

# Hope Education (1765 HK)

## Strong organic growth outlook

Adj. NP +61% to RMB576mn, in line with our estimates, within guidance of RMB550-600mn and 5% below consensus. The 39% total student enrollment growth and strong enrollments for overseas programs in FY21E again showed the Company's strong execution skills in improving performance of acquisition targets. We forecast the Company to deliver 25.4% EPS CAGR in FY21-23E, above peers' average of 22%. We estimate conversion of four independent colleges could further lift FY23E NP by 19%. Maintain Buy and lifted TP to HK\$3.41.

- **Results in line.** Revenue jumped 45% to RMB1,568mn, led by 63% growth of student enrollment to 140,125, in line with our estimates and 5% below consensus. Adj. GPM widened 5.4ppt to 52.4% thanks to better scale and cost control. SG&A expenses ratio reduced by 3.3ppt to 16.4%. The Company declared a RMB0.8 cents dividend for the 8M20 period. Payout ratio will be kept at 30% in future.
- **Strong overseas study demand to drive Inti Education's growth.** The Company saw enrollments for its overseas programs (including Intl. Education and other programs) soared from 1,964 in FY19 to 17,315 in FY20. These enrollments will gradually become overseas students in 2-3 years. Management targets to achieve 40% net profit CAGR from 2018 to 2024E for Intl. Education.
- **Conversion of four independent colleges to lift earnings.** In FY20, total management fees paid by the independent colleges was RMB170m, representing 29% of adj. NP in FY20. Management expects to convert two independent colleges by end of 2021 and another two by end of 2022. We estimate these conversion could further lift FY23E NP by 19%.
- **Strong organic and M&A growth drivers.** Total student enrollment jumped 39% to 194,554 in FY21E. The Company acquired a vocational college in Nanchang (2,753 students) in Oct and plans to open two vocational colleges each in FY22E and FY23E. On organic basis, management targets to achieve 15-20% revenue CAGR and a faster NP CAGR, in 3-5 years. The Company had RMB3.1bn cash as at 31 Aug and will seek acquisitions.
- **Maintain Buy.** We raised FY21/22E adj. NP by 2/4% mainly to reflect strong student enrollment but partly offset by higher finance cost and effective tax rate. Our TP is lifted from HK\$3.05 to HK\$3.41, at 25.4x FY21E P/E, as we rolled forward our valuation basis which is still at 1x PEG. **Catalysts:** (1) M&A; (2) policy overhang removed; (3) unpeg of independent colleges. **Risk:** surge of teachers' costs.

### Earnings Summary

(YE 31 Dec/31 Aug)	FY19A-D	FY20A	FY21E	FY22E	FY23E
Revenue (RMB mn)	1,331	1,568	2,468	3,095	3,590
YoY growth (%)	29	NA	57	25	16
Net profit (RMB mn)	490	456	785	1,053	1,278
Adj. net profit (RMB mn)	474	576	859	1,127	1,352
Adj. EPS (RMB)	0.071	0.086	0.119	0.156	0.187
YoY growth (%)	26	NA	39	31	20
Consensus EPS (RMB)	NA	NA	0.115	0.150	0.185
Adj. P/E (x)	27.7	23.6	16.6	12.7	10.5
Yield (%)	1.1	0.4	1.9	2.5	3.0
AROE (%)	10.9	11.5	14.2	16.6	17.7
Net cash (RMB mn)	255	329	759	947	1,561

Source: Company data, Bloomberg, CMBIS estimates

### BUY (Maintain)

Target Price	HK\$3.41
(Previous TP	HK\$3.05
Up/Downside	+53%
Current Price	HK\$2.23

### China Education Sector

**Albert Yip, CFA**  
 (852) 3900 0838  
 albertyip@cmbi.com.hk

### Stock Data

Mkt Cap (HK\$ mn)	16,131
Avg 3 mths t/o (HK\$ mn)	49.52
52w High/Low (HK\$)	2.93/ 1.30
Total Issued Shares (mn)	6,736.4

Source: Bloomberg

### Shareholding Structure

Credit Suisse Trust	57.86%
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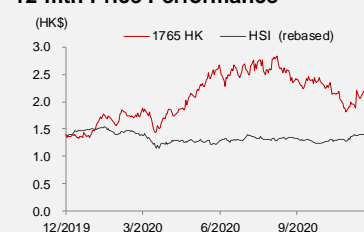
Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	11.2%	1.6%
3-mth	-11.1%	-15.9%
6-mth	-19.0%	-30.8%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

### Auditor: EY

### Related Reports

1. "Hope Education – Acquisition to develop asset light model" – 15 Oct 2020
2. "Hope Education – More optimistic on FY21E student enrollment" – 8 Jun 2020
3. "Strong 1H FY20, multiple growth drivers" – 4 May 2020
4. "Strong FY19 results" – 31 Mar 2020
5. "Acquisition of Malaysia's Inti Education" – 3 Mar 2020
6. "Reverse roadshow takeaways" – 21 Oct 2019

**Figure 1: FY21 results review**

Y/E Aug (RMB mn)	FY20	FY19	change (%)	Remarks
<b>Revenue</b>	<b>1,568</b>	<b>1,079</b>	<b>45%</b>	strong student enrollment growth and acquisitions of Hebi, Suzhou TOP and Yinchuan schools
Cost of sales	(791)	(575)	37%	Increase in teaching resources and D&A upon acq. better scale and cost control
Gross profit	777	504	54%	
Other income	268	264	1%	increased marketing expenses consolidation of new acq. but offset by decreased ESOP increase of forex loss
Selling expenses	(61)	(26)	139%	
Administrative expenses	(195)	(186)	5%	
Other expenses	(52)	(35)	47%	
Operating profit	736	521	41%	
Finance costs	(209)	(155)	34%	increased amortization cost and finance cost from acq.
Share profit of associates	10	(4)	-339%	
Profit before tax	537	362	49%	
Tax expense	(81)	(20)	308%	Colleges in Sichuan made 15% income tax provision
Profit after tax	456	342	34%	
<b>Net profit</b>	<b>456</b>	<b>342</b>	<b>34%</b>	
<b>Adj. net profit</b>	<b>576</b>	<b>358</b>	<b>61%</b>	
<b>Margin &amp; Ratio (%)</b>				
Gross margin	49.6	46.7	2.9	
Adj. gross margin	52.4	47.0	5.4	
Operating margin	47.0	48.3	(1.3)	
SG&A expense/revenue	16.4	19.7	(3.3)	
Net margin	29.1	31.7	(2.6)	
Adj. net margin	36.7	33.2	3.5	
Effective tax rate	15.1	5.5	9.6	
	<b>Aug-20</b>	<b>Dec-19</b>	<b>change (%)</b>	
Net cash (RMB mn)	329	255	29%	

Source: Company data, CMBIS estimates

**Figure 2: Changes of our estimates**

RMB mn	New			Old			Diff (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	2,468	3,095	3,590	2,253	2,885	na	10%	7%	na
Gross Profit	1,312	1,684	1,985	1,188	1,553	na	10%	8%	na
Operating Profit	998	1,301	1,561	913	1,165	na	9%	12%	na
Net profit	859	1,127	1,352	846	1,079	na	2%	4%	na
Gross Margin	53.1%	54.4%	55.3%	52.7%	53.8%	na	+0.4ppt	+0.6ppt	na
Operating Margin	40.4%	42.0%	43.5%	40.5%	40.4%	na	-0.1ppt	+1.6ppt	na
Net Margin	34.8%	36.4%	37.7%	37.5%	37.4%	na	-2.7ppt	-1.0ppt	na

Source: Company data, CMBIS estimates

**Figure 3: CMBIS estimates vs consensus**

RMB mn	CMBIS			Consensus			Diff (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	2,468	3,095	3,590	2,498	3,013	3,503	-1%	3%	2%
Gross Profit	1,312	1,684	1,985	1,289	1,600	1,909	2%	5%	4%
Operating Profit	998	1,301	1,561	1,291	1,681	2,074	-23%	-23%	-25%
Net profit	859	1,127	1,352	835	1,081	1,333	3%	4%	1%
Gross Margin	53.1%	54.4%	55.3%	51.6%	53.1%	54.5%	+1.5ppt	+1.3ppt	+0.8ppt
Operating Margin	40.4%	42.0%	43.5%	51.7%	55.8%	59.2%	-11.3ppt	-13.8ppt	-15.7ppt
Net Margin	34.8%	36.4%	37.7%	33.4%	35.9%	38.1%	+1.4ppt	+0.5ppt	-0.4ppt

Source: Company data, CMBIS estimates

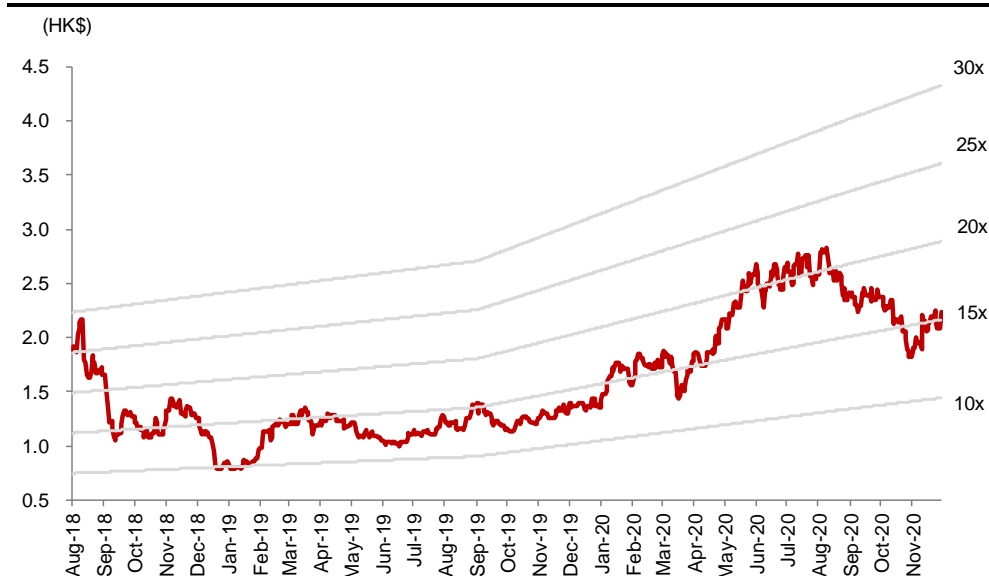
Figure 4: 9% CAGR of student enrolment from 2020/21 to 2022/23 school year

Student enrolment (school year)	2017/2018	2018/2019	2019/2020E	2020/2021E	2021/2022E	2022/2023E	2-yr CAGR
<b>Universities (not incl Guizhou Univ)</b>							
Southwest Jiaotong University Hope College	15,123	17,268	20,454	24,016	25,907	27,235	4%
Business College of Guizhou University of Finance and Econon	14,356	15,548	18,128	21,733	24,341	26,532	7%
Jinci College of Shanxi Medical University	4,801	5,953	7,149	9,500	10,070	10,574	4%
College of Science and Technology of Guizhou University *			9,959	10,986	11,425	11,882	3%
Yinchuan schools			15,569	18,622	22,022	25,322	11%
Inti Education				14,478	16,650	18,315	8%
<b>Junior colleges</b>							
Sichuan Tianyi University	11,765	10,971	11,521	12,890	15,468	17,788	11%
Sichuan Hope Automotive Vocational College	4,559	4,373	6,563	9,500	11,210	11,771	7%
Sichuan Vocational College of Culture&Communication	7,371	8,920	10,349	13,682	14,777	15,515	4%
Guizhou Vocational Institute of Technology	2,989	5,903	8,021	17,652	19,064	20,017	4%
Sichuan TOP IT Vocational Institute	12,548	12,869	13,731	14,174	14,883	15,627	3%
Hebi Automotive College			5,434	6,881	8,881	10,881	17%
Suzhou Top Institute			5,012	8,440	11,440	14,440	20%
Jiangxi Zhangshu					1,500	3,000	na
Xingtai					1,500	3,000	na
Nanchang school					2,753	4,000	na
Chongqing Zhongxian						1,500	na
Gansu Baiyin						1,500	na
<b>Technician colleges</b>							
Sichuan Hope Automotive Technician College	2,127	4,193	8,235	12,000	13,800	15,870	49%
<b>Total students</b>	<b>75,639</b>	<b>86,033</b>	<b>140,125</b>	<b>194,554</b>	<b>225,690</b>	<b>254,769</b>	<b>38%</b>

Source: Company data, CMBIS estimates

\*Assume the investment of the school is financially consolidated by equity method.

Figure 5: P/E band chart



Source: Company data, Bloomberg, CMBIS estimates

**Figure 6: Peers valuation table**

Figure 6: P/E Ratio Valuation Table																			
	Ticker	Rating	Mkt Cap (US\$ m)	Price	TP	Year end	FY1	P/E (x)				Adj. EPS growth (%)				PEG (x)		Revenue growth (%)	
								FY2	FY3	FY4	FY1	FY2	FY3	FY2	FY1	FY2	FY3		
Higher Education services providers																			
China Education	839 HK	NR	4,294	15.48	na	Aug-19	29.0	21.5	17.4	14.7	32	25	24	1.02	36	41	17		
Yuhua Education	6169 HK	NR	3,149	7.31	na	Aug-19	23.3	16.2	14.1	12.7	28	22	15	1.24	43	12	10		
Hope Education	1765 HK	Buy	2,081	2.23	3.41	Aug-19	23.6	16.6	12.7	10.5	na	39	31	0.65	na	57	25		
Kepei Education	1890 HK	NR	1,560	6.00	na	Dec-19	16.6	13.1	11.3	na	34	27	16	na	30	33	15		
Cahtay Media	1981 HK	NR	1,090	5.09	na	Dec-19	24.8	16.6	13.2	na	(12)	49	26	na	7	36	21		
Edvantage	382 HK	NR	1,051	8.00	na	Aug-19	23.2	17.8	13.9	11.6	0	25	28	0.74	16	25	20		
New Higher Education	2001 HK	NR	1,002	4.90	na	Dec-19	11.6	9.6	8.1	na	39	21	19	na	28	17	15		
Minsheng Education	1569 HK	NR	620	1.14	na	Dec-19	11.5	7.9	7.0	na	(14)	46	13	na	16	14	10		
Xinhua Education	2779 HK	Buy	531	2.56	2.97	Dec-19	10.8	9.7	8.9	na	13	12	9	na	14	16	9		
Huali University	1756 HK	NR	461	2.98	na	Aug-19	9.9	7.4	6.0	5.5	41	14	24	0.40	18	16	18		
Neusoft Education	9616 HK	NR	451	5.24	na	Dec-19	16.9	12.7	10.0	7.3	na	33	26	0.39	21	23	19		
Average							18.4	13.6	11.1	10.4	18	29	21	0.74	23	26	17		

Source: Bloomberg estimates, CMBIS estimates

## Financial Summary

### Income statement

YE 31 Dec/Aug (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Revenue</b>	<b>1,331</b>	<b>1,568</b>	<b>2,468</b>	<b>3,095</b>	<b>3,590</b>
Tuition fees	1,093	1,317	2,062	2,625	3,076
Boarding fees	103	102	172	207	237
Others	136	149	234	263	277
Cost of sales	(657)	(791)	(1,157)	(1,411)	(1,605)
Gross profit	675	777	1,312	1,684	1,985
Other income	130	260	187	230	258
Selling expenses	(45)	(61)	(99)	(121)	(133)
Administrative expenses	(152)	(195)	(321)	(390)	(431)
Other expenses	(16)	(52)	(81)	(102)	(118)
EBIT	591	728	998	1,301	1,561
Finance income	94	na	103	107	111
Finance costs	(171)	(209)	(191)	(176)	(170)
Share of JV	5	10	18	21	23
Non-operating items	36	8	10	10	10
Pre-tax profit	556	537	937	1,262	1,535
Income tax	(66)	(81)	(152)	(208)	(256)
Less: Minority interests	0	0	0	0	0
<b>Net profit</b>	<b>490</b>	<b>456</b>	<b>785</b>	<b>1,053</b>	<b>1,278</b>
<b>Adjusted net profit</b>	<b>474</b>	<b>576</b>	<b>859</b>	<b>1,127</b>	<b>1,352</b>

### Cash flow summary

YE 31 Dec/Aug (RMB mn)	FY19A	FY20E	FY21E	FY22E	FY23E
<b>Profit before tax</b>	<b>556</b>	<b>492</b>	<b>785</b>	<b>1,053</b>	<b>1,278</b>
Depreciation and amortization	218	294	335	372	401
Change in working capital	(47)	251	2,138	502	470
Others	(29)	19	(147)	2	3
<b>Net cash from operating</b>	<b>697</b>	<b>1,056</b>	<b>3,112</b>	<b>1,929</b>	<b>2,153</b>
Capex & investments	(279)	(500)	(900)	(900)	(900)
Acquisitions	(447)	(56)	(1,236)	(385)	(93)
Others	(1,137)	1,056	25	12	2
<b>Net cash from investing</b>	<b>(1,865)</b>	<b>500</b>	<b>(2,111)</b>	<b>(1,273)</b>	<b>(991)</b>
Equity raised	-	1,128	-	-	-
Change of borrowings	313	1,033	(100)	-	-
Dividend paid	(105)	(150)	(60)	(275)	(361)
Others	(272)	122	(208)	(194)	(188)
<b>Net cash from financing</b>	<b>(65)</b>	<b>2,133</b>	<b>(369)</b>	<b>(468)</b>	<b>(548)</b>
<b>Net change in cash</b>	<b>(1,232)</b>	<b>3,689</b>	<b>633</b>	<b>188</b>	<b>614</b>
Cash at the beginning of the year	3,039	829	2,894	3,527	3,715
Exchange difference	1,806	4,518	3,527	3,715	4,328
<b>Cash at the end of the year</b>	<b>1,690</b>	<b>4,518</b>	<b>3,527</b>	<b>3,715</b>	<b>4,328</b>

### Balance sheet

YE 31 Dec/Aug (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Non-current assets</b>	<b>7,348</b>	<b>8,458</b>	<b>10,476</b>	<b>11,038</b>	<b>11,546</b>
PPE	4,564	5,065	6,649	7,267	7,862
Prepaid lease payments	1,163	1,319	1,251	1,178	1,098
JV	196	196	214	234	258
Others	1,425	1,877	2,361	2,358	2,329
<b>Current assets</b>	<b>3,508</b>	<b>3,958</b>	<b>4,611</b>	<b>4,821</b>	<b>5,459</b>
Cash	1,690	2,894	3,527	3,715	4,328
Prepayments	252	202	222	244	268
Others	1,565	847	847	847	847
<b>Current liabilities</b>	<b>3,143</b>	<b>3,368</b>	<b>5,296</b>	<b>5,384</b>	<b>5,719</b>
Contract liabilities	806	404	2,549	2,982	3,366
Other payables	1,176	1,345	1,328	983	933
Borrowings	1,003	1,443	1,243	1,243	1,243
Current income tax	65	88	88	88	88
Others	91	88	88	88	88
<b>Non-current liabilities</b>	<b>3,149</b>	<b>3,361</b>	<b>3,379</b>	<b>3,284</b>	<b>3,178</b>
Deferred income	1,073	1,253	1,197	1,129	1,050
Borrowings	1,594	1,670	1,770	1,770	1,770
Others	482	439	412	385	358
<b>Total net assets</b>	<b>4,565</b>	<b>5,686</b>	<b>6,411</b>	<b>7,190</b>	<b>8,108</b>
<b>Shareholders' equity</b>	<b>4,562</b>	<b>5,683</b>	<b>6,408</b>	<b>7,187</b>	<b>8,104</b>
<b>Minority Interest</b>	<b>3</b>	<b>3</b>	<b>3</b>	<b>4</b>	<b>4</b>

### Key ratios

YE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Sales mix (%)</b>					
Tuition & boarding fees	82.1	84.0	83.5	84.8	85.7
Ancillary services	7.7	6.5	7.0	6.7	6.6
Others	10.2	9.5	9.5	8.5	7.7
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>P&amp;L ratios (%)</b>					
Gross profit margin	50.7	49.6	53.1	54.4	55.3
EBIT margin	44.4	46.4	40.4	42.0	43.5
Effective tax rate	11.8	15.1	16.2	16.5	16.7
Adj. net profit margin	35.6	35.0	34.8	36.4	37.7
Payout ratio	31.7	11.0	32.0	32.0	32.0
<b>Balance sheet ratios</b>					
Current ratio (x)	1.1	1.2	0.9	0.9	1.0
Asset turnover (x)	0.1	0.1	0.2	0.2	0.2
Net cash (RMB mn)	255	329	759	947	1,561
<b>Returns (%)</b>					
Adj. ROAE	10.9	11.5	14.2	16.6	17.7
Adj. ROAA	4.9	3.8	6.2	7.3	8.2
<b>Per share data</b>					
Adj. EPS (RMB)	0.071	0.086	0.119	0.156	0.187
DPS (RMB)	0.023	0.008	0.038	0.050	0.060
BVPS (RMB)	0.684	0.786	0.886	0.993	1.120

Source: Company data, CMBIS estimates

Year-end is changed to Aug from FY20E onwards

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**Address:** 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

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