. From the top of the funnel, you'd get traffic. Traffic converts to lead, lead converts to an application, application converts to enrollment. And I think what we're seeing is, is actually strong conversion rates and improving conversion rates. And what we see in our enrollment center is that

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families have a better appreciation, understanding of the programs that we're offering. So therefore, they're converting at higher rates.

And we saw that improve during the pandemic, through the pandemic. And now sort of we see that sustained level because the families still they have that appreciation, understanding of what the programs are and why they may or may not be a good fit for their needs. And so we are seeing higher conversion rates all through the funnel, including application to enrollment, and we're seeing on a pretty sustained level.

Matthew Filek
Analyst, William Blair & Co. LLC

Q

Great. Thank you.

Operator: There are no further questions. This does conclude today's conference call. Thank you for joining. You may now disconnect.

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