

China East Education (667 HK)

Fundamentals remain intact despite 1H20E profit affected by COVID-19

The Company expected 1H20E adj. NP to drop by 45-50% as new student enrollment was affected due to outbreak of COVID-19. That said, we think the fundamentals of the Company remains intact. The new beauty school performs better than management's expectation. This segment could be a new growth driver and serve as re-rating catalyst. Our TP is adjusted from HK\$15.80 to HK\$21.10, 31.7x FY21E P/E (at 15% discount to education sub-sector leaders' average of 37.3x). Maintain Buy.

- Profit alert.** Due to outbreak of COVID-19, schools were suspended temporarily and number of new student enrollments fell by around 20%, which caused revenue to decline by 15-20% in 1H20E. The Company expects 1H20E NP and adj. NP to fall by 20-25% and 45-50%, respectively.
- Recovering notably since end of Zhongkao.** Percentage of schools reopened increased from 50% in end of May to 90% in end of June and >90% currently. On the other hand, certain schools in Beijing, Xinjiang and Northeastern China are still affected by COVID-19. However, since the end of Zhongkao in mid-July, number of new student enrollments has been picking up notably.
- Ramp-up of new beauty school better-than-expected.** The beauty training school opened in Chengdu has around 300 students. Because Jul-Sep is the biggest new student enrollment in a year, number of students of the schools could exceed target of 400-500 students in FY20E. The Company plans to open two new beauty training schools in Zhengzhou and Changsha in 2H20E. If the ramp-up of these two schools are strong, the Company could accelerate beauty training expansion. The beauty services industry is fragmented. Some large beauty services operators provide in-house training for its staff. Competitors mainly offer short-term courses which cannot control graduates' quality well. There is opportunity for the Company to provide quality training through long-term courses to meet the industry's demand for talents.
- Maintain Buy.** We revised down FY20/21/22E adj. NP by 9%/3%/4% to factor in lower student enrollments. Our TP is revised from HK\$15.80 to HK\$21.10, based on 31.7x FY21E adj. P/E which is at 15% discount to education sub-sector leaders' average of 37.3x (vs 26x average FY20E and FY21E adj. EPS previously). We forecast the Company to post 25% adj. EPS CAGR in FY20-22E. **Catalyst:** M&A. **Risk:** lower-than-expected student enrollment.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenues (RMB mn)	3,265	3,905	4,074	5,085	5,773
Net profit (RMB mn)	515	848	879	1,248	1,504
Adj. net profit (RMB mn)	547	900	959	1,308	1,504
Adj. EPS (RMB)	0.314	0.411	0.438	0.597	0.686
YoY change (%)	na	30.9	6.6	36.4	15.0
Consensus EPS (RMB)	na	na	0.473	0.575	0.690
Adj. P/E (x)	na	39.1	37.3	27.4	23.8
Ex-net cash adj. P/E (x)	na	32.1	30.5	21.8	18.3
P/B (x)	na	5.7	5.4	4.6	4.0
Yield (%)	na	1.2	0.7	1.0	1.3
Adj. ROAE (%)	44.1	25.7	15.0	18.2	18.2
Net cash (RMB mn)	6242	6536	6536	7323	8242

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price	HK\$21.10
(Previous TP)	HK\$15.80
Up/Downside	+16%
Current Price	HK\$18.20

China Education Sector

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Stock Data

Mkt Cap (HK\$ mn)	39,897
Avg 3 mths t/o (HK\$ mn)	70.81
52w High/Low (HK\$)	20.30/ 10.62
Total Issued Shares (mn)	2,190.9

Source: Bloomberg

Shareholding Structure

Wu Junbao	34.13%
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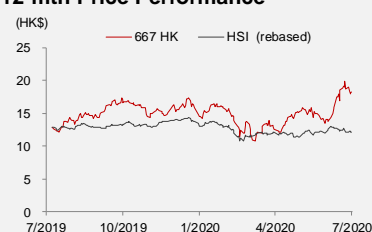
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	30.0%	32.8%
3-mth	45.4%	45.7%
6-mth	25.2%	33.9%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Deloitte

Related Reports

- "China East Education – Earnings cut could be priced in" – 2 Apr 2020
- "China East Education – The leading vocational training education provider" – 27 Aug 2019

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Figure 1: Changes of our estimates

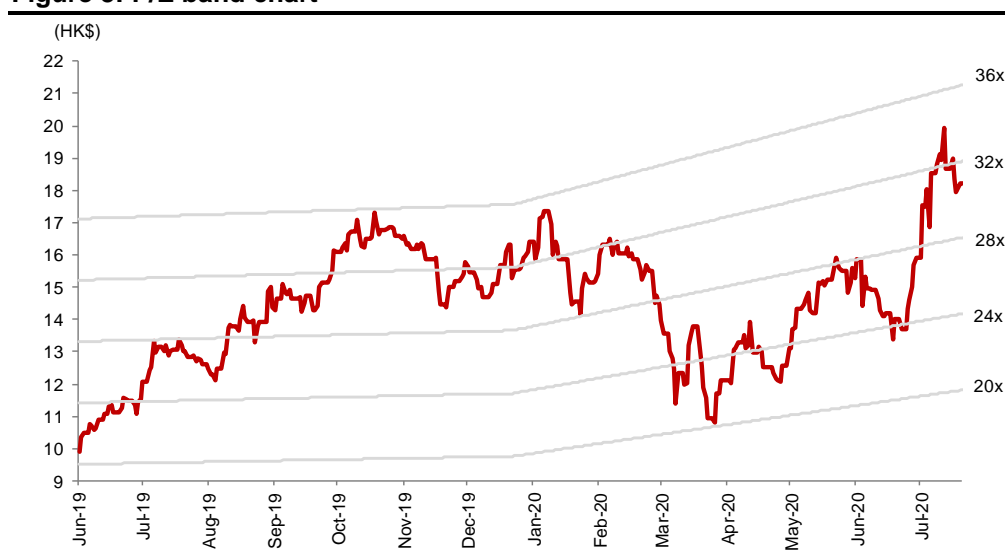
US\$ mn	CMBIS			Consensus			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	4,074	5,085	5,773	4,372	5,183	5,882	-6.8%	-1.9%	-1.9%
Gross Profit	2,395	3,084	3,545	2,603	3,166	3,635	-8.0%	-2.6%	-2.5%
EBIT Profit	1,095	1,552	1,861	1,223	1,601	1,932	-10.5%	-3.0%	-3.7%
Net profit	959	1,308	1,504	1,052	1,343	1,563	-8.9%	-2.6%	-3.8%
Gross Margin	58.8%	60.6%	61.4%	59.5%	61.1%	61.8%	-0.7ppt	-0.5ppt	-0.4ppt
EBIT Margin	26.9%	30.5%	32.2%	28.0%	30.9%	32.9%	-1.1ppt	-0.4ppt	-0.7ppt
Net Margin	23.5%	25.7%	26.0%	24.1%	25.9%	26.6%	-0.6ppt	-0.2ppt	-0.6ppt

Source: Company data, CMBIS estimates

Figure 2: CMBIS estimates vs consensus

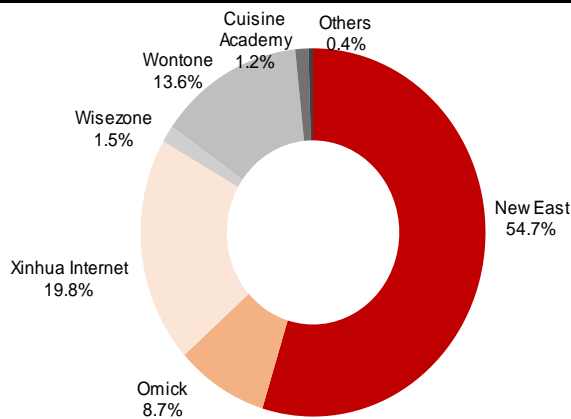
US\$ mn	CMBIS			Consensus			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	4,074	5,085	5,773	4,385	5,305	6,328	-7%	-4%	-9%
Gross Profit	2,395	3,084	3,545	2,545	3,143	3,794	-6%	-2%	-7%
EBIT Profit	1,095	1,552	1,861	1,261	1,572	2,041	-13%	-1%	-9%
Net profit	959	1,308	1,504	1,033	1,277	1,544	-7%	2%	-3%
Gross Margin	58.8%	60.6%	61.4%	58.1%	59.3%	60.0%	+0.7ppt	+1.3ppt	+1.4ppt
EBIT Margin	26.9%	30.5%	32.2%	28.8%	29.6%	32.3%	-1.9ppt	+0.9ppt	-0.1ppt
Net Margin	23.5%	25.7%	26.0%	23.6%	24.1%	24.4%	-0.1ppt	+1.6ppt	+1.6ppt

Source: Company data, CMBIS estimates

Figure 3: P/E band chart

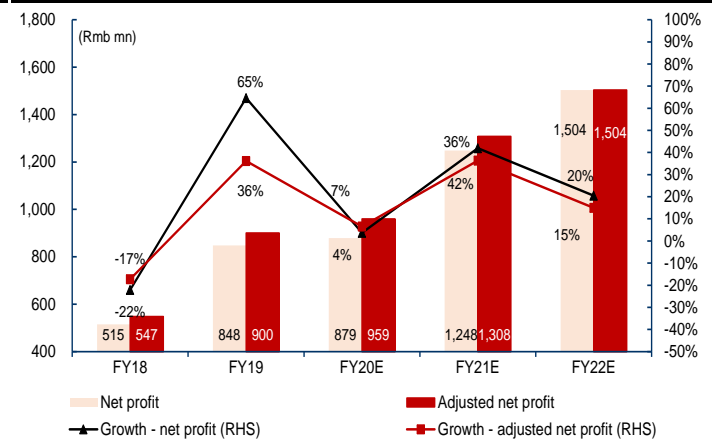
Source: Company data, Bloomberg, CMBIS estimates

Figure 4: Revenue breakdown by brand in FY19



Source: Company data

Figure 5: Adj. NP to grow at 25% CAGR in FY20-22E



Source: Company data, CMBIS estimates

Figure 6: Peers valuation table

Company	Ticker	Rating	Mkt Cap (US\$ m)	Crncy	Price	TP	Year end	P/E (x)			Adj. net profit growth (%)			Adj. EPS growth (%)			PEG (x)			Revenue growth (%)		
								FY1	FY2	FY3	FY1	FY2	FY3	FY1	FY2	FY3	FY1	FY2	FY3	FY1	FY2	FY3
K12 tutoring services providers																						
New Oriental Education	EDU US	NR	22,212	USD	140.20	na	May-20	37.2	27.1	20.7	23	38	33	23	37	31	1.10	18	31	29		
TAL Education	TAL US	NR	46,928	USD	78.17	na	Feb-20	94.6	54.0	37.0	205	81	49	8,160	75	46	1.58	34	42	36		
Onesmart Education	ONE US	NR	609	USD	3.75	na	Aug-19	na	11.6	8.2	(108)	(2,040)	43	(231)	na	41	na	(13)	51	18		
Scholar Education	1769 HK	NR	1,139	HKD	15.88	na	Dec-19	49.8	37.9	27.9	71	36	37	51	31	36	1.48	27	37	37		
Beststudy Education	3978 HK	Buy	334	HKD	3.05	5.14	Dec-19	14.6	8.6	6.9	(4)	69	24	(4)	69	24	0.32	12	30	22		
Average								49.1	27.9	20.1	38	-363	37	1,600	53	36	1.12	16	38	28		
Non-formal vocational education services provider																						
China East Education	667 HK	Buy	5,148	HKD	18.20	21.10	Dec-19	37.3	27.4	23.8	7	36	15	7	36	15	1.48	4	25	14		
K12 education services providers																						
Tianli Education	1773 HK	NR	2,169	HKD	8.10	na	Dec-19	42.9	33.6	26.5	31	25	33	35	28	27	1.58	29	25	46		
Maple Leaf	1317 HK	NR	1,036	HKD	2.68	na	Aug-19	11.4	9.6	8.5	(8)	19	16	(4)	19	12	0.73	5	26	12		
Bright Scholar	BEDU US	NR	863	USD	7.18	na	Aug-19	18.4	12.8	11.1	33	40	24	5	44	15	0.64	33	23	11		
Virscend Education	1565 HK	NR	1,144	HKD	2.87	na	Dec-19	19.9	15.7	12.6	2	28	22	0	27	24	1.57	16	26	17		
Wisdom Education	6068 HK	Buy	1,162	HKD	4.40	6.38	Aug-19	17.4	12.7	10.3	29	37	23	32	37	23	0.59	7	32	20		
Average								22.0	16.9	13.8	18	30	23	14	31	20	1.02	18	26	21		
Higher Education services providers																						
China Education	839 HK	NR	3,832	HKD	14.70	na	Aug-19	29.1	24.1	20.0	29	22	20	23	21	20	1.41	36	15	14		
Yuhua Education	6169 HK	NR	3,228	HKD	7.49	na	Aug-19	27.5	18.5	16.1	22	30	14	0	49	15	0.90	45	12	8		
Hope Education	1765 HK	Buy	2,266	HKD	2.60	3.19	Aug-19	26.6	19.3	15.1	na	38	28	na	38	28	0.81	na	39	27		
Kepei Education	1890 HK	NR	1,536	HKD	5.95	na	Dec-19	17.7	14.5	12.6	32	22	17	32	23	15	0.95	29	25	15		
New Higher Education	2001 HK	NR	1,068	HKD	5.37	na	Dec-19	14.3	11.7	10.0	34	22	18	32	22	17	0.73	26	17	14		
Edvantage	382 HK	NR	795	HKD	6.05	na	Aug-19	18.2	14.2	11.6	27	27	23	(1)	28	23	0.71	16	17	20		
Minsheng Education	1569 HK	NR	588	HKD	1.08	na	Dec-19	9.0	7.7	6.9	10	17	13	10	18	11	0.63	19	14	12		
Xinhua Education	2779 HK	Buy	515	HKD	2.48	2.85	Dec-19	11.2	10.0	9.2	8	11	9	8	11	9	1.11	14	11	9		
Huali University	1756 HK	NR	477	HKD	3.08	na	Aug-19	10.9	8.7	6.9	20	30	25	21	25	25	0.43	18	18	18		
Average								18.3	14.3	12.0	23	24	19	16	26	18	0.85	26	19	15		
Education sector average								26.7	19.0	15.1	24	(71)	24	432	34	23	0.99	20	26	20		

Source: Bloomberg estimates, CMBIS estimates

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	3,265	3,905	4,074	5,085	5,773
Cost of sales	(1,560)	(1,625)	(1,679)	(2,001)	(2,228)
Gross profit	1,705	2,280	2,395	3,084	3,545
Other income	38	45	44	51	54
Other gains and losses	58	131	45	45	45
Selling expenses	(648)	(698)	(786)	(976)	(1,114)
Administrative expenses	(438)	(576)	(571)	(610)	(623)
R&D expenses	(28)	(31)	(33)	(41)	(46)
EBIT	687	1,151	1,095	1,552	1,861
Net finance income	24	(60)	14	21	35
Listing expenses	(24)	(22)	0	0	0
Profit before tax	687	1,070	1,109	1,574	1,896
Income tax expenses	(172)	(222)	(229)	(326)	(393)
Net profit	515	848	879	1,248	1,504
Net profit	515	848	879	1,248	1,504
Net forex loss	0	(85)	0	0	0
Listing expenses	24	22	0	0	0
Share-based expenses	8	116	80	60	0
Adjusted net profit	547	900	959	1,308	1,504

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before tax	682	1,070	1,109	1,574	1,896
D&A	360	543	525	543	565
Change in working capital	182	108	213	186	211
Others	(245)	(124)	(375)	(494)	(635)
Net cash from operating	980	1,596	1,472	1,808	2,037
Capex	(666)	(371)	(750)	(750)	(750)
Others	93	(2,265)	201	208	222
Net cash from investing	(573)	(2,637)	(549)	(542)	(528)
Equity raised	1	4,289	0	0	0
Dividend paid	(874)	(34)	(413)	(264)	(374)
Change of borrowings	0	0	0	0	0
Others	(582)	(347)	(216)	(216)	(216)
Net cash from financing	(1,456)	3,908	(629)	(480)	(590)
Net change in cash	296	2,868	294	787	919
Cash at the beginning of the year	1,739	986	3,883	4,177	4,964
Exchange difference	0	29	0	0	0
Cash at the end of the year	2,035	3,883	4,177	4,964	5,883

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	3,066	3,180	3,899	4,518	5,115
PPE	1,361	1,406	1,896	2,399	2,897
Right-of-use assets	1,675	1,712	1,936	2,048	2,143
Prepayments for rental	0	24	27	30	33
Others	30	38	39	41	42
Current assets	1,165	6,498	6,803	7,652	8,614
Cash	986	3,883	4,177	4,964	5,883
Time deposits	0	1,892	1,892	1,892	1,892
Receivables	140	203	212	265	300
Others	39	520	522	532	539
Current liabilities	2,031	2,272	2,527	2,835	3,137
Contract liabilities	1,233	1,383	1,549	1,766	1,978
Payables	478	443	482	538	593
Tax payables	108	138	138	138	138
Lease liabilities	178	307	358	393	428
Others	34	0	0	0	0
Non-current liabilities	1,327	1,285	1,507	1,624	1,752
Lease liabilities	1,267	1,207	1,405	1,542	1,679
Others	60	79	102	82	73
Total net assets	873	6,120	6,667	7,711	8,840
Shareholders' equity	873	6,120	6,667	7,711	8,840

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
New East	58.2	54.7	52.1	50.1	48.6
Omick	6.5	8.7	10.0	11.4	12.6
Xinhua Internet	18.5	19.8	20.1	20.8	20.9
Wisezone	2.2	3.2	1.4	1.2	1.1
Wontone	13.6	13.6	14.4	14.4	14.4
Cuisine Academy	0.6	1.2	1.4	1.6	1.7
Others	0.4	0.4	0.5	0.5	0.6
P&L ratios (%)					
Gross profit margin	52.2	58.4	58.8	60.6	61.4
EBIT margin	21.0	29.5	26.9	30.5	32.2
Effective tax rate	25.0	20.7	20.7	20.7	20.7
Net profit margin	15.8	21.7	21.6	24.5	26.0
Adj. net profit margin	16.8	23.0	23.5	25.7	26.0
Payout ratio	na	48.7	30.0	30.0	30.0
Balance sheet ratios					
Current ratio (x)	0.7	0.5	2.7	2.7	2.7
Average inv. turnover days	7.8	10.0	11.4	10.7	11.0
Asset turnover (x)	1.2	0.9	0.4	0.4	0.4
Total asset/total equity (x)	3.2	0.7	1.6	1.6	1.6
Net cash (RMB mn)	986	6,242	6,536	7,323	8,242
Returns (%)					
Adjusted ROAE	44.1	25.7	15.0	18.2	18.2
Adjusted ROAA	17.3	25.5	12.8	11.4	11.6

Source: Company data, CMBIS estimates

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