

Hope Education (1765 HK)

Strong FY19 results

Adj. NP +48% to RMB474mn, in line with our estimates but 6% above consensus. We trimmed FY20/21E adj. NP by 1%/3% as we delay tuition fee increase by one year to 2021/22 school year because of softening economic growth. Our TP is fine tuned from HK\$2.33 to HK\$2.31, still based on 21.4x FY20E P/E (vs 34% adj. EPS CAGR in FY19-21E). Hope Education is still our top pick because it has both good organic and M&A growth drivers. Compared to peers, its provision of 15% income tax for Sichuan colleges in FY19 has released most risk of rising tax rate in advance due to registration as for-profit schools.

- Strong FY19 results.** Revenue rose 29% to RMB1,331mn, in line with our estimates and consensus, led by 20% organic revenue growth (21% organic student enrollment growth) and acquisitions. GPM surprisingly jumped 5.3ppt to 50.7%, beating our estimates/consensus by 3.4/3.1ppt as organic portion teachers' costs only up ~2% and utilization rate rose from 80% to 82%. The Company unexpectedly recorded RMB66mn tax expenses by making 15% tax provision for its Sichuan colleges because the Company would submit its intention to convert its colleges in Sichuan to for-profit schools by Sep 2020.
- Expect increase of admission quota.** COVID-19 does not have negative impact on the Company as tuition and boarding fees of spring semester were received and offline lectures were replaced by online learning. On the other hand, due to the softening employment market, management expects the government to further increase admission quota in 2020/21 school year after raising quota of diploma-to-degree in Feb. The Company has enrolled 7,042 part-time diploma students from veteran soldiers and unemployed workers.
- Organic and M&A growth drivers.** As at end of 2019, the Company had cash and structured deposit of RMB2.9bn. For M&A, it plans to acquire universities. For organic growth, it will strive to increase enrollment scale and registration rate, enhance employee services and provide overseas study services. It also has three new greenfield projects of vocational colleges (Chongqing, Jiangxi and Gansu projects) as long-term growth drivers.
- Maintain Buy.** Due to softening economic growth, we delay tuition fee increase by one year to 2021/22 school year. We trimmed FY20/21E adj. net profit estimates by 1%/3% and fine tuned our TP from HK\$2.33 to HK\$2.31, still based on 21.4x FY20E P/E. We expect the Company to deliver 34% adj. EPS CAGR in FY19-21E, which is stronger than peers' average of 26%. **Catalysts:** (1) M&A; (2) removal of policy overhang. **Risk:** surge of teachers' costs.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	1,030	1,331	1,751	2,492	2,776
YoY growth (%)	37	29	31	42	11
Net profit (RMB mn)	168	490	648	857	995
Adj. net profit (RMB mn)	320	474	648	857	995
Adj. EPS (RMB)	0.056	0.071	0.097	0.128	0.149
YoY growth (%)	na	26	37	32	16
Consensus EPS (RMB)	na	0.069	0.094	0.116	na
Adj. P/E (x)	25.2	20.8	15.5	11.7	10.1
Yield (%)	1.1	1.5	2.1	2.7	3.2
Yield (%)	13.3	10.9	13.5	15.9	16.4
Net cash (RMB mn)	907	255	323	962	1,310

Source: Bloomberg, Company data, CMBIS estimates

BUY (Maintain)

Target Price **HK\$2.31**
(Previous TP **HK\$2.33**)
Up/Downside **+38%**
Current Price **HK\$1.68**

China Education Sector

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Stock Data

Mkt Cap (HK\$ mn)	11,208
Avg 3 mths t/o (HK\$ mn)	9.70
52w High/Low (HK\$)	1.88/1
Total Issued Shares (mn)	6,672

Source: Bloomberg

Shareholding Structure

Hope Education Investment	62.75%
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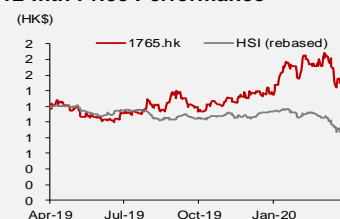
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-2.3%	-11.3%
3-mth	21.7%	-18.2%
6-mth	47.4%	-11.2%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: EY

Related Reports

- "Acquisition of Malaysia's Inti Education" – 3 Mar 2020
- "Reverse roadshow takeaways" – 21 Oct 2019
- "Solid 1H19 results; 31% EPS CAGR in FY20-21E" – 2 Sep 2019
- "Undemanding valuation at 25% 3-YR EPS CAGR" – 26 Mar 2019

Figure 1: FY19 results review

Y/E Dec (RMB mn)	FY19	FY18	change (%)	Remarks
Revenue	1,331	1,030	29%	Excl acquisitions of Yinchuan schools, Hebi College and Suzhou Top, revenue increased 20%
tuition fees	1,093	854	28%	student enrollment grew 21% to 104,151 organically
boarding fees	103	85	20%	
others	136	90	51%	
Cost of sales	(657)	(562)	17%	teachers' costs +11%
Gross profit	675	467	44%	
Other income	186	133	41%	
Selling expenses	(45)	(21)	118%	
Administrative expenses	(172)	(267)	-36%	ESOP expenses reduced from RMB122mn to RMB21mn
Other expenses	(16)	(28)	-41%	
Operating profit	627	284	121%	
Finance income	94	79	20%	
Finance costs	(171)	(201)	-15%	
Share profit of associates	5	(2)	-379%	
Profit before tax	556	159	248%	
Tax expense	(66)	8	-938%	Colleges in Sichuan made 15% income tax provision
Profit after tax	490	167	193%	
Non-controlling interests	0	(1)	-127%	
Net profit	490	168	192%	
Adj. net profit	474	320	48%	
Margin & Ratio (%)				
Gross margin	50.7	45.4	5.3	
Operating margin	47.1	27.5	19.5	
SG&A expense/revenue	16.4	28.0	(11.6)	
Net margin	36.8	16.3	20.5	
Adj. net margin	35.6	31.1	4.5	
Effective tax rate	11.8	(4.9)	16.7	
Payout ratio (%)	31.7	31.3	0.5	
	FY19	FY18	change (%)	
Net cash (RMB mn)	255	907	-72%	

Source: Company data, CMBIS

Figure 2: Changes of our estimates

US\$ mn	CMBIS			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,751	2,492	2,776	1,784	2,515	na	-2%	-1%	na
Gross Profit	931	1,323	1,491	851	1,245	na	9%	6%	na
Operating Profit	854	1,094	1,240	757	1,015	na	13%	8%	na
Net profit	648	857	995	653	882	na	-1%	-3%	na
Gross Margin	53.2%	53.1%	53.7%	47.7%	49.5%	na	+5.5ppt	+3.6ppt	na
Operating Margin	48.8%	43.9%	44.7%	42.4%	40.4%	na	+6.6ppt	+3.5ppt	na
Net Margin	37.0%	34.4%	35.8%	36.6%	35.1%	na	+0.4ppt	-0.7ppt	na

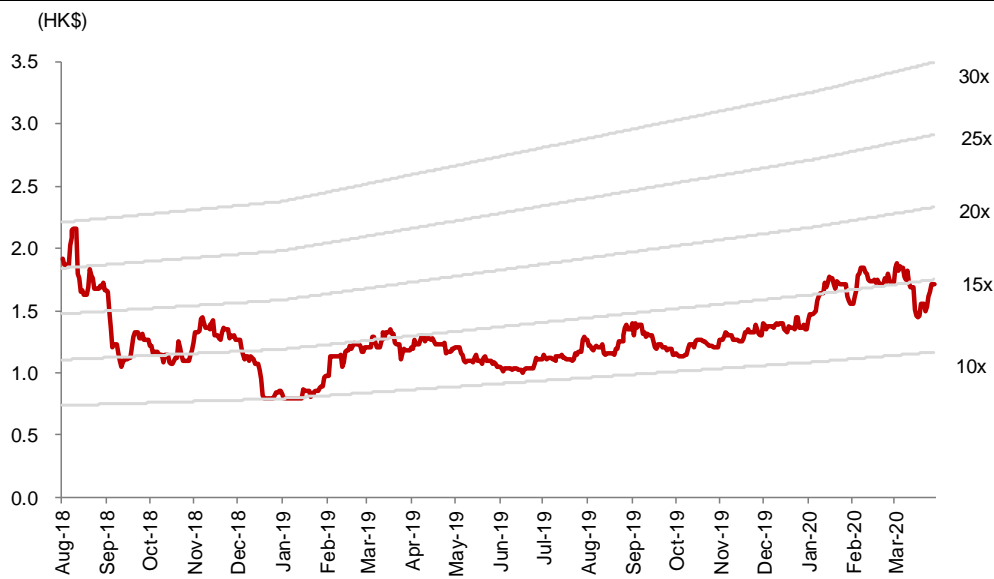
Source: Company data, CMBIS estimates

Figure 3: CMBIS estimates vs consensus

US\$ mn	CMBIS			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,751	2,492	2,776	1,758	2,159	na	0%	15%	na
Gross Profit	931	1,323	1,491	847	1,038	na	10%	27%	na
Operating Profit	854	1,094	1,240	762	920	na	12%	19%	na
Net profit	648	857	995	634	794	na	2%	8%	na
Gross Margin	53.2%	53.1%	53.7%	48.2%	48.1%	na	+0.2ppt	-0.2ppt	na
Operating Margin	48.8%	43.9%	44.7%	43.3%	42.6%	na	+2.3ppt	+0.3ppt	na
Net Margin	37.0%	34.4%	35.8%	36.1%	36.8%	na	+1.5ppt	-0.2ppt	na

Source: Company data, CMBIS estimates

Figure 4: P/E band chart



Source: Company data, CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	1,030	1,331	1,751	2,492	2,776
Tuition fees	854	1,093	1,446	2,116	2,362
Boarding fees	85	103	147	167	185
Others	90	136	157	210	229
Cost of sales	(562)	(657)	(819)	(1,169)	(1,285)
Gross profit	467	675	931	1,323	1,491
Other income	101	130	175	205	216
Selling expenses	(21)	(45)	(53)	(82)	(89)
Administrative expenses	(111)	(152)	(193)	(341)	(366)
Other expenses	(5)	(16)	(8)	(10)	(12)
EBIT	431	591	854	1,094	1,240
Finance income	79	94	56	42	51
Finance costs	(201)	(171)	(206)	(196)	(196)
Share of JV	(2)	5	21	21	23
Non-operating items	(148)	36	10	10	10
Pre-tax profit	159	556	735	971	1,128
Income tax	8	(66)	(87)	(115)	(133)
Less: Minority interests	(1)	0	0	0	0
Net profit	168	490	648	857	995
Adjusted net profit	320	474	648	857	995

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before tax	159	556	735	971	1,128
Depreciation and amortization	161	218	311	361	368
Change in working capital	249	(47)	198	142	124
Others	233	(29)	32	(14)	(40)
Net cash from operating	802	697	1,275	1,461	1,581
Capex & investments	(624)	(279)	(400)	(400)	(400)
Acquisitions	(15)	(447)	(936)	(56)	(401)
Others	(130)	(1,139)	515	38	38
Net cash from investing	(769)	(1,865)	(821)	(418)	(763)
Equity raised	2,705	-	-	-	-
Change of borrowings	259	313	-	-	-
Dividend paid	-	(105)	(150)	(207)	(274)
Others	(595)	(272)	(237)	(196)	(196)
Net cash from financing	2,369	(65)	(387)	(403)	(470)
Net change in cash	2,402	(1,232)	67	639	348
Cash at the beginning of the year	181	3,039	1,690	1,758	2,397
Exchange difference	2,584	1,806	1,758	2,397	2,745
Cash at the end of the year	3,039	1,690	1,758	2,397	2,745

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	5,119	7,348	8,339	8,399	8,453
PPE	3,448	4,564	5,280	5,421	5,556
Prepaid lease payments	590	1,163	1,087	1,004	920
JV	-	196	217	239	262
Others	1,081	1,425	1,754	1,735	1,716
Current assets	3,172	3,508	3,132	3,799	4,177
Cash	3,039	1,690	1,758	2,397	2,745
Prepayments	129	252	277	305	336
Others	4	1,565	1,097	1,097	1,097
Current liabilities	1,851	3,143	3,279	3,393	3,146
Contract liabilities	591	806	1,002	1,143	1,267
Other payables	637	1,176	1,148	1,121	751
Borrowings	527	1,003	1,003	1,003	1,003
Current income tax	34	65	65	65	65
Others	62	91	60	60	60
Non-current liabilities	2,280	3,149	3,124	3,088	3,046
Deferred income	658	1,073	1,076	1,068	1,054
Borrowings	1,605	1,594	1,594	1,594	1,594
Others	17	482	455	427	399
Total net assets	4,160	4,565	5,067	5,717	6,438
Shareholders' equity	4,157	4,562	5,064	5,714	6,434
Minority Interest	3	3	3	3	4

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Tuition & boarding fees	83.0	82.1	82.6	84.9	85.1
Ancillary services	8.3	7.7	8.4	6.7	6.7
Others	8.7	10.2	9.0	8.4	8.3
Total	100.0	100.0	100.0	100.0	100.0
P&L ratios (%)					
Gross profit margin	45.4	50.7	53.2	53.1	53.7
EBIT margin	41.9	44.4	48.8	43.9	44.7
Effective tax rate	31.1	35.6	37.0	34.4	35.8
Adj. net profit margin	(4.9)	11.8	11.8	11.8	11.8
Payout ratio	31.3	31.7	32.0	32.0	32.0
Balance sheet ratios					
Current ratio (x)	1.7	1.1	1.0	1.1	1.3
Asset turnover (x)	0.1	0.1	0.2	0.2	0.2
Net cash (RMB mn)	907	255	323	962	1,310
Returns (%)					
Adj. ROAE	13.3	10.9	13.5	15.9	16.4
Adj. ROAA	4.6	4.9	5.8	7.2	8.0
Per share data					
Adj. EPS (RMB)	0.056	0.071	0.097	0.128	0.149
DPS (RMB)	0.015	0.023	0.031	0.041	0.048
BVPS (RMB)	0.624	0.684	0.759	0.856	0.964

Source: Company data, CMBIS estimates

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