Siena Market Line
2nd week of February 2015

Chegg, Inc.

NYSE:CHGG

Analyst: Jacky Cheng
Sector: Services

BUY

Price Target: $13.20

Key Statistics as of 4/24/2015

Market Price:	$8.06
Industry:	Education & Training Services
Market Cap:	$681.08 M
52-Week Range:	$4.82-8.85
Beta:	N/A

Thesis Points:

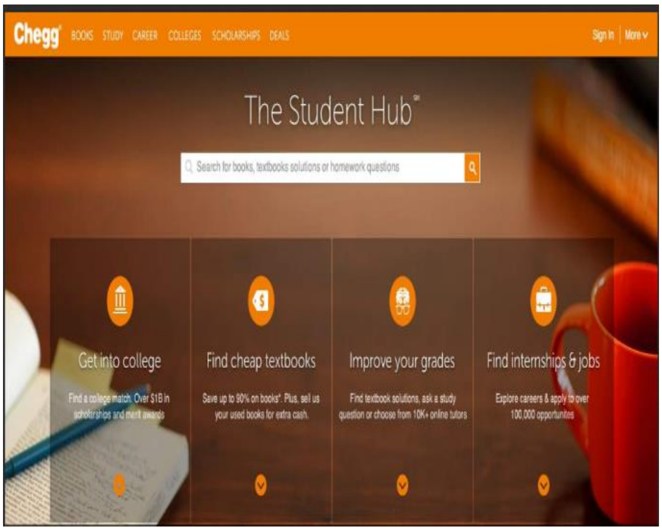
- Change in Model to Increase Margins
- Strategic Partnerships to Increase Cash Flows
- Growing Revenue

Company Description:

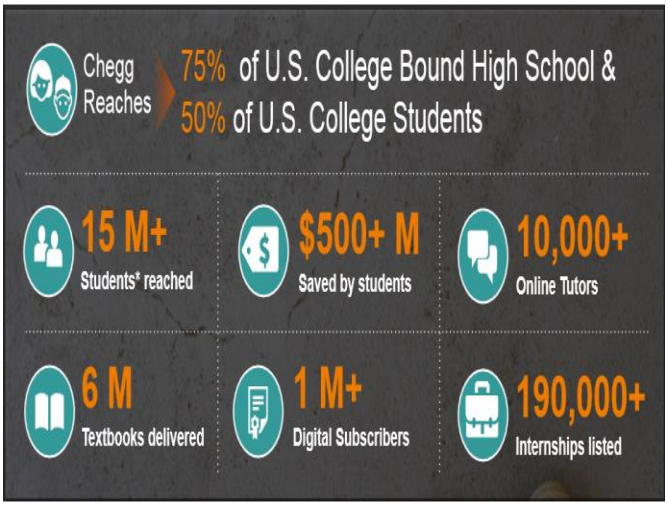
Chegg, Inc. operates student-first connected learning platform that empowers students to take control of their education to save time, save money, and get smarter. The company, through its Student Hub, rents and sells print textbooks; and provides eTextbooks, supplemental materials, Chegg Study service, textbook buyback, courses, internships, and college admissions and scholarship services, as well as offers enrollment marketing and brand advertising services. Chegg, Inc. has a strategic alliance with Ingram Content Group Inc. The company was founded in 2005 and is headquartered in Santa Clara, California.

Thesis

Chegg Inc. has been helping students make higher education a little more affordable. From firsthand experiences, the college bookstore marks up the prices on their textbook to a ridiculous price which is just creating more of a burden financially on college students. Luckily, Chegg's rental services helps provide books at a reasonable and affordable/competitive price along with other helpful tools that benefit students today and future students entering their first year of undergrad. Chegg is now switching its focus from physical textbooks to digital textbooks and expanding their digital platform in order to stay competitive in its industry and generate higher profit and margins. Having the majority of the market share, Chegg looks to partner up with strategic companies to further their business and grow.



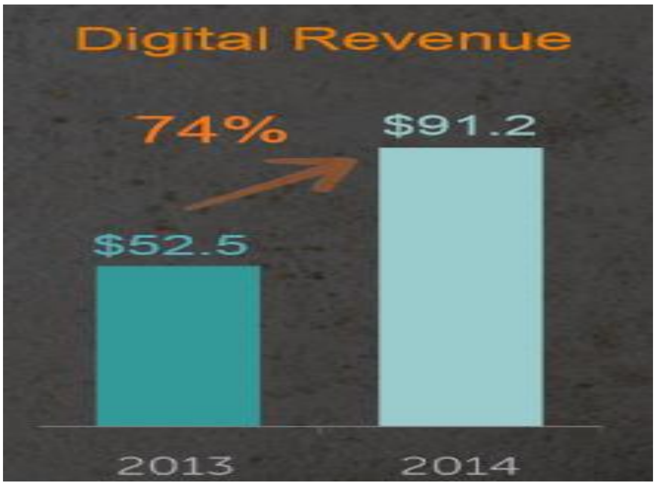
**Above shows the main portal when browsing Chegg's website.*



**Above shows Chegg's outreach and their impact in the industry.*

Change in Business Model

Chegg, Inc. realized that holding onto books was becoming obsolete and has suffered in its stock value since going public by going well below the initial price offering of $12.50. Housing and shipping the books was consuming nearly all of Chegg's working capital while competitors like Amazon were emerging into the market. Chegg is now switching its model to go completely digitalized as it is the next big thing with the growing trend of tablets usage such as the iPad and Kindles. Chegg would still deal with its hard copy book rentals, but would have another company handle it as they have already signed a partnership with Ingram Content Group and collect commission from it, discussed in the next section.



**Above shows growth in digital revenue between 2013-2014.*

By switching to this new digital model, Chegg would have more free cash flows instead of spending it on operating expenses. This would allow them to further expand their digital footprint by partnering up with other educational enterprises and acquire other companies as they already have to build onto their model. Chegg plans on being completely digitalized by 2017 where the company will generate revenue all commission-based from both rental and digital sales.

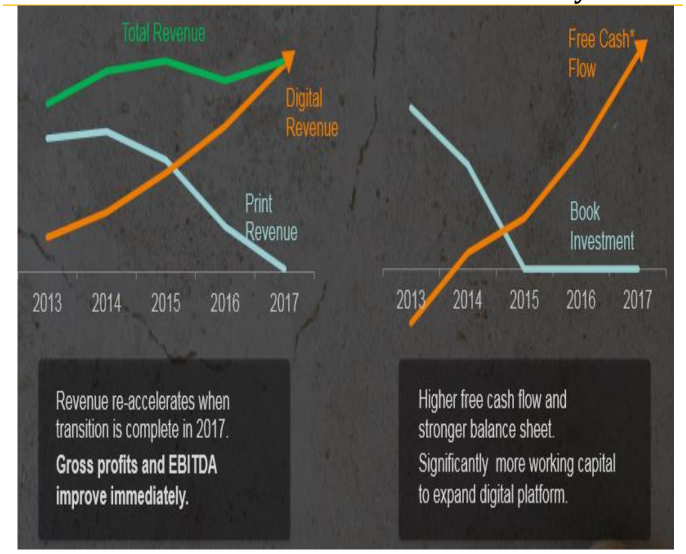
Chegg has already put its acquisitions into good use from using Chegg Tutors, which was known as InstaEDU and Chegg Study which was formally known as Cramster. Chegg Tutors is an online tutoring company that matches students who need help with online tutors. Chegg Study provides online homework and textbook help for college and high school students in areas such as math, science, engineering, humanities, business, and writing help. Both of these platforms run on a subscription based model and it has been very beneficial for high school and college students in success. There are already over 1 million paying digital subscribers. Chegg plans to buy more services like InstaEDU and Cramster to further integrate its platform.

Strategic Partnerships

Ingram Content Group

Chegg Inc. has partnered up with Ingram Content Group, who is the world's largest B2B distributor of physical and digital content and is known for having world-class inventory, logistics and distribution capabilities. Last year, Chegg entered into a test partnership with Ingram to determine the feasibility of outsourcing the logistics and inventory financing and determined it was feasible, entering into a five year partnership, in which Chegg will maintain the front-end direct to student relationships, while Ingram will be responsible for purchasing all future inventory, and well as managing all back-end logistics. This would mean that Chegg would be shrinking their inventory to basically zero as it would make Ingram responsible for inventory while Chegg would be dealing with their digital model. Chegg would be getting 20% commission from Ingram.

This partnership will greatly benefit Chegg as they continue on their complete switch towards digital and allow Ingram to handle all the physical textbooks which is what Ingram specializes in. This partnership will free up a lot of operating expenses and allow Chegg to use their cash towards further expanding their digital footprint in their industry such as acquiring other educational platforms.



**Above shows the financial projection of the partnership with Ingram and its projected outcome in total revenue and free cash flows.*

Blackboard Inc.

To further their digital footprint and provide a better educational service to their clients, Chegg partnered up with Blackboard Inc. that would allow Chegg's self-directed learning services (Chegg Study, Chegg Tutors, and Chegg Career Center) to be accessible within Blackboard Inc.'s market-leading teaching and learning environment. With what Blackboard already offers with Blackboard Learn, which is a virtual learning environmental and course management system, that is used in already over 17,000 institutions in 100 countries, the partnership would create more exposure for Chegg and its products. This would greatly increase the market share in their industry that Chegg already dominates. The impact of this integration is expected to be in the second half of the year.

Financials

Over the years, revenue has been substantially growing. With the transition from the physical to digital, it is expected that revenue will continue to grow. At the moment, the company has a negative net income due to high operating expenses from shipping and storing books. Operating expenses is expected to go down as Chegg is transitioning its inventory to Ingram where they will handle all of the physical copy textbooks.

Along with growing revenue, free cash flow is also growing at a steady rate. It is expected in the future that the cash flow will be greater as they eliminate a substantial amount of operating expenses, giving them more options to expand the company.

Future Outlook

By 2017, Chegg is expected to be at its prime becoming completely digitalized, generating all of its revenue from commission and digital sales. Operating expenses is expected to drop substantially, making Chegg a profitable company and also boosting their free cash flow. With the partnership of Ingram already in effect and Blackboard starting in the second half of the year, Chegg will have more exposure which will result in higher revenue.

Conclusion

Chegg was quick at adjusting their business strategy and now they are off to a better start than ever. With their acquisitions and recent partnerships, Chegg further expanded their market share that they already have the majority in. Despite not generating a profit currently, the changes Chegg has made to the company will significantly boost revenue, lower costs, and most importantly generate profit. For these reasons, Chegg Inc. is a BUY.

CENTER FOR GLOBAL FINANCIAL STUDIES

Chegg, Inc.	CHGG	Analyst	Current Price	Intrinsic Value	Target Value	Divident Yield	Target Return	BULLISH
		JACKY CHENG	$8.04	$14.52	$13.20	0%	1-y Return: 64.2%	

General Info

Sector	Consumer Discretionary
Industry	Diversified Consumer Services
Last Guidance	Jan-00-1900
Next earnings date	5/6/2015

Market Data

Enterprise value	$589.93
Market Capitalization	$2,032.29
Daily volume	0.25
Shares outstanding	84.50
Diluted shares outstanding	83.21
% shares held by institutions	99.58%
% shares held by insiders	9.16%
Short interest	10.28%
Days to cover short interest	11.92
52 week high	$8.85
52-week low	$4.82
5y Beta	0.00
6-month volatility	49.53%

Peers	Market Cap.
eBay Inc.	$68,411.71
Amazon.com Inc.	$181,657.73
Google Inc.	$366,476.52
Barnes & Noble, Inc.	$1,497.04

Current Capital Structure

Total debt/market cap	0.00%
Cost of Borrowing	#DIV/0!
Interest Coverage	3.9x
Altman Z	3.92
Debt Rating	D
Levered Beta	1.26
WACC (based on market value we	9.47%

Past Earning Surprises

	Revenue	EBITDA	Norm. EPS
Last Quarter	-1.0%	33.8%	26.7%
Last Quarter-1	4.3%	NM	NM
Last Quarter -2	0.8%	-91.9%	NM
Last Quarter -3	4.7%	NM	NM
Last Quarter -4	2.8%	-2.7%	81.8%

Management

Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Rosensweig, Daniel	Chairman, Chief Executive Of	$3,303,152	$8,969,812	$0
Brown, Andrew	Chief Financial Officer	$555,044	$3,097,362	$0
Geiger, Charles	Chief Technology Officer	$797,585	$3,369,171	$0
Phumbhra, Aayush	Co-Founder and Advisor	$0	$0	$0
Tomasello, Robin	Principal Accounting Officer,	$0	$0	$0
Osier, Michael	Chief Information Officer	$825,391	$0	$0

Historical Median Performance

	CHGG	Peers	Industry	All U.S. firms
Growth	18.2%	22.0%	9.8%	7.4%
ROIC	4.9%	11.2%	20.9%	14.3%
NOPLAT Margin	11.1%	13.8%	10.2%	10.4%
Revenue/Invested Capital	0.44	0.81	2.04	1.37
Excess Cash/Rev.	N/A	51.5%	13.5%	12.9%
Total Cash /Rev.	29.3%	51.8%	12.3%	15.2%
Unlevered Beta		1.25	0.65	0.95
TEV/REV	2.2x	3.6x	2.4x	2.5x
TEV/EBITA	11.3x	26.7x	13.7x	13.1x
PE (normalized and diluted EF	23.1x	28.4x	25.3x	23.5x
P/BV	0.8x	3.1x	2.7x	2.2x

Non-GAAP Adjustments in estimates computations

Operating Leases Capitalizatic	100%	Straightline	10 years
R&D Exp. Capitalization	100%	Straightline	10 years
Expl./Drilling Exp. Capitalizatio	0%	N/A	N/A
SG&A Capitalization	53%	Straightline	10 years

Proforma Assumptions

Money market rate as of today	0.54%
Annual increase (decrease) in interes	0.1%
Yield Spread accelaration	1.2
Marginal Tax Rate	37.5%
Risk-Free rate	2.6%
Tobin's Q	0.80
Op. Cash/Rev.	7%
Growth in PPE	NPPE Growth follows Revenue Growth
Long term Growth	7.6%
Base Year Unlevered Beta	is equal to 1.25
Long term Unlevered Beta	1.25

Forecast

Period	Rev. Growth	Adj. Op. Cost/Rev	Invested Capital	NOPLAT Margin	ROIC	WACC
LTM	19.3%	80.1%	$749.83	11%	4.5%	9.5%
NTM	18.1%	80.1%	$494.71	10%	4.9%	9.5%
NTM+1	16.9%	80.2%	$538.82	11%	9.1%	9.6%
NTM+2	15.8%	80.3%	$562.42	11%	10.0%	15.7%
NTM+3	14.6%	80.4%	$629.05	11%	11.0%	10.0%
NTM+4	13.5%	80.5%	$640.98	12%	11.9%	10.3%
NTM+5	12.3%	80.5%	$688.22	12%	13.1%	10.2%
NTM+6	11.1%	80.6%	$736.80	12%	13.5%	10.3%
NTM+7	10.0%	80.7%	$786.66	12%	14.2%	10.4%
NTM+8	8.8%	80.8%	$838.19	12%	14.5%	10.6%
Continuing Period	7.6%	80.9%	$727.06	10%	15.7%	10.7%

Valuation

Period	Invested Capital x (ROIC-WACC)	Total Debt	ıer non-interest bearing clai	Shares Outstanding
LTM	$0.00	$0.00	$11.49	84.50
NTM	-$34.34	$0.00	$46.00	84.50
NTM+1	-$2.35	$0.00	$78.97	84.50
NTM+2	$0.46	$0.00	$86.36	84.50
NTM+3	$5.83	$9.85	$106.49	84.50
NTM+4	$8.26	$19.62	$113.76	84.50
NTM+5	$18.41	$25.02	$121.17	84.50
NTM+6	$21.50	$38.76	$127.89	84.50
NTM+7	$27.54	$50.66	$140.60	84.50
NTM+8	$30.96	$64.36	$153.06	84.50
Continuing Value	$1,317.00			

Pricing Model

DCF (Weight = 100%)	Relative (Weight =	Distress (Weight :	Weighted Average Price P
$15.49	$8.53	$16.42	$15.49
$13.95	$9.33	$13.59	$13.95
$15.16	$10.85	$14.86	$15.16
$16.37	$12.83	$16.09	$16.37
$17.62	$14.29	$17.30	$17.62
$19.08	$16.74	$18.71	$19.08
$20.46	$18.89	$20.11	$20.46
$21.97	$21.08	$21.63	$21.97
$23.50	$23.17	$23.10	$23.50
$24.64	$25.13	$24.71	$24.64

Monte Carlo Simulation Assumptions

	Base	Stdev	Min	Max	Distribution
Revenue Variation	0	10%	N/A	N/A	Normal
Op. Costs Variation	0	10%	N/A	N/A	Normal
Country Risk Premium	6%	N/A	5%	7%	Triangular
Long term Growth	8%	N/A	3%	22%	Triangular

Monte Carlo Simulation Results

	Intrinsic Value	1y-Target
Mean est.	$15.49	$13.95
σ(ε)	$0.32	$0.25
σ(ε) adjusted pric	$14.53	$13.20
Current Price	$8.04	
Analysts' median est.		$10.14