Case 19: Chic Cosmetology University

By: Peter Manoogian (Kellogg Class of '12)

Case Question

- Our client is a for-profit, specialty college named Chic Cosmetology University (CCU). Founded in 2005, CCU is a program for high school graduates seeking their professional cosmetology license. CCU is currently the market leader for cosmetology education with campuses in ten major metropolitan areas in the US.
- *CCU has capital to invest in a new campus and is considering Chicagoland as a location – should they do it?*
- *(If interviewee asks about OTHER objectives or defining success for opening the new location):* The client considers a successful launch as achieving positive operating profit for the new campus two years after opening

7
Quants.
8
Structure

B/E
Mkt. Stgy
Mkt Share
Invest.

Case tracker

- **Industry:** Education
- **Level of Difficulty:** **Medium**
- **Case Format:** Opportunity Assessment
- **Concepts Tested:**
  - Break-Even Analysis
  - Marketing Strategy
  - Market Share
  - Investments

Fit Questions

Spend first 15 min on fit

- Tell me about a difficult or sensitive situation that required careful communication
- Describe a project or idea that was introduced or implemented because of your efforts

Guide to interviewer

- This case involves some number crunching but is more structurally focused. It is critical to ensure that the interviewee lands on the figures presented (or is course corrected toward them) in order to proceed with the later parts of the case.
- The interviewee should be able to develop a variant of the following question:
  Will CCU be able to enroll enough students to offset the initial investment and achieve positive profit?
- Key case steps:
  1. Evaluate CCU revenue and cost structures
  2. Project CCU's market share
  3. Estimate CCU Chicago enrollments
  4. Identify qualitative issues to consider

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Clarifying answers and case guide

Clarifying answers to provide

Client Characteristics

- Enrolled students take classes at a physical campus for one school year to earn degree (FY begins on 9/1)
- CCU boasts the best campuses in the industry with state of the art equipment
- Strong job placement due to CCU's relationships with top salons in local areas
- CCU and industry enrollments growing at 5% per year

Competitive Dynamics

- 2-3 other large specialty colleges, some of which are in the same geographies as CCU
- Community colleges beginning to offer cosmetology degrees at lower prices
- All ten CCU campuses have been present for at least three full school years
- All competitor campuses have also been present for similar lengths of time

Industry Characteristics/Economics

- H.S. Diploma and cosmetology degree required to enter the field
- 98% of cosmetologists are women

Guide to case / Guide to handouts

Share **Exhibit 1** with interviewee after probing questions are received about CCUs revenues and costs . Interviewee should be able to compute the following:

- Average revenue per enrollment = $15K (revenue / total enrollments)
- Total annual fixed cost per campus = $4.8M ($48M / 10)
- Total variable cost per student = $8K ($80M / 10K)
- Gross profit per student = $7K ($15K - $8K)

After that, the interviewee should begin to tackle the overall opportunity in the area as well as how many enrollments CCU could reasonably expect to obtain in year 1

Share **Exhibit 2** with interviewee after some of the qualitative aspects of CCU's targeting and marketing strategy are covered. Additionally, the interviewee should have asked about competitor information or made some attempt to assess what share of the market they should expect in Chicago.

- See "Market Share" section in next slide for further information on **Exhibit 2**

Key elements to analyze

Break-even analysis

- How many students will CCU need to break-even in year 1?

Notes to interviewer

- Interviewee should ask about the investment cost of building a new campus in Chicagoland
- After asking, tell interviewee that the total cost is $4.5M in initial building costs to renovate its chosen site. These costs can be amortized evenly over a three year period.
- Assume fixed costs remain flat per year

Interviewee should calculate

- Total fixed costs per year = $6.3M ($4.8M + $1.5M from amortization).
- Gross profit per student = $7K
- Break-even number of enrollments per year = 900 ($63M / $7K)

Marketing strategy

- What types of schools / students do you think CCU targets?

Notes to interviewer

Possible responses (schools):

-Public schools (private HS more likely to have grads go to 4yr univ)

-HS's in middle-class cities (may be an affordability issue w/lo income)

-Closest to the campus (geography)

Possible responses (students)

-Women HS graduates

-Not attending 4yr college

-Interested in cosmetology

After a few of the above criteria are noted, share:

- CCU has identified 1,000 targeted high schools in the Chicagoland area
- Within these HS, CCU's market research estimates that on average 6 students per HS have "potential" for CCU enrollment

Market share

- What is the highest share we could expect CCU Chicago to capture in Y1?

Notes to interviewer

- Show **Exhibit 2** to interviewee
- Interviewee should recognize:
  - Campuses w/competitors present tend to have a lower share (10%) than those w/out (15%)
  - However, presence of >1 competitor does not have an increased negative impact on market share (Boston has 8% share w/only one competitor)
  - Interviewee should assume a projected 10% market share for a Chicago campus (one competitor)
- **Also share the following :**
  80% of enrolled students directly from high school, the other 20% of students come from the "Adult" market

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Calculations

Math questions

1. What is the breakeven number of students required for CCU Chicago?
2. How many students should CCU Chicago expect to enroll in year 1, at the most?
3. (If time permits) = Suppose CCU finds a lot with a one time construction cost of $300K with the same amortization schedule. Should they enter Chicago now?

Calculations

1. **Break-even: (Estimated campus fixed cost + Yearly amortization) / gross profit per student**

   ($4.8M + $1.5M) / $7K = 900 students

2. **Students: Total potential students x maximum projected market share**

   Total potential students = Potential (HS) + Potential (Adult) = 7,500 students

   Potential (HS) = 6 / HS X 1,000 targeted HS = 6,000 students

   Potential (Adult) = 6,000 students * 25% = 1,500 students

   Total potential students (year 1) = 7,500 students x 10% share = 750 students

   Total potential students (year 2) = 750 students x 1.05 (growth) = 788 students

3. **Break-even: (Estimated campus fixed cost + new yearly amortization) / gross profit per student**

   ($4.8M + $0.1M) / $7K = 700 students

Solution and recommendations

Solution & Recommendations

- Overall, our client should NOT enter the Chicago market under the current cost structure. Even with a 10% market share assumption in year 1, the Chicago campus will enroll only 750 students, this is 150 fewer than the 900 required to break-even.
- The client should also consider several qualitative issues:
  - — Consider offering scholarships to increase the number of potential students and/or conversion rate of potential students
  - — Consider other cities beyond Chicagoland that currently do not have a CCU presence, or add a second campus to a city such as NYC that has high market share and potentially low capacity
  - — Perform market research in other cities to understand if there is a greater potential per target high school to increase ROI
  - — Consider ways to reduce fixed costs (*e.g.,* transporting equipment / materials from campuses that are not at capacity)

Bonus/Guide to an Excellent Case

- Excellent interviewees will recognize that the 10% market share is for campuses that have been in place for at least three years , therefore Chicago is unlikely to achieve that share in year 1 or 2; this rules out the feasibility of the follow-up question that suggests the possibility of reducing the one-time investment from $4.5M to $300K.
- Additionally, a strong interviewee will identify several of the qualitative issues listed above as ways in which CCU could proceed

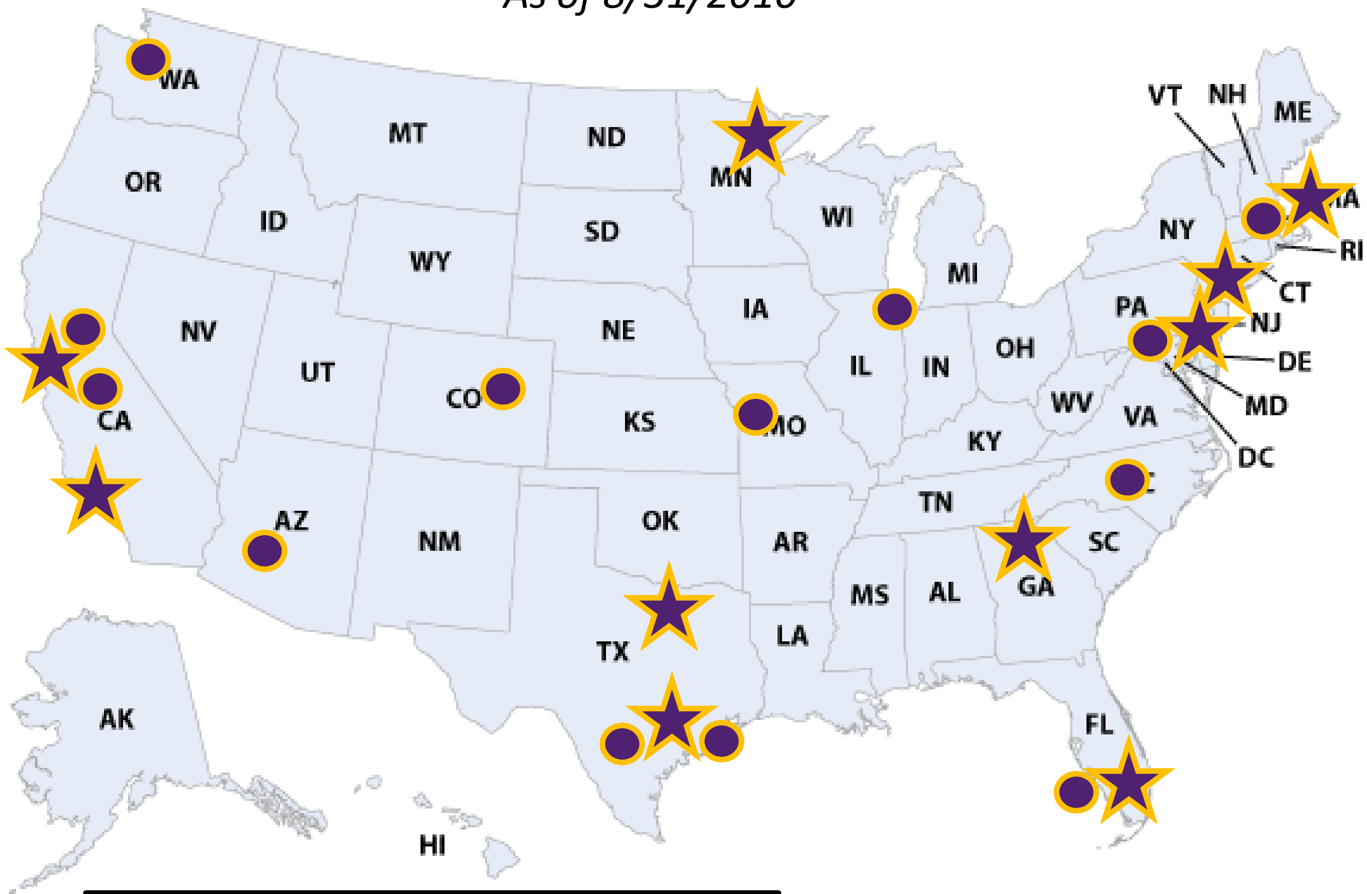
Exhibit 1: 2010 CCU Financials

CCU Financials as of 8/31/2010 ('000s)

Student enrollments (all campuses)	10
Revenue from enrollments	$150,000
Total fixed campus costs	$48,000
Buildings and equipment	$32,000
Recruiting, general, and administrative	$16,000
Total variable campus costs	$80,000
Instructors	$40,000
Student supplies	$40,000
Operating profit	$22,000

Exhibit 2: CCU and major competitor campus locations

As of 8/31/2010



★ **CCU Campus**

● **Major competitor campus**

Campus	2010 share*
San Fran	8%
LA	14%
Minneapolis	15%
Dallas	14%
Houston	10%
Atlanta	16%
Miami	12%
Philly	12%
New York City	16%
Boston	8%

* Measured as share of total “potential” students, as defined by CCU

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