

# Mossberg's Investor Digest

## Best Idea Profile

## The Geo Group, Inc. (NYSE: GEO)

### DESCRIPTION:

Headquartered in Boca Raton, Florida, The Geo Group is the nation's 2<sup>nd</sup> largest provider of government-outsourcing for correctional, detention and mental health services. The company also operates facilities in Canada, Australia, South Africa and the United Kingdom. The Geo Group manages 58 facilities totaling approximately 53,400 beds worldwide which have occupancy rates in excess of 94%. The company operates in 4 business segments; US (66% of revenue), International (13% of revenue), Geo Care (11% of revenue), which provides mental health and residential treatment services, and Construction (13% of revenue).

### KEY INVESTMENT CONSIDERATIONS:

#### Imbalance in demand and supply of prison beds

**Demand** – According to the Pew Charitable Trusts, state and federal prison populations are expected to grow by approximately 192,000 between 2007 and 2011, or approximately 38,000 per year. There are three factors driving demand for prison beds. **1) Crackdown on illegal immigration** – There are 11.8 million unauthorized immigrants in the U.S., up from 8.5 million in 2000. Within this population about ½ million are criminal aliens and another ½ million are non-criminals, who have been ordered for deportation, but are still living here. By comparison, there are only 100,000 beds allocated to house illegal aliens. **2) Overcrowded prisons** – The federal prison system operates at 135% of capacity and on average the state systems operate at 105% to 110%. To reduce occupancy to 100% of capacity would require 167,000 new beds. **3) Lengthening of mandatory sentences for certain crimes.**

**Supply** – Difficulties in credit markets combined with a tax base affected by weak economy and declining property values are likely to affect state, local and federal governments' ability to fund new projects. According to BofA, there are approximately 30,000 new beds coming online over the next two years. This won't meet the incremental demand of 38,000 new beds and is far less than the 167,000 needed to bring supply and demand into balance.

**Large untapped markets** – Private management represents approximately 8.35% of U.S. corrections marketplace. Therefore the U.S. alone represents a large untapped market. GEO's International expertise also gives GEO a platform to leverage its expertise on an international basis. As governments struggle with debt and needed capacity, private management provides a ready solution.

**Superior risk/reward profile** – Some of GEO's competitors have significant exposure to prisoners transferred out of state for budgetary or overcrowding concerns. In California, several legal proceedings have challenged the State's ability to send inmates out-of-state. Arizona has recently decided to pull some inmates back in state for internal budgetary reasons, though the state system is running at 113% of capacity. GEO does not have significant exposure to the temporary, out-of-state market, and has closely aligned its assets with long-term contracts inside the states it serves.

### VALUATION:

GEO has a proven and successful 22 year operating history. Management has achieved compound revenue and EBITDA growth rates of 8.6% and 32% over the last 4 years. With high occupancy rates (94%) and additional capacity on the horizon, GEO should continue to see the bottom line accelerate faster than the top line. With \$24 MM in cash, a recent refinancing and free cash flow of \$32MM, GEO has the financial strength to continue to develop new facilities. Shares of GEO and it's peers have recently seen a significant decline, likely due to concerns over developments that have cast doubt on the out-of-state corrections market. Even though GEO does not have significant exposure to this risk, GEO's shares have declined in sympathy with the group, which appears unjustified. Shares of GEO trade for 14x EPS, an attractive valuation for anyone seeking exposure to the correctional Industry.

### (NYSE: GEO)

Investment Data (as of 2/12/10)

<b>Recent Price</b>	<b>\$19.34</b>
52-Week Range	23.18 - 10.98
Fiscal Year End	December
Shares Outstanding	51 MM
Average Trading Volume (3 mos)	320,000
Market Capitalization	993 MM
Cash	24 MM
Long Term Debt	545 MM
Enterprise Value (EV)	1.5 B
LT Debt/ Equity	0.85
BV/ Share	13
TTM Revenue	1B
P/ Revenue	0.9x
2009 EPS (estimate)	1.41
P/ EPS	14x
TTM EBITDA (Adjusted)	176 MM
EV/ EBITDA	8.5x

We attempt to provide subscribers with reasoned opinions based on our analysis of publicly available information from sources believed to be reliable, but make no representations as to its accuracy or completeness. Best Idea profiles are not based upon individual needs of subscribers nor are they an offer to buy or sell securities. Additional disclosures can be found under the Disclosures portion of the Mossberg's Investor Digest website.