

Beststudy Education (3978 HK)

Worst behind; Expect strong recovery in 2H19E

We expect a better 2H19E with YoY rev/adj. NP growth of 24%/117% YoY because (1) revenue growth of small group tutoring is recovering and (2) loss-making online education business has been divested.

- **Satisfactory student admission in 2H19E.** Due to regulatory impact, YoY revenue growth for small group tutoring moderated from 33% in 2H18 to 22% in 1H19. That said, as regulatory impact faded, we expect YoY revenue growth to recover from 20% in 1H19 to 24% in 2H19E, and 2H19E full class rate to improve from 62.5% in 1H19.
- **Loss-making online education business divested.** The Company has been investing R&D and advertising for online small group tutoring and recorded RMB34mn expenses in 1H19, which eroded 4.0ppt OPM in 1H19. This business will rely on heavy investment to obtain online users traffic, which would put pressure on the Company's financial performance in short term. The Company has lowered its stake from 60% to 30% by introducing external investment in Aug to achieve balance for profitability. We expect overall OPM to improve significantly in 2H19E.
- **Education center expansion plan unchanged.** Though net openings was 18 in 1H19 (mainly in major cities in Greater Bay Area), management maintains its target of adding 40-50 centers in FY19E and 150 centers in 2018-2020E. According to Frost & Sullivan, number of students enrolled in K12 after-school tutoring in Guangdong was 5.5mn in 2018, only representing 28% of Guangdong's K12 formal education student number. Such penetration rate is lower than tier 1 cities' 62.9% in 2017. We think there is still large room for the Company to penetrate its school network.
- **1H19 after tax profit fell 9%.** Revenue rose 20% to RMB867mn, driven by 12% growth of tutoring hours and 7% tuition fee growth. GPM dropped 0.9ppt to 41.4% due to opening and renovation of new education centers. After tax profit fell 9% to RMB75mn due to after tax loss of RMB26mn incurred for online small group tutoring, RMB10mn reduced fair value gain on investments and RMB8mn cost for adoption of new IFRS 16.
- **Maintain Buy but lowered TP.** We revised down FY19/20/21E adj. net profit by 21%/5%/3% to reflect lower student enrollment, IFRS 16 impact and loss in online education. Our TP is changed from HK\$3.72 to HK\$3.41, representing 13.0x FY20E P/E, which is still at 20% discount to sector average but rolled forward. Valuation is undemanding as net cash and investments totaled RMB1.15bn as 30 Jun 2019, equivalent to 74% of market cap. **Catalysts:** (1) better-than-expected student enrollment; (2) M&A. **Risks:** (1) fierce competition; (2) teacher cost pressure; (3) government policies.

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (RMB mn)	1,142	1,474	1,798	2,209	2,672
YoY growth (%)	22	37	29	34	15
Adj. net profit (RMB mn)	90	102	131	200	249
YoY growth (%)	88	14	28	53	25
Adj. EPS (RMB)	N/A	0.15	0.15	0.24	0.29
YoY growth (%)	N/A	N/A	1	53	25
Adj. P/E (x)	N/A	11.3	12.0	7.8	6.3
Yield (%)	N/A	0.0	4.0	5.8	7.6
P/B (x)	N/A	2.4	2.0	1.7	1.4
Net cash (RMB mn)	162	470	697	986	1,314

Source: Company data, CMBIS estimates

BUY (Maintain)

Target Price	HK\$3.41
(Previous TP	HK\$3.72
Up/Downside	+66%
Current Price	HK\$2.05

China Education Sector

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Stock Data

Mkt Cap (HK\$ mn)	9,000
Avg 3 mths t/o (HK\$ mn)	9.38
52w High/Low (HK\$)	1.75/0.75
Total Issued Shares (mn)	6,666.7

Source: Bloomberg

Shareholding Structure

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

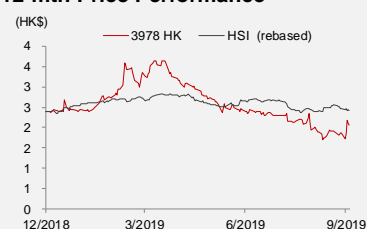
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	9.5%	19.8%
3-mth	27.8%	35.4%
6-mth	15.0%	28.1%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: EY

Related Reports

1. "Beststudy Education – FY18 beat with network expansion accelerated" – 15 Mar 2019
2. "Beststudy Education – Regional K12 tutoring leader surfing on booming demand" – 19 Feb 2019

Figure 1: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,798	2,209	2,672	1,844	2,309	2,860	-3%	-4%	-7%
Gross Profit	730	895	1,079	754	947	1,177	-3%	-6%	-8%
Operating Profit	170	258	319	182	235	295	-7%	10%	8%
Adj. net profit	131	200	249	165	211	258	-21%	-5%	-3%
Gross Margin	40.6%	40.5%	40.4%	40.9%	41.0%	41.2%	-0.3ppt	-0.5ppt	-0.8ppt
Operating Margin	9.4%	11.7%	12.0%	9.9%	10.2%	10.3%	-0.5ppt	+1.5ppt	+1.7ppt
Adj. Net Margin	7.3%	9.1%	9.3%	8.9%	9.2%	9.0%	-1.6ppt	-0.1ppt	+0.3ppt

Source: Company data, CMBIS estimates

Figure 2: CMBI estimates vs consensus

RMB mn	CMBI			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,798	2,209	2,672	1,797	2,182	2,633	0%	1%	1%
Gross Profit	730	895	1,079	724	877	1,053	1%	2%	2%
Operating Profit	170	258	319	183	240	305	-7%	8%	5%
Adj. Net profit	131	200	249	129	164	206	1%	22%	21%
Gross Margin	40.6%	40.5%	40.4%	40.3%	40.2%	40.0%	+0.3ppt	+0.3ppt	+0.4ppt
Operating Margin	9.4%	11.7%	12.0%	10.2%	11.0%	11.6%	-0.8ppt	+0.7ppt	+0.4ppt
Adj. Net Margin	7.3%	9.1%	9.3%	7.2%	7.5%	7.8%	+0.1ppt	+1.6ppt	+1.5ppt

Source: Company data, CMBIS estimates

Figure 3: Key assumptions

Total tutoring hours ('000)	FY17	FY18	FY19E	FY20E	FY21E	FY19-21E CAGR
Premium learning program	10,753	13,013	15,049	17,893	20,990	17%
Small group tutoring	8,725	10,728	12,434	14,894	17,575	18%
Individualized tutoring	2,028	2,285	2,616	2,999	3,414	14%
Elite talent program	426	550	686	790	862	16%
Total	11,180	13,563	15,735	18,684	21,851	17%

Revenue (RMB mn)	FY17	FY18	FY19E	FY20E	FY21E	FY19-21E CAGR
Premium Learning Program	1,013	1,302	1,602	1,991	2,432	23%
Small group tutoring	555	750	939	1,192	1,477	25%
Individualized tutoring	459	552	663	798	954	20%
Elite Talent Program	27	40	53	64	74	23%
Full-time Test Preparation Program	100	130	139	151	163	8%
Others	2	3	3	3	3	6%
Total	1,142	1,474	1,798	2,209	2,672	22%

YoY growth	FY17	FY18	FY19E	FY20E	FY21E
Premium Learning Program	29%	28%	23%	24%	22%
Small group tutoring	33%	35%	25%	27%	24%
Individualized tutoring	25%	20%	20%	20%	20%
Elite Talent Program	95%	48%	33%	22%	14%
Full-time Test Preparation Program	3%	30%	8%	8%	8%
Others		77%	20%	0%	0%
Total	27%	29%	22%	23%	21%

Share	FY17	FY18	FY19E	FY20E	FY21E
Premium Learning Program	89%	88%	89%	90%	91%
Small group tutoring	49%	51%	52%	54%	55%
Individualized tutoring	40%	37%	37%	36%	36%
Elite Talent Program	2%	3%	3%	3%	3%
Full-time Test Preparation Program	9%	9%	8%	7%	6%
Others	0%	0%	0%	0%	0%
Total	100%	100%	100%	100%	100%

Average tuition fee per hour (RMB)	FY17	FY18	FY19E	FY20E	FY21E	FY19-21E CAGR
Premium Learning Program						
Small group tutoring	64	70	76	80	84	6%
YoY Growth (%)	5%	9%	8%	6%	5%	
Individualized tutoring	226	241	253	266	279	5%
YoY Growth (%)	7%	7%	5%	5%	5%	
Elite Talent Program	63	72	77	82	86	6%
YoY Growth (%)	11%	14%	7%	6%	5%	

Average tuition fee per student (RMB)	FY17	FY18	FY19E	FY20E	FY21E	FY19-21E CAGR
Full-time Test Preparation Program	20,632	23,892	24,490	25,224	25,981	3%
YoY Growth (%)	1%	16%	2%	3%	3%	

Source: Company data, CMBIS estimates

Figure 4: 1H19 results review

Y/E Dec (RMBmn)	1H19	1H18	Change (%)
Revenue	867.4	723.1	20
Cost of sales	(508.6)	(417.2)	22
Gross profit	358.8	305.9	17
Other income	10.5	4.0	159
Investment income	0.0	0.2	(99)
Selling expenses	(60.7)	(54.9)	11
Research and development expenses	(82.3)	(78.7)	5
Administrative expenses	(95.8)	(79.0)	21
Other expenses	(38.0)	(16.5)	130
Operating profit	92.5	81.0	14
Finance costs	(25.1)	0.0	na
FV gain of investments	23.5	33.3	(30)
Share of loss of associates and JVs	(0.1)	(1.0)	(89)
Profit before taxation	90.7	113.3	(20)
Taxation	(15.5)	(31.4)	(51)
Profit from discontinued operations	0.0	0.9	(100)
Profit for the year	75.3	82.8	(9)
Non-controlling interests	0.5	(22.8)	(102)
Profit attributable to shareholders	75.8	60.1	26
Adjusted net profit	75.3	99.6	(24)
Margin & Ratio (%)			
GPM	41.4	42.3	(0.9)
OPM	10.7	11.2	(0.5)
Selling expenses/revenue	7.0	7.6	(0.6)
Research expenses/revenue	9.5	10.9	(1.4)
Administrative expenses/revenue	11.0	10.9	0.1
NPM	8.7	8.3	0.4
Adjusted NPM	8.7	13.8	(5.1)
Student retention rate	80.4	74.5	5.9
Full class rate	62.5	67.0	(4.5)

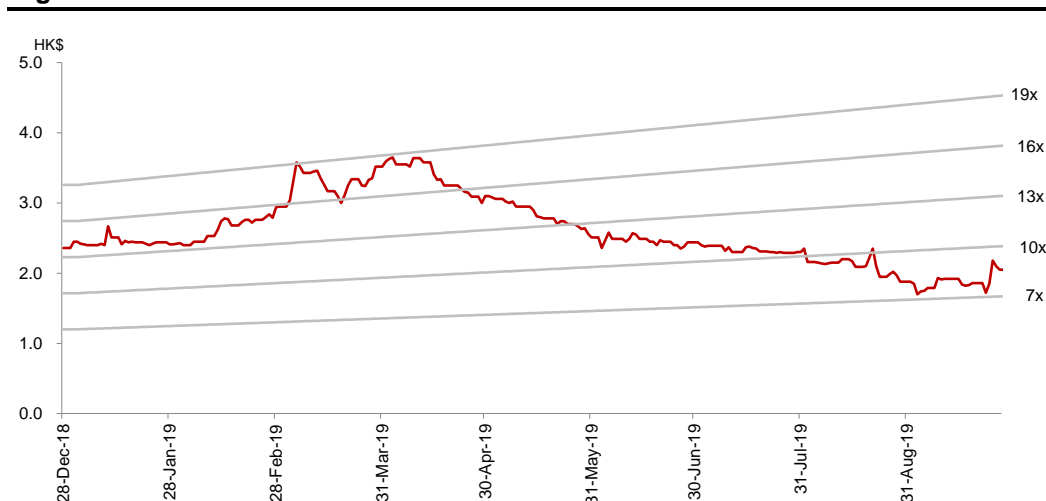
Source: Company data

Figure 5: Peers valuation

	Ticker	Mkt Cap (US\$ m)	Price	Year end	P/E (x)			Adj. net profit growth (%)			EPS growth (%)			PEG (x)	Revenue growth (%)			Yield (%)
					FY1	FY2	FY3	FY1	FY2	FY3	FY1	FY2	FY3	FY1	FY1	FY2	FY3	FY1
K12 tutoring services providers																		
New Oriental Education	EDU US	16,827	106.21	May-19	31.4	23.7	19.0	31	33	27	31	32	25	1.10	28	26	21	0.5
TAL Education	TAL US	19,983	33.77	Feb-19	49.5	31.6	22.4	(11)	63	43	(8)	57	41	1.02	34	33	32	0.0
Onesmart Education	ONE US	1,190	7.41	Aug-18	22.0	17.0	12.6	59	30	36	na	30	36	0.68	40	33	26	na
Scholar Education	1769 HK	566	7.99	Dec-18	39.2	26.9	21.7	59	31	24	na	46	24	1.14	40	43	26	0.0
Beststudy Education	3978 HK	222	2.05	Dec-18	12.0	7.8	6.3	28	53	25	1	53	25	0.31	22	23	21	4.0
Average					30.8	21.4	16.4	33	42	31	8	44	30	0.85	33	32	25	1.1
Average - excl Beststudy					35.5	24.8	18.9	35	39	33	12	41	31	0.98	35	34	26	0.2
Non-formal vocational education services provider																		
China East Education	667 HK	4,108	14.74	Dec-18	31.5	24.8	20.3	67	27	20	na	27	20	1.34	25	20	18	0.8
K12 education services providers																		
Wisdom Education	6068 HK	841	3.22	Aug-18	14.3	12.6	9.3	35	14	35	33	14	33	0.62	40	18	23	3.1
Tianli Education	1773 HK	807	3.05	Dec-18	20.8	15.8	12.6	28	37	32	na	32	26	0.73	36	36	34	1.5
Maple Leaf	1317 HK	944	2.47	Aug-18	10.3	8.8	7.4	18	18	19	15	17	19	0.57	22	19	18	4.0
Bright Scholar	BEDU US	1,176	9.45	Aug-18	23.1	20.5	17.7	42	33	15	45	13	16	1.62	40	35	13	0.0
Vircend Education	1565 HK	949	2.41	Dec-18	14.1	10.4	7.8	20	52	32	29	35	33	0.41	28	27	25	2.2
Average					16.5	13.6	10.9	28	31	27	30	22	25	0.79	33	27	23	2.2
Higher Education services providers																		
China Education	839 HK	2,994	11.62	Aug-18	27.9	22.5	18.9	na	23	19	na	24	19	1.30	na	24	13	1.0
Yuhua Education	6169 HK	1,705	4.07	Aug-18	17.1	13.7	12.0	18	29	16	13	25	14	0.88	37	31	8	2.9
Hope Education	1765 HK	1,012	1.19	Dec-18	15.0	10.9	8.5	50	38	25	28	38	25	0.48	29	34	15	2.0
Minsheng Education	1569 HK	676	1.32	Dec-18	11.6	9.7	8.1	22	19	21	22	20	19	0.59	59	23	18	0.4
Kepei Education	1890 HK	1,005	3.94	Dec-18	16.5	14.1	12.2	24	19	16	(6)	17	16	1.01	23	19	15	1.7
Xinhua Education	2779 HK	523	2.55	Dec-18	13.2	9.1	7.6	12	17	16	1	45	18	0.43	18	18	15	2.3
New Higher Education	2001 HK	596	3.03	Dec-18	10.8	8.4	7.1	31	28	17	28	28	18	0.47	89	25	14	2.6
Edvantage	382 HK	457	3.52	Aug-18	14.2	11.5	9.6	37	25	21	na	24	20	0.66	9	13	17	2.0
Chunlai Education	1969 HK	230	1.50	Aug-18	11.4	7.6	6.2	(4)	54	24	(14)	50	22	0.32	15	33	13	3.4
Average					15.3	11.9	10.0	24	28	19	10	30	19	0.68	35	24	14	2.0
Education sector average					19.8	15.0	12.0	34	31	24	17	31	24	0.76	34	27	19	1.6
Education sector average - Excl Beststudy					20.7	15.8	12.7	30	31	24	17	30	23	0.81	34	27	19	1.7

Source: Bloomberg, CMBIS estimates

Figure 6: P/E band chart



Source: Company data, CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue	1,142	1,474	1,798	2,209	2,672
Premium Learning	1,013	1,302	1,602	1,991	2,432
Elite Talent	27	40	53	64	74
Full-time Test Preparation	100	130	139	151	163
Others	2	3	3	3	3
Cost of sales	(659)	(876)	(1,068)	(1,314)	(1,592)
Gross profit	483	598	730	895	1,079
Other income	20	7	16	14	18
Selling expenses	(95)	(130)	(144)	(192)	(248)
Administrative expenses	(178)	(186)	(209)	(250)	(294)
R&D expenses	(140)	(171)	(180)	(203)	(230)
Other expenses	(6)	(44)	(44)	(6)	(6)
Operating profit	83	74	170	258	319
Fair value gains	33	35	39	39	39
Finance costs	-	-	(48)	(50)	(51)
Share of asso and JVs	(4)	(1)	(5)	(10)	(10)
Pre-tax profit	113	108	156	237	297
Income tax	(37)	(35)	(26)	(37)	(49)
Less: Minority interests	17	19	(1)	(1)	(1)
Net profit	49	55	126	182	239
Adjusted net profit	90	102	131	200	249

Cash flow summary

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Profit before tax	103	109	151	219	287
Depreciation and amortization	26	44	69	78	82
Change in working capital	138	119	115	123	137
Others	(29)	(70)	195	189	161
Net cash from operating	238	202	529	609	668
Capex	(74)	(152)	(100)	(100)	(100)
Change of investments	(377)	52	(12)	29	29
Others	51	39	(34)	(0)	(0)
Net cash from investing	(401)	(61)	(146)	(71)	(71)
Equity raised	-	258	44	-	-
Dividend paid	(220)	(100)	-	(63)	(91)
Others	28	(1)	(200)	(186)	(178)
Net cash from financing	(192)	158	(157)	(249)	(269)
Net change in cash	(354)	298	227	289	328
Cash at the beginning	526	170	468	695	984
Exchange difference	(3)	0	-	-	-
Cash at the end	170	468	695	984	1,312
Cash at balance sheet	162	468	695	984	1,312
Cash at discontinued op.	8	N/A	N/A	N/A	N/A

Balance sheet

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Non-current assets	171	302	1,272	1,242	1,217
PPE	56	161	194	218	238
Right-of-use assets	-	-	910	869	836
Asso & JV	22	21	49	39	29
Others	94	121	119	116	114
Current assets	868	1,137	1,386	1,696	2,047
Cash	162	468	695	984	1,312
Short-term investments	572	518	569	579	589
Prepayments	77	148	118	130	143
Others	57	4	4	4	4
Current liabilities	686	776	1,085	1,222	1,375
Contract liabilities	517	563	666	777	902
Other payables	128	192	191	214	240
Tax payables	15	21	21	21	21
Others	26	-	207	209	212
Non-current liabilities	15	41	777	785	799
Lease liabilities	-	-	777	785	799
Rental payables	15	41	-	-	-
Total net assets	338	622	796	932	1,090
Shareholders' equity	255	623	797	935	1,093
Minority Interest	83	(1)	(2)	(2)	(3)

Key ratios

YE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Sales mix (%)					
Premium Learning	88.8	88.3	89.1	90.1	91.0
Elite Talent	2.3	2.7	2.9	2.9	2.8
Full-time Test Preparatory	8.8	8.8	7.8	6.8	6.1
Others	0.1	0.2	0.2	0.1	0.1
P&L ratios (%)					
Gross profit margin	42.3	40.6	40.6	40.5	40.4
OP margin	7.3	5.0	9.4	11.7	12.0
Effective tax rate	33.1	32.2	17.0	17.0	17.0
Adj. net profit margin	7.9	6.9	7.3	9.1	9.3
Payout ratio	N/A	N/A	50.0	50.0	50.0
Balance sheet ratios					
Current ratio (x)	1.3	1.5	1.3	1.4	1.5
Asset turnover (x)	1.1	1.0	0.7	0.8	0.8
Net cash (RMB mn)	162	470	697	986	1,314
Returns (%)					
Adj. ROAE	27.9	23.3	18.4	23.1	24.6
Adj. ROAA	8.9	8.2	6.4	7.1	8.0
Per share data					
Adj. EPS (RMB)	N/A	0.15	0.15	0.24	0.29
DPS (RMB)	N/A	N/A	0.07	0.11	0.14
BVPS (RMB)	N/A	0.73	0.94	1.10	1.29

Source: Company data, CMBIS estimates

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