

Hope Education (1765 HK)

Reverse roadshow takeaways

We visited the Company's new acquisitions, Yinchuan University of Energy and Suzhou TOP IT Institute, during the reverse roadshow last week. We think the quality of University of Energy is decent. Management targets to grow net profit of the Yinchuan schools and Suzhou TOP IT Institute by CAGR of 60% and 89%, respectively, from FY19E to FY22E. Because the Company has good track records of post-acquisition integration and enhancement, we think these targets are achievable. Maintain Buy.

- **Decent quality of University of Energy.** It is the only private university that can enroll foreign students in Ningxia. Its ICT Industry & Education Innovation Center, established by MOE and ZTE, is the only one in Ningxia. The university has one national-level laboratory and three provincial-level teaching demonstrative centers.
- **High growth potential of Yinchuan schools.** Management targets to grow the schools' net profit at a CAGR of 60% from around RMB25-30mn in FY19E to RMB100mn+ in FY22E by raising student enrollment and tuition fees, controlling expenses and replacing high-cost borrowings. Total student enrollment is expected to increase from current 15,496 to 30,000+ in five years. Through increase of admission quota, registration rate and enrollment of non Ningxia students, total student enrollment of degree and diploma is anticipated to double from ~12,000 to ~24,000. Management looks for 30%+ tuition fees growth in five years.
- **Suzhou TOP IT Institute 3-yr net profit CAGR of 89%.** Management targets to grow its net profit from ~RMB6mn in FY19E to ~RMB40mn in FY22E. Management plans to improve the school's registration rate (70%+) and increase student enrollment from non-Jiangsu provinces (20% now). Helped by the Company's student enrollment capability, management expects to grow new student enrollment from 1,700 in Sep 2019 to 4,000 in Sep 2020 and lower the schools' student acquisition cost. Annual tuition fees of certain majors can be raised to RMB14,000-15,000 from current RMB12,000 by filing when timing is appropriate. Capacity of students can be raised from current 6,000 to 9,000 by Sep 2020 and further to 15,000 when the development of Phase 2 completes.
- **Our FY19-21E EPS are 6-8% above consensus; Maintain Buy.** We forecast the company to post 31% adj. EPS CAGR in FY20-21E (vs peers' average of 25%). Our TP of HK\$1.96 is based on 18.0x FY20E P/E (at historical average plus 1sd). **Catalysts:** (1) policy overhang removes; (2) M&A. **Risk:** surge of teachers' costs.

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (RMB mn)	752	1,030	1,329	1,784	2,053
YoY growth (%)	22	37	29	34	15
Net profit (RMB mn)	212	168	454	653	819
Adj. net profit (RMB mn)	183	315	474	653	819
YoY growth (%)	2	72	50	38	25
Adj. EPS (RMB)	na	0.056	0.071	0.098	0.123
YoY growth (%)	na	na	28.0	37.6	25.5
Adj. P/E (x)	na	19.3	16.0	11.6	9.3
Yield (%)	na	1.4	1.9	2.7	3.5
P/B (x)	na	1.7	1.7	1.5	1.3
Net cash (RMB mn)	(2,327)	907	705	1,015	1,609

Source: Company data, CMBIS estimates

BUY (Maintain)

Target Price	HK\$1.96
(Previous TP	HK\$1.96
Up/Downside	+54%
Current Price	HK\$1.27

China Education Sector

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

Stock Data

Mkt Cap (HK\$ mn)	8,467
Avg 3 mths t/o (HK\$ mn)	14.76
52w High/Low (HK\$)	1.47/ 0.75
Total Issued Shares (mn)	6,666.7

Source: Bloomberg

Shareholding Structure

Hope Education Investment	62.1%
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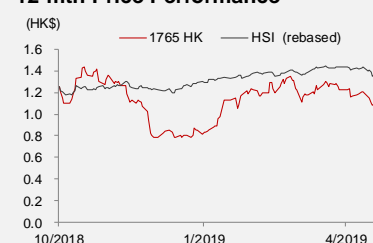
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	3.3%	2.2%
3-mth	14.4%	23.2%
6-mth	3.3%	15.8%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: EY

Related Reports

1. "Hope Education –Solid 1H19 results; 31% EPS CAGR in FY20-21E" – 2 Sep 2019
2. "Hope Education – Undemanding valuation at 25% 3-YR EPS CAGR" – 26 Mar 2019
3. "China Education Sector – Undemanding valuation; higher education segment more preferred" – 22 Mar 2019

Yinchuan University of Energy

Background information

Founded in 1999, Yinchuan University of Energy was upgraded to a university from a vocational college in 2012. The university has 32 degree majors and 26 diploma majors. The Yinchuan schools (University of Energy, a vocational school, a technician school, a training center and an auto repair factory) has total students of 15,496. Average tuition fees of university and vocational college are RMB18,000 and RMB9,000, respectively.

A private university with decent quality

- The only private university that can enroll foreign students in Ningxia.
- The only university in Ningxia and one of the sixty universities in China has established the ICT Industry & Education Innovation Center by Ministry of Education and ZTE (教育部-中兴通讯 ICT 产教融合创新基地). Management said its first batch of around 180 students has received around 200 job offers from industry chains of ZTE and Huawei.
- It has one national-level coal-based chemicals key inspection and testing laboratory (国家级煤化工检测重点实验室).
- It has three provincial-level experimental teaching demonstrative centers (省级实验教学示范中心).
- It has established 65 school-enterprise cooperative training bases and 182 practical training rooms.

Huge growth potential of Yichuan schools

In FY18, the schools recorded RMB201mn revenue, RMB79mn EBITDA and RMB30mn net profit. The company targets to grow its net profit at a CAGR of 60% from around RMB20-30mn in 2019E to >RMB100mn in 2022E, led by increasing student enrollment and tuition fees, controlling expenses and replacing high-cost borrowings. Because Yinchuan University of Energy is a private university (not an independent college), the NPM of the Yinchuan schools is anticipated to reach >40%, higher than the Company's 30-40% NPM for its universities (all are independent colleges which are required to pay management fees to cooperating public universities).

It targets to raise number of student enrollment to >30,000 in five years. (1) Degree: Current total student enrollment is >6,000. The Company expects its admission quota can increase from 2,000+ to 3,000 in 2-3 years. Registration rate is low at 85%. Around 64%/36% of its degree students came from Ningxia/other provinces. Given the Company is strong at student enrollment, it can help the university to enroll non-Ningxia students. (2) Diploma: the Company's Head of Teaching Management Committee (教学管理委员会) expects the vocational college can pass a review by the Ministry of Education next year so its admission quota could be raised to around 4,000. Therefore, total student enrollment of both degree and diploma can reach around 24,000 in five years. The remaining 6,000 students is expected to be filled by increasing vocational and technician schools student enrollment.

Moreover, the Company targets to raise tuition fees by 30%+ in five years.

Old campus has sufficient land resources to expand capacity

The new campus (buildings and land with site area of 469mu) will be publicly auctioned because the ass

Suzhou TOP IT Vocational Institute

Background information

The school, established in 2002, is an electronic and information technology focused vocational college. It currently offers more than 30 majors and has around 5,000 students. The school was awarded as an outstanding school with cooperation between government, school and enterprises for successively six years between 2013 and 2018. In FY18, total revenue of the school was RMB60mn.

Employment rate boosted by the advanced economic development of Kunshan

The campus is located in Bacheng Town of Jiangsu Kunshan, which is strategically located between Shanghai and Suzhou. Kunshan has two national-level economic development zone, one provincial-level economic development zone and two software parks. The school has entered into school-enterprise cooperation programs with 60-70 enterprises. Its graduate employment rate was high at 98%+ between 2016 and 2018. Average monthly salary of its graduates was around RMB4,300, ranked the fifth among 44 private and 80 public institutes.

Capacity expansion potential

The school has land site area of 313mu. The land certificates were obtained by transfer therefore the school is not required to pay land premium if it chooses as a for-profit school in future. It will renovate its dormitories to expand capacity from >6,000 to 9,000 by Sep 2020 by around RMB10mn capex. Furthermore, the development of Phase Two, with total GFA of 65,476 sq.m., has got planning permit and can kick off when necessary. Total capacity can be lifted to 15,000.

Leverage on student enrollment capability of Hope Education

Currently, around 80% and 20% of students came from Jiangsu and other provinces, respectively. Registration rate is a bit low at 70%+ (vs the Company's around 80% for diploma students in 2018). The school's student enrollment team only has 15 people, which was far below the Company's around 1,000 people. Hope Education plans to help the school to enroll more students outside Jiangsu given its strong student enrollment capability in Southwestern China. There is demand from students in southwest region to study and find jobs in Yangtze River Delta. The school's per student acquisition cost is >RMB1,000, which is higher than the Company's RMB233. There is room to lower the school's per student acquisition cost. Management targets to raise new student enrollment from around 1,700 in 2019 to around 4,000 in 2020 (2,500 from diploma and 1,500 from technician school)

Tuition fees upside

In Jiangsu, a school can change its tuition fees by filing to the authority. However, the province has set limits on tuition fees for each majors. Such limits will be revised per three years in general. Currently, the average tuition fee of the school is around RMB12,000/year. Given the caps of certain majors are between RMB14,000-15,000, the school can raise its tuition fees when the timing is appropriate. .

Profit growth outlook

The Company targets to grow the school's net profit from around RMB6mn in FY19E to RMB40mn in 2022E, representing 89% CAGR.

Figure 1: Site area of Yinchuan University of Energy was 1,002mu



Source: CMBIS

Figure 2: A large piece of land (lower right corner of the map) is available for expansion



Source: CMBIS

Figure 3: The ICT industry and education innovation center is jointly set up by ZTE, MOE and the college



Source: CMBIS

Figure 4: Cloud computing laboratory in the ICT industry and education innovation center



Source: CMBIS

Figure 5: Cloud computing demonstration of the ICT industry and education innovation center



Source: CMBIS

Figure 6: Collaborative development demonstration of the ICT industry and education innovation center



Source: CMBIS

Figure 7: 4G mobile communication demonstration of the ICT industry and education innovation center



Source: CMBIS

Figure 8: Elementary communication demonstration of the ICT industry and education innovation center



Source: CMBIS

Figure 9: The laboratory jointly set up by Trace Software International and school of electric power



Source: CMBIS

Figure 10: The drone is designed for spraying farms by the School of innovation & Entrepreneurship



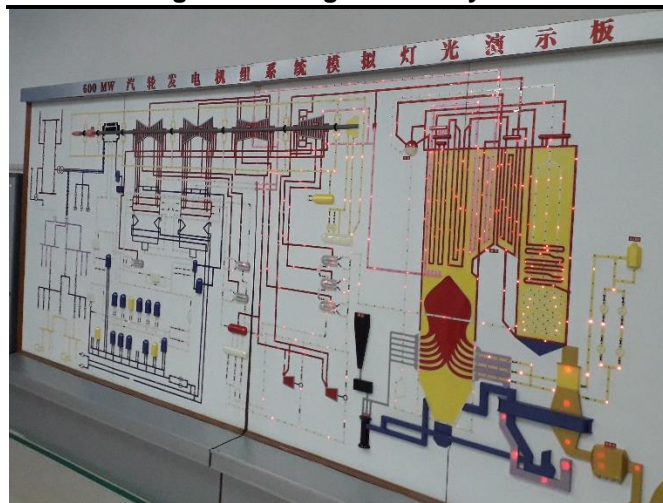
Source: CMBIS

Figure 11: The national-level coal-based chemicals key inspection and testing laboratory



Source: CMBIS

Figure 12: The simulation and demonstration board of a 600 MW gas turbine generator system



Source: CMBIS

Figure 13: Suzhou TOP IT Institute is located at the lakeside of Yangcheng Lake



Source: CMBIS

Figure 14: School-enterprise training base with Baijiahui Pharmacy Shop in Suzhou TOP IT Institute



Source: CMBIS

Figure 15: 24% CAGR of student enrolment from 2018/19 to 2021/22 school year

Student enrolment (school year)	2016/2017	2017/2018	2018/2019	2019/2020E	2020/2021E	2021/2022E	3-yr CAGR
Universities							
Southwest Jiaotong University Hope College							
Bachelor's degree program	9,767	10,855	12,049	13,254	13,917	14,473	6%
Junior college diploma program	4,783	4,268	5,219	6,211	7,142	8,071	16%
Subtotal:	14,550	15,123	17,268	19,465	21,059	22,544	9%
Business College of Guizhou University of Finance and Econon	10,642	14,356	15,548	16,636	17,302	18,340	6%
Jinci College of Shanxi Medical University	3,621	4,801	5,953	7,441	8,185	8,676	13%
College of Science and Technology of Guizhou University *				9,325	9,604	9,892	na
Yinchuan schools				19,908	25,008	27,108	na
Junior colleges							
Sichuan Tianyi University	10,716	11,765	10,971	13,055	14,361	15,223	12%
Sichuan Hope Automotive Vocational College	3,642	4,559	4,373	5,904	7,379	8,486	25%
Sichuan Vocational College of Culture&Cummunication	5,959	7,371	8,920	11,150	12,823	13,977	16%
Guizhou Vocational Institute of Technology	1,177	2,989	5,903	9,091	11,363	11,931	26%
Sichuan TOP IT Vocational Institute		12,548	12,869	13,641	14,323	15,039	5%
Hebi Automotive College				5,400	6,200	7,000	na
Suzhou Top Institute				5,000	6,000	7,000	na
Technician education services							
Sichuan Hope Automotive Technician College	1,365	2,127	4,193	4,822	5,545	6,377	15%
Kunshan Technician School				500	500	500	na
Total:	51,672	75,639	85,998	132,013	150,049	162,202	24%
Total students - degree	24,030	30,012	33,550	57,240	64,412	68,598	27%
Total students - others	27,642	45,627	52,448	74,773	85,637	93,604	21%

Source: Company data, CMBIS estimates

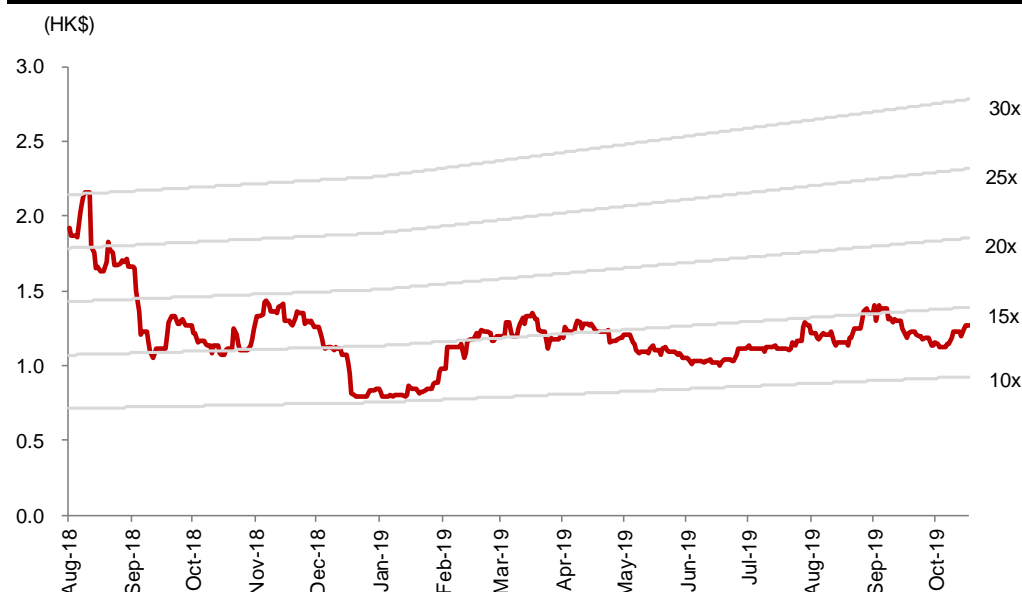
*Assume the investment of the school is financially consolidated by equity method.

Figure 16: 24% CAGR of revenue in FY20-21E

Revenue (RMB mn)	FY17	FY18	FY19E	FY20E	FY19E	2-yr CAGR
Tuition fees	621	856	1,120	1,518	1,757	25%
Regular higher education						
Southwest Jiaotong University Hope College	201	227	257	288	321	12%
Business College of Guizhou University of Finance and Econ	147	179	185	191	211	7%
Jinci College of Shanxi Medical University	61	82	102	122	138	16%
Yinchuan schools			75	248	295	99%
Sichuan Tianyi University	95	105	115	135	149	14%
Sichuan Hope Automotive Vocational College	32	37	46	63	79	31%
Sichuan Vocational College of Culture & Cummunication	62	70	93	124	154	28%
Guizhou Vocational Institute of Technology	18	30	53	75	91	32%
Sichuan Top IT Vocational Institute	0	116	140	154	170	10%
Hebi Automotive College			12	32	40	79%
Suzhou Top Institute			27	67	85	79%
Subtotal	616	846	1,104	1,498	1,733	25%
Technician education services						
Sichuan Hope Automotive Technician College	4	10	14	17	20	19%
Kunshan Technician School			1	3	3	57%
Boarding fees	63	85	115	167	192	30%
Others	68	90	94	99	104	5%
Total revenue	752	1,030	1,329	1,784	2,053	24%

Source: Company data, CMBIS estimates

Figure 17: P/E band chart



Source: Company data, CMBIS estimates

Figure 18: CMBI estimates vs consensus

US\$ mn	CMBI			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	1,329	1,784	2,053	1,304	1,651	2,009	2%	8%	2%
Gross Profit	628	851	1,015	614	802	989	2%	6%	3%
Operating Profit	558	756	922	537	723	961	4%	5%	-4%
Net profit	474	653	819	449	609	756	6%	7%	8%
Gross Margin	47.2%	47.7%	49.4%	47.1%	48.6%	49.2%	+0.1ppt	-0.9ppt	+0.2ppt
Operating Margin	42.0%	42.4%	44.9%	41.1%	43.8%	47.8%	+0.9ppt	-1.4ppt	-2.9ppt
Net Margin	35.7%	36.6%	39.9%	34.4%	36.9%	37.6%	+1.3ppt	-0.3ppt	+2.3ppt

Source: Company data, CMBIS estimates

Figure 19: Peers valuation table

	Ticker	Rating	Mkt Cap		Year end	P/E (x)			EV/EBITDA		Adj. net profit growth (%)			EPS growth (%)			PEG (x)	Revenue growth (%)		
			(US\$ m)	Price		FY1	FY2	FY3	FY1	FY2	FY1	FY2	FY3	FY1	FY2	FY3		FY1	FY2	FY3
Higher Education services providers																				
China Education	839 HK	NR	3,117	12.10	Aug-18	29.2	23.5	19.7	20.2	16.1	na	23	19	na	24	19	1.35	na	24	13
Yuhua Education	6169 HK	NR	1,881	4.49	Aug-18	18.9	15.0	13.1	12.9	9.8	18	32	18	13	26	14	0.95	37	31	8
Hope Education	1765 HK	Buy	1,080	1.27	Dec-18	16.0	11.6	9.1	9.0	6.2	50	38	25	28	38	25	0.51	29	34	15
Minsheng Education	1569 HK	NR	671	1.31	Dec-18	11.5	9.5	8.0	8.5	7.1	22	18	21	22	20	19	0.58	59	23	18
Kepei Education	1890 HK	NR	1,041	4.08	Dec-18	17.2	14.7	12.7	12.6	10.8	23	19	16	(7)	17	16	1.04	23	19	15
Xinhua Education	2779 HK	Buy	572	2.79	Dec-18	14.4	9.9	8.3	11.6	5.5	12	17	16	1	45	18	0.47	18	18	15
New Higher Education	2001 HK	NR	574	2.92	Dec-18	10.5	8.2	7.0	9.2	7.6	31	28	17	26	28	18	0.46	91	25	16
Edvantage	382 HK	NR	505	3.89	Aug-18	15.5	12.5	10.3	10.5	8.8	38	25	22	na	24	21	0.69	10	13	19
Chunlai Education	1969 HK	NR	237	1.55	Aug-18	11.7	7.8	6.4	8.9	6.6	(4)	54	24	(14)	50	22	0.33	15	33	13
Average						16.1	12.5	10.5	11.5	8.7	24	28	20	10	30	19	0.71	35	24	15

Source: Bloomberg estimates, CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue	752	1,030	1,329	1,784	2,053
Tuition fees	621	854	1,120	1,518	1,757
Boarding fees	63	85	115	167	192
Others	68	90	94	99	104
Cost of sales	(392)	(562)	(701)	(932)	(1,038)
Gross profit	360	467	628	851	1,015
Other income	78	101	117	150	171
Selling expenses	(29)	(21)	(33)	(41)	(43)
Administrative expenses	(79)	(111)	(149)	(200)	(216)
Other expenses	(3)	(5)	(5)	(5)	(5)
EBIT	328	431	558	756	922
Finance income	19	79	93	55	51
Finance costs	(145)	(201)	(171)	(179)	(172)
Share of JV	(2)	(2)	15	41	43
Non-operating items	29	(148)	(20)	-	-
Pre-tax profit	229	159	474	673	845
Income tax	(20)	8	(20)	(20)	(25)
Less: Minority interests	(2)	(1)	0	0	0
Net profit	212	168	454	653	819
Adjusted net profit	183	315	474	653	819

Cash flow summary

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Profit before tax	229	159	474	673	845
Depreciation and amortization	121	161	220	276	284
Change in working capital	80	249	(15)	191	172
Others	70	233	118	103	87
Net cash from operating	501	802	798	1,243	1,387
Capex & investments	(925)	(624)	(300)	(400)	(400)
Acquisitions	(750)	(15)	(499)	(515)	(50)
Others	710	(100)	70	306	38
Net cash from investing	(965)	(739)	(729)	(609)	(412)
Equity raised	-	2,705	-	-	-
Change of borrowings	207	259	200	(20)	(20)
Dividend paid	-	-	(100)	(145)	(209)
Others	296	(595)	(171)	(179)	(172)
Net cash from financing	503	2,369	(71)	(345)	(401)
Net change in cash	39	2,432	(2)	289	575
Cash at the beginning of the year	143	181	3,039	3,037	3,326
Exchange difference	181	2,614	3,037	3,326	3,901
Cash at the end of the year	181	3,039	3,037	3,326	3,901

Balance sheet

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Non-current assets	4,551	5,119	6,418	6,583	6,743
PPE	3,195	3,448	5,062	5,209	5,348
Prepaid lease payments	595	590	566	551	537
JV	143	-	163	204	247
Others	618	1,081	628	619	610
Current assets	1,044	3,172	3,631	3,486	4,077
Cash	181	3,039	3,037	3,326	3,901
Prepayments	121	129	142	156	171
Others	741	4	452	4	4
Current liabilities	2,098	1,851	2,397	2,422	2,609
Contract liabilities	535	591	892	1,048	1,191
Other payables	732	637	701	750	795
Borrowings	614	527	527	527	527
Current income tax	54	34	34	34	34
Others	163	62	242	62	62
Non-current liabilities	2,817	2,280	3,118	2,606	2,557
Deferred income	629	658	685	708	729
Borrowings	1,265	1,605	1,805	1,785	1,765
Others	922	17	628	113	63
Total net assets	679	4,160	4,535	5,043	5,653
Shareholders' equity	649	4,157	4,532	5,039	5,649
Minority Interest	30	3	3	3	4

Key ratios

YE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Sales mix (%)					
Tuition & boarding fees	82.5	83.0	84.3	85.1	85.6
Ancillary services	8.4	8.3	8.6	9.3	9.4
Others	9.1	8.7	7.1	5.6	5.1
Total	100.0	100.0	100.0	100.0	100.0
P&L ratios (%)					
Gross profit margin	47.8	45.4	47.2	47.7	49.4
EBIT margin	43.5	41.9	42.0	42.4	44.9
Effective tax rate	24.3	30.6	35.7	36.6	39.9
Adj. net profit margin	8.6	(4.9)	4.2	3.0	3.0
Payout ratio	na	31.7	32.0	32.0	32.0
Balance sheet ratios					
Current ratio (x)	0.5	1.7	1.5	1.4	1.6
Asset turnover (x)	0.1	0.1	0.1	0.2	0.2
Net cash (RMBmn)	(2,327)	907	705	1,015	1,609
Returns (%)					
Adj. ROAE	32.9	13.1	10.9	13.6	15.3
Adj. ROAA	3.6	4.6	5.2	6.5	7.8
Per share data					
Adj. EPS (RMB)	NA	0.056	0.071	0.098	0.123
DPS (RMB)	NA	0.015	0.022	0.031	0.039
BVPS (RMB)	NA	0.624	0.680	0.756	0.847

Source: Company data, CMBIS estimates

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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

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