

Wisdom Education (6068 HK)

Explore new businesses opportunities

1HFY20 NP rose 38% YoY, representing 58% of our FY20E NP. The results were better than our expectation driven by better GPM, SG&A expenses and other income. We raised FY20-22E net profit by 3-4% and our TP from HK\$4.40 to HK\$4.60. Trading at 13.4x FY20E P/E, valuation is attractive compared to 27% EPS CAGR from FY19 to FY22E. Maintain Buy.

- **Results beat.** Revenue climbed 12% to RMB1,682mn, representing 46% of our FY20E revenue, less than our estimates because ancillary services revenue only rose 2% given that certain services were suspended due to COVID-19 outbreak. GPM widened 1.4ppt to 46.7% due to 5% ASP growth and costs control. Other income jumped four times due to RMB40mn increase of government grant. SG&A expenses reduced by 1.5ppt to 17.2% thanks to costs control. Effective tax rate rose from 14.8% to 19.4% mainly due to tax on government grant.
- **COVID-19 impact insignificant.** During the coronavirus outbreak, the Company provides online learning activities for students. Management expects physical classes would gradually resume in Apr and May. We estimate the loss of revenue of ancillary services such as canteen, supermarket, school bus, etc could be around two months.
- **High visibility of growth potential.** Management plans to add one asset-light school in Dongguan or Foshan in 2020-21 school year, and open Chaozhou and Jiangmen schools in 2021-22 school year. Total expected maximum capacity of existing schools and planned new schools would exceed 142,870, representing 138% of current student enrollment of 60,116.
- **Explore new businesses in mid to long-term.** The Company plans to diversify its businesses in three ways: (1) Online education. A subsidiary is set up to explore the provision of online parent-child learning activities, extra-curricular activity classes and teacher training courses at weekends; (2) Higher education. The Company is seeking cooperation with renowned universities to provide high-end talent training in Guangdong; (3) School management. The Company is considering to provide school management services underpinned by its 20 years of experience.
- **Maintain Buy.** We lifted FY20-22E net profit estimates by 3-4% due to better GPM, SG&A expenses and other income assumptions. Our TP is revised from HK\$4.40 to HK\$4.60, still based on 18x FY20E P/E. We continue to like the Company's Guangdong-focused expansion strategy and expansion visibility. **Catalysts:** (1) better-than-expected student enrolment or tuition fee growth; (2) M&A; (3) removal of policy overhang. **Risks:** (1) policy risks; (2) lower-than-expected student enrollment or tuition fee growth; (3) surge of teachers' costs.

Earnings Summary

(YE 31 Aug)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	1,247	1,682	1,832	2,376	2,854
YoY growth (%)	27	35	9	30	20
Net profit (RMB mn)	310	359	475	615	745
EPS (RMB)	0.152	0.172	0.228	0.292	0.354
YoY growth (%)	38	13	33	28	21
Consensus EPS (RMB)	na	na	0.258	0.296	0.355
P/E (x)	18.6	17.8	13.4	10.5	8.6
Yield (%)	2.4	2.9	3.0	3.8	4.6
P/B (x)	3.0	2.9	2.4	2.1	1.8
Net gearing (%)	47	66	41	34	27

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price	HK\$4.60
(Previous TP	HK\$4.40)
Up/Downside	+35%
Current Price	HK\$3.40

China Education Sector

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

Stock Data

Mkt Cap (HK\$ mn)	6,960
Avg 3 mths t/o (HK\$ mn)	6.21
52w High/Low (HK\$)	4.76/ 2.10
Total Issued Shares (mn)	2,047.2

Source: Bloomberg

Shareholding Structure

Mr. Liu Xuebin	45.45%
Ms. Li Suwen	27.95%

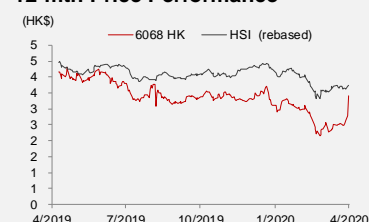
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	16.9%	13.0%
3-mth	-10.6%	2.9%
6-mth	-16.6%	-8.4%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Deloitte

Related Reports

1. "Wisdom Education – Explore asset-light model to enhance return" – 27 Nov 2019
2. "Wisdom Education – Student enrollment missed but organic growth still strong" – 9 Sep 2019
3. "Wisdom Education – 2019/20 school year tuition fees in line; Reiterate Buy" – 9 Jul 2019
4. "Wisdom Education – Upside potential on tuition fee level" – 15 May 2019

Figure 1: 1HFY20 results review

Y/E Feb 29 (RMB mn)	1H20	1H19	% change	Remarks
Revenue	932.2	835.6	12%	Student enrollment rose 10.5%, ASP up 4.9%
Cost of sales	(496.5)	(456.8)	9%	
Gross profit	435.6	378.7	15%	
Other income	50.3	9.9	408%	including gov't grant of RMB47mn
Other gains and losses	38.7	19.3	101%	interest income from investment products rose by RMB10mn
Selling and distribution expenses	(20.2)	(25.0)	-19%	decrease in student enrollment costs
Administrative expenses	(140.1)	(131.1)	7%	increase mainly due to increase in staff costs
Operating profit	364.4	251.9	45%	
Finance income	7.4	9.6	-23%	
Finance costs	(52.1)	(38.7)	35%	total loans increased 9% to RMB2.1bn
Change in FV of inv prop and CB	1.0	(0.4)	na	
Listing expenses	0.0	0.0	na	
Profit before tax	320.6	222.4	44%	
Tax expense	(62.2)	(32.9)	89%	RMB47m gov't grant taxed at 25%
MI	(8.1)	(3.5)	131%	
Net profit	266.5	193.0	38%	
Adj net profit	296.4	219.9	35%	
DPS (HK\$)	0.06	0.05	27%	
Margin & Ratio (%)				
Gross margin	46.7	45.3	1.4	
Operating margin	39.1	30.1	9.0	
SG&A expenses ratio	17.2	18.7	(1.5)	
Net margin	28.6	23.1	5.5	
Effective tax rate	19.4	14.8	4.6	
Payout ratio	43.8	44.5	(0.7)	
	1H20	1H19	change (%)	
Student number	60,116	54,420	10%	
Net cash (RMBmn)	(1,675)	(1,128)	48%	

Source: Company data

Figure 2: 2019/20 school year tuition and boarding fees changes

Schools	Annual tuition and boarding fee		
	2018/19 school year	2019/20 school year	Change (%)
Dongguan Guangming High School	36,800	43,800	19%
Dongguan Guangzheng High School	30,800	43,800	42%
Jieyang Jiedong Guangzheng High School	15,000	19,600	31%
Jieyang Jiedong Guangzheng Middle School	13,600	18,000	32%
Jieyang Jiedong Guangzheng Primary School	12,400	16,000	29%
Weifang Guangzheng High School	18,600	23,000	24%
Weifang Guangzheng Middle School	16,600	20,200	22%
Weifang Weizhou Foreign Language School	12,800	13,200	3%
Yunfu Guangming High School	na	26,000	na
Yunfu Guangming Middle School	na	31,200	na
Yunfu Guangming Primary School	na	33,200	na
Foshan Guangzheng High School	na	51,400	na
Foshan Guangzheng Middle School	na	43,800	na
Foshan Guangzheng Middle School	na	42,000	na

Source: Company data

Figure 3: Current student number and expected maximum capacity of existing schools

School/location	Year of opening	Student number in 2018/19	Student number in 2019/20	Growth (%)	Estimated capacity in 2018/19	Expected max. capacity	Heavy-asset
Dongguan Guangming Secondary and Primary Schools	2003	17,358	17,623	2%	18,300	18,300	Y
Dongguan Guangzheng Preparatory School	2013	12,645	14,773	17%	17,000	20,000	Y
Huizhou Guangzheng Preparatory School	2014	8,413	9,694	15%	10,500	12,000	Y
Panjin Guangzheng Preparatory School	2014	3,119	4,070	30%	4,000	6,200	Y
Weifang Guangzheng Preparatory School	2016	2,133	2,522	18%	4,000	8,000	Y
Jieyang, Guangdong	2017	5,375	4,769	-11%	7,000	18,000	Y
Weifang Weizhou School	2017	2,318	2,195	-5%	2,200	2,200	Y
Guang'an, Sichuan	2018	159	598	276%	1,000	9,280	Y
Zhang Pu Longcheng Schools	2018	2,900	2,894	0%	3,000	3,500	Y
Bazhong Guangzheng Preparatory School	2019	na	488	na	1,500	10,000	Y
Yunfu Guangming Foreign Language School	2019	na	445	na	1,500	10,680	Y
Shunde Guangzheng Preparatory School	2019	na	45	na	na	9,210	Y
Total		54,420	60,116	10%	70,000	127,370	

Source: Company data, CMBIS

Figure 4: New projects provide at least 15,500 student capacity

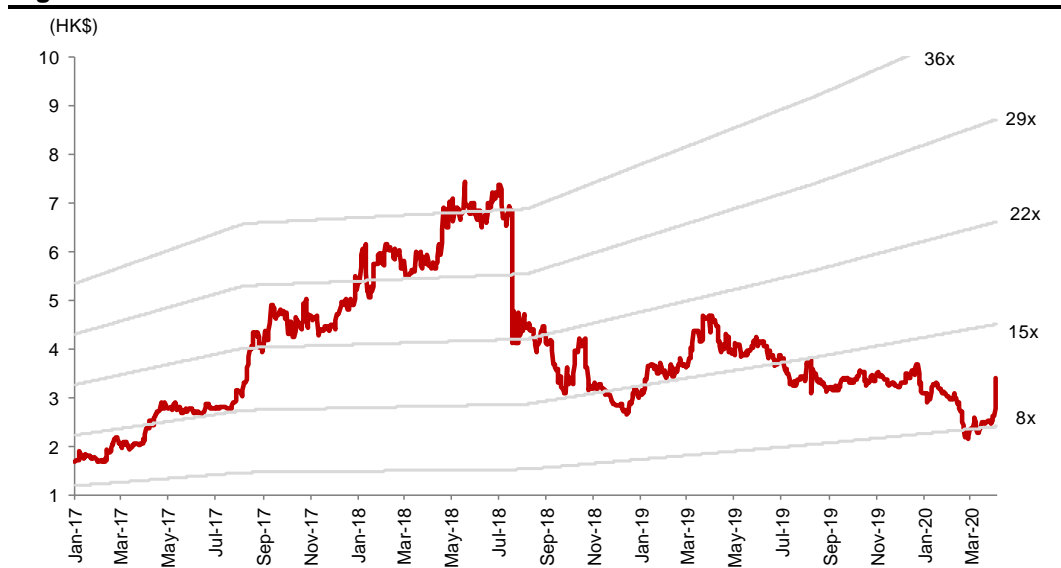
Location	Expected year of opening	Target max. capacity
Dongguan/Foshan (light asset projects)	Sep-20	TBC
Chaozhou, Guangdong	Sep-21	8,000
Jiangmen, Guangdong	Sep-21	7,500
Guangzhou, Guangdong	TBC	TBC
Zhaoqing, Guangdong	TBC	TBC
Total		15,500

Source: Company data, CMBIS

Figure 5: 15% CAGR of student enrolment from FY20E to FY22E

School year	2016/17	2017/18	2018/19	2019/20	2020/21E	2021/22E	2-yr CAGR
Dongguan Guangming Secondary and Primary Schools	16,483	16,477	17,358	17,623	17,957	17,957	1%
Dongguan Guangzheng Preparatory School	9,094	10,620	12,645	14,773	16,693	18,530	12%
Huizhou Guangzheng Preparatory School	3,903	6,011	8,413	9,694	10,450	11,450	9%
Panjin Guangzheng Preparatory School	1,590	2,170	3,119	4,070	4,870	5,670	18%
Weifang Guangzheng Preparatory School	718	1,401	2,133	2,522	2,822	3,322	15%
Jieyang School		4,501	5,375	4,769	5,169	5,669	9%
Weifang Weizhou School		2,050	2,318	2,195	2,195	2,195	0%
Guang'an Guangzheng Preparatory School			159	598	1,098	1,618	64%
Zhang Pu Longcheng Schools			2,900	2,894	2,900	2,900	0%
Yunfu School				445	1,245	2,145	120%
Foshan School				45	700	1,500	477%
Bazhong School				488	1,050	1,700	87%
Kaiping School					700	1,400	na
Chaozhou School					700	1,400	na
Zengcheng School						700	na
Zhaoqing School						700	na
Total	31,788	43,230	54,420	60,116	68,549	78,856	15%

Source: Company data, CMBIS estimates

Figure 6: P/E band

Source: Bloomberg, Company data, CMBIS estimates

Figure 7: Key assumptions

Year-end Aug 31 (RMB mn)	FY18	FY19	FY20E	FY21E	FY22E
Total revenue	1,247	1,682	1,832	2,376	2,854
growth %	27.3%	34.9%	9.0%	29.6%	20.1%
Tuition and boarding fees	841	1,145	1,341	1,675	2,024
growth %	25.3%	36.2%	17.1%	24.9%	20.8%
Others	406	536	492	701	830
growth %	31.7%	32.1%	-8.3%	42.5%	18.5%
Gross profit margin	43.7%	44.1%	45.3%	46.5%	46.0%
Selling expenses ratio	1.6%	1.5%	1.2%	1.1%	1.1%
Administrative expenses ratio	17.7%	15.0%	15.5%	14.1%	13.6%
Operating profit margin	28.9%	29.5%	34.7%	33.1%	32.9%
Effective tax rate	11.1%	13.6%	16.0%	14.0%	14.0%
Net profit	310	359	475	615	745
growth %	55.0%	15.8%	32.2%	29.5%	21.1%
Payout ratio	43.5%	39.4%	40.0%	40.0%	40.0%
Average tuition and boarding fee (RMB)	19,893	21,049	22,305	24,434	25,662
growth %	-5.8%	8.2%	6.0%	9.5%	5.0%
Student enrollment	43,230	54,420	60,116	68,549	78,856
growth %	36.0%	25.9%	10.5%	14.0%	15.0%
Utilization rate	86.8%	86.4%	85.9%	84.9%	87.9%

Source: Company data, CMBIS estimates

Figure 8: Earnings revision

US\$ mn	New			Old			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,832	2,376	2,854	2,006	2,470	2,971	-9%	-4%	-4%
Gross Profit	830	1,105	1,312	895	1,124	1,330	-7%	-2%	-1%
Operating Profit	636	785	938	610	776	923	4%	1%	2%
Net profit	475	615	745	461	597	716	3%	3%	4%
Gross Margin	45.3%	46.5%	46.0%	44.6%	45.5%	44.8%	+0.7ppt	+1.0ppt	+1.2ppt
Operating Margin	34.7%	33.1%	32.9%	30.4%	31.4%	31.1%	+4.3ppt	+1.7ppt	+1.8ppt
Net Margin	25.9%	25.9%	26.1%	23.0%	24.2%	24.1%	+2.9ppt	+1.7ppt	+2.0ppt

Source: CMBIS estimates

Figure 9: CMBIS estimates vs consensus

US\$ mn	CMBIS			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,832	2,376	2,854	2,044	2,360	2,721	-10%	1%	5%
Gross Profit	830	1,105	1,312	920	1,043	1,197	-10%	6%	10%
Operating Profit	636	785	938	655	773	863	-3%	2%	9%
Net profit	475	615	745	502	608	706	-5%	1%	6%
Gross Margin	45.3%	46.5%	46.0%	45.0%	44.2%	44.0%	+0.3ppt	+2.3ppt	+2.0ppt
Operating Margin	34.7%	33.1%	32.9%	32.0%	32.8%	31.7%	+2.7ppt	+0.3ppt	+1.2ppt
Net Margin	25.9%	25.9%	26.1%	24.5%	25.8%	25.9%	+1.4ppt	+0.1ppt	+0.2ppt

Source: Bloomberg estimates, CMBIS estimates

Financial Summary

Income statement

YE 31 Aug (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	1,247	1,682	1,832	2,376	2,854
Tuition & boarding fees	841	1,145	1,341	1,675	2,024
Ancillary services	406	536	492	701	830
Cost of sales	(702)	(940)	(1,003)	(1,270)	(1,542)
Gross profit	545	742	830	1,105	1,312
Other income	54	33	60	30	30
Other gains and losses	2	(1)	52	10	15
Selling expenses	(19)	(26)	(22)	(26)	(31)
Administrative expenses	(221)	(253)	(283)	(334)	(388)
EBIT	360	496	636	785	938
Finance costs, net	(11)	(87)	(85)	(87)	(92)
Listing expenses	0	0	0	0	0
FV change of inv. prop.	(3)	1	0	0	0
Pre-tax profit	346	409	551	698	846
Income tax	(38)	(56)	(88)	(98)	(118)
Less: Minority interests	(3)	(6)	(12)	(15)	(18)
Net profit	310	359	475	615	745

Cash flow summary

YE 31 Aug (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before tax	346	409	551	698	846
Depreciation and amortization	106	149	160	173	191
Change in working capital	191	(1)	237	245	283
Others	(19)	19	(31)	4	(38)
Net cash from operating	623	577	918	1,120	1,282
Capex & investments	(743)	(904)	(750)	(750)	(750)
Acquisitions	(267)	(70)	0	0	0
Others	(338)	(32)	159	18	(82)
Net cash from investing	(1,349)	(1,006)	(591)	(732)	(832)
Equity raised	3	3	0	0	0
Change of borrowings	1,485	462	(179)	100	100
Dividend paid	(122)	(155)	(175)	(216)	(271)
Others	(118)	(141)	(102)	(105)	(110)
Net cash from financing	1,248	169	(457)	(221)	(281)
Net change in cash	522	(260)	(130)	167	169
Cash at the beginning of the year	378	911	662	533	700
Exchange difference	11	11	0	0	0
Cash at the end of the year	911	662	533	700	869

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	4,003	4,676	5,236	5,813	6,371
PPE	2,492	3,036	3,658	4,258	4,838
Prepaid lease payments	502	781	764	747	730
Deposits	520	631	631	631	631
Others	489	228	182	176	172
Current assets	1,468	1,595	1,361	1,561	1,860
Cash	911	662	533	700	869
Pledged deposit	282	499	499	499	499
Prepayments	162	97	106	137	165
Others	113	337	224	225	327
Current liabilities	1,643	2,480	2,247	2,537	2,838
Borrowings	282	1,108	629	629	629
Contract liabilities	617	751	952	1,147	1,372
Trade and other payables	616	503	548	631	719
Others	128	118	118	129	118
Non-current liabilities	1,851	1,545	1,545	1,645	1,745
Borrowings	1,847	1,540	1,540	1,640	1,740
Deferred revenue	0	0	0	0	0
Others	4	4	4	4	4
Total net assets	1,977	2,247	2,805	3,192	3,649
Shareholders' equity	1,911	2,161	2,732	3,134	3,609
Minority Interest	66	86	74	59	41

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Tuition & boarding fees	67.5	68.1	73.2	70.5	70.9
Ancillary services	32.5	31.9	26.8	29.5	29.1
Total	100.0	100.0	100.0	100.0	100.0
P&L ratios (%)					
Gross profit margin	43.7	44.1	45.3	46.5	46.0
EBIT margin	28.9	29.5	34.7	33.1	32.9
Effective tax rate	11.1	13.6	16.0	14.0	14.0
Net profit margin	24.9	21.4	25.9	25.9	26.1
Payout ratio	43.5	39.4	40.0	40.0	40.0
Balance sheet ratios					
Current ratio (x)	0.9	0.6	0.6	0.6	0.7
Asset turnover (x)	0.2	0.3	0.3	0.3	0.3
Net gearing ratio (%)	47	66	41	34	27
Returns (%)					
ROAE	17.0	17.7	19.4	21.0	22.1
ROAA	7.0	6.0	7.2	8.6	9.3
Per share					
EPS (RMB)	0.15	0.20	0.22	0.29	0.35
DPS (HK\$)	0.08	0.10	0.10	0.13	0.16
BVPS (RMB)	0.94	1.06	1.3	1.5	1.7

Source: Company data, CMBIS estimates

Disclosures & Disclaimers

Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

CMBIS Ratings

BUY	: Stock with potential return of over 15% over next 12 months
HOLD	: Stock with potential return of +15% to -10% over next 12 months
SELL	: Stock with potential loss of over 10% over next 12 months
NOT RATED	: Stock is not rated by CMBIS

OUTPERFORM	: Industry expected to outperform the relevant broad market benchmark over next 12 months
MARKET-PERFORM	: Industry expected to perform in-line with the relevant broad market benchmark over next 12 months
UNDERPERFORM	: Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Securities Limited

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

CMB International Securities Limited ("CMBIS") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIS does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIS recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIS, solely for the purpose of supplying information to the clients of CMBIS or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIS nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIS has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIS provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIS may issue other publications having information and/or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIS may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIS may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIS does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIS may have a conflict of interest that could affect the objectivity of this report and CMBIS will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIS.

Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I) falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time) ("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.") of the Order, and may not be provided to any other person without the prior written consent of CMBIS.

For recipients of this document in the United States

This report is intended for distribution in the United States to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, and may not be furnished to any other person in the United States. Each major US, institutional investor that receives a copy of this research report by its acceptance hereof represents and agrees that it shall not distribute or provide this research report to any other person.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.