

Beststudy Education (3978 HK)

Benefit from accelerating industry consolidation

Despite short-term business disruption by COVID-19, we expect this could accelerate industry consolidation and provide the Company with M&A opportunities. The Company would benefit from increasing tutoring demand in the Greater Bay Area. After 25%/1% earnings cut in FY20/21E, our TP is adjusted from HK\$5.16 to HK\$5.14, representing 18.7x average FY20E and FY21E EPS (vs 18.7x FY20E P/E previously). Maintain Buy.

- **COVID-19 impact.** The Company suspended all offline classes as required by government and switched them to online teaching given that it has online teaching systems. The conversion rate of winter-break classes from offline to online was satisfactory at 85%, while the withdrawal rate was 4.2%. For spring semester classes, the conversion rate was 82%, similar to 83% in 2019, while the withdrawal rate was 2.5%.
- **Accelerating industry consolidation.** Guangdong's K12 after-school tutoring sector is fragmented with top five players accounting for 7.6% market share in 2018. Given that certain small industry players do not have online teaching capability, we expect these players could be forced to exit due to cash flow problems. In addition, the Company could make acquisitions to expand its school network thanks to its strong cash position (RMB1.3bn cash and investments at end of FY19). The Company had track record in establishing its presences in Shanghai, Jiangsu and Zhuhai through acquisitions. Therefore, we think the Company could benefit from accelerating industry consolidation.
- **FY20E outlook.** Various provinces have announced K12 school reopening dates. We expect Guangdong could follow this month and after-school tutoring services could be resumed after school reopening. Tuition hours of summer-break classes could be shortened as Gaokao and Zhongkao are delayed by one month. We expect FY20E GPM to decline due to slowing revenue growth. Number of centers opening will be reduced to around 20 due to COVID-19 disruption and accelerated promotion of OMO education. Because of high conversion rate (93%) of individualized tutoring from offline to online winter-break classes, planned openings of individualized tutoring centers are reduced.
- **FY19 results beat.** Adj. NP jumped 62% to RMB166mn, 10%/5% above our estimates/profit alert's guidance of 30%+ adj. NP growth. The results beat was mainly due to 0.8ppt stronger-than-expected GPM. Revenue +24% in line. SG&A and research expenses ratio fell 1.0ppt and 2.6ppt, respectively, thanks to operating leverage. Effective tax rate lowered from 32% in FY18? to 14% in FY19? as Guangzhou Beststudy obtained high-tech enterprise qualification.
- **Maintain Buy.** We lowered FY20/21E adj. net profit estimates by 25%/1% to reflect COVID-19 impact and stronger-than-expect FY19 GPM. Our TP is revised from HK\$5.16 to HK\$5.14, representing 18.7x average FY20E and FY21E EPS. **Catalysts:** (1) better-than-expected student enrollment; (2) M&A. **Risks:** (1) uncertainties from COVID-19; (2) teacher cost pressure; (3) government policies.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	1,474	1,832	2,049	2,667	3,252
YoY growth (%)	29	24	12	30	22
Adj. net profit (RMB mn)	102	166	158	261	324
Adj. EPS (RMB)	0.15	0.20	0.19	0.31	0.38
YoY growth (%)	N/A	28	(4)	65	24
Consensus EPS (RMB)	N/A	N/A	0.23	0.30	0.38
Adj. P/E (x)	19.6	16.0	17.0	10.3	8.3
Yield (%)	0.0	1.9	1.8	2.9	3.6
P/B (x)	4.1	3.3	3.0	2.4	2.0

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price **HK\$5.14**
 (Previous TP **HK\$5.16**)
 Up/Downside **+45%**
 Current Price **HK\$3.54**

China Education Sector

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Stock Data

Mkt Cap (HK\$ mn)	3,008
Avg 3 mths t/o (HK\$ mn)	4.51
52w High/Low (HK\$)	5.05/ 1.70
Total Issued Shares (mn)	849.7

Source: Bloomberg

Shareholding Structure

Junjing Tang	20.1%
Junying Tang	16.9%
Gui Zhou	16.7%

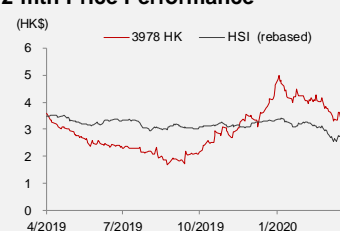
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-11.7%	-2.8%
3-mth	-13.7%	2.6%
6-mth	70.2%	85.0%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: EY

Related Reports

1. "Beststudy Education – Takeaways from Investor Day" – 9 Jan 2020
2. "Beststudy Education – Worst behind; expect strong recovery in 2H19E" – 30 Sep 2019
3. "Beststudy Education – FY18 beat with network expansion accelerated" – 15 Mar 2019

Figure 1: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	2,049	2,667	3,252	2,264	2,762	na	-10%	-3%	na
Gross Profit	836	1,107	1,356	924	1,124	na	-10%	-2%	na
Operating Profit	211	323	393	275	341	na	-23%	-5%	na
Adj. net profit	158	261	324	210	263	na	-25%	-1%	na
Gross Margin	40.8%	41.5%	41.7%	40.8%	40.7%	na	flat	+0.8ppt	na
Operating Margin	10.3%	12.1%	12.1%	12.2%	12.3%	na	-1.9ppt	-0.2ppt	na
Adj. Net Margin	7.7%	9.8%	10.0%	9.3%	9.5%	na	-1.6ppt	+0.3ppt	na

Source: Company data, CMBIS estimates

Figure 2: CMBIS estimates vs consensus

RMB mn	CMBIS			Consensus			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	2,049	2,667	3,252	2,242	2,848	3,279	-9%	-6%	-1%
Gross Profit	836	1,107	1,356	910	1,159	1,377	-8%	-5%	-2%
Operating Profit	211	323	393	236	327	na	-11%	-1%	na
Adj. Net profit	158	261	324	191	281	322	-17%	-7%	1%
Gross Margin	40.8%	41.5%	41.7%	40.6%	40.7%	42.0%	+0.2ppt	+0.8ppt	-0.3ppt
Operating Margin	10.3%	12.1%	12.1%	10.5%	11.5%	na	-0.2ppt	+0.6ppt	na
Adj. Net Margin	7.7%	9.8%	10.0%	8.5%	9.9%	9.8%	-0.8ppt	-0.1ppt	+0.2ppt

Source: Bloomberg, CMBIS estimates

Figure 3: FY19 results review

Y/E Dec (RMBmn)	FY19	FY18	Change (%)	Remarks
Revenue	1,831.7	1,473.7	24	tutoring hours +14%, ASP +9%
Cost of sales	(1,064.0)	(875.7)	22	
Gross profit	767.6	598.0	28	
Other income	18.8	6.6	183	
Investment income	0.0	0.2	(99)	
Selling expenses	(162.7)	(130.4)	25	
Research and development expenses	(165.5)	(170.7)	(3)	
Administrative expenses	(212.2)	(185.8)	14	adjustment of employees' packages
Other expenses	(44.7)	(43.5)	3	
Operating profit	201.5	74.3	171	
Finance costs	(48.0)	0.0	na	HKFRS 16 lease liabilities interest
FV gain of investments	36.9	34.5	7	mainly from wealth management products
Share award expenses	(30.1)	0.0	na	
Share of loss of associates and JVs	(3.5)	(1.1)	225	
Profit before taxation	156.8	107.8	46	
Taxation	(21.9)	(34.7)	(37)	Guangzhou Beststudy obtained high-tech enterprise qualification
Profit from discontinued operations	0.0	0.9	(100)	
Profit for the year	134.9	74.0	82	
Non-controlling interests	0.7	(19.1)	(103)	
Profit attributable to shareholders	135.5	54.9	147	
Adjusted net profit	165.7	102.2	62	
Margin & Ratio (%)				
GPM	41.9	40.6	1.3	maturing of centers opened in 2018
OPM	11.0	5.0	6.0	
Selling expenses/revenue	8.9	8.9	0.0	
Research expenses/revenue	9.0	11.6	(2.6)	
Administrative expenses/revenue	11.6	12.6	(1.0)	
NPM	7.4	3.7	3.7	
Adjusted NPM	9.0	6.9	2.1	
Student retention rate	83.0	84.2	(1.2)	
Full class rate	64.1	64.7	(0.6)	

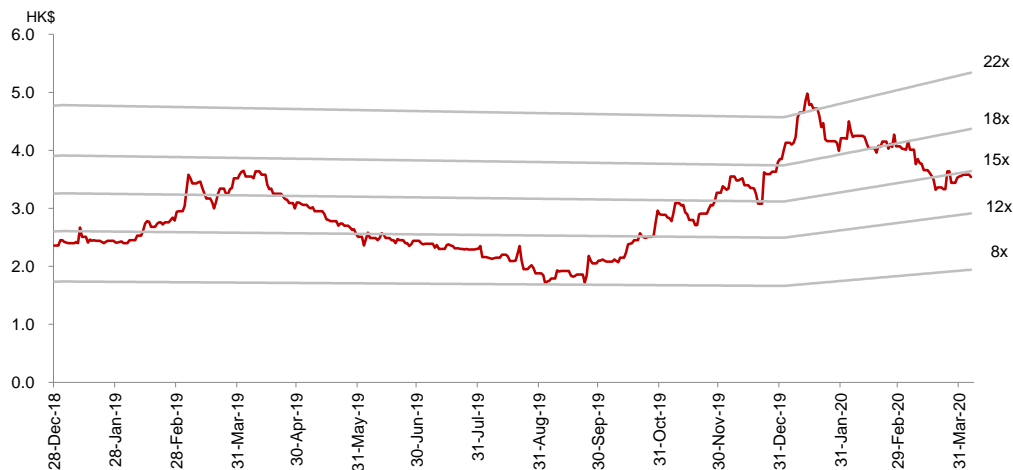
Source: Company, CMBIS estimates

Figure 4: Peers valuation

		Mkt Cap		Year	P/E (x)			PEG (x)	Adj. net profit growth (%)			Adj. EPS growth (%)			Revenue growth (%)		
	Ticker	(US\$ m)	Price	end	FY1	FY2	FY3	FY1	FY1	FY2	FY3	FY1	FY2	FY3	FY1	FY2	FY3
K12 tutoring services providers																	
New Oriental Education	EDU US	17,586	111.00	May-20	23.4	17.8	12.3	0.63	44	30	48	43	32	44	32	26	22
TAL Education	TAL US	31,812	53.76	Feb-20	52.6	34.6	26.5	0.53	255	48	na	161	52	31	40	35	37
Onesmart Education	ONE US	801	4.95	Aug-19	18.2	12.7	9.5	0.04	26	45	34	1,977	43	34	18	24	18
Scholar Education	1769 HK	722	10.08	Dec-19	32.4	24.6	18.3	0.81	70	36	35	48	32	34	26	38	37
Beststudy Education	3978 HK	388	3.54	Dec-19	16.9	10.0	8.1	0.61	(4)	69	24	(4)	69	24	12	30	22
Average					28.7	19.9	15.0	0.53	78	46	35	445	46	33	26	30	27
Average - excl Beststudy					31.7	22.4	16.7	0.50	99	40	39	557	40	36	29	31	28
Non-formal vocational education services provider																	
China East Education	667 HK	3,313	11.72	Dec-19	21.9	17.2	14.7	0.99	17	28	16	17	28	16	12	19	13
K12 education services providers																	
Wisdom Education	6068 HK	623	2.36	Aug-19	9.6	7.5	6.2	0.34	28	30	20	29	28	20	19	23	20
Tianli Education	1773 HK	926	3.46	Dec-19	17.2	15.0	13.1	0.63	30	24	18	41	15	14	29	25	16
Maple Leaf	1317 HK	892	2.31	Aug-19	7.8	7.1	7.1	0.50	18	16	17	22	10	(1)	15	15	13
Bright Scholar	BEDU US	811	6.73	Aug-19	14.3	12.3	10.9	0.65	55	16	16	28	16	13	57	11	11
Virscend Education	1565 HK	637	1.60	Dec-19	na	na	na	na	na	na	na	na	na	na	na	na	na
Average					12.2	10.5	9.3	0.53	33	21	18	30	17	12	30	19	15
Higher Education services providers																	
China Education	839 HK	2,788	10.70	Aug-19	21.7	18.7	15.7	1.16	22	23	22	22	16	20	33	15	13
Yuhua Education	6169 HK	2,468	5.73	Aug-19	17.3	15.2	13.4	0.65	111	16	11	40	14	13	42	8	8
Hope Education	1765 HK	1,549	1.80	Dec-19	16.6	12.6	10.8	0.48	37	32	16	37	32	16	31	42	11
Minsheng Education	1569 HK	539	1.04	Dec-19	8.5	7.3	6.8	0.37	32	14	7	31	16	9	21	14	7
Kepei Education	1890 HK	1,068	4.14	Dec-19	12.5	10.3	9.1	0.48	31	20	17	31	22	13	29	23	15
Xinhua Education	2779 HK	434	2.09	Dec-19	9.4	8.5	7.8	0.97	8	11	9	8	11	9	14	11	9
New Higher Education	2001 HK	602	3.03	Dec-19	8.2	7.0	6.1	0.36	33	20	17	29	18	15	27	16	15
Edvantage	382 HK	583	4.44	Aug-19	12.7	10.5	9.1	0.98	43	22	20	5	22	15	18	18	16
Chunlai Education	1969 HK	238	1.54	Aug-19	na	na	na	na	na	na	na	na	na	na	na	na	na
Average					13.4	11.3	9.8	0.68	40	20	15	25	19	14	27	19	12

Source: Bloomberg, CMBIS estimates

Figure 5: P/E band chart



Source: Company data, CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	1,474	1,832	2,049	2,667	3,252
Premium Learning	1,302	1,617	1,806	2,386	2,934
Elite Talent	40	56	62	79	92
Full-time Test Preparation	130	157	179	201	224
Others	3	2	2	2	2
Cost of sales	(876)	(1,064)	(1,213)	(1,560)	(1,896)
Gross profit	598	768	836	1,107	1,356
Other income	7	19	14	19	25
Selling expenses	(130)	(163)	(213)	(296)	(390)
Administrative expenses	(186)	(212)	(246)	(307)	(377)
R&D expenses	(171)	(165)	(180)	(200)	(221)
Other expenses	(44)	(45)	0	0	0
Operating profit	74	201	211	323	393
Fair value gains	35	37	31	31	31
Finance costs	0	(48)	(46)	(39)	(35)
Share of asso and JVs	(1)	(3)	(10)	(10)	(10)
Pre-tax profit	108	187	185	305	379
Income tax	(35)	(22)	(26)	(43)	(53)
Less: Minority interests	19	(1)	1	2	2
Net profit	55	136	158	261	324
Adjusted net profit	102	166	158	261	324

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19E	FY20E	FY21E	FY22E
Profit before tax	109	157	185	305	379
Depreciation and amortization	44	73	80	77	72
Change in working capital	119	228	190	210	224
Others	(70)	221	183	136	112
Net cash from operating	202	679	638	728	787
Capex	(152)	(112)	(60)	(80)	(80)
Change of investments	52	18	31	31	31
Others	39	(34)	0	0	0
Net cash from investing	(61)	(128)	(29)	(49)	(49)
Equity raised	258	44	0	0	0
Dividend paid	(100)	0	(57)	(48)	(78)
Others	(1)	(178)	(211)	(184)	(171)
Net cash from financing	158	(134)	(268)	(231)	(249)
Net change in cash	298	416	341	448	489
Cash at the beginning	170	468	884	1,225	1,672
Exchange difference	0	0	0	0	0
Cash at the end	468	884	1,225	1,672	2,161
Cash at balance sheet	468	884	1,225	1,672	2,161
Cash at discontinued op.	0	0	0	0	0

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	302	1,476	1,319	1,233	1,162
PPE	161	202	185	190	200
Right-of-use assets	0	894	766	688	619
Asso & JV	21	76	66	56	46
Others	121	305	302	300	298
Current assets	1,137	1,289	1,636	2,091	2,588
Cash	468	196	537	985	1,473
Short-term investments	518	880	880	880	880
Prepayments	148	140	147	154	162
Others	4	72	72	72	72
Current liabilities	776	1,235	1,447	1,670	1,906
Contract liabilities	563	775	986	1,191	1,406
Other payables	192	200	224	262	302
Tax payables	21	34	34	34	34
Others	0	226	203	183	165
Non-current liabilities	41	733	608	540	483
Lease liabilities	0	733	608	540	483
Rental payables	41	0	0	0	0
Total net assets	622	797	900	1,114	1,362
Shareholders' equity	623	797	899	1,112	1,358
Minority Interest	(1)	(1)	0	2	4

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Premium Learning	88.3	88.3	88.2	89.4	90.2
Elite Talent	2.7	3.1	3.0	3.0	2.8
Full-time Test Preparatory	8.8	8.5	8.7	7.5	6.9
Others	0.2	0.1	0.1	0.1	0.1
P&L ratios (%)					
Gross profit margin	40.6	41.9	40.8	41.5	41.7
OP margin	5.0	11.0	10.3	12.1	12.1
Effective tax rate	32.2	14.0	14.0	14.0	14.0
Adj. net profit margin	6.9	9.0	7.7	9.8	10.0
Payout ratio	N/A	41.8	30.0	30.0	30.0
Balance sheet ratios					
Current ratio (x)	1.5	1.0	1.1	1.3	1.4
Asset turnover (x)	1.0	0.7	0.7	0.8	0.9
Net cash (RMB mn)	470	252	592	1,040	1,529
Returns (%)					
Adj. ROAE	23.3	23.3	18.7	25.9	26.2
Adj. ROAA	8.2	7.9	5.5	8.3	9.2
Per share data					
Adj. EPS (RMB)	0.15	0.20	0.19	0.31	0.38
DPS (RMB)	N/A	0.06	0.06	0.09	0.11
BVPS (RMB)	0.73	0.94	1.06	1.31	1.60

Source: Company data, CMBIS estimates

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