Apollo Group
(APOL-NASDAQ)

Stock Rating: Market Perform
Industry Rating: Outperform

Downgrading to MARKET PERFORM; “Right Thing to Do” Hurts Near Term

Event
We are downgrading APOL to MARKET PERFORM from OUTPERFORM. Last night, APOL reported FY1Q10 EPS of $1.47 (excl. tax benefit) vs. $1.12, more than our and the consensus $1.46 estimate. New degreed enrollment grew 13.7% y/y and total degreed enrollment grew 18.4% y/y, below our 17.9% and 19.9% estimates.

Impact
The slower enrollment growth was somewhat owing to a pilot University Orientation program where it attempts to focus on “new enrollment that retains.” We definitely agree this is “the right thing to do.” The company has been under tremendous scrutiny given its position as the largest user of Title IV funds and any program which improves the quality of its student base should help improve the value proposition for its students; this should dovetail well with the increased focus on outputs by regulatory entities. While management reiterated its long-term growth targets, unfortunately, what helps long term likely hurts near term. As we are reducing our estimates, we believe the stock deserves a lower multiple – especially with the recent multiple expansion with the stock’s run-up into the earnings release.

Forecasts
We are reducing our FY2Q10 EPS estimate to $0.89 from $0.99; our FY2010 EPS estimate to $4.87 from $5.23; and our FY2011 EPS estimate to $5.73 from $6.07.

Valuation
APOL closed last night at 13.1x our new CY2010 EPS estimate of $5.13 – a discount to the peer group median of roughly 16.5x. We are reducing our target to $64 from $73 (see Valuation for risks and methodology).

Recommendation
We are downgrading APOL to MARKET PERFORM from OUTPERFORM.
ENROLLMENT ANALYSIS

Annual growth in new degreed enrollment slows. New degreed enrollment (i.e., starts) are defined as “any individual student enrolled in a University of Phoenix (UOP) degree program who is a new student and started a course in the quarter, any individual student who previously graduated from one degree program and started a new degree program in the quarter (for example, a graduate of an associate’s degree program returns for a bachelor’s degree program or a graduate of a bachelor’s degree program returns for a master’s degree), as well as any individual student who started a degree program in the quarter and had been out of attendance for longer than 12 months. In addition, this includes students who in the quarter started participating in UOP certificate programs of at least 18 credit hours in length with some course applicability into a related degree program.”

New degreed enrollments increased 13.7% y/y to 98,100 from 86,300 in FY1Q09 (see Exhibit 1), down from FY4Q09’s 22.7% growth. Management attributed the slowing growth to its strategy of shifting focus toward enrolling students better prepared for college level work, and toward increasing the mix of students at the bachelor’s degree level. To help accomplish this, management has been piloting over recent quarters a new orientation program called University Orientation to screen out potential students not prepared for college level education (see details at end of note). Without this orientation program, management estimates new starts would have been up another few hundred basis points annually.

Exhibit 1: Apollo Group New Degreed Enrollment (FY1Q06–FY1Q10)

Source: BMO Capital Markets and company reports.

Annual growth in degreed enrollment also slows. Total degreed enrollment was up 18.4% y/y to 455,600 from 384,900 in FY1Q09. This was down sequentially from FY4Q09’s 22.3% annual increase, reversing the trend of six straight quarters of accelerating growth (see Exhibit 2).
Sequential persistence rates (our calculation) down y/y. We have attempted to provide a sequential persistence rate calculated as follows: the sum of (a) beginning degreed enrollment (disclosed as ending degreed enrollment the prior quarter) and (b) new degreed enrollment (as disclosed) and subtracting the ending degreed enrollment this quarter, then dividing that by the beginning degreed enrollment and subtracting the resulting quotient from one. Because of the lack of disclosure of graduating students and reenters (most publicly held companies also do not disclose this data), it is difficult to actually determine sequential persistence rates solely due to drop-outs, although we believe a trend analysis such as this is still insightful.

As shown in Exhibit 3, the company’s sequential persistence rate was 80.7% in FY1Q10 – down from 82.5% in FY1Q09, and down sequentially from FY4Q09’s 81.1%. Per our calculation, persistence rates were down year-over-year at the associate’s, bachelor’s, and master’s level, but up at the doctoral degree level. While our analysis is not complete as we did not have all the needed data (e.g., graduation rates), management cited an overall decline in this metric, giving us some confidence in our estimates. However, management noted that retention rates - which include graduates - were not as weak as persistence.

Exhibit 3: Apollo Group Sequential Retention Rate (FY1Q07-FY1Q10)

<table>
<thead>
<tr>
<th></th>
<th>F1Q07</th>
<th>F2Q07</th>
<th>F3Q07</th>
<th>F4Q07</th>
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<th>F2Q08</th>
<th>F3Q08</th>
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<th>F1Q09</th>
<th>F2Q09</th>
<th>F3Q09</th>
<th>F4Q09</th>
<th>F1Q10</th>
</tr>
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<tbody>
<tr>
<td>Prior quarter ending enrollment (a)</td>
<td>282,300</td>
<td>291,800</td>
<td>298,400</td>
<td>311,100</td>
<td>313,700</td>
<td>325,000</td>
<td>330,200</td>
<td>345,300</td>
<td>362,100</td>
<td>384,900</td>
<td>397,700</td>
<td>420,700</td>
<td>443,000</td>
</tr>
<tr>
<td>Add: New starts (b)</td>
<td>62,500</td>
<td>61,200</td>
<td>65,000</td>
<td>69,800</td>
<td>68,700</td>
<td>65,000</td>
<td>71,400</td>
<td>83,100</td>
<td>86,300</td>
<td>80,000</td>
<td>87,500</td>
<td>102,000</td>
<td>98,100</td>
</tr>
<tr>
<td>Add: Students acquired ©</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Less: Current quarter ending enrollment (d)</td>
<td>(291,800)</td>
<td>(298,400)</td>
<td>(311,100)</td>
<td>(313,700)</td>
<td>(325,000)</td>
<td>(330,200)</td>
<td>(345,300)</td>
<td>(362,100)</td>
<td>(384,900)</td>
<td>(397,700)</td>
<td>(420,700)</td>
<td>(443,000)</td>
<td>(455,600)</td>
</tr>
<tr>
<td>Students not retained (e=a+b+c-d)</td>
<td>53,000</td>
<td>54,600</td>
<td>52,300</td>
<td>67,200</td>
<td>57,400</td>
<td>59,800</td>
<td>56,300</td>
<td>66,300</td>
<td>63,500</td>
<td>67,200</td>
<td>79,700</td>
<td>85,500</td>
<td></td>
</tr>
<tr>
<td>Sequential attrition rate (f=e/a)</td>
<td>18.8%</td>
<td>18.7%</td>
<td>17.5%</td>
<td>21.6%</td>
<td>18.3%</td>
<td>18.4%</td>
<td>17.1%</td>
<td>19.2%</td>
<td>17.5%</td>
<td>17.5%</td>
<td>16.2%</td>
<td>18.9%</td>
<td>19.3%</td>
</tr>
<tr>
<td>Sequential persistence rate (g=1-f)</td>
<td>81.2%</td>
<td>81.3%</td>
<td>82.5%</td>
<td>78.4%</td>
<td>81.7%</td>
<td>81.6%</td>
<td>82.9%</td>
<td>80.8%</td>
<td>82.5%</td>
<td>82.5%</td>
<td>83.8%</td>
<td>81.1%</td>
<td>80.7%</td>
</tr>
<tr>
<td>y/y change</td>
<td>N.A.</td>
<td>-0.2%</td>
<td>0.4%</td>
<td>-1.6%</td>
<td>0.5%</td>
<td>0.3%</td>
<td>0.5%</td>
<td>2.4%</td>
<td>0.8%</td>
<td>0.9%</td>
<td>0.3%</td>
<td>-1.8%</td>
<td></td>
</tr>
<tr>
<td>seq. change</td>
<td>1.2%</td>
<td>0.1%</td>
<td>1.2%</td>
<td>-4.1%</td>
<td>3.3%</td>
<td>-0.1%</td>
<td>1.3%</td>
<td>-2.2%</td>
<td>1.7%</td>
<td>0.1%</td>
<td>1.2%</td>
<td>-2.7%</td>
<td>-0.4%</td>
</tr>
</tbody>
</table>


Annual revenue growth (including BPP) accelerates, beats estimates. Revenue of $1.27 billion increased 30.8% y/y from $971 million in FY1Q09 (see Exhibit 4). This was more than our forecast of roughly $1.24 billion and the consensus $1.23 billion. Annual growth accelerated from FY4Q09’s 29.4%. In its first full quarter of consolidation, BPP (acquired July
2009) contributed roughly $88.7 million. Excluding this, revenues increased 21.7% y/y and were below estimates. Management attributed the non-BPP growth to increased degreed enrollments, better retention rates, and tuition increases implemented last July. Gross revenues per degree-seeking enrollment increased 4.1% y/y to $2,439 from $2,342; this was the slowest y/y growth since FY2Q09.

As shown in Exhibit 5, the bulk of revenues (roughly 87.5%) derive from degree-seeking students. Degree-seeking net revenues (net of discounts) increased 23.3% y/y, down from FY4Q09’s record 29.5% annual increase. Revenue from non-degree-seeking students (roughly 0.8% of revenues) increased 6.5% y/y, down sequentially from an 11.4% increase in FY4Q09. Revenue was up 147.7% y/y in the other revenue category, which consists of the company’s newer programs (BPP, Apollo Global, Insight Schools). Excluding BPP, other revenues were up 0.4% y/y.

Discounts up y/y. The rate of discounts increased y/y to 5.3% of gross revenues from 4.5% in FY1Q09. Sequentially, discounts decreased from 5.7% of revenues in FY4Q09. We believe the recent increase in Stafford loan limits has helped keep this rate relatively in line with historical trends, though management said it is offering higher discounts to active duty military students and veterans. As such, it is likely discounts will increase in future quarters.

We have removed our estimated SFAS-123R stock-based compensation expense from our expense line item discussion to show a more “apples to apples” comparison.
Adjusted EBITDA increases. Adjusted EBITDA (excluding stock-based compensation) increased 27.4% y/y to $439.4 million from $344.9 million. Adjusted EBITDA margins, however, fell to 34.6% from 35.5%.

Costs and expenses increase at a faster rate than revenues. Total costs and expenses (excluding stock-based compensation) were $863.3 million, up 33% from FY1Q09’s $649 million and above our $842.9 million estimate. The y/y increase was larger than the 30.8% y/y increase in revenues. Instructional costs (up 40.8% y/y) and G&A (up 30.5% y/y) were each above our forecast, while Selling and Promotional costs (up 20.7% y/y) came in below.

- Instructional costs and services. Instructional costs and services (ICS) increased 40.8% y/y to $525.7 million (41.4% of revenues) from $373.3 million (38.4% of revenues) in FY1Q09, well above our $500.2 million estimate. ICS costs as a percentage of revenues is a proxy for “cost of services,” and therefore, y/y gross margins decreased roughly 530 basis points (bp). Management attributed the decrease mainly to the addition of BPP, as its cost structure is more heavily weighted toward ICS. However, the increase was also owing to increased bad debt expense, partially offset by improved fixed cost leverage. Additionally, the anniversaried cost savings associated with renegotiated third-party vendors of financial aid processing added to the increase.

  Bad debt expense increased 80% y/y and rose as a percentage of revenues to 4.9% from 3.6% in FY1Q09. Sequentially, bad debt expense increased from 4.2% of revenues in FY4Q09. As in prior quarters, management attributed this to an increasing share of aged receivables, which have lower collection rates in an economic downturn, and the shift in the student body to more associate-level students. Additionally, some changes implemented in FY1Q10 - including the 30-day Title IV disbursement delay, and the evaluation of transfer credits prior to loan certification - have had a permanent impact on bad debt. However, this increase was partially offset by the impact of BPP, which reduced bad debt expense by roughly 40 basis points (bp), according to management. We expect this rate could increase going forward.

- Selling and promotional expenses. Selling and promotional expenses (S&P) increased 20.7% y/y to $274.1 million (21.6% of revenues) from $227.1 million (23.4% of revenues) in FY1Q09, below our $281.9 million estimate. The increase was mainly attributed to investments in the company’s non-internet long-term branding initiative. The reduction as a percentage of revenue was attributed to increased enrollment counselor effectiveness, and the impact of BPP – which accounted for roughly 120 bp of the decline as a percentage of revenue owing to its lower marketing cost structure.

Using the data provided, we have attempted to analyze cost per start for the company. We acknowledge the limitations of this analysis (i.e., spending in the current quarter likely leads to starts in future quarters. BPP starts are not disclosed), but nevertheless, we believe the trend analysis is insightful. As shown in Exhibit 6, costs per start were roughly $2,794 in FY1Q10, up 6.2% from $2,632 in FY1Q09 and up sequentially from FY4Q09’s $2,558.
### Exhibit 6: Apollo Group Costs per Start (FY1Q07 – FY1Q10)

<table>
<thead>
<tr>
<th></th>
<th>F1Q07</th>
<th>F2Q07</th>
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<th>F3Q08</th>
<th>F4Q08</th>
<th>F1Q09</th>
<th>F2Q09</th>
<th>F3Q09</th>
<th>F4Q09</th>
<th>F1Q10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of starts (new degreed enrollment)</td>
<td>62,500</td>
<td>61,200</td>
<td>65,000</td>
<td>69,800</td>
<td>68,700</td>
<td>65,000</td>
<td>71,400</td>
<td>83,100</td>
<td>86,300</td>
<td>80,000</td>
<td>87,500</td>
<td>102,000</td>
<td>96,100</td>
</tr>
<tr>
<td>Selling and promotional expense per start</td>
<td>$2,469.6</td>
<td>$2,711.7</td>
<td>$2,492.5</td>
<td>$2,488.1</td>
<td>$2,564.4</td>
<td>$2,083.9</td>
<td>$2,640.5</td>
<td>$2,675.7</td>
<td>$2,631.9</td>
<td>$2,011.4</td>
<td>$2,772.9</td>
<td>$2,557.9</td>
<td>$2,794.3</td>
</tr>
<tr>
<td>y/y % change</td>
<td>-3.4%</td>
<td>12.0%</td>
<td>-0.3%</td>
<td>-1.8%</td>
<td>3.8%</td>
<td>13.7%</td>
<td>14.0%</td>
<td>7.5%</td>
<td>2.6%</td>
<td>-9.2%</td>
<td>-2.4%</td>
<td>-4.4%</td>
<td>6.2%</td>
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</tbody>
</table>


### General and administrative costs.
Excluding stock-based compensation, general and administrative (G&A) expenses increased 30.5% y/y (roughly in line with revenues) to $63.4 million from $48.6 million. This was above our expected $60.8 million. As a percentage of revenues, G&A was flat y/y at 5%. According to management, BPP’s operations had little impact on this expense item.

### Operating margins well above expectations.
Operating margins (excluding stock-based compensation and one-time charges) of 32% decreased from FY1Q09’s 33.2%, and were roughly in line with our estimate. Operating income (excluding stock-based compensation) of $407 million increased 26.4% from FY1Q09’s $322 million and was above our $397.6 million forecast.

Including stock-based compensation costs, operating income was $392.9 million (30.9% margins), up from $306.9 million (31.6% margins) in FY1Q09.

Stock-based compensation decreased to $14.2 million from $15.1 million. Management reiterated it expects this expense to be in the range of $65-$70 million for FY2009.

### Net income up y/y.
Net income (including the tax benefit) of roughly $240.1 million was up from FY1Q09’s $180.4 million and above our $227.1 million forecast.

### EPS above consensus.
Excluding the tax benefit, FY1Q10 EPS of $1.47 was above FY1Q09’s $1.12, and above our and the consensus forecast of $1.46. Including this benefit, EPS was $1.54.

### Key balance sheet and cash flow measures.
Cash and marketable securities (excluding restricted cash) decreased to $905.3 million from $968.2 million at the end of FY4Q09. The company had drawn the maximum $500 million under its revolving credit facility for liquidity purposes and related to the BPP acquisition, but paid down $396.3 million of this in FY1Q10.

DSOs per management (excluding Apollo Global) were 32 days, up from 26 days in FY1Q09 and flat sequentially. Cash flow from operations was roughly $405.2 million in FY1Q10, up from $380.8 million in FY1Q09. Capital expenditures were $37.6 million versus roughly $30.6 million in FY1Q09, leading to free cash flow of $367.7 million ($2.36/share) in FY1Q10, up from $350.2 million ($2.18/share) in FY1Q09.
UOP SEGMENT OVERVIEW

Exhibit 7: Apollo Group: Associates Degree Segment (FY1Q07 – FY1Q10)

<table>
<thead>
<tr>
<th></th>
<th>F1Q07</th>
<th>F2Q07</th>
<th>F3Q07</th>
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<tbody>
<tr>
<td>New degreed enrollment</td>
<td>27,400</td>
<td>26,300</td>
<td>31,000</td>
<td>31,300</td>
<td>33,700</td>
<td>31,100</td>
<td>37,100</td>
<td>41,500</td>
<td>45,800</td>
<td>41,700</td>
<td>48,800</td>
<td>55,400</td>
<td>52,200</td>
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<tr>
<td>Total degreed enrollment</td>
<td>83,000</td>
<td>88,300</td>
<td>98,600</td>
<td>104,500</td>
<td>114,300</td>
<td>121,200</td>
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<td>146,500</td>
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<td>170,500</td>
<td>186,600</td>
<td>201,200</td>
<td>205,400</td>
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<tr>
<td>Revenues ($ mil.)</td>
<td>$124.5</td>
<td>$130.0</td>
<td>$164.8</td>
<td>$165.6</td>
<td>$218.6</td>
<td>$204.1</td>
<td>$245.2</td>
<td>$253.2</td>
<td>$327.9</td>
<td>$302.3</td>
<td>$378.6</td>
<td>$399.9</td>
<td>$447.2</td>
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<td>Gross revs. per student</td>
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<td>$1,472</td>
<td>$1,671</td>
<td>$1,813</td>
<td>$1,684</td>
<td>$1,797</td>
<td>$2,027</td>
<td>$1,773</td>
<td>$2,029</td>
<td>$1,988</td>
<td>$2,177</td>
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<td>Sequential retention rate</td>
<td>75.1%</td>
<td>74.7%</td>
<td>76.6%</td>
<td>74.2%</td>
<td>77.1%</td>
<td>78.2%</td>
<td>79.2%</td>
<td>79.6%</td>
<td>80.8%</td>
<td>81.5%</td>
<td>76.1%</td>
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<td>y/y change:</td>
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</tr>
<tr>
<td>New degreed enrollment</td>
<td>51.4%</td>
<td>39.2%</td>
<td>45.5%</td>
<td>28.8%</td>
<td>18.3%</td>
<td>19.7%</td>
<td>32.6%</td>
<td>35.9%</td>
<td>34.1%</td>
<td>31.5%</td>
<td>35.5%</td>
<td>14.0%</td>
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<tr>
<td>Total degreed enrollment</td>
<td>69.4%</td>
<td>60.8%</td>
<td>55.0%</td>
<td>41.2%</td>
<td>37.7%</td>
<td>37.3%</td>
<td>36.2%</td>
<td>40.2%</td>
<td>41.6%</td>
<td>40.7%</td>
<td>38.9%</td>
<td>37.3%</td>
<td>26.9%</td>
</tr>
<tr>
<td>Revenues ($ mil.)</td>
<td>70.1%</td>
<td>53.9%</td>
<td>66.4%</td>
<td>70.8%</td>
<td>75.6%</td>
<td>56.9%</td>
<td>50.6%</td>
<td>41.8%</td>
<td>50.0%</td>
<td>48.1%</td>
<td>52.6%</td>
<td>51.9%</td>
<td>36.4%</td>
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<tr>
<td>Gross revs. per student</td>
<td>0.4%</td>
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<td>7.3%</td>
<td>20.9%</td>
<td>27.5%</td>
<td>14.4%</td>
<td>10.6%</td>
<td>1.2%</td>
<td>6.0%</td>
<td>5.3%</td>
<td>9.8%</td>
<td>10.6%</td>
<td>7.4%</td>
</tr>
<tr>
<td>Sequential persistence rate</td>
<td>N.A.</td>
<td>-0.5%</td>
<td>-3.9%</td>
<td>2.0%</td>
<td>4.1%</td>
<td>3.6%</td>
<td>3.9%</td>
<td>2.1%</td>
<td>0.8%</td>
<td>0.6%</td>
<td>-3.0%</td>
<td></td>
<td></td>
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<tr>
<td>% of total company:</td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>New degreed enrollment</td>
<td>43.8%</td>
<td>43.0%</td>
<td>47.7%</td>
<td>44.8%</td>
<td>49.1%</td>
<td>47.8%</td>
<td>52.0%</td>
<td>49.9%</td>
<td>53.1%</td>
<td>52.1%</td>
<td>55.8%</td>
<td>54.3%</td>
<td>53.2%</td>
</tr>
<tr>
<td>Total degreed enrollment</td>
<td>28.4%</td>
<td>29.6%</td>
<td>31.7%</td>
<td>33.3%</td>
<td>35.2%</td>
<td>36.7%</td>
<td>38.9%</td>
<td>40.5%</td>
<td>42.0%</td>
<td>42.9%</td>
<td>44.4%</td>
<td>45.4%</td>
<td>45.1%</td>
</tr>
<tr>
<td>Revenues ($ mil.)</td>
<td>19.0%</td>
<td>21.6%</td>
<td>23.0%</td>
<td>26.3%</td>
<td>28.3%</td>
<td>29.5%</td>
<td>30.4%</td>
<td>32.1%</td>
<td>34.7%</td>
<td>35.4%</td>
<td>36.6%</td>
<td>37.6%</td>
<td>38.1%</td>
</tr>
</tbody>
</table>


**Associate degree level.** While virtually non-existent before the summer of 2004, this unit, which is represented by Axia College, the company’s “online community college,” has been the key growth driver for APOL over recent years. However, we expect this to slow as management switches its focus toward enrolling students with a “reasonable chance to succeed,” as part of an effort to boost retention and persistence rates while lowering cohort default rates. As Axia contains “lower quality” students (i.e., lower revenue per student, higher attrition rate, shorter length of stay), we believe it is important, both financially and academically, for the company to enhance the quality of this student base.

In FY1Q10, new degreed enrollment increased 14% to 52,200 from 45,800 in FY1Q09 and represented roughly 53.2% of the starts for the company overall in the quarter. This was significantly down from 33.5% y/y growth in FY4Q09, as management is focusing on enrolling better prepared students, and the new University Orientation program had the biggest adverse impact here. Total degreed enrollments increased 26.9% y/y to 205,400 from 161,800 at the end of FY1Q09 – a solid result, in our view, though down significantly from FY4Q09’s 37.3%.

Axia revenues increased 36.4% y/y to roughly $447.2 million from $327.9 million in FY1Q09, but slowing from prior quarters. This was driven by the increased degreed enrollment and a 7.4% y/y increase in gross revenues per student, decelerating from FY4Q09’s 10.6% y/y increase.

The sequential persistence rate (BMO calculation) was roughly 76.1%, down from 79.2% in FY1Q09, and down sequentially from 78.1% in FY4Q09.
### Exhibit 8: Apollo Group: Bachelors Degree Segment (FY1Q07 – FY1Q10)

<table>
<thead>
<tr>
<th></th>
<th>F1Q07</th>
<th>F2Q07</th>
<th>F3Q07</th>
<th>F4Q07</th>
<th>F1Q08</th>
<th>F2Q08</th>
<th>F3Q08</th>
<th>F4Q08</th>
<th>F1Q09</th>
<th>F2Q09</th>
<th>F3Q09</th>
<th>F4Q09</th>
<th>F1Q10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>New degreed enrollment</strong></td>
<td>22,600</td>
<td>22,700</td>
<td>21,800</td>
<td>23,800</td>
<td>21,800</td>
<td>21,500</td>
<td>21,900</td>
<td>27,200</td>
<td>26,100</td>
<td>25,100</td>
<td>26,000</td>
<td>31,700</td>
<td>32,100</td>
</tr>
<tr>
<td><strong>Total degreed enrollment</strong></td>
<td>139,900</td>
<td>139,300</td>
<td>141,400</td>
<td>138,700</td>
<td>137,800</td>
<td>136,400</td>
<td>137,900</td>
<td>141,800</td>
<td>146,800</td>
<td>150,200</td>
<td>156,100</td>
<td>163,600</td>
<td>171,000</td>
</tr>
<tr>
<td><strong>Revenues ($ mil.)</strong></td>
<td>$347.1</td>
<td>$311.3</td>
<td>$367.3</td>
<td>$345.9</td>
<td>$360.3</td>
<td>$315.1</td>
<td>$366.0</td>
<td>$361.6</td>
<td>$401.6</td>
<td>$361.2</td>
<td>$435.4</td>
<td>$446.4</td>
<td>$487.3</td>
</tr>
<tr>
<td><strong>Gross revs. per student</strong></td>
<td>$2,481</td>
<td>$2,235</td>
<td>$2,568</td>
<td>$2,494</td>
<td>$2,615</td>
<td>$2,310</td>
<td>$2,654</td>
<td>$2,550</td>
<td>$2,736</td>
<td>$2,405</td>
<td>$2,789</td>
<td>$2,717</td>
<td>$2,850</td>
</tr>
<tr>
<td><strong>Sequential retention rate</strong></td>
<td>83.4%</td>
<td>83.3%</td>
<td>85.9%</td>
<td>81.3%</td>
<td>83.6%</td>
<td>83.4%</td>
<td>85.0%</td>
<td>83.1%</td>
<td>85.1%</td>
<td>85.2%</td>
<td>86.6%</td>
<td>84.5%</td>
<td>84.9%</td>
</tr>
</tbody>
</table>

**y/y change:**
- **New degreed enrollment:** 11.3% - 8.6% -1.8% 2.6% -3.5% -5.3% 0.5% 14.3% 19.7% 16.7% 18.7% 16.5% 23.0%  
- **Total degreed enrollment:** -6.2% -4.3% -1.4% -1.5% -2.1% -2.5% 2.2% 6.5% 10.1% 13.2% 15.4% 16.5%  
- **Revenues ($ mil.)** -5.4% -1.3% 2.9% 3.4% 5.4% 3.4% 2.2% 4.6% 4.1% 5.1% 6.5%  

**Sequential persistence rate**
- N.A. -0.2% 1.3% 0.3% 0.0% -0.8% 1.8% 1.5% 1.6% 1.4% -0.2%  

**% of total company:**
- **New degreed enrollment:** 36.2% 37.1% 33.5% 34.1% 31.7% 30.7% 32.7% 30.2% 31.4% 29.7% 31.1% 32.7%  
- **Total degreed enrollment:** 47.9% 46.7% 45.5% 44.2% 43.9% 39.9% 39.2% 38.1% 37.8% 37.1% 36.9% 37.5%  
- **Revenues ($ mil.)** 53.0% 51.7% 51.2% 46.6% 45.6% 44.8% 44.1% 42.5% 42.0% 41.8% 41.5%  


**Bachelor’s degree level.** These students attend classes via both campus-based and online classes. While this segment has been overtaken by Axia in terms of enrollment, it is still the largest in terms of revenue generation (41.5% of total in FY1Q10) owing to its relatively higher price points.

New degreed enrollment in bachelor’s programs increased 23% y/y to 32,100 from 26,100 in FY1Q09, the largest increase we have on record for this segment. Degreed enrollment increased 16.5% y/y to 171,600 from 146,800 in FY1Q09, also the best performance since we started keeping records, attributed to an increased focus on growing the mix of higher level degree students.

Bachelor’s degree revenues increased 21.3% y/y to about $487.3 million from $401.6 million in FY1Q09, down slightly from FY4Q09’s 23% y/y growth. This was driven by enrollment growth and a 4.2% y/y increase in gross revenues per student.

The sequential persistence rate (BMO calculation) decreased to 84.9% from 85.1% in FY1Q09, but was up sequentially from FY3Q09’s 84.5%.

### Exhibit 9: Apollo Group: Masters Degree Segment (FY1Q07 – FY1Q10)

<table>
<thead>
<tr>
<th></th>
<th>F1Q07</th>
<th>F2Q07</th>
<th>F3Q07</th>
<th>F4Q07</th>
<th>F1Q08</th>
<th>F2Q08</th>
<th>F3Q08</th>
<th>F4Q08</th>
<th>F1Q09</th>
<th>F2Q09</th>
<th>F3Q09</th>
<th>F4Q09</th>
<th>F1Q10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>New degreed enrollment</strong></td>
<td>11,800</td>
<td>11,500</td>
<td>11,600</td>
<td>13,900</td>
<td>12,400</td>
<td>11,800</td>
<td>11,600</td>
<td>13,600</td>
<td>13,300</td>
<td>12,500</td>
<td>11,900</td>
<td>14,200</td>
<td>13,100</td>
</tr>
<tr>
<td><strong>Total degreed enrollment</strong></td>
<td>64,400</td>
<td>66,100</td>
<td>66,200</td>
<td>65,300</td>
<td>67,300</td>
<td>67,000</td>
<td>67,300</td>
<td>67,700</td>
<td>69,800</td>
<td>70,500</td>
<td>71,200</td>
<td>71,200</td>
<td>71,900</td>
</tr>
<tr>
<td><strong>Revenues ($ mil.)</strong></td>
<td>$171.5</td>
<td>$149.1</td>
<td>$171.7</td>
<td>$160.4</td>
<td>$179.4</td>
<td>$158.6</td>
<td>$185.7</td>
<td>$178.7</td>
<td>$197.8</td>
<td>$174.1</td>
<td>$202.0</td>
<td>$198.5</td>
<td>$216.9</td>
</tr>
<tr>
<td><strong>Gross revs. per student</strong></td>
<td>$2,663</td>
<td>$2,256</td>
<td>$2,594</td>
<td>$2,462</td>
<td>$2,666</td>
<td>$2,368</td>
<td>$2,760</td>
<td>$2,639</td>
<td>$2,834</td>
<td>$2,469</td>
<td>$2,838</td>
<td>$2,788</td>
<td>$3,017</td>
</tr>
<tr>
<td><strong>Sequential retention rate</strong></td>
<td>83.0%</td>
<td>84.8%</td>
<td>82.6%</td>
<td>77.6%</td>
<td>84.1%</td>
<td>82.0%</td>
<td>83.1%</td>
<td>80.4%</td>
<td>83.5%</td>
<td>83.1%</td>
<td>84.1%</td>
<td>80.1%</td>
<td>82.6%</td>
</tr>
</tbody>
</table>

**y/y change:**
- **New degreed enrollment:** 7.3% 7.5% 6.4% 13.0% 5.1% 2.6% 0.0% -2.2% 7.3% 5.9% 2.6% 4.4% -1.5%  
- **Total degreed enrollment:** -5.3% -0.9% 2.6% 3.0% 4.5% 1.4% 1.7% 3.7% 5.2% 5.8% 5.2% 3.0%  
- **Revenues ($ mil.)** -0.1% -1.4% 2.4% 2.8% 4.6% 6.4% 8.2% 11.2% 10.2% 9.7% 8.8% 11.1% 9.7%  
- **Gross revs. per student** 5.5% -0.6% -0.2% -0.1% 0.1% 5.0% 6.4% 7.2% 6.3% 4.3% 2.8% 5.6% 6.5%  
- **Sequential persistence rate** N.A. 2.4% 2.2% -1.6% 1.1% -2.6% 0.5% 2.7% -0.6% 1.1% 1.0% -0.3% -0.9%  

**% of total company:**
- **New degreed enrollment:** 18.9% 18.8% 17.9% 19.9% 18.0% 18.2% 16.2% 16.4% 15.4% 15.6% 13.6% 13.9% 13.4%  
- **Total degreed enrollment:** 22.1% 22.2% 21.3% 20.8% 20.7% 20.3% 19.5% 18.7% 18.1% 17.7% 16.9% 16.1% 15.8%  
- **Revenues ($ mil.)** 26.2% 24.8% 23.9% 22.8% 23.2% 22.9% 22.8% 21.8% 20.9% 20.4% 19.5% 18.7% 18.5%  


**Masters degree level.** These students also attend classes via both campus-based and online classes. This is the third-largest component of total degreed enrollment, although it has also
been “losing share” to the associate’s degree segment (down to 16% of total enrollment at the end of FY1Q10).

New degreed enrollment decreased 1.5% y/y to 13,100 from 13,300 in FY1Q09, following four quarters of y/y growth. Total degreed enrollment improved 3% y/y to 71,900 from 69,800 in FY1Q09, although this slowed from FY4Q09’s 5.2% y/y growth.

Master’s degree revenues increased 9.7% y/y to roughly $216.9 million from $197.8 million in FY1Q09, driven by the y/y enrollment growth, and a 6.5% increase in gross revenue per student.

According to our calculations, the sequential persistence rate was down y/y to 82.6% from 83.5% in FY1Q09, but up from 80.1% in FY4Q09.

### Exhibit 10: Apollo Group: Doctoral Degree Segment (FY1Q07 – FY1Q10)

<table>
<thead>
<tr>
<th></th>
<th>F1Q07</th>
<th>F2Q07</th>
<th>F3Q07</th>
<th>F4Q07</th>
<th>F1Q08</th>
<th>F2Q08</th>
<th>F3Q08</th>
<th>F4Q08</th>
<th>F1Q09</th>
<th>F2Q09</th>
<th>F3Q09</th>
<th>F4Q09</th>
<th>F1Q10</th>
</tr>
</thead>
<tbody>
<tr>
<td>New degreed enrollment</td>
<td>700</td>
<td>700</td>
<td>600</td>
<td>800</td>
<td>500</td>
<td>800</td>
<td>600</td>
<td>800</td>
<td>1,100</td>
<td>700</td>
<td>800</td>
<td>700</td>
<td>700</td>
</tr>
<tr>
<td>Total degreed enrollment</td>
<td>4,500</td>
<td>4,700</td>
<td>5,200</td>
<td>5,600</td>
<td>5,700</td>
<td>5,800</td>
<td>6,100</td>
<td>6,400</td>
<td>7,000</td>
<td>7,000</td>
<td>7,000</td>
<td>7,300</td>
<td>7,300</td>
</tr>
<tr>
<td>Revenues ($ mil.)</td>
<td>$11.9</td>
<td>$11.8</td>
<td>$13.3</td>
<td>$13.8</td>
<td>$14.7</td>
<td>$14.5</td>
<td>$16.4</td>
<td>$16.7</td>
<td>$17.0</td>
<td>$17.2</td>
<td>$19.6</td>
<td>$20.7</td>
<td>$22.0</td>
</tr>
<tr>
<td>Gross revs. per student</td>
<td>$2,640</td>
<td>$2,511</td>
<td>$2,712</td>
<td>$2,661</td>
<td>$2,631</td>
<td>$2,594</td>
<td>$2,627</td>
<td>$2,732</td>
<td>$2,614</td>
<td>$2,649</td>
<td>$2,680</td>
<td>$2,955</td>
<td>$3,016</td>
</tr>
<tr>
<td>Sequential persistence rate</td>
<td>90.5%</td>
<td>88.9%</td>
<td>91.5%</td>
<td>89.8%</td>
<td>92.3%</td>
<td>89.3%</td>
<td>91.4%</td>
<td>86.5%</td>
<td>92.9%</td>
<td>92.3%</td>
<td>92.6%</td>
<td>94.3%</td>
<td>92.6%</td>
</tr>
</tbody>
</table>

**y/y change:**
- New degreed enrollment: 40.0% - 0.0% - 0.0% - 14.3% - 14.3% - 14.3% - 33.3% - 0.0% - 37.5% - 35.7% - 17.6% - 0.0% - 12.5% - 36.4%
- Total degreed enrollment: 40.6% - 27.0% - 25.6% - 23.8% - 24.4% - 19.1% - 18.4% - 17.3% - 16.1% - 16.1% - 17.2% - 14.8% - 12.3%
- Revenues ($ mil.): 39.8% - 35.9% - 27.1% - 19.3% - 24.0% - 23.1% - 23.4% - 20.4% - 15.3% - 18.5% - 19.4% - 24.1% - 29.6%
- Gross revs. per student: 0.6% - 7.0% - 1.2% - 3.7% - 0.3% - 3.3% - 4.2% - 2.7% - 0.6% - 2.1% - 1.9% - 8.2% - 15.4%
- Sequential retention rate: N.A. - 4.9% - 2.3% - 0.1% - 1.8% - 0.4% - 2.2% - 1.6% - 3.8% - 0.1% - 3.0% - 1.3% - 5.8%

**% of total company:**
- New degreed enrollment: 1.1% - 1.1% - 0.9% - 1.1% - 1.2% - 0.9% - 1.1% - 1.0% - 1.3% - 0.9% - 0.9% - 0.7% - 0.7%
- Total degreed enrollment: 1.5% - 1.6% - 1.6% - 1.7% - 1.7% - 1.7% - 1.7% - 1.7% - 1.6% - 1.6% - 1.6% - 1.6% - 1.6%
- Revenues ($ mil.): 1.8% - 2.0% - 1.9% - 2.0% - 1.9% - 2.1% - 2.0% - 2.0% - 1.8% - 2.0% - 1.9% - 1.9% - 1.9%


**Doctoral degree level.** These students also attend classes via both campus-based and online classes, although it is by far the smallest of the company’s four segments.

New degreed enrollment was down 36.4% y/y with 700 new enrollees versus 1,100 in FY1Q09 (although this may be skewed by rounding as the unit is so small). Sequentially, this was worse than FY4Q09’s 12.5% decline. Total degreed enrollment increased 12.3% y/y to 7,300 from 6,500 in FY1Q09, decelerating from the 14.8% y/y increase FY4Q09.

Doctoral degree revenues increased roughly 29.6% y/y to $22 million from $17 million, driven by y/y enrollment growth, and a 15.4% y/y increase in gross revenue per student.

The sequential persistence rate (BMO calculation) for FY1Q10 was up y/y to 94.3% from 88.5%. This was also up sequentially from FY4Q09’s 92.6%. As we believe the company’s student base increases in quality as it moves up the “degree chain,” this is reflected in this data as doctoral degree students have the highest retention rate in the company.

**OPERATING SEGMENT OVERVIEW**

Exhibit 11 contains operating results for the company’s other segments beyond University of Phoenix (UOP). We note UOP revenues increased 23% y/y in FY1Q10 – down sequentially
from 29% y/y growth in FY4Q09 – while UOP operating margins of 34.8% increased from FY1Q09’s 34%.

### Exhibit 11: Apollo Group Results by Segment (FY1Q08 – FY1Q10)

<table>
<thead>
<tr>
<th>University of Phoenix:</th>
<th>F1Q08</th>
<th>F2Q08</th>
<th>F3Q08</th>
<th>F4Q08</th>
<th>F1Q09</th>
<th>F2Q09</th>
<th>F3Q09</th>
<th>F4Q09</th>
<th>F1Q10</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenues</strong></td>
<td>$743.4</td>
<td>$658.0</td>
<td>$794.5</td>
<td>$791.8</td>
<td>$913.2</td>
<td>$829.3</td>
<td>$1,005.2</td>
<td>$1,018.9</td>
<td>$1,122.4</td>
</tr>
<tr>
<td><strong>Operating Income</strong></td>
<td>229.4</td>
<td>129.2</td>
<td>245.7</td>
<td>213.3</td>
<td>310.2</td>
<td>230.1</td>
<td>360.2</td>
<td>311.4</td>
<td>391.0</td>
</tr>
<tr>
<td><strong>Operating Margin</strong></td>
<td>30.9%</td>
<td>19.6%</td>
<td>30.9%</td>
<td>26.9%</td>
<td>34.0%</td>
<td>27.7%</td>
<td>35.8%</td>
<td>30.6%</td>
<td>34.8%</td>
</tr>
<tr>
<td><strong>y/y change:</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>23%</td>
<td>26%</td>
<td>27%</td>
<td>29%</td>
<td>23%</td>
</tr>
<tr>
<td><strong>% of total:</strong></td>
<td>95%</td>
<td>95%</td>
<td>96%</td>
<td>95%</td>
<td>94%</td>
<td>95%</td>
<td>96%</td>
<td>95%</td>
<td>88%</td>
</tr>
<tr>
<td><strong>Operating Income</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>35%</td>
<td>78%</td>
<td>47%</td>
<td>46%</td>
<td>26%</td>
</tr>
<tr>
<td><strong>Operating Margin</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>34.0%</td>
<td>27.7%</td>
<td>35.8%</td>
<td>30.6%</td>
<td>34.8%</td>
</tr>
<tr>
<td><strong>y/y change:</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>23%</td>
<td>26%</td>
<td>27%</td>
<td>29%</td>
<td>23%</td>
</tr>
<tr>
<td><strong>% of total:</strong></td>
<td>95%</td>
<td>95%</td>
<td>96%</td>
<td>95%</td>
<td>94%</td>
<td>95%</td>
<td>96%</td>
<td>95%</td>
<td>88%</td>
</tr>
<tr>
<td><strong>Apollo Global - BPP:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Revenues</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
</tr>
<tr>
<td><strong>Operating Income/(Loss)</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>(6.6)</td>
<td>$15.6</td>
</tr>
<tr>
<td><strong>Operating Margin</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>-50.6%</td>
<td>17.6%</td>
</tr>
<tr>
<td><strong>y/y change:</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>26%</td>
<td>78%</td>
<td>47%</td>
<td>46%</td>
<td>26%</td>
</tr>
<tr>
<td><strong>% of total:</strong></td>
<td>98%</td>
<td>100%</td>
<td>100%</td>
<td>103%</td>
<td>100%</td>
<td>104%</td>
<td>103%</td>
<td>109%</td>
<td>96%</td>
</tr>
<tr>
<td><strong>Apollo Global - Other:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Revenues</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
</tr>
<tr>
<td><strong>Operating Income/(Loss)</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>(6.6)</td>
<td>$15.6</td>
</tr>
<tr>
<td><strong>Operating Margin</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>-50.6%</td>
<td>17.6%</td>
</tr>
<tr>
<td><strong>y/y change:</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
</tr>
<tr>
<td><strong>% of total:</strong></td>
<td>98%</td>
<td>100%</td>
<td>100%</td>
<td>103%</td>
<td>100%</td>
<td>104%</td>
<td>103%</td>
<td>109%</td>
<td>96%</td>
</tr>
<tr>
<td><strong>Insight Schools:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Revenues</strong></td>
<td>$2.1</td>
<td>$3.1</td>
<td>$2.1</td>
<td>$0.3</td>
<td>$7.7</td>
<td>$6.6</td>
<td>$3.8</td>
<td>$2.6</td>
<td>$11.6</td>
</tr>
<tr>
<td><strong>Operating Income/(Loss)</strong></td>
<td>(2.3)</td>
<td>(2.7)</td>
<td>(6.3)</td>
<td>(7.6)</td>
<td>(3.9)</td>
<td>(6.0)</td>
<td>(9.1)</td>
<td>(9.6)</td>
<td>(1.2)</td>
</tr>
<tr>
<td><strong>Operating Margin</strong></td>
<td>-112.3%</td>
<td>-87.0%</td>
<td>-299.3%</td>
<td>-2964.7%</td>
<td>-51.0%</td>
<td>-90.7%</td>
<td>-241.7%</td>
<td>-374.9%</td>
<td>-10.3%</td>
</tr>
<tr>
<td><strong>y/y change:</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>26%</td>
<td>115%</td>
<td>81%</td>
<td>892%</td>
<td>51%</td>
</tr>
<tr>
<td><strong>% of total:</strong></td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
</tr>
<tr>
<td><strong>Operating Income/(Loss)</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
</tr>
<tr>
<td><strong>% of total:</strong></td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
</tr>
<tr>
<td><strong>Total non-Univ. of Phoenix:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Revenues</strong></td>
<td>$34.6</td>
<td>$28.4</td>
<td>$30.9</td>
<td>$28.6</td>
<td>$32.0</td>
<td>$25.6</td>
<td>$30.2</td>
<td>$29.0</td>
<td>$31.2</td>
</tr>
<tr>
<td><strong>Operating Income/(Loss)</strong></td>
<td>5.3</td>
<td>0.1</td>
<td>(0.4)</td>
<td>(5.5)</td>
<td>1.3</td>
<td>(9.3)</td>
<td>(9.4)</td>
<td>(25.3)</td>
<td>15.3</td>
</tr>
<tr>
<td><strong>Operating Margin</strong></td>
<td>14.6%</td>
<td>0.3%</td>
<td>-1.1%</td>
<td>-14.5%</td>
<td>2.4%</td>
<td>-20.1%</td>
<td>-20.9%</td>
<td>-44.6%</td>
<td>10.3%</td>
</tr>
<tr>
<td><strong>y/y change:</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>-41%</td>
<td>-147%</td>
<td>-49%</td>
<td>-80%</td>
<td>-38%</td>
</tr>
<tr>
<td><strong>% of total:</strong></td>
<td>5%</td>
<td>5%</td>
<td>4%</td>
<td>5%</td>
<td>6%</td>
<td>5%</td>
<td>4%</td>
<td>5%</td>
<td>12%</td>
</tr>
<tr>
<td><strong>Operating Income/(Loss)</strong></td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
<td>N.A.</td>
</tr>
<tr>
<td><strong>% of total:</strong></td>
<td>5%</td>
<td>5%</td>
<td>4%</td>
<td>5%</td>
<td>6%</td>
<td>5%</td>
<td>4%</td>
<td>5%</td>
<td>12%</td>
</tr>
</tbody>
</table>


**Apollo Global:** The company has an 80.1% ownership interest in Apollo Global, which pursues investments primarily in the international education services industry, and which has completed acquisitions of Universidad de Artes, Ciencias y Comunicación (“UNIACC”) in Chile, and
Universidad Latinoamericana (“ULA”) in Mexico. Most recently, it purchased UK-based BPP Holdings in a deal that closed at the end of July 2009. Excluding BPP – which generated $88.7 million in revenues in its first full quarter of consolidation – this segment reported revenues of $16.4 million, down 4% y/y, with an operating loss of $1.9 million. BPP reported operating income of $15.6 million with an operating margin of 17.6%.

**Insight Schools:** This is the company’s K-12 virtual school offering, acquired in October 2006. Insight’s revenues increased 51% to $11.6 million in FY1Q10 from $7.7 million in FY1Q09, and its operating loss narrowed to $1.2 million from $3.9 million in FY1Q09. The unit has never been profitable as far as we are aware. Additionally, the segment has been plagued by administrative challenges, which led it to exit two states in FY2009. In light of these issues, management recently announced its intention to “explore the sale” of Insight Schools in order to focus primarily on postsecondary schools, and reported it was still exploring this opportunity as of November 30, 2009. As such, the results of this segment may be reported as discontinued operations going forward. We believe this is a positive development and would rid APOL of a nonperforming asset that we view as outside of its core competency.

**Other Schools:** This segment contains Western International University (WIU), Institute for Professional Development (IPD), College of Financial Planning (CFP) and Meritus University, the company’s Canadian school which began operations in September 2008. Segment revenues decreased 2% y/y to $31.2 million in FY1Q10. The unit recorded operating income of $2.8 million in FY1Q10 versus $4 million in FY1Q09, with operating margins declining to 9% from 14.1%.

**OTHER TIDBITS FROM THE CALL/10Q**

**New University Orientation program.** Recently, the company has expanded a pilot program in which it is attempting to improve the quality of its incoming student base by ensuring they have “new enrollments that retain”. The program requires perspective students at selected campuses with less than 24 credit hours to take a free 3-week orientation course before enrolling. That target student base skews heavily toward its Axia (associates) program. Management stated new enrollment growth in FY1Q10 was negatively impacted by a few hundred basis points during the quarter owing to this program. Given this pilot may be expanding (management would not elaborate), it may have a greater impact going forward.

We definitely agree this is “the right thing to do.” The company has been under tremendous scrutiny given its position as the largest user of Title IV funds and any program which improves the quality of its student base should help improve the value proposition for its students. In addition, this should dovetail well with the increased focus on outputs by regulatory entities.

Unfortunately, what helps long-term likely hurts near term. Slowing Axia growth (and potentially growth in other areas as well) is the major reason we have reduced our estimates today.

**Program review results.** A program review is a periodic review by the US Department of Education (ED) for compliance with applicable standards and regulations. In February 2009,
the ED performed a program review of UOP’s policies and procedures involving Title IV programs. On December 31, 2009, UOP received a preliminary program review report.

The report contains six findings – something the company needs to respond to within an action plan:

- Three of the findings generally relate to procedures for determining the date on which a student withdraws from UOP. Per management, the issue revolves around whether the date is the actual withdrawal date or when there was some indication of intent to withdraw.

- One finding cites exceptions to the ED’s rules regarding the timing of returning unearned Title IV funds. **No errors were identified in UOP’s calculation of the amounts of Title IV funds to be returned** – the issue is rather the timing of when the funds needed to be returned (typically within 45 days after a student is deemed to have withdrawn). The average delay has been about 6 days, per management.

- Another finding relates to isolated clerical errors in verifying student-supplied information.

- The two remaining findings were self reported by UOP in its 2008 Annual Compliance Audit and involve the calculation of student financial need in certain cases without taking into account tuition and fee waivers and discounts, principally for APOL eligible for tuition assistance, and the use of Title IV funds for non-program purposes such as transcript, application and late fees.

There was also one “concern” – a broader comment, per management:

- The ED expressed a concern that some students enroll and begin attending classes before completely understanding the implications of enrollment, including their eligibility for student financial aid. The ED believes prospective students should be more extensively counseled prior to incurring any tuition liability about total program charges, the number of credits that are transferable, the total number of credits required to complete their chosen program and the financial aid available for each academic year of the program.

The school has until March 31, 2010 to submit a response to these findings. After the ED receives this response, it will issue a Final Program Review Determination letter that will specify any required corrective action or amounts owed to the ED.

The company believes its liability resulting from these findings will be approximately $1.5 million, which was accrued for in FY1Q10; assuming this was fully tax deductible, we believe this reduced EPS by roughly a half-penny. In addition, the ED require certain institutions to post a letter of credit where a preliminary program review report cites untimely return of unearned Title IV funds for more than 10% of the sampled students. The company believes this could be as much as $125 million, which will be required to be posted by January 30, 2010 and maintained until at least September 30, 2011. This equates to roughly $0.80 per share.

While there had been some speculation that UOP would be under an annual program review, a new program review has not been initiated.
SEC inquiry. No update was provided re: the recent SEC informal inquiry regarding revenue recognition.

CHANGES TO OUR MODEL

On its FY4Q09 earnings call, management provided its long-term targets – something it reiterated last night, despite the shift from inputs to outputs. Over the next three to five years, it hopes to generate:

- “Low-double-digit” revenue growth
- “Mid-teens” operating profit growth

During last quarter’s call, management clarified this by stating this goal was for the entire company, both domestic and international, but excluded acquisitions. In addition, it assumes pricing increases of roughly 3%-5%, implying (by our estimates), enrollment growth in the high-single-digit range.

As its custom, management did not provide near-term guidance, though indicated that in the near-term slower growth may continue, bad debt expense may increase and the company would continue to invest in its recently acquired BPP Holdings.

We are reducing our FY2Q10 EPS estimate to $0.89 from $0.99; our FY2010 EPS estimate to $4.87 from $5.23; and our FY2011 EPS estimate to 5.73 from $6.06 (see Exhibit 14). Our reductions are mainly driven by lower enrollment growth expectations.

Exhibit 14: BMO Capital Markets Forecasts for Apollo Group (FY2Q10E, FY2010E and FY2011E)

<table>
<thead>
<tr>
<th>($ mil. except EPS)</th>
<th>NEW</th>
<th>FY2Q10E</th>
<th>OLD</th>
<th>NEW</th>
<th>FY2010E</th>
<th>OLD</th>
<th>NEW</th>
<th>FY2011E</th>
<th>OLD</th>
</tr>
</thead>
<tbody>
<tr>
<td>New degreed enrollment (i.e., starts)</td>
<td>88,687</td>
<td>Reduced</td>
<td>93,326</td>
<td>Reduced</td>
<td>393,275</td>
<td>Reduced</td>
<td>412,581</td>
<td>Reduced</td>
<td>419,696</td>
</tr>
<tr>
<td>% chg y/y</td>
<td>10.9%</td>
<td>Reduced</td>
<td>16.7%</td>
<td>Reduced</td>
<td>10.5%</td>
<td>Reduced</td>
<td>16.0%</td>
<td>Reduced</td>
<td>6.7%</td>
</tr>
<tr>
<td>Total degreed enrollment</td>
<td>454,892</td>
<td>Reduced</td>
<td>468,750</td>
<td>Reduced</td>
<td>492,837</td>
<td>Reduced</td>
<td>506,661</td>
<td>Reduced</td>
<td>531,789</td>
</tr>
<tr>
<td>% chg y/y</td>
<td>14.4%</td>
<td>Reduced</td>
<td>17.9%</td>
<td>Reduced</td>
<td>11.2%</td>
<td>Reduced</td>
<td>14.4%</td>
<td>Reduced</td>
<td>7.9%</td>
</tr>
<tr>
<td>Revenue</td>
<td>$1,052.4</td>
<td>Reduced</td>
<td>$1,108.9</td>
<td>Reduced</td>
<td>$4,838.8</td>
<td>Reduced</td>
<td>$4,941.5</td>
<td>Reduced</td>
<td>$5,388.4</td>
</tr>
<tr>
<td>% chg y/y</td>
<td>20.1%</td>
<td>Reduced</td>
<td>26.6%</td>
<td>Reduced</td>
<td>21.8%</td>
<td>Reduced</td>
<td>24.3%</td>
<td>Reduced</td>
<td>11.4%</td>
</tr>
<tr>
<td>Operating Income (bef. stock-based comp)</td>
<td>$252.5</td>
<td>Reduced</td>
<td>$273.4</td>
<td>Reduced</td>
<td>$1,361.6</td>
<td>Reduced</td>
<td>$1,431.8</td>
<td>Reduced</td>
<td>$1,587.9</td>
</tr>
<tr>
<td>% chg y/y</td>
<td>13.6%</td>
<td>Reduced</td>
<td>23.0%</td>
<td>Reduced</td>
<td>14.6%</td>
<td>Reduced</td>
<td>20.5%</td>
<td>Reduced</td>
<td>16.6%</td>
</tr>
<tr>
<td>% margins</td>
<td>24.0%</td>
<td>Reduced</td>
<td>24.7%</td>
<td>Reduced</td>
<td>28.1%</td>
<td>Reduced</td>
<td>29.0%</td>
<td>Reduced</td>
<td>29.5%</td>
</tr>
<tr>
<td>EPS</td>
<td>$0.89</td>
<td>Reduced</td>
<td>$0.99</td>
<td>Reduced</td>
<td>$4.87</td>
<td>Reduced</td>
<td>$5.23</td>
<td>Reduced</td>
<td>$5.73</td>
</tr>
<tr>
<td>% chg y/y</td>
<td>16.1%</td>
<td>Reduced</td>
<td>28.4%</td>
<td>Reduced</td>
<td>15.6%</td>
<td>Reduced</td>
<td>24.1%</td>
<td>Reduced</td>
<td>17.6%</td>
</tr>
</tbody>
</table>

Source: BMO Capital Markets estimates.

VALUATION

We are reducing our 12-month price target to $64 from $73 based on the methodologies presented below. Risks to our target include a slower than expected ramp-down in enrollment growth, worse than expected margin contraction and more regulatory scrutiny.

Forward-looking P/E. As of last night’s close, APOL was valued at roughly 12.5x our revised CY2010 EPS estimate of $5.13, a discount to the industry median of roughly 16.5x. Given our reduced estimates, we believe a lower multiple is warranted – especially in light of the recent multiple expansion leading into the earnings release. Assuming that APOL trades at 10x using
our new CY2011 EPS estimate of $5.95, this methodology yields a 12-month price target of roughly $60.

**Forward-looking EV/EBITDA.** As of last night’s close, APOL was valued at 6.6x enterprise value/trailing 12-month (TTM) EBITDA of roughly $1.38 billion (through 11/30/09), a discount to the industry median of roughly 9.7x. This excludes roughly four month’s worth of BPP, and as such, we believe APOL’s TTM EBITDA would be even higher and therefore its multiple even lower. As such, we have only slightly reduced our target multiple and assume that in one year, APOL trades at roughly 6x using estimated TTM EBITDA for the 12 months ended 11/30/10 (which we project will be about $1.55 billion). This methodology yields a 12-month price target of roughly $70.

**Discounted cash flow.** Our final methodology used a discounted cash flow (DCF) approach with the following assumptions:

- Free cash flow (cash flow from operations less capital expenditures) grows at a slower annual rate after 2011 before normalizing at 10%;

- Discount rate of 25%. We have increased our discount rate owing to the added uncertainty created by the SEC inquiry.

- Multiple of 5x for terminal value.

Based on these assumptions, we calculate APOL is currently worth $58 per share and in one year (using one less discount period) will be worth roughly $63 per share.

We believe APOL could be worth $60–$70 per share over the next 12 months (see Exhibit 15). As such, we are reducing our 12-month target price from $73 to $64, the average of this range.

**Exhibit 15. Summary of APOL Valuations**

<table>
<thead>
<tr>
<th>Methodology</th>
<th>Est. APOL Share Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Forward-looking P/E Multiple</td>
<td>$60</td>
</tr>
<tr>
<td>Forward-looking EV/EBITDA</td>
<td>70</td>
</tr>
<tr>
<td>Discounted cash flow</td>
<td>63</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td><strong>$64</strong></td>
</tr>
</tbody>
</table>

Source: BMO Capital Markets.
<table>
<thead>
<tr>
<th>Revenues:</th>
<th>Actual FY1Q</th>
<th>Nov-09</th>
<th>% Change</th>
<th>Est FY1Q</th>
<th>% Dif. from</th>
<th>Actual</th>
<th>% Change</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Degree Seeking Gross Revenues</td>
<td>$944.4</td>
<td>$1,173.5</td>
<td>24.3%</td>
<td>$1,150.7</td>
<td>2.0%</td>
<td></td>
<td></td>
<td>Slightly better than expected</td>
</tr>
<tr>
<td>Loss: Discounts</td>
<td>(42.9)</td>
<td>(66.2)</td>
<td>45.0%</td>
<td>(57.0)</td>
<td>8.2%</td>
<td></td>
<td></td>
<td>Much better than expected</td>
</tr>
<tr>
<td>Degree seeking net revenues</td>
<td>901.5</td>
<td>1,111.3</td>
<td>23.3%</td>
<td>1,093.3</td>
<td>1.6%</td>
<td></td>
<td></td>
<td>Slightly better than expected</td>
</tr>
<tr>
<td>Non-Degree Seeking Revenues</td>
<td>9.3</td>
<td>9.9</td>
<td>6.5%</td>
<td>11.3</td>
<td>-12.2%</td>
<td></td>
<td></td>
<td>Much worse than expected</td>
</tr>
<tr>
<td>Other revenues</td>
<td>60.2</td>
<td>149.1</td>
<td>147.7%</td>
<td>136.0</td>
<td>8.6%</td>
<td></td>
<td></td>
<td>Much better than expected</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,011.0</strong></td>
<td><strong>1,348.4</strong></td>
<td><strong>23.3%</strong></td>
<td><strong>1,240.5</strong></td>
<td><strong>2.4%</strong></td>
<td></td>
<td>Slightly better than expected; consensus was $1,229.6 mil.</td>
<td></td>
</tr>
<tr>
<td><strong>Tuition and Other, Net</strong></td>
<td>471.0</td>
<td>1,270.3</td>
<td>30.8%</td>
<td>1,240.0</td>
<td>2.4%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Costs and Expenses:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Instruction Costs and Services</td>
<td>373.3</td>
<td>525.7</td>
<td>40.8%</td>
<td>500.2</td>
<td>-4.9%</td>
<td></td>
<td></td>
<td>Worse than expected</td>
</tr>
<tr>
<td>Selling and Promotional</td>
<td>227.1</td>
<td>274.1</td>
<td>20.7%</td>
<td>281.9</td>
<td>2.8%</td>
<td></td>
<td></td>
<td>Better than expected</td>
</tr>
<tr>
<td>General and Administrative</td>
<td>48.6</td>
<td>63.4</td>
<td>30.5%</td>
<td>60.8</td>
<td>-4.1%</td>
<td></td>
<td></td>
<td>Worse than expected</td>
</tr>
<tr>
<td>Total Costs and Expenses</td>
<td>649.0</td>
<td>863.3</td>
<td>33.0%</td>
<td>842.9</td>
<td>-2.4%</td>
<td></td>
<td></td>
<td>Slightly worse than expected</td>
</tr>
<tr>
<td><strong>Operating Income (bef. stock-based comp.)</strong></td>
<td><strong>322.0</strong></td>
<td><strong>407.0</strong></td>
<td><strong>26.4%</strong></td>
<td><strong>397.6</strong></td>
<td><strong>2.4%</strong></td>
<td></td>
<td>Slightly better than expected</td>
<td></td>
</tr>
<tr>
<td>Stock-based Compensation</td>
<td>15.1</td>
<td>14.2</td>
<td>6.5%</td>
<td>17.0</td>
<td>-20.2%</td>
<td></td>
<td></td>
<td>Much worse than expected</td>
</tr>
<tr>
<td>Operating Income (excl. one-time costs)</td>
<td>306.9</td>
<td>392.9</td>
<td>28.0%</td>
<td>380.6</td>
<td>3.2%</td>
<td></td>
<td>Better than expected</td>
<td></td>
</tr>
<tr>
<td>One-Time Charges</td>
<td>0.0</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Operating Income</strong></td>
<td>306.9</td>
<td>392.9</td>
<td>28.0%</td>
<td>380.6</td>
<td>3.2%</td>
<td></td>
<td></td>
<td>Better than expected</td>
</tr>
<tr>
<td>Interest Income</td>
<td>5.4</td>
<td>9.9</td>
<td>-82.7%</td>
<td>1.4</td>
<td>-31.4%</td>
<td></td>
<td></td>
<td>Much worse than expected</td>
</tr>
<tr>
<td>Interest (Expense)</td>
<td>(1.4)</td>
<td>(2.9)</td>
<td>103.3%</td>
<td>(2.6)</td>
<td>-13.5%</td>
<td></td>
<td></td>
<td>Much worse than expected</td>
</tr>
<tr>
<td>Other, Net</td>
<td>(2.4)</td>
<td>(9.9)</td>
<td>64.4%</td>
<td>(3.2)</td>
<td>N.A.</td>
<td></td>
<td></td>
<td>N.A. N.A.</td>
</tr>
<tr>
<td><strong>Net Income/(Loss)</strong></td>
<td>180.3</td>
<td>240.1</td>
<td>33.2%</td>
<td>223.9</td>
<td>7.3%</td>
<td></td>
<td></td>
<td>Slightly better than expected</td>
</tr>
<tr>
<td>Net loss attributable to noncontrolling interests</td>
<td>0.1</td>
<td>0.1</td>
<td>0.0%</td>
<td>0.0</td>
<td>-98.4%</td>
<td></td>
<td></td>
<td>Much worse than expected</td>
</tr>
<tr>
<td><strong>Net Income attributable to Apollo Group</strong></td>
<td>$180.4</td>
<td>$240.2</td>
<td>33.2%</td>
<td>$227.1</td>
<td>5.8%</td>
<td></td>
<td>Much better than expected</td>
<td></td>
</tr>
<tr>
<td>EPS (excl. one-time items)</td>
<td>$1.12</td>
<td>$1.47</td>
<td>30.7%</td>
<td>$1.46</td>
<td>0.5%</td>
<td></td>
<td></td>
<td>Roughly in line; consensus was $1.46</td>
</tr>
<tr>
<td>Diluted Shares Outstanding</td>
<td>160.8</td>
<td>156.0</td>
<td>-2.9%</td>
<td>155.7</td>
<td>-0.2%</td>
<td></td>
<td></td>
<td>Roughly in line</td>
</tr>
<tr>
<td><strong>EBITDA (excluding stock-based comp.)</strong></td>
<td><strong>$344.9</strong></td>
<td><strong>$439.4</strong></td>
<td><strong>27.4%</strong></td>
<td><strong>$428.3</strong></td>
<td><strong>2.6%</strong></td>
<td></td>
<td>Better than expected</td>
<td></td>
</tr>
</tbody>
</table>

**New degree enrollments:**
- Associates: 45,800 -> 52,200 (14.0%) 56,560 7.7% Worse than expected
- Bachelors: 26,100 -> 32,100 (23.0%) 30,157 6.4% Much better than expected
- Masters: 13,300 -> 13,100 (-1.5%) 13,887 -5.7% Much worse than expected
- Doctoral: 1,100 -> 700 (-36.4%) 1,155 -39.4% Much worse than expected
- **Total** 86,300 -> 98,100 (13.7%) 101,759 -3.6% Worse than expected

**Revenue per degree-seeking student** $2,342 -> $2,439 (4.1%) $2,369 3.0% Better than expected

** Margin Analysis/% of Total Revenues**
- Instruction Costs and Services: 38.4% 41.4% -2.9% 40.3% -1.1% Much worse than expected
- Selling and Promotional: 23.4% 21.6% 1.8% 22.7% 1.1% Much better than expected
- General and Administrative: 5.0% 5.0% 0.0% 4.9% -0.1% Roughly in line
- EBITDA Margin: 35.9% 34.6% -0.9% 34.8% 0.1% Roughly in line
- Operating Margin (bef. stock-based comp): 33.2% 32.0% -1.1% 32.1% 0.0% Roughly in line
- Stock-based Compensation: 1.6% 1.1% -0.4% 1.4% 0.3% Better than expected
- Operating Income (excl. one-time costs): 37.6% 36.9% -0.7% 36.7% 0.2% Slightly better than expected
- Operating Income: 31.6% 30.9% -0.7% 30.7% 0.2% Slightly better than expected
- Pretax Margin: 31.8% 30.7% -1.1% 30.6% 0.1% Slightly better than expected
- Tax Rate: 41.5% 38.4% 3.1% 41.0% 2.6% Much better than expected
- **Net Margin** 18.6% 18.9% 0.3% 18.0% 0.9% Much better than expected

**Revenue per degree-seeking student** $2,342 -> $2,439 (4.1%) $2,369 3.0% Better than expected

** N.A. - Not Available. N.M. - Not Meaningful.**

Source: BMO Capital Markets estimates and company reports.
### Apollo Group (APOL) Quarterly Income Statements (FY2009-FY2011E)

($ Millions; FY Ending August 31)

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenues</th>
<th>Selling and Promotional</th>
<th>Instruction Costs and Services</th>
<th>Pretax Margin</th>
<th>Tax Rate</th>
<th>Net Income</th>
<th>EPS (excl. one-time items)</th>
<th>Diluted Shares Outstanding</th>
<th>ROE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009A</td>
<td>$919.0</td>
<td>$181.1</td>
<td>$737.9</td>
<td>31.8%</td>
<td>41.5%</td>
<td>$180.3</td>
<td>$1.12</td>
<td>160.8</td>
<td>77.1%</td>
</tr>
<tr>
<td>2009Q1</td>
<td>$239.3</td>
<td>$52.8</td>
<td>$186.5</td>
<td>23.9%</td>
<td>41.5%</td>
<td>$43.9</td>
<td>$0.77</td>
<td>156.0</td>
<td>43.5%</td>
</tr>
<tr>
<td>2009Q2</td>
<td>$237.4</td>
<td>$56.2</td>
<td>$181.2</td>
<td>23.6%</td>
<td>41.5%</td>
<td>$34.1</td>
<td>$0.77</td>
<td>156.0</td>
<td>43.5%</td>
</tr>
<tr>
<td>2009Q3</td>
<td>$241.5</td>
<td>$57.0</td>
<td>$184.5</td>
<td>23.9%</td>
<td>41.5%</td>
<td>$41.3</td>
<td>$0.89</td>
<td>156.4</td>
<td>43.5%</td>
</tr>
<tr>
<td>2009Q4</td>
<td>$251.7</td>
<td>$62.1</td>
<td>$189.6</td>
<td>24.7%</td>
<td>41.5%</td>
<td>$42.7</td>
<td>$1.06</td>
<td>156.7</td>
<td>43.5%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenues</th>
<th>Selling and Promotional</th>
<th>Instruction Costs and Services</th>
<th>Pretax Margin</th>
<th>Tax Rate</th>
<th>Net Income</th>
<th>EPS (excl. one-time items)</th>
<th>Diluted Shares Outstanding</th>
<th>ROE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010Q1</td>
<td>$264.2</td>
<td>$55.2</td>
<td>$209.0</td>
<td>24.6%</td>
<td>41.5%</td>
<td>$51.5</td>
<td>$1.26</td>
<td>157.2</td>
<td>43.5%</td>
</tr>
<tr>
<td>2010Q2</td>
<td>$262.4</td>
<td>$58.8</td>
<td>$203.6</td>
<td>24.8%</td>
<td>41.5%</td>
<td>$54.0</td>
<td>$1.24</td>
<td>157.5</td>
<td>43.5%</td>
</tr>
<tr>
<td>2010Q3</td>
<td>$252.5</td>
<td>$61.3</td>
<td>$191.2</td>
<td>23.9%</td>
<td>41.5%</td>
<td>$42.5</td>
<td>$0.96</td>
<td>157.7</td>
<td>43.5%</td>
</tr>
<tr>
<td>2010Q4</td>
<td>$252.9</td>
<td>$62.3</td>
<td>$190.6</td>
<td>23.7%</td>
<td>41.5%</td>
<td>$43.0</td>
<td>$1.06</td>
<td>158.0</td>
<td>43.5%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenues</th>
<th>Selling and Promotional</th>
<th>Instruction Costs and Services</th>
<th>Pretax Margin</th>
<th>Tax Rate</th>
<th>Net Income</th>
<th>EPS (excl. one-time items)</th>
<th>Diluted Shares Outstanding</th>
<th>ROE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011Q1</td>
<td>$252.9</td>
<td>$62.3</td>
<td>$190.6</td>
<td>23.7%</td>
<td>41.5%</td>
<td>$43.0</td>
<td>$1.06</td>
<td>158.0</td>
<td>43.5%</td>
</tr>
<tr>
<td>2011Q2</td>
<td>$252.9</td>
<td>$62.3</td>
<td>$190.6</td>
<td>23.7%</td>
<td>41.5%</td>
<td>$43.0</td>
<td>$1.06</td>
<td>158.0</td>
<td>43.5%</td>
</tr>
<tr>
<td>2011Q3</td>
<td>$252.9</td>
<td>$62.3</td>
<td>$190.6</td>
<td>23.7%</td>
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<td>$43.0</td>
<td>$1.06</td>
<td>158.0</td>
<td>43.5%</td>
</tr>
<tr>
<td>2011Q4</td>
<td>$252.9</td>
<td>$62.3</td>
<td>$190.6</td>
<td>23.7%</td>
<td>41.5%</td>
<td>$43.0</td>
<td>$1.06</td>
<td>158.0</td>
<td>43.5%</td>
</tr>
</tbody>
</table>

### Margin Analysis/Net Revenues:

- **Instruction Costs and Services:** 38.4% (2009A) to 23.7% (2011Q4)
- **Selling and Promotional:** 23.4% (2009A) to 23.7% (2011Q4)
- **Instruction Costs and Services:** 31.8% (2009A) to 23.7% (2011Q4)
- **Pretax Margin:** 31.8% (2009A) to 23.7% (2011Q4)
- **Tax Rate:** 41.5% (2009A) to 41.5% (2011Q4)
- **Net Income:** $180.3 (2009A) to $43.0 (2011Q4)
- **EPS (excl. one-time items):** $1.12 (2009A) to $1.06 (2011Q4)
- **Diluted Shares Outstanding:** 160.8 (2009A) to 158.0 (2011Q4)
- **ROE:** 77.1% (2009A) to 16.6% (2011Q4)

### Year/Year Changes:

- **Revenues:** 24.4% (2009A) to 18.4% (2011Q4)
- **Instruction Costs and Services:** 13.7% (2009A) to 9.1% (2011Q4)
- **Selling and Promotional:** 25.4% (2009A) to 21.8% (2011Q4)
- **Instruction Costs and Services:** 31.8% (2009A) to 16.6% (2011Q4)
- **Pretax Margin:** 31.8% (2009A) to 16.6% (2011Q4)
- **Tax Rate:** 41.5% (2009A) to 16.6% (2011Q4)
- **Net Income:** $180.3 (2009A) to $43.0 (2011Q4)
- **EPS (excl. one-time items):** $1.12 (2009A) to $1.06 (2011Q4)
- **Diluted Shares Outstanding:** 160.8 (2009A) to 158.0 (2011Q4)
- **ROE:** 77.1% (2009A) to 16.6% (2011Q4)

### Additional Notes:

- **EPS:** Excluding one-time charges and SFAS 123
- **Diluted Shares Outstanding:** Including employee stock options
- **ROE:** Annualized

Source: BMO Capital Markets and company reports.
## Apollo Group (APOL) Quarterly Cash Flow Statements (FY2009-FY2011E)

($ Millions; FY Ending August 31)

<table>
<thead>
<tr>
<th>Category</th>
<th>1Q09A</th>
<th>2Q09A</th>
<th>3Q09A</th>
<th>4Q09A</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash Flows From Operating Activities:</td>
<td>$180.3</td>
<td>$125.1</td>
<td>$200.6</td>
<td>$87.8</td>
<td>$593.8</td>
</tr>
<tr>
<td>Net Income/(Loss)</td>
<td>$180.3</td>
<td>$125.1</td>
<td>$200.6</td>
<td>$87.8</td>
<td>$593.8</td>
</tr>
<tr>
<td>Stock-based Compensation Expense</td>
<td>15.1</td>
<td>16.2</td>
<td>18.0</td>
<td>16.7</td>
<td>68.0</td>
</tr>
<tr>
<td>Depreciation and Amortization</td>
<td>22.9</td>
<td>23.4</td>
<td>26.5</td>
<td>27.7</td>
<td>100.5</td>
</tr>
<tr>
<td>Other Non-Cash Items</td>
<td>2.1</td>
<td>(0.3)</td>
<td>(2.3)</td>
<td>8.2</td>
<td>7.6</td>
</tr>
<tr>
<td>Provision for Uncollectible Accounts</td>
<td>34.9</td>
<td>36.1</td>
<td>36.0</td>
<td>46.6</td>
<td>152.5</td>
</tr>
<tr>
<td>Minority Interest</td>
<td>(0.1)</td>
<td>(0.3)</td>
<td>(0.5)</td>
<td>(3.7)</td>
<td>(4.5)</td>
</tr>
<tr>
<td>Estimated Securities Litigation Loss</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Deferred Income Taxes, Net</td>
<td>(8.8)</td>
<td>(3.8)</td>
<td>16.6</td>
<td>(17.8)</td>
<td>(13.8)</td>
</tr>
<tr>
<td>Tax Benefits of Stock Options Exercised</td>
<td>4.0</td>
<td>(7.2)</td>
<td>(0.3)</td>
<td>7.0</td>
<td>18.5</td>
</tr>
<tr>
<td>Changes in Operating Assets and Liabilities</td>
<td>138.3</td>
<td>94.7</td>
<td>39.1</td>
<td>(8.7)</td>
<td>(16.0)</td>
</tr>
<tr>
<td>Changes in Operating Assets and Liabilities</td>
<td>380.8</td>
<td>94.5</td>
<td>333.7</td>
<td>151.2</td>
<td>960.2</td>
</tr>
<tr>
<td>Changes in Operating Assets and Liabilities</td>
<td>405.2</td>
<td>(33.5)</td>
<td>404.5</td>
<td>196.1</td>
<td>972.3</td>
</tr>
<tr>
<td>Free Cash Flow</td>
<td>350.2</td>
<td>61.2</td>
<td>302.8</td>
<td>118.8</td>
<td>832.9</td>
</tr>
<tr>
<td>Cash Flows From Investing Activities:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net Additions to Property and Equipment</td>
<td>(30.6)</td>
<td>(3.3)</td>
<td>(30.9)</td>
<td>(32.5)</td>
<td>(127.4)</td>
</tr>
<tr>
<td>Maturities/(Purchase) of Marketable Sec., Net</td>
<td>1.7</td>
<td>0.0</td>
<td>1.0</td>
<td>5.4</td>
<td>8.0</td>
</tr>
<tr>
<td>Cash Paid for Acquisition</td>
<td>(523.8)</td>
<td>(523.8)</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Other</td>
<td>(58.6)</td>
<td>(55.6)</td>
<td>8.8</td>
<td>57.3</td>
<td>42.5</td>
</tr>
<tr>
<td>Net Cash Used in Investing Activities</td>
<td>(87.6)</td>
<td>(89.0)</td>
<td>(21.1)</td>
<td>(493.6)</td>
<td>(691.3)</td>
</tr>
<tr>
<td>Net Cash Provided/(Used) by Financing Activities</td>
<td>367.7</td>
<td>71.1</td>
<td>366.9</td>
<td>158.5</td>
<td>822.0</td>
</tr>
<tr>
<td>Purchase of Common Stock</td>
<td>(2.5)</td>
<td>0.0</td>
<td>(406.3)</td>
<td>(43.7)</td>
<td>(452.5)</td>
</tr>
<tr>
<td>Proceeds from/(Payments on) Long-Term Debt</td>
<td>1.6</td>
<td>(3.4)</td>
<td>47.4</td>
<td>475.8</td>
<td>(397.9)</td>
</tr>
<tr>
<td>Tax Benefits of Stock Options Exercised</td>
<td>4.0</td>
<td>7.2</td>
<td>0.3</td>
<td>18.5</td>
<td>0.2</td>
</tr>
<tr>
<td>Borrowings/(Repayments) on Line of Credit</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>(61.7)</td>
<td>(61.7)</td>
</tr>
<tr>
<td>Minority Interest Contributions</td>
<td>0.0</td>
<td>57.0</td>
<td>59.0</td>
<td>(0.5)</td>
<td>(1.0)</td>
</tr>
<tr>
<td>Net Cash Provided/(Used) by Financing Activities</td>
<td>21.3</td>
<td>81.9</td>
<td>(402.2)</td>
<td>5.8</td>
<td>217.9</td>
</tr>
<tr>
<td>Change in Cash and Equivalents</td>
<td>313.7</td>
<td>87.2</td>
<td>(89.2)</td>
<td>173.4</td>
<td>485.1</td>
</tr>
<tr>
<td>Cash and Cash Equivalents, Beginning of Period</td>
<td>313.7</td>
<td>87.2</td>
<td>(89.2)</td>
<td>173.4</td>
<td>485.1</td>
</tr>
<tr>
<td>Cash and Cash Equivalents, End of Period</td>
<td>$796.9</td>
<td>$884.1</td>
<td>$734.9</td>
<td>$916.8</td>
<td>$988.2</td>
</tr>
</tbody>
</table>

Source: BMO Capital Markets and company reports.
APOLLO GROUP INC (APOL)

Quarterly Price (US$)

- APOL Relative to S&P 500
- APOL Relative to Diversified Consumer Services

EPS (4 Qtr Trailing) - (US$)
Price / Earnings

APOL Relative to S&P 500 Y/Y (%)
APOL Relative to Diversified Consumer Services Y/Y (%)

Date       Rating Change        Share Price
1  29-Jun-07  Mkt to OP  $50.78

Last Daily Data Point: January 5, 2010
Important Disclosures

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Methodology and Risks to Our Price Target

Methodology: Average of forward looking P/E, forward looking EV/EBITDA and Discounted Cash Flow

Risks: Worse than expected enrollment trends in postsecondary education, state and federal regulatory issues,

Breakdown of Rating Distribution and Banking Clients
(As of September 30, 2009)

<table>
<thead>
<tr>
<th>Rating Category</th>
<th>Buy</th>
<th>Hold</th>
<th>Sell</th>
<th>Unrated</th>
</tr>
</thead>
<tbody>
<tr>
<td>% of total</td>
<td>29.1%</td>
<td>64.1%</td>
<td>6.8%</td>
<td>0.0%</td>
</tr>
<tr>
<td>% of stocks</td>
<td>12.8%</td>
<td>9.8%</td>
<td>0.0%</td>
<td>0.0%</td>
</tr>
</tbody>
</table>

BMO Capital Markets Corp. Rating System

**OP = Outperform:** We believe the stock's total return, including dividends, will exceed the S&P 500's return by more than 15%.

**Mkt = Market Perform:** We believe the stock's total return will generally match that of the S&P 500.

**Und = Underperform:** We believe the stock's total return will fall short of the S&P 500's return by more than 15%.

**NR = Not rated.**

(R) = Restricted: Dissemination of research is currently restricted.

In addition, apart from our stock ratings, we apply the Speculative investment (S) postscript to those companies that have de minimis revenue and whose enterprise value appears to be contingent upon unprovable assumptions (e.g., the future approval of a drug or the successful completion of an oil well).

**SECTOR RATINGS**

**OUTPERFORM -** We believe the sector will outperform the S&P 500 Index.

**MARKET PERFORM -** We believe the sector's return will generally match that of the S&P 500.

**UNDERPERFORM -** We believe the sector will underperform the S&P 500 Index.

**Prior BMO Capital Markets Corp. Rating System (prior to June 19, 2006)**

Our rating system prior to June 19, 2006, compared a stock's expected performance with that of an index of comparable companies over a 9-15 month horizon. Our sector ratings were based on the expected performance of the sector compared with that of a broader market index over the same time period. Additionally, before June 19, 2006, we did not use the (S)-Speculative postscript.

**PRIOR STOCK RATINGS**

**OUTPERFORM -** We believe the stock's total return, including dividends, will exceed the group average by over 15%.

**NEUTRAL -** We believe the stock’s total return will generally match the group average.
UNDERPERFORM - We believe the stock’s total return will fall short of the group average by more than 15%.

PRIOR SECTOR RATINGS
POSITIVE - We believe the sector will outperform the S&P 500 Index.
NEGATIVE - We believe the sector will underperform the S&P 500 Index.

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