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A Strategic Audit of Chegg

An undergraduate Honors Thesis Submitted in Partial fulfillment of University Honors Program Requirements
University of Nebraska-Lincoln

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Abstract

The paper researches and discusses the strategy of Chegg in the past and future with regards to what was taught in UNL’s MNGT 495H course. The data was compiled from online resources including the company’s website and financials along with insights learned during an internship and interviews done in the Summer of 2016 and Spring of 2018.

The insights of how Chegg went from a textbook rental company to the student learning hub it is today include experienced leaders, acquisitions and mergers, and being ahead of the curve in the industry. The final recommendation for Chegg’s strategy is to widen its market to actuarial science exam takers as part of the general test prep solution.

Key Words: Chegg, Computer Science, Economics, Strategy, Audit
Appreciation

I would first like to thank my family for the support throughout my academic career, for always pushing me to be my best and helping me succeed in everything I put my mind to. A special thank you to my grandpa Gene Bentley for helping set up my academic foundation and being there whenever I needed you, I wish you could be here with me to celebrate.

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A Strategic Audit of Chegg

Chegg was started in 2005 at Iowa State University by 3 partners and an investor, while the predecessor to Chegg was Cheggpost.com which began in 2001. Chegg’s name is a portmanteau of the words ‘Chicken’ and ‘Egg’ with the names origin being a story of how it costs money to buy textbooks, which you need to graduate college, to earn money, a ‘Chicken or the Egg’ dilemma (Helft).

Chegg currently has approximately 700 employees with its current HQ is in Santa Clara, but also having offices in San Francisco, New York City, Israel, Germany and Ukraine. Chegg’s services currently reach 10 million unique visitors yearly along with having a revenue of $186 million in the last fiscal year (2016 Annual Report).

Background and issues

Chegg is the leading online student resource website that specializes in books, test prep, and homework help.

Its products are considered to be split into two groups, Required Materials and Chegg Services. Chegg Services include Chegg Study, Chegg Tutors, Test Prep and Chegg Writing Tools.

The required materials division covers the sale of physical and e-books. Chegg has recently partnered with Ingram Content Group so that it doesn’t deal with the physical storing and delivering of the books. Chegg has a native e-book reader that can be used to read the books.
purchased. The Required Materials market is almost solely college for the United States, as high schools provide books for the students unlike colleges where the students have to buy for their own books.

Chegg Services reached an annual revenue of $129 million in the Fiscal Year 2017 (2016 Annual Report). It also reached its record number of users with 1.5 million users at the end of FY ‘17.

Test Prep covers both high school and grad school test preps and has recently partnered with Kaplan. High school test prep covers the ACT, SAT and AP exams. The AP exams they cover are Calculus AB, U.S. History, World History and Biology. The graduate tests offered the GRE and GMAT, standard tests required for grad schools no matter your major, and specific ones. The specific ones are the LSAT, for law school, MCAT, for medical school, and the NCELX exams for nursing.

Study includes both Chegg Tutors and homework solutions and Q&A. Chegg Tutors is a service that pairs students who need help with tutors who are knowledgeable in that area with either text or video tutoring sessions through the platform. Chegg Tutors has primarily been focused towards the college market for both logistics and financial reasons. Financially college students are more willing to pay $15-20 an hour for tutoring than high schoolers. Also, there is more standardization across subjects or courses in college than in high school, where a student tutoring in Intro to Microeconomics to a college student will have a better sense of what will be covered and at what level than teaching Economics to a High Schooler.
Chegg Writing Tools is a new division with the acquisition of Imagine Easy Solutions, the company behind commonly used bibliography for $42 million in 2015. Imagine Easy’s tools include EasyBib, BibMe, Citation Machine and Cite This For Me (Lardinois).

Chegg has gone through three different mission statements, they all have the same goal in mind but built onto each other. Its first until approximately 2012 was “Chegg puts students first” in which point it changed to “save time, save money and get smarter” until 2016 where it currently is “Leading student-first connected learning platform to save student outcomes” (Jackson).

Financials

Financially Chegg had its IPO in November 2013 at an evaluation of $1.1 that raised $187.5 million (Merced). This was the first tech IPO after Twitter’s which according to investors led to a wary opening with the opening stock price being $11 but closing the week at $9, an 18% decline. Chegg’s stock price had stayed course since its opening before gradually increasing in April 2017 and reaching its current price of $22, twice the original opening price (“CHEGG: Summary for Chegg, Inc.”). Chegg has also finished another round of funding in the beginning months of 2018.

With regards to the business costs, there are three main costs for Chegg: textbooks, services, and employees. Textbooks are a very capital-intensive product, the costs that go into it are buying the book, storing the book, and the shipping and handling to send to the consumer. It was internally calculated that the average textbook needed to be rented out three times before a profit could be made on the book. This was both a significant upfront cost and risk, as the
book has to be paid for in full before being rented out, and the demand for the book had to maintain or else the book’s price would drop and take longer for a profit to be made.

Services for Chegg include Chegg Tutor and Chegg Study. These two are grouped together because the costs are outside of Chegg through contractors, instead of normal employees. People can apply to be tutors for Chegg, although they are considered contractors and do not get benefits. Chegg will likely make a profit on average for every tutoring session, as tutors are only paid per session instead of hourly, and the cost of the tutor will be lower than the price to the consumer. The only promotions usually done are a free tutoring session for the first time. For Chegg Study, questions are answered by the users for free in an open forum for help. The cost is with regards to the solution guides, as they are a mix of solution guides from the publishers and solutions done by an outsourced team. The solution guides from the publishers likely come at a little cost, while the solutions done by the team abroad is higher as it is hourly, and it are done by people who have to understand the subject material.

The third major cost component for Chegg is the employees. The employees can be split up into two main divisions, product development and marketing. Product development is made up of product managers, designers, researchers and engineers. There is a cost for researchers to pay incentives for users to come in for their time, with this knowledge the researchers work together to think of new products which the designers draw out and the engineers build. The costs for product development are both fixed and variable, if no new features were to be built out, there would still be a cost incurred for the upkeep. The marketing team is made up of sales
and marketing. These employees’ jobs are to get more customers to the website through emails, marketing events or SEO.

Current Situation

This section will discuss an analysis of Chegg’s current situation internally and the industry at large.

Competitors

Due to Chegg being in many different markets with its products, it is important to see what competition it is facing. In the textbook industry, the main competition sources are other bookstores and online stores in the large market, and individuals in the small market. In the large market the two main competitors are Amazon.com and BarnesandNoble.com, while in the small market it is individual students selling to other students. In the tutoring market the competition is from both local tutors and large corporations that provide tutoring, although one differentiator is location, as those tutoring providers are often in person while Chegg’s tutoring is online at any time. Test prep’s market is split into two, high school test prep and graduate/professional test prep. In high school test prep, there are companies who write manuals to help students learn along with companies who provide in person lectures to help, both local and regional. With graduate/professional test prep, most of the competition has manuals that can be used along with online paid resources that help you learn at your own pace.

Goals
Chegg’s currently has two main goals: increase brand awareness and increase revenue within Chegg Services. Increasing brand awareness is needed to help grow the original market and make Chegg a household name for every college student and hopefully high school and younger. Increasing the revenue of Chegg Services is a business goal as Chegg expects more revenue coming from Services compared to Required Materials and is basing the goals off of the Services category. Brand awareness and Services revenue go hand in hand, brand awareness increases the top of the funnel, which is how many people know about Chegg, which should in turn increase revenue as more people decide to use the website, the bottom of the funnel.

Increasing brand awareness is difficult to evaluate criteria concretely on, the total number of subscribers and the total number of unique visitors are both accurate proxies. The total number of subscribers tells how many people have signed up for any service, while the total number of visitors can show the potential interest. For the FY 2017, the subscribers were 2.2 million while the unique visitors were 10 million (“Q4-17 And FY 17 Investor Presentation”).

Revenue is easier to estimate, as it is a financial number. For the FY 2017, Chegg Services had a revenue of $186 million. With an estimated FY 2018 revenue of $242 million, a 30% YoY increase (“Q4-17 And FY 17 Investor Presentation”).

Strengths

One of Chegg’s main strengths is the company’s ability to acquire companies and successfully work them into its brand. The majority of the products at Chegg have been acquired and grown as it started just as the textbook company, the division now known as required materials.
Chegg’s partnership with Ingram has allowed it to worry less about the logistics of textbooks and put more money and time into new products. Chegg has gradually moved more of the textbook logistics to Ingram with Ingram now being in charge of 100% of the physical textbooks to allow Chegg to focus on digital rentals.

The C-level staff and directors are also a large asset for the company, as it brought in an experienced staff when the first round of private funding went through. This includes bringing in a CPO, Chuck Geiger, who had experience at Expedia, Ebay and Paypal along with a CEO, Dan Rosensweig, who had experience at GuitarHero, Yahoo!, and CNET (2016 Annual Report). This experience has also assisted in the acquisitions and mergers as both companies they headed had prior experience.

Externally one of Chegg’s strengths and opportunities is both the growing textbook market and the growing rental market. With textbook prices increasingly rising, the market for rentals has also increased, as it decreases the upfront cost and risk to the user. This trend continues with the rise of e-books which have a higher profit margin, and less cost in general as there is no need to physically store an e-book, access to the e-book is revoked when the paid period is done, and they can be updated much quicker than a physical textbook can be.

Weaknesses

Competition within each product is both a weakness and threat to Chegg depending on the category. With textbooks, the bargaining power of the buyer is significant. If Amazon sells a book for $2 cheaper, it is very likely that the consumer will buy from Amazon instead, this low switching cost drives the chance of profits from books down. Also, with textbooks the
bargaining price of the suppliers is significant, with publishing companies partially able to dictate how much e-books can go for as they are the sole owner of them and there is no after-market as there is with physical textbooks (Helft).

**Strategic Recommendation**

This section will discuss the strategic recommendation, which goals it will complete and how to measure it, any alternatives and how to implement it.

**Initial Recommendation**

Looking forward, Chegg should branch out and focus on a new market to supplement its current strategy, actuarial scientists. The actuarial science market is a niche market, but with actuarial scientists needing five preliminary exams in their field, the market exists for that test prep. This will not only increase brand awareness within this market, it will also be able to be another revenue source for the company.

The actuarial science market is currently underserved with how important it is compared to other graduate professions, this is partially due to the size of the market. When students are taking their MCATs, the pressure is on and they study for weeks, actuarial scientists have to do almost the same thing at least 5 times in their career. The difference between passing and failing a preliminary exam may be the difference between getting an internship over the summer or a level of the starting salary for a new grad. There are also many cases where school programs will pay for the test fee if it is passed, creating a large incentive to pass financially. For this reason, it is not unusual for potential test takers to pay over $200 for study materials
before the test, with some online programs costing between $175 and $400 for a review of one test (“P Pricing”).

Implementation: Actuarial Scientists

This implementation would require some research on understanding what can differentiate Chegg’s new product compared to the other ones already out there and would skip the original phases of researching the industry as a whole.

Chegg likely could put this new market under the same test prep team as before but add more people as the amount of tests that would be covered would increase. With the test platform reasonably being already built out, the only new addition would be building the actual questions and any other additions that actuarial scientists need that isn’t already available through the general tests. This would require a group to write questions for the tests and keep up to date, which would likely be done through a partnership or contracting work, as few if any current Chegg employees have taken these exams.

This implementation should take under six months to go into a private beta program, with full roll out with at least one actuarial science exam within a year, with more to come. It should cost under a million dollars, with some of this original money being the partnership mentioned earlier, that is a more upfront cost than continual.

With the example of the ‘P’ exam, there are 6 exams each year, with approximately 2,500 exam takers each test giving an approximate total market of 15,000 (“Edu-Exam-Results-Detail”). If Chegg sold their product at $200, which was the lower average of comparable products, and
retained the same 5% attainable market percentage the revenue would be $150,000. While this seems low compared to the $1 million first cost, this is only for one test in the first year. After the first year of the product, there will no longer need to be development or research work on the product and the only work needed will be addition contracting at a lower price.

For year 2 estimates with adding in another test, the projected revenue would increase to $300,000 if assuming the same market percentage. These numbers are not large compared to the overall Chegg Services revenue, but as the product grows and gains more of the market, it can slowly become a larger and larger part as well as be a consistent revenue stream. The current total projected market for this product would be $15,000,000 for the five preliminary tests.

To be successful, this recommendation would need to contribute to both of Chegg’s goals. With regards to brand awareness, increasing the products given would bring a new market into the Chegg universe. It must be said though that it is likely that these students may already know about Chegg as they are in college, but it will bring more recognition and awareness regardless. With regards to revenue, this will easily increase revenue as it will be a profit that makes money. The increase to revenue will be relatively small in comparison to the overall revenue but the key is to think about with profit. This product will be a low-cost solution that should be able to bring in 6x profits to cost after the first year. This profit growth also increases as the cost is fixed while the profits would not be.
Alternatives

In order to attack the younger market, specifically middle schoolers and underclassmen in high school, Chegg could build a platform that rivals Turnitin.com so that teachers and students become aware of Chegg early on. This could potentially also be paired with IES’s products to check citations creating a better all-around product.

An alternative for attacking the younger market is to key in on the home-schooled demographic, as this is another niche market that can be won. This would allow for potentially all the materials used in the family be from Chegg, along with tutoring and test prep.

Another alternative with regards to capturing a niche graduate market, is to focus on prep for qualifying exams for various graduate programs. While these aren’t standardized tests, it is likely that many math programs, for example, have similar questions or subjects.

Conclusion

Chegg has journeyed from selling and renting textbooks out of college student’s dorms to becoming a one-shop-stop for students needs through a strategy of forward thinking and brilliant acquisitions. The company is currently set up to go into any new market with the same success it has before, with the proper research and knowledge from the CEO down. For this reason, Chegg should consider moving into the Actuarial Science Exam prep market, as it can add to the test prep infrastructure currently in place, quickly and cost effective. This movement into the market can bring in consistent revenue and increase as it adds more exams and more users to prep for.
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