

Wisdom Education (6068 HK)

Tuition fees increase beat; lift TP to HK\$6.38

2020-21 tuition fees increase was stronger than expected. We raised FY20-22E EPS by 3-9% and lifted our TP from HK\$4.60 to HK\$6.38. Trading at 15.5x FY20E P/E, the Company's valuation is lower than K12 peers' average of 21.2x. At 29.7% EPS CAGR from FY20E to FY22E (higher than peers' average of 17%), its 0.52x PEG is far below peers' average of 1.25x. We think the Company's low valuation is attractive and unjustified. Maintain Buy.

- **2020-21 school year tuition fees increases beat.** The Company will increase tuition and boarding fees of new students in 8 schools by 9-38%, better than our estimates of 10-15% increase in 5 schools. Key schools such as Dongguan Guangming, Dongguan Guangzheng and Huizhou school were covered. The fees increase was also stronger than previous big tuition fee year in FY19 (5-28% in 5 schools). We estimate avg. ASP to increase by low-teens in FY21E (vs +5% in 1H20), stronger than the 8% growth in FY19 when two Dongguan schools raised fees for all sections.
- **Entry to higher education a re-rating catalyst.** The Company plans to form a JV with HIT Big Data to be the sponsor of the Dongguan Guangzheng Institute of Technology ("DGIT"). The project is supported by Dongguan authority according to management. We think the stock deserves re-rating as the entry to higher education could diversify operation risks, lower policy risks (higher education institutes can choose for-profit). Companies operate both K12 and higher education (Yuhua (6169 HK) and Virscend (1565 HK)) trade at higher P/E and PEG than the Company (Figure 3).
- **Redemption of Ping An CB avoids 6% dilution.** Recently, the EGM voted against the issue of new shares for the conversion of CBs. Conversion prices of HK\$200mn mandatory CB and HK\$100mn discretionary CB is set at 20% and 10% discount of average closing price of the 90 trading days before 16 Jul 2020 (HK\$2.89, equal to 15.1x FY19 P/E), respectively. Share conversion at low valuation was avoided. The Company will repay the CB by financing and internal cash.
- **Maintain Buy.** We trimmed FY20E net profit est. by 2% to reflect boarding fees refund, but raised FY21/22E net profit est. by 4/5% mainly to factor in higher tuition fees growth. Our FY20/21/22E EPS is lifted by 3%/7%/9% because of redemption of CB. Our TP is upped from HK\$4.60 to HK\$6.38, based on 18.4x FY21E P/E (rolled forward from 18x FY20E P/E). **Catalysts:** (1) better-than-expected student enrolment or tuition fee growth; (2) gov't approval of DGIT; (3) removal of policy overhang. **Risks:** (1) policy risks; (2) lower-than-expected student enrolment; (3) surge of teachers' costs.

Earnings Summary

(YE 31 Aug)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	1,247	1,682	1,799	2,381	2,846
YoY growth (%)	27	35	7	32	20
Net profit (RMB mn)	310	359	465	637	782
EPS (RMB)	0.152	0.172	0.227	0.311	0.382
YoY growth (%)	38	13	32	37	23
Consensus EPS (RMB)	na	na	0.237	0.289	0.339
P/E (x)	21.5	20.5	15.5	11.3	9.2
Yield (%)	2.0	2.5	2.6	3.5	4.3
P/B (x)	3.5	3.3	2.9	2.5	2.1
Net gearing (%)	47	66	58	48	40

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price	HK\$6.38
(Previous TP	HK\$4.60)
Up/Downside	+62%
Current Price	HK\$3.93

China Education Sector

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Stock Data

Mkt Cap (HK\$ mn)	8,045
Avg 3 mths t/o (HK\$ mn)	13.58
52w High/Low (HK\$)	4.33/ 2.10
Total Issued Shares (mn)	2,047.2

Source: Bloomberg

Shareholding Structure

Mr. Liu Xuebin	45.43%
Ms. Li Suwen	27.84%

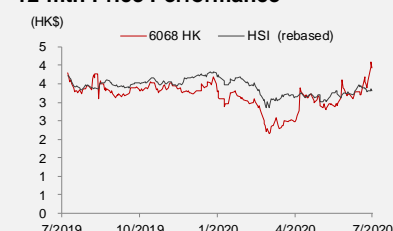
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	21.7%	17.0%
3-mth	64.3%	52.5%
6-mth	24.3%	35.7%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Deloitte

Related Reports

1. "Wisdom Education – Explore new business opportunities" – 29 Apr 2020
2. "Wisdom Education – Explore asset-light model to enhance return" – 27 Nov 2019
3. "Wisdom Education – Student enrollment missed but organic growth still strong" – 9 Sep 2019

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Entry to higher education a re-rating catalyst

Background information

The Company has planned to establish Dongguan Guangzheng Institute of Technology (东莞光正科技学院) in Dongguan to train talents in areas of big data, robotics, smart manufacturing and artificial intelligence. The Company has entered a cooperative agreement with each of Harbin Institute of Technology (‘‘HIT’’) (哈尔滨工业大学) and HIT Big Data Group (哈工大大数据集团) respectively. HIT Big Data Group will be responsible for the design of the curriculum, syllabus and teaching plan, as well as the formation of professional teaching team, of the Institute.

Supported by Dongguan authority

HIT Big Data Group is invested by Harbin government and HIT. HIT is a 985 university, which is ranked 16th among universities in China according to www.cuaa.net. According to management, the junior college project is supported by Dongguan authority to enhance higher education quality of the city. Dongguan authority will find a suitable site for the college. The Company and HIT Big Data Group will form a JV to be the sponsor of the college, while the Company expects it to have majority stakes in the JV. When the site is secured, the JV would apply for the establishment of the college.

Re-rating catalyst

Firstly, the entry into higher education could diversify the operation risks of the Company. Secondly, higher education institution can opt for for-profit school, where we think its risk profile is lower than compulsory education. Thirdly, companies operate both K12 and higher education (Yuhua (6169 HK) (17.9x FY21E P/E) and Virscend (1565 HK) (12.6x FY21E P/E) trade at higher multiple than the Company. The valuation of higher education sector (companies with market cap >US\$1bn trade at 17.6x FY21E P/E) is higher than Wisdom Education (11.3x FY21E P/E). This could be a re-rating catalyst to the Company.

Figure 1: Earnings revision

US\$ mn	New			Old			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,799	2,381	2,846	1,832	2,376	2,854	-2%	0%	0%
Gross Profit	807	1,136	1,364	830	1,105	1,312	-3%	3%	4%
Operating Profit	631	818	989	636	785	938	-1%	4%	5%
Net profit	465	637	782	475	615	745	-2%	4%	5%
Gross Margin	44.8%	47.7%	47.9%	45.3%	46.5%	46.0%	-0.5ppt	+1.2ppt	+1.9ppt
Operating Margin	35.1%	34.3%	34.8%	34.7%	33.1%	32.9%	+0.4ppt	+1.2ppt	+1.9ppt
Net Margin	25.8%	26.8%	27.5%	25.9%	25.9%	26.1%	-0.1ppt	+0.9ppt	+1.4ppt

Source: CMBIS estimates

Figure 2: CMBIS estimates vs consensus

US\$ mn	CMBIS			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,799	2,381	2,846	1,899	2,325	2,648	-5%	2%	7%
Gross Profit	807	1,136	1,364	862	1,081	1,235	-6%	5%	10%
Operating Profit	631	818	989	624	749	871	1%	9%	14%
Net profit	465	637	782	492	593	687	-5%	7%	14%
Gross Margin	44.8%	47.7%	47.9%	45.4%	46.5%	46.6%	-0.6ppt	+1.2ppt	+1.3ppt
Operating Margin	35.1%	34.3%	34.8%	32.9%	32.2%	32.9%	+2.2ppt	+2.1ppt	+1.9ppt
Net Margin	25.8%	26.8%	27.5%	25.9%	25.5%	25.9%	-0.1ppt	+1.3ppt	+1.6ppt

Source: Bloomberg estimates, CMBIS estimates

Figure 3: Peers valuation table

	Ticker	Rating	Mkt Cap (US\$ m)	Cnncy	Price	Year end	FY1	FY2	FY3	Adj. EPS growth (%)	PEG (x)	Revenue growth (%)	FY1	FY2	FY3	
K12 tutoring services providers																
New Oriental Education	EDU US	NR	23,273	USD	146.90	May-20	35.7	26.3	17.1	34	36	54	0.80	26	30	31
TAL Education	TAL US	NR	47,096	USD	78.45	Feb-20	93.1	55.1	37.7	8,330	69	46	1.63	37	39	35
Onesmart Education	ONE US	NR	753	USD	4.64	Aug-19	na	14.4	10.1	(231)	na	41	na	(13)	51	18
Scholar Education	1769 HK	NR	1,199	HKD	16.72	Dec-19	52.6	40.0	29.4	51	31	36	1.56	27	37	37
Beststudy Education	3978 HK	Buy	337	HKD	3.07	Dec-19	14.7	8.7	7.0	(4)	69	24	0.33	12	30	22
Average							49.0	28.9	20.3	1,636	51	40	1.08	18	38	28
Non-formal vocational education services provider																
China East Education	667 HK	Buy	5,362	HKD	18.96	Dec-19	35.4	27.8	23.9	17	28	16	1.62	12	19	13
K12 education services providers																
Tianli Education	1773 HK	NR	1,898	HKD	7.09	Dec-19	36.6	30.5	26.7	39	20	14	2.14	29	25	16
Maple Leaf	1317 HK	NR	1,001	HKD	2.59	Aug-19	10.9	9.1	8.3	(3)	19	11	0.74	5	26	11
Bright Scholar	BEDU US	NR	1,046	USD	8.70	Aug-19	21.5	15.8	13.8	10	36	14	0.87	33	23	11
Virscend Education	1565 HK	NR	921	HKD	2.31	Dec-19	16.0	12.6	10.2	0	27	24	1.27	16	26	17
Wisdom Education	6068 HK	Buy	1,038	HKD	3.93	Aug-19	15.5	11.3	9.2	32	37	23	0.52	7	32	20
Average							20.1	15.9	13.6	16	28	17	1.11	18	27	15
Sector average excluding Wisdom							21.2	17.0	14.7	12	26	16	1.25	21	25	14
Higher Education services providers																
China Education	839 HK	NR	3,727	HKD	14.30	Aug-19	28.3	23.5	19.5	23	21	20	1.39	36	15	14
Yuhua Education	6169 HK	NR	3,132	HKD	7.27	Aug-19	26.3	17.9	15.7	2	47	14	0.89	45	12	8
Hope Education	1765 HK	Buy	2,310	HKD	2.65	Aug-19	27.1	19.7	15.4	na	38	28	0.83	na	39	27
Kepei Education	1890 HK	NR	1,642	HKD	6.36	Dec-19	18.8	15.6	13.7	34	21	14	1.09	29	22	14
New Higher Education	2001 HK	NR	1,038	HKD	5.22	Dec-19	13.9	11.5	9.9	32	21	17	0.74	27	17	14
Edvantage	382 HK	NR	830	HKD	6.32	Aug-19	19.1	14.9	12.1	(1)	28	23	0.75	16	17	20
Minsheng Education	1569 HK	NR	577	HKD	1.06	Dec-19	8.9	7.5	6.8	10	18	11	0.62	19	14	12
Xinhua Education	2779 HK	Buy	494	HKD	2.38	Dec-19	10.7	9.6	8.8	8	11	9	1.07	14	11	9
Huali University	1756 HK	NR	474	HKD	3.06	Aug-19	10.8	8.6	6.9	21	25	25	0.43	18	18	18
Average							18.2	14.3	12.1	16	25	18	0.87	26	18	15

Source: Bloomberg estimates, CMBIS estimates

Figure 4: 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, CMBIS estimates

Figure 5: 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 6: New projects provide at least 15,500 student capacity

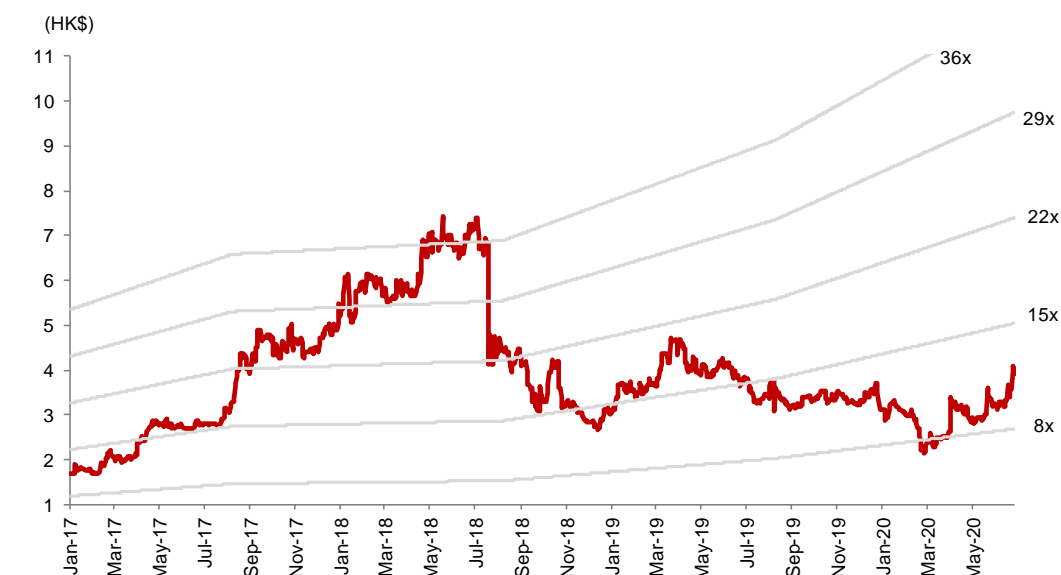
Location	Expected year of opening	Target max. capacity
Dongguan/Foshan (light asset projects)	Sep-20	TBC
Chaozhou, Guangdong	Sep-21	8,000
Jiangmen, Guangdong	Sep-21	7,500
Guangzhou, Guangdong	TBC	TBC
Zhaoqing, Guangdong	TBC	TBC
Total		15,500

Source: Company data, CMBIS

Figure 7: 12% 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	11,000	11,980	11%
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	4,269	4,419	-4%
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	1,100	1,750	89%
Kaiping School						700	na
Chaozhou School						700	na
Total	31,788	43,230	54,420	60,116	66,849	75,386	12%

Source: Company data, CMBIS estimates

Figure 8: P/E band

Source: Bloomberg, Company data, CMBIS estimates

Figure 9: Key assumptions

Year-end Aug 31 (RMB mn)	FY18	FY19	FY20E	FY21E	FY22E
Total revenue	1,247	1,682	1,799	2,381	2,846
growth %	27.3%	34.9%	7.0%	32.3%	19.5%
<i>Tuition and boarding fees</i>	<i>841</i>	<i>1,145</i>	<i>1,308</i>	<i>1,698</i>	<i>2,052</i>
growth %	25.3%	36.2%	14.2%	29.8%	20.9%
<i>Others</i>	<i>406</i>	<i>536</i>	<i>492</i>	<i>683</i>	<i>794</i>
growth %	31.7%	32.1%	-8.3%	39.0%	16.2%
Gross profit margin	43.7%	44.1%	44.8%	47.7%	47.9%
Selling expenses ratio	1.6%	1.5%	1.2%	1.1%	1.1%
Administrative expenses ratio	17.7%	15.0%	14.8%	13.9%	13.7%
Operating profit margin	28.9%	29.5%	35.1%	34.3%	34.8%
Effective tax rate	11.1%	13.6%	16.0%	14.0%	14.0%
Net profit	310	359	465	637	782
growth %	55.0%	15.8%	29.4%	37.0%	22.8%
Payout ratio	43.5%	39.4%	40.0%	40.0%	40.0%
Average tuition and boarding fee (RMB)	19,893	21,049	21,754	25,395	27,220
growth %	-5.8%	8.2%	3.4%	16.7%	7.2%
Student enrollment	43,230	54,420	60,116	66,849	75,386
growth %	36.0%	25.9%	10.5%	11.2%	12.8%

Source: Company data, CMBIS estimates

Financial Summary

Income statement

YE 31 Aug (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	1,247	1,682	1,799	2,381	2,846
Tuition & boarding fees	841	1,145	1,308	1,698	2,052
Ancillary services	406	536	492	683	794
Cost of sales	(702)	(940)	(992)	(1,245)	(1,482)
Gross profit	545	742	807	1,136	1,364
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)	(266)	(332)	(388)
EBIT	360	496	631	818	989
Finance costs, net	(11)	(87)	(95)	(100)	(105)
Listing expenses	0	0	0	0	0
FV change of inv. prop.	(3)	1	0	0	0
Pre-tax profit	346	409	536	718	884
Income tax	(38)	(56)	(86)	(100)	(124)
Less: Minority interests	(3)	(6)	(15)	(20)	(22)
Net profit	310	359	465	637	782

Cash flow summary

YE 31 Aug (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before tax	346	409	536	718	884
Depreciation and amortization	106	149	171	176	193
Change in working capital	191	(1)	267	245	282
Others	(19)	19	(48)	5	(39)
Net cash from operating	623	577	926	1,144	1,320
Capex & investments	(743)	(904)	(750)	(750)	(750)
Acquisitions	(267)	(70)	0	0	0
Others	(338)	(32)	159	17	(82)
Net cash from investing	(1,349)	(1,006)	(591)	(733)	(832)
Equity raised	3	3	0	0	0
Change of borrowings	1,485	462	(305)	100	100
Dividend paid	(122)	(155)	(173)	(218)	(282)
Others	(118)	(141)	(128)	(133)	(138)
Net cash from financing	1,248	169	(607)	(251)	(320)
Net change in cash	522	(260)	(272)	160	167
Cash at the beginning of the year	378	911	662	391	551
Exchange difference	11	11	0	0	0
Cash at the end of the year	911	662	391	551	718

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	4,003	4,676	5,648	6,222	6,779
PPE	2,492	3,036	3,658	4,266	4,853
Prepaid lease payments	502	781	0	0	0
Deposits	520	631	631	631	631
Others	489	228	182	176	172
Current assets	1,468	1,595	1,217	1,412	1,708
Cash	911	662	391	551	718
Pledged deposit	282	499	499	499	499
Prepayments	162	97	104	137	164
Others	113	337	224	225	327
Current liabilities	1,643	2,480	2,300	2,592	2,891
Borrowings	282	1,108	629	629	629
Contract liabilities	617	751	982	1,182	1,411
Trade and other payables	616	503	546	627	709
Others	128	118	118	129	118
Non-current liabilities	1,851	1,545	2,035	2,110	2,186
Borrowings	1,847	1,540	1,740	1,840	1,940
Deferred revenue	0	0	0	0	0
Others	4	4	4	4	4
Total net assets	1,977	2,247	2,530	2,932	3,410
Shareholders' equity	1,911	2,161	2,460	2,882	3,382
Minority Interest	66	86	71	51	29

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Tuition & boarding fees	67.5	68.1	72.7	71.3	72.1
Ancillary services	32.5	31.9	27.3	28.7	27.9
Total	100.0	100.0	100.0	100.0	100.0
P&L ratios (%)					
Gross profit margin	43.7	44.1	44.8	47.7	47.9
EBIT margin	28.9	29.5	35.1	34.3	34.8
Effective tax rate	11.1	13.6	16.0	14.0	14.0
Net profit margin	24.9	21.4	25.8	26.8	27.5
Payout ratio	43.5	39.4	40.0	40.0	40.0
Balance sheet ratios					
Current ratio (x)	0.9	0.6	0.5	0.5	0.6
Asset turnover (x)	0.2	0.3	0.3	0.3	0.3
Net gearing ratio (%)	47	66	58	48	40
Returns (%)					
ROAE	17.0	17.7	20.1	23.9	25.0
ROAA	7.0	6.0	6.9	8.5	9.4
Per share					
EPS (RMB)	0.15	0.17	0.23	0.31	0.38
DPS (HK\$)	0.08	0.10	0.10	0.14	0.17
BVPS (RMB)	0.94	1.06	1.20	1.41	1.65

Source: Company data, CMBIS estimates

Disclosures & Disclaimers

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