

Wisdom Education (6068 HK)

Explore asset-light model to enhance return

FY19 adjusted NP rose 34% YoY, 5% above consensus. The Company is exploring asset-light model in Dongguan and Foshan to meet education demand. We think this could accelerate expansion pace and enhance return. We trimmed FY20/21E EPS by 3%/7%. Maintain Buy.

- Adjusted NP above consensus.** NP increased 16% YoY to RMB359mn. Adjusted NP rose 34% to RMB434mn, 5% above consensus and 4% below our estimates. Revenue climbed 35% to RMB1,682mn, 2%/4% below consensus/our estimates. GPM increased 0.4ppt to 44.1%, 1.2ppt/1.4ppt lower than consensus/our estimates, mainly due to 50% growth of teacher costs (28% growth of teachers and salaries increase). SG&A expenses reduced by 2.7ppt to 16.6%, 1.0ppt lower than our estimates due to less than expected administrative expenses.
- Explore asset-light model to enhance return.** Given the strong demand in certain Guangdong cities, the Company has identified certain properties in Dongguan and Foshan, and is negotiating with property owners and authorities to transform these properties to school properties (3,000-5,000 student capacity). If successful, some asset-light schools could be opened in Sep 2020. We think the Company has strong brand equity in Dongguan so it could admit students easily. Asset-light approach could accelerate expansion pace (vs finding a new site to build school) and improve ROE.
- Focus on Greater Bay Area.** Besides the existing schools in Dongguan, Huizhou and Foshan, the Company has entered into agreements with local governments of Jiangmen, Guangzhou and Zhaoqing to set up new schools. The Company also plans to raise the maximum capacity of Dongguan Guangzheng school (from 18,000 to 20,000) and Huizhou school (from 10,500 to 12,000). The Company intends to cover all nine cities of the Greater Bay Area in future.
- High visibility of expansion potential.** Total expected maximum capacity of existing schools and planned new schools rose 10% to 142,870, representing 138% of current student enrollment of 60,116.
- Maintain Buy.** We lowered FY20/21E net profit estimates by 3%/7% to mainly factor in lower revenue and GPM assumptions. Our TP is fine-tuned from HK\$4.60 to HK\$4.40, still based on 18x FY20E P/E. The stock trades at 14.2x FY20E P/E. We think valuation is attractive compared to 26% EPS CAGR from FY19 to FY22E. We continue to like the Company's Guangdong-focused expansion strategy and expansion visibility. **Catalysts:** (1) better-than-expected student enrolment or tuition fee growth; (2) more new projects in the Greater Bay Area. **Risks:** (1) policy risks; (2) lower-than-expected student enrollment or tuition fee growth; (3) surge of teachers' costs.

Earnings Summary

(YE 31 Aug)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	1,247	1,682	2,006	2,470	2,971
YoY growth (%)	27	35	19	23	20
Net profit (RMB mn)	310	359	461	597	716
YoY growth (%)	55	16	28	30	20
EPS (RMB)	0.152	0.172	0.221	0.283	0.340
YoY growth (%)	38	13	29	28	20
P/E (x)	19.2	18.3	14.2	11.1	9.3
Yield (%)	2.3	2.8	2.8	3.6	4.3
P/B (x)	3.1	3.0	2.4	2.1	1.9
Net gearing (%)	47	66	38	34	28

Source: Company data, CMBIS estimates

BUY (Maintain)

Target Price HK\$4.40
 (Previous TP) HK\$4.60
Up/Downside +25%
Current Price HK\$3.51

China Education Sector

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Stock Data

Mkt Cap (HK\$ mn)	7,186
Avg 3 mths t/o (HK\$ mn)	8.00
52w High/Low (HK\$)	4.85/ 2.65
Total Issued Shares (mn)	2,043.0

Source: Bloomberg

Shareholding Structure

Mr. Liu Xuebin	45.5%
Ms. Li Suwen	27.9%

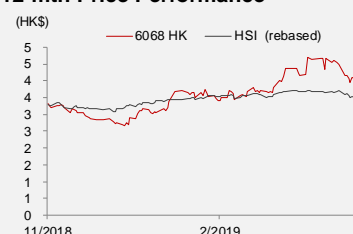
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	2.4%	1.2%
3-mth	-1.2%	-4.1%
6-mth	-14.1%	-13.0%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Deloitte

Related Reports

- "Wisdom Education – Student enrollment missed but organic growth still strong" – 9 Sep 2019
- "Wisdom Education – 2019/20 school year tuition fees in line; Reiterate Buy" – 9 Jul 2019
- "Wisdom Education – Upside potential on tuition fee level" – 15 May 2019

Figure 1: FY19 results review

Y/E Aug 31 (RMB mn)	FY19	FY18	% change	Remarks
Revenue	1,681.5	1,246.9	35%	Student enrollment rose 26%, adjusted ASP up 6%
Cost of sales	(939.8)	(702.1)	34%	Teacher costs jumped 50% on 28% growth of number of teachers and salaries increase
Gross profit	741.7	544.9	36%	
Other income	33.4	54.1	-38%	Government grant reduced by RMB15mn
Other gains and losses	(0.8)	1.7	-146%	RMB17mn exchange loss (RMB depreciation); RMB18mn fair value gain of financial assets
Selling and distribution expenses	(25.8)	(19.5)	33%	
Administrative expenses	(253.0)	(220.9)	15%	
Operating profit	495.5	360.3	38%	
Finance income	20.3	46.2	-56%	RMB18mn investment income stated in other gains and losses in FY19
Finance costs	(107.1)	(57.5)	86%	Total loans increased 27% to RMB2.2bn. Full-year booking of interests of CB
Change in FV of inv prop and CB	0.6	(3.4)	-118%	
Profit before tax	409.3	345.6	18%	
Tax expense	(55.7)	(38.4)	45%	
MI	(5.9)	(3.2)	83%	
Net profit	359.5	310.4	16%	
Adj net profit	434.5	325.2	34%	
DPS (RMB)	0.08	0.07	24%	
Margin & Ratio (%)				
Gross margin	44.1	43.7	0.4	
Operating margin	29.5	28.9	0.6	
SG&A expenses ratio	16.6	19.3	(2.7)	
Net margin	21.4	24.9	(3.5)	
Effective tax rate	13.6	11.1	2.5	
Payout ratio	39.4	43.5	(4.1)	Maintained at around 40%
	FY19	FY18	change (%)	
Student number	54,420	42,230	29%	
Net cash (RMBmn)	(1,145)	(477)	140%	

Source: Company data

Figure 2: 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

Figure 3: 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 4: New projects provide at least 15,500 student capacity

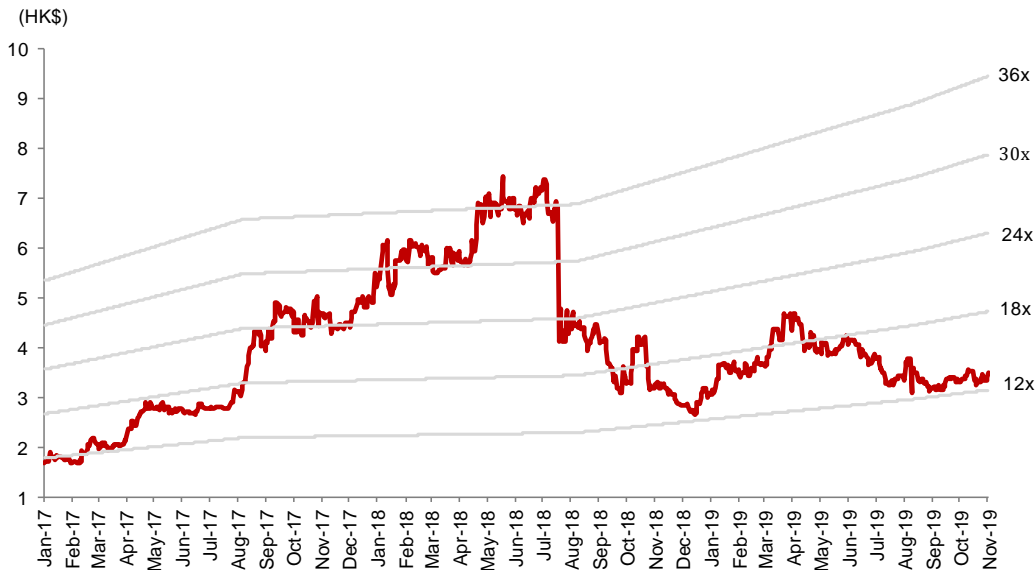
Location	Expected year of opening	Target max. capacity
Dongguan/Foshan (light asset projects)	Sep-20	TBC
Chaozhou, Guangdong	Sep-21	8,000
Jiangmen, Guangdong	Sep-21	7,500
Guangzhou, Guangdong	TBC	TBC
Zhaoqing, Guangdong	TBC	TBC
Total		15,500

Source: Company data, CMBIS

Figure 5: 15% 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	10,450	11,450	9%
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	5,169	5,669	9%
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 Scholls			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	1,050	1,700	87%
Kaiping School					700	1,400	na
Chaozhou School					700	1,400	na
Zengcheng School						700	na
Zhaoqing School						700	na
Total	31,788	43,230	54,420	60,116	68,549	78,856	15%

Source: Company data, CMBIS estimates

Figure 6: P/E band

Source: Bloomberg, Company data, CMBIS estimates

Figure 7: Key assumptions

Year-end Aug 31 (RMB mn)	FY18	FY19	FY20E	FY21E	FY22E
Total revenue	1,247	1,682	2,006	2,470	2,971
growth %	27.3%	34.9%	19.3%	23.2%	20.3%
<i>Tuition and boarding fees</i>	841	1,145	1,354	1,691	2,029
growth %	25.3%	36.2%	18.2%	24.8%	20.0%
<i>Others</i>	406	536	651	780	942
growth %	31.7%	32.1%	21.5%	19.7%	20.8%
Gross profit margin	43.7%	44.1%	44.6%	45.5%	44.8%
Selling expenses ratio	1.6%	1.5%	1.5%	1.5%	1.5%
Administrative expenses ratio	17.7%	15.0%	14.5%	13.9%	13.4%
Operating profit margin	28.9%	29.5%	30.4%	31.4%	31.1%
Effective tax rate	11.1%	13.6%	14.0%	14.0%	14.0%
Net profit	310	359	461	597	716
growth %	55.0%	15.8%	28.2%	29.6%	19.9%
Payout ratio	43.5%	39.4%	40.0%	40.0%	40.0%
Average tuition and boarding fee (RMB)	19,893	21,049	22,528	24,661	25,733
growth %	-5.8%	8.2%	7.0%	9.5%	4.3%
Student enrollment	43,230	54,420	60,116	68,549	78,856
growth %	36.0%	25.9%	10.5%	14.0%	15.0%

Source: Company data, CMBIS estimates

Figure 8: Peers valuation table

Ticker	Rating	Mkt Cap		Price	Year end	P/E (x)			Net profit growth (%)			EPS growth (%)			PEG (x)			Revenue growth (%)		
		(US\$ m)	Cnncy			FY1	FY2	FY3	ee	FY2	FY3	FY1	FY2	FY3	FY1	FY1	FY2	FY3		
K12 tutoring services providers																				
New Oriental Education	EDU US	NR	19,442	USD	122.72	May-19	35.6	27.0	21.1	35	33	28	34	32	28	1.20	27	27	23	
TAL Education	TAL US	NR	25,971	USD	43.89	Feb-19	75.9	39.8	27.4	(28)	110	42	(22)	91	45	1.14	36	34	33	
Onesmart Education	ONE US	NR	1,152	USD	7.17	Aug-18	21.1	16.3	12.0	59	30	36	na	30	36	0.65	40	33	26	
Scholar Education	1769 HK	NR	724	HKD	10.20	Dec-18	49.6	34.0	27.4	59	31	24	na	46	24	1.43	40	43	26	
Beststudy Education	3978 HK	Buy	332	HKD	3.06	Dec-18	18.0	17.8	11.4	28	53	25	na	1	53	0.74	22	23	21	
Average							40.0	27.0	19.9	31	51	31	6	40	37	1.03	33	32	26	
Average - excl Beststudy							45.5	29.3	22.0	31	51	33	6	50	33	1.11	36	34	27	
Non-formal vocational education services provider																				
China East Education	667 HK	Buy	4,439	HKD	15.86	Dec-18	33.9	26.7	21.8	67	27	20	na	27	20	1.44	25	20	18	
K12 education services providers																				
Wisdom Education	6068 HK	Buy	918	HKD	3.51	Aug-18	18.3	14.2	11.1	16	28	30	13	29	28	0.65	35	19	23	
Tianli Education	1773 HK	NR	846	HKD	3.19	Dec-18	22.1	16.2	12.2	28	42	37	na	36	33	0.64	38	35	34	
Maple Leaf	1317 HK	NR	888	HKD	2.32	Aug-18	9.8	8.3	7.0	15	18	17	12	18	18	0.54	21	19	17	
Bright Scholar	BEDU US	NR	1,203	USD	9.66	Aug-18	23.3	21.3	17.8	39	13	29	45	10	19	1.62	42	60	13	
Virscond Education	1565 HK	NR	844	HKD	2.14	Dec-18	12.4	9.2	6.9	20	52	32	29	35	33	0.36	28	27	25	
Average							17.2	13.8	11.0	24	31	29	25	26	26	0.76	33	32	22	
Higher Education services providers																				
China Education	839 HK	NR	2,937	HKD	11.38	Aug-18	27.8	21.8	18.0	na	27	20	na	28	21	1.15	na	27	13	
Yuhua Education	6169 HK	NR	2,029	HKD	4.83	Aug-18	20.2	15.9	13.7	18	32	17	13	27	15	0.95	40	33	8	
Hope Education	1765 HK	Buy	1,175	HKD	1.38	Dec-18	17.4	12.6	9.9	50	38	25	28	38	25	0.55	29	34	15	
Minsheng Education	1569 HK	NR	693	HKD	1.35	Dec-18	11.8	9.8	8.2	22	18	21	22	20	19	0.59	59	23	18	
Kepei Education	1890 HK	NR	948	HKD	3.71	Dec-18	15.3	13.3	11.5	23	18	16	(5)	15	16	0.99	22	19	15	
Xinhua Education	2779 HK	Buy	512	HKD	2.49	Dec-18	12.9	8.9	7.4	12	17	16	1	45	18	0.42	18	18	15	
New Higher Education	2001 HK	NR	532	HKD	2.70	Dec-18	9.6	7.4	6.4	31	30	16	26	29	17	0.42	92	26	14	
Edvantage	382 HK	NR	578	HKD	4.44	Aug-18	17.7	13.8	11.3	38	30	21	na	28	21	0.71	10	16	17	
Chunlai Education	1969 HK	NR	235	HKD	1.53	Aug-18	11.5	7.6	6.3	(4)	54	24	(14)	50	22	0.32	15	33	13	
Average							16.0	12.3	10.3	24	30	20	10	31	19	0.68	36	25	14	
Education sector average							22.6	16.6	13.0	26	36	25	14	32	26	0.79	34	29	20	

Source: Bloomberg estimates, CMBIS estimates

Figure 9: Earnings revision

US\$ mn	New			Old			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	2,006	2,470	2,971	2,068	2,546	na	-3%	-3%	na
Gross Profit	895	1,124	1,330	935	1,186	na	-4%	-5%	na
Operating Profit	610	776	923	609	802	na	0%	-3%	na
Net profit	461	597	716	477	645	na	-3%	-7%	na
Gross Margin	44.6%	45.5%	44.8%	45.2%	46.6%	na	-0.6ppt	-1.1ppt	na
Operating Margin	30.4%	31.4%	31.1%	29.4%	31.5%	na	+1.0ppt	-0.1ppt	na
Net Margin	23.0%	24.2%	24.1%	23.1%	25.3%	na	-0.1ppt	-1.1ppt	na

Source: CMBIS estimates

Figure 10: CMBI estimates vs consensus

US\$ mn	CMBI			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	2,006	2,470	2,971	2,058	2,429	2,854	-3%	2%	4%
Gross Profit	895	1,124	1,330	919	1,121	1,293	-3%	0%	3%
Operating Profit	610	776	923	610	754	854	0%	3%	8%
Net profit	461	597	716	497	604	668	-7%	-1%	7%
Gross Margin	44.6%	45.5%	44.8%	44.7%	46.2%	45.3%	-0.1ppt	-0.7ppt	-0.5ppt
Operating Margin	30.4%	31.4%	31.1%	29.6%	31.0%	29.9%	+0.8ppt	+0.4ppt	+1.2ppt
Net Margin	23.0%	24.2%	24.1%	24.1%	24.9%	23.4%	-1.1ppt	-0.7ppt	-1.7ppt

Source: Bloomberg estimates, CMBIS estimates

Financial Summary

Income statement

YE 31 Aug (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	1,247	1,682	2,006	2,470	2,971
Tuition & boarding fees	841	1,145	1,354	1,691	2,029
Ancillary services	406	536	651	780	942
Cost of sales	(702)	(940)	(1,111)	(1,346)	(1,641)
Gross profit	545	742	895	1,124	1,330
Other income	54	33	25	25	25
Other gains and losses	2	(1)	11	6	9
Selling expenses	(19)	(26)	(30)	(36)	(43)
Administrative expenses	(221)	(253)	(291)	(343)	(398)
EBIT	360	496	610	776	923
Finance costs, net	(11)	(87)	(84)	(87)	(92)
Listing expenses	0	0	0	0	0
FV change of inv. prop.	(3)	1	0	0	0
Pre-tax profit	346	409	525	689	831
Income tax	(38)	(56)	(74)	(96)	(116)
Less: Minority interests	(3)	(6)	(9)	(4)	(1)
Net profit	310	359	461	597	716

Cash flow summary

YE 31 Aug (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before tax	346	525	689	831	923
Depreciation and amortization	106	166	180	199	
Change in working capital	191	226	237	280	
Others	(19)	(21)	5	(36)	
Net cash from operating	623	577	896	1,111	1,275
Capex & investments	(743)	(750)	(750)	(750)	
Acquisitions	(267)	0	0	0	
Others	(338)	260	(82)	(82)	
Net cash from investing	(1,349)	(490)	(832)	(832)	
Equity raised	3	0	0	0	
Change of borrowings	1,485	(179)	100	100	
Dividend paid	(122)	(173)	(210)	(261)	
Others	(118)	(102)	(105)	(110)	
Net cash from financing	1,248	(454)	(214)	(271)	
Net change in cash	522	(48)	64	172	
Cash at the beginning of the year	378	911	662	614	678
Exchange difference	11	0	0	0	0
Cash at the end of the year	911	662	614	678	850

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	4,003	4,676	5,231	5,800	6,351
PPE	2,492	3,036	3,652	4,245	4,817
Prepaid lease payments	502	781	764	747	730
Deposits	520	631	631	631	631
Others	489	228	183	177	173
Current assets	1,468	1,595	1,353	1,546	1,848
Cash	911	662	614	678	850
Pledged deposit	282	499	499	499	499
Prepayments	162	97	116	143	171
Others	113	337	124	226	328
Current liabilities	1,643	2,480	2,246	2,523	2,823
Borrowings	282	1,108	629	629	629
Contract liabilities	617	751	933	1,121	1,340
Trade and other payables	616	503	566	644	736
Others	128	118	118	129	118
Non-current liabilities	1,851	1,545	1,545	1,645	1,745
Borrowings	1,847	1,540	1,540	1,640	1,740
Deferred revenue	0	0	0	0	0
Others	4	4	4	4	4
Total net assets	1,977	2,247	2,793	3,178	3,632
Shareholders' equity	1,911	2,161	2,716	3,106	3,561
Minority Interest	66	86	77	73	72

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Tuition & boarding fees	67.5	68.1	67.5	68.4	68.3
Ancillary services	32.5	31.9	32.5	31.6	31.7
Total	100.0	100.0	100.0	100.0	100.0
P&L ratios (%)					
Gross profit margin	43.7	44.1	44.6	45.5	44.8
EBIT margin	28.9	29.5	30.4	31.4	31.1
Effective tax rate	11.1	13.6	14.0	14.0	14.0
Net profit margin	24.9	21.4	23.0	24.2	24.1
Payout ratio	43.5	39.4	40.0	40.0	40.0
Balance sheet ratios					
Current ratio (x)	0.9	0.6	0.6	0.6	0.7
Asset turnover (x)	0.2	0.3	0.3	0.3	0.4
Net gearing ratio (%)	47	66	38	34	28
Returns (%)					
ROAE	17.0	17.7	18.9	20.5	21.5
ROAA	7.0	6.0	7.0	8.5	9.2
Per share					
EPS (RMB)	0.15	0.20	0.22	0.28	0.34
DPS (HK\$)	0.08	0.10	0.10	0.13	0.15
BVPS (RMB)	0.94	1.06	1.29	1.47	1.69

Source: Company data, CMBIS estimates

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