



# INSTITUTIONAL RESEARCH

## Health & Commercial Services

### COMPANY UPDATE

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## The GEO Group Inc. (NYSE/GEO)

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### BUY Q1 on-track; 2010 moving ahead

*GEO is a provider of correctional and mental health services*

### Investment Highlights

1) The GEO Group (“GEO”) reportedly in-line financial results for their Q1/2010 earlier this week, earning \$0.34 per share on both GAAP and non-GAAP bases versus \$0.29 per share in the prior year period. Revenues grew to \$287.5 million in Q1/2010 versus \$259.1 million in Q1/2009, or an increase of 11.0%, led by sharp increases in GEO Care revenues (21.3%) from last year’s Columbia (SC) Regional activation and International Services (78.7%) due to new contracts in Australia and the UK. US Corrections revenues were essentially flat year-over-year, as new beds from expansions in Florida and Washington State offset the discontinuation of three contracts at managed facilities in Texas. Operating margins were essentially level year-over-year, as operating expenses as a percentage of revenue grew slightly in Q1/2010 due to a greater reliance on International and GEOCare, offset by lower general & admin expenses as the Company was able to reduce these costs through cost-cutting measures implemented over the past 12 months. Combined with lower depreciation and amortization expenses, a reduced tax rate, and a slightly lower share count from stock repurchases, GEO was able to improve earnings per share in Q1/2010 over Q1/2009. Adjusted EBITDA rose a solid 14% year-over-year to \$35.6 million, or nearly \$0.50 per share.

2) GEO management also provided guidance for Q2/2010, very close to results achieved in Q1, including earnings per share of \$0.34-\$0.36 before a \$0.01 charge for start-up costs for the new facility in Florida, on revenues of \$280-\$285 million, including \$7 million in construction revenues. For the year, GEO management has guided to revenues of \$1.10 to \$1.12 billion (an increase of 5% year-over-year) and earnings per share of \$1.40-\$1.48, above last year’s earnings at least on the upper end of the range. For our estimates, we are trending toward the upper end of the range of guidance for both the second quarter and the full year 2010, at earnings per share of \$0.36 for Q2/2010 and \$1.45 for the year as a whole. Our estimates assume slightly improving operating margins and earnings per share as the year progresses,

**Current Price \$20.26**

**Price Target \$27.50**

Estimates	F2008A	F2009A	F2010E
<b>Sales(\$mil)</b>	<b>\$968.7</b>	<b>\$1,043.1</b>	<b>\$1,094.1</b>
1Q	232.9	246.1	273.1 A
2Q	250.1	250.0	275.0 E
3Q	240.6	257.0	268.5 E
4Q	245.1	290.1	277.5 E
Prev. Rev. Estimate (\$ mil.)			<b>\$1,095.0</b>

EPS	\$1.27	\$1.42	\$1.45
1Q	0.25	0.31	0.34 A
2Q	0.31	0.33	0.36 E
3Q	0.33	0.38	0.37 E
4Q	0.37	0.40	0.38 E
Previous EPS Estimate			<b>\$1.43</b>
P/E (x)	16.0	14.2	13.9

EBITDA/Share	\$2.95	\$3.44	\$3.54
EV/EBITDA (x)	10.2	8.8	8.5

Stock Data	
52-Week Range	\$15.45-\$23.18
Shares Outstanding (mil.)	49.2
Market Capitalization (mil.)	\$996.8
Enterprise Value (mil.)	\$1,484.2
Debt to Capital (3/10)	46.7%
Book Value/Share (3/10)	\$12.54
Price/Book	1.6 x
Average Trading Volume (10-Day)	769,000
Insider Ownership	14.2%
Institutional Ownership	83.7%
Short interest (Million shares)	2.3
Dividend / Yield	\$0.00/0.0%



Price target and ratings changes over the past 3 yrs:  
Initiated - January 2, 2010 - Buy -Price Target \$27.50

**Please find Important Disclosures beginning on Page 4.**

thanks to cost saving measures, share buybacks, and the opening late in the year of the new facility in the Florida panhandle. Our assumptions do not include any effect from the pending Cornell acquisition.

3) An uncertain economic and funding environment for corrections (among other areas) has allowed GEO Care to focus on finishing up existing expansions in Michigan and Colorado and a new build in Florida, as well as improving operating efficiencies in the US corrections market, both through paring less profitable contracts and through economy-driven cost-cutting initiatives. International and GEOCare divisions have picked up the slack growth-wise this year, however, and next year should see growth in the US through the pending consolidation with Cornell at the very least. Solid cash flow and share price uncertainty have also allowed the Company to step up their share repurchase program this year, and with more authorization available and a recent market correction, GEO may be able to buy back more this year, setting the stage for earnings per share growth especially in 2011.

## **Conclusion/Stock Valuation**

GEO shares bounced back this spring on investor enthusiasm over the pending Cornell acquisition, at least until recently. With a strengthened balance sheet, positive revenue growth and earnings, a pending positive acquisition, improving margins, and new openings and contracts, GEO has an enviable position in a growing industry, and current discount valuation multiples warrant a Buy rating and a 12-18 month price target of \$27.50, just 19X estimated 2010 earnings of \$1.45 per share.

## **Risk Factors**

GEO is reliant on funding from state governments, the US federal government, and other foreign governments to provide reimbursement for its prison facilities. Currently, several large US states including California and Florida are experiencing budget difficulties which could inhibit the growth of the Company's business, despite severe overcrowding for many states. In addition, GEO has experienced several cases where inmates or families of inmates sue the prison facility operator, and the increasing incidence of inmates being sent outside their home state has exacerbated this trend.

**The GEO Group, Inc.**  
**Consolidated Statements of Income**  
 (In 000s, except per share data)

Calendar Year	2004	2005	2006	2007	2008	1Q09	2Q09	3Q09	4Q09	2009	1Q10	2Q10E	3Q10E	4Q10E	2010E
Revenues	\$614,549	\$626,540	\$860,882	\$1,024,833	\$1,054,551	\$259,061	\$276,379	\$294,865	\$310,785	\$1,141,090	\$287,542	\$282,000	\$270,000	\$277,500	\$1,117,042
Pass-through revenues			74,139	109,600	85,834	13,010	26,384	37,869	20,722	97,985	14,451	7,000	1,500	0	22,951
Net revenues			\$786,743	\$915,233	\$968,717	246,051	249,995	256,996	290,063	\$1,043,105	273,091	275,000	268,500	277,500	\$1,094,091
Operating expenses	516,173	552,811	644,038	721,035	746,859	189,317	192,473	196,539	221,042	799,371	211,931	213,100	206,200	213,700	844,931
Depreciation & amortization	14,321	16,184	22,235	33,870	37,578	9,816	9,630	9,616	10,244	39,306	9,238	9,200	9,300	9,400	37,138
General & administrative expenses	45,879	48,958	56,268	64,491	69,151	17,236	17,015	15,685	19,304	69,240	17,448	17,900	18,000	18,600	71,948
Operating income (loss)	38,176	8,587	64,202	95,837	115,129	29,682	30,877	35,156	39,473	135,188	34,474	34,800	35,000	35,800	140,074
Interest and other expense, net	(12,873)	(13,841)	(17,665)	(29,765)	(18,098)	(5,836)	(4,676)	(4,405)	(12,326)	(27,243)	(5,995)	(6,200)	(5,900)	(5,600)	(23,695)
Income (loss) before tax	25,303	(5,254)	46,537	66,072	97,031	23,846	26,201	30,751	27,147	107,945	28,479	28,600	29,100	30,200	116,379
Income tax expense (benefit)	7,873	(11,614)	16,505	24,226	34,350	9,141	9,690	11,493	11,667	41,991	10,807	10,870	11,060	11,480	44,217
Net income (loss)	17,430	6,360	30,032	41,846	62,681	14,705	16,511	19,258	15,480	65,954	17,672	17,730	18,040	18,720	72,162
Basic income per share	\$1.24	\$0.22	\$0.87	\$0.88	\$1.24	\$0.29	\$0.33	\$0.38	\$0.30	\$1.30	\$0.35	\$0.36	\$0.37	\$0.39	\$1.47
Diluted income per share	\$1.19	\$0.21	\$0.84	\$0.85	\$1.21	\$0.28	\$0.32	\$0.37	\$0.30	\$1.27	\$0.34	\$0.35	\$0.37	\$0.38	\$1.44
Pro-Forma income per share			\$0.91	\$1.04	\$0.96	\$0.29	\$0.33	\$0.38	\$0.40	\$1.40	\$0.34	\$0.36	\$0.37	\$0.38	\$1.45
Pro-Forma EPS net of start-up/int'l			\$0.91	\$1.04	\$1.27	\$0.31	\$0.33	\$0.38	\$0.40	\$1.42	\$0.34	\$0.36	\$0.37	\$0.38	\$1.45
Basic shares outstanding	28,152	14,076	34,441	47,727	50,539	50,697	50,802	50,900	51,110	50,877	50,711	49,400	48,200	48,300	49,153
Diluted shares outstanding	29,214	14,607	35,744	49,175	51,774	51,723	51,835	51,950	52,164	51,918	51,640	50,300	49,200	49,300	50,110
Key ratios:															
Revenue growth	8.3%	2.0%	25.6%	16.3%	5.8%	5.7%	-0.1%	6.8%	18.3%	7.7%	11.0%	10.0%	4.5%	-4.3%	4.9%
Operating expenses/revenues	84.0%	88.2%	81.9%	78.8%	77.1%	76.9%	77.0%	76.5%	76.2%	76.6%	77.6%	77.5%	76.8%	77.0%	77.2%
G & A/ Revenues	7.5%	7.8%	7.2%	7.0%	7.1%	7.0%	6.8%	6.1%	6.7%	6.6%	6.4%	6.5%	6.7%	6.7%	6.6%
Tax Rate	31.1%	N/A	35.5%	36.7%	35.4%	39.9%	38.3%	39.0%	39.6%	38.9%	36.7%	38.0%	38.0%	38.0%	38.0%
Cash Flow/share	\$2.18	\$0.75	\$1.46	\$1.52	\$1.94	\$0.47	\$0.50	\$0.56	\$0.57	\$2.11	\$0.52	\$0.54	\$0.56	\$0.57	\$2.18
EBITDA/share	\$3.60	\$0.83	\$2.43	\$2.64	\$2.95	\$0.76	\$0.78	\$0.86	\$1.03	\$3.44	\$0.85	\$0.87	\$0.90	\$0.92	\$3.54

**Balance Sheets**

	(\$000s)	
Assets:	1/3/10	4/4/10
Cash and equivalents	\$33,856	\$30,276
Restricted cash	13,313	13,306
Accounts receivable, net	200,756	179,848
Other current assets	31,709	30,136
Total current	279,634	253,566
Property & equip., net	998,560	1,003,917
Restricted cash	20,755	23,300
Goodwill	57,669	57,179
Other	91,200	88,778
TOTAL ASSETS	1,447,818	1,426,740
Liabilities:		
Accounts payable	\$51,856	\$44,591
Accrued expenses	105,968	120,909
Other	19,624	19,990
Total current	177,448	185,490
Long-term debt	550,651	554,313
Other long-term liabilities	54,621	55,349
Shareholders' equity	665,098	631,588
TOTAL LIAB & EQ	1,447,818	1,426,740

**Quarterly Earnings Comparisons**

	March	June	Sept	Decem	Total
<b>Revenues (in \$Mill) (Before pass-throughs)</b>					
2000					\$535,557
2001					562,073
2002					517,162
2003	133,574	140,268	144,757	148,842	567,441
2004	146,058	150,308	152,035	166,148	614,549
2005	154,030	158,179	149,457	164,874	626,540
2006	184,778	191,152	200,409	210,404	786,743
2007	215,304	231,883	233,009	235,037	915,233
2008	232,868	250,139	240,620	245,090	968,717
2009	246,051	249,995	256,996	290,063	1,043,105
2010E	273,091	275,000	268,500	277,500	1,094,091
<b>Earnings per Share (Pro-forma)</b>					
2000					\$0.81
2001					0.91
2002					0.28
2003	0.13	0.16	1.51	0.18	0.78
2004	0.14	0.27	0.40	0.38	1.19
2005	0.09	0.15	0.01	(0.04)	0.21
2006	0.16	0.23	0.23	0.27	0.91
2007	0.22	0.26	0.29	0.27	1.04
2008	0.25	0.31	0.33	0.37	1.27
2009	0.31	0.33	0.38	0.40	1.42
2010E	0.34	0.36	0.37	0.38	1.45

Source: Dawson James Securities, Inc. estimates; Company documents

## Important Disclosures:

### Price Chart:



### Price target and ratings changes over the past 3 years:

Initiated – January 2, 2010 – Target \$27.50

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**Ratings definitions:** **1) Buy:** the stock is expected to appreciate and produce a total return of at least 20% over the next 12-18 months; **2) Neutral:** the stock is fairly valued for the next 12-18 months; and **3) Sell:** the stock is expected to decline at least 20% over the next 12-18 months and should be sold.

Ratings Distribution	Company Coverage		Investment Banking	
	# of Companies	% of Total	# of Companies	% of Totals
Buy	12	86%	6	50%
Neutral	2	14%	2	100%
Sell	0	0%	0	0%
Total	14	100%	8	57%

**Information about valuation methods and risks can be found in the “CONCLUSION/STOCK VALUATION” and “RISKS” sections of this report.**

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