

# China Edu Group (839 HK)

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## Company Update

**BUY**

UNCHANGED

Close price: HK\$7.18

Target Price: HK\$10.60(+47.6%)

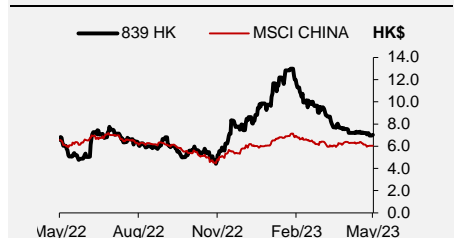
Prior TP: HK\$10.10

### Key Data

HKEx code	839	HK
12 Months High (HK\$)	13.90	
12 Month Low (HK\$)	4.50	
3M Avg Dail Vol. (mn)	10.21	
Issue Share (mn)	2,551.43	
Market Cap (HK\$m)	18,319.24	
Fiscal Year	08/2022	
Major shareholder (s)	Mr. Yu Guo and Mr Xie Ketao(59.36%)	

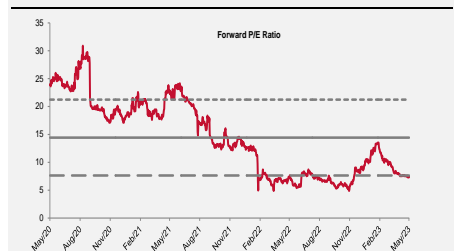
Source: Company data, Bloomberg, OP Research  
Closing price are as of 04/05/2022

### Price Chart



	1mth	3mth	6mth
Absolute %	-4.3	-40.0	+28.9
Rel. MSCI CHINA %	+1.9	-25.9	+10.4

### PE



### Company Profile

China Education Group is a private higher education provider in China. The Company operates universities and vocational colleges and enrolls students across all provinces in mainland China. The Company provides bachelor's degree programs, junior college diploma programs and vocational education programs.

## FY1H23 results up to expectations

- Adjusted net profit rose 15.1% yoy to RMB 1.045bn on the back of 18.0% yoy increase of revenue to RMB2.775bn.
- Solid outlook through the capacity expansion and the increase in tuition.
- Maintain Buy with new TP of HK\$10.60 on 12.0x FY23E PER.

**CEG's adjusted profit in-line in FY1H23.** Higher vocational education led the growth. Revenue of the segment rose 20.6% yoy to RMB2.348bn, contributing 85% of the total revenue. CEG continued to focus on the connotation construction of schools and promote high-quality development of schools. GPM down 1.9p.p. to 57.4%, which is believed to be due to the increase in investment in teachers and teaching. CEG further optimized OPEX, and the administrative cost rose only 3.8% yoy. CEG declared an interim DPS of RMB0.1638 (equivalent to HK\$0.1858), representing a payout ratio of 40.9%.

**Campus expansion.** CEG expects the physical capacity of Guangzhou College of Applied Science & Technology ("GCAS") to reach 50,000 in FY23/24 (compared to 17,500 without new campus in FY19/20) after it completes the construction of new campus in Zhaoqing City. On the other hand, CEG is building 9,400 new accommodations and refurbishing >20,000 accommodations across its schools. This allows CEG to grow the student enrolment capacity and increase the accommodation fee. For FY1H23, Capex reached RMB1.22bn. We expect the full-year Capex to be close to FY22 level (RMB2.144bn).

**Optimization of capital structure.** CEG raised HK\$1.6bn through equity placement in Jan 2023. As of Feb 2023, net gearing ratio was down 10.2p.p. yoy to 14.0%, and cash reserve climbed RMB827mn to RMB5.87bn. The optimisation of capital structure partly offset the higher borrowing costs. In FY1H23, finance costs increased 40.7% yoy to RMB190mn.

**Earnings growth is expected to slow down in FY23E.** This is partly due to the reduction of Hainan School's profit sharing rate (from 100% to 60%) starting in Feb 2023. Looking forward, the sizable capacity expansion plans and the increase in tuition enable CEG to sustain organic student growth even in the absence of new M&A. We expect CEG's net profit to grow at a CAGR of 9.7% in FY23E-25E.

**Maintain BUY with new TP of HK\$10.60.** We tune up CEG's EPS by 4.9%/8.2% in FY23E/24E to reflect the lower taxes which offset the lower GPM and the effect of share dilution due to the share placement. The new TP represents FY23E/24E PER of 12.0x/10.2x.

### Exhibit 1: Forecast and Valuation

Year to Aug (RMB mn)	FY21	FY22	FY23E	FY24E	FY25E
Revenue	3,682	4,756	5,558	6,393	7,165
Growth (%)	+37.5	+29.2	+16.9	+15.0	+12.1
Adj. net profit	1,606	1,800	1,970	2,309	2,374
Growth (%)	+63.2	+12.1	+9.4	+17.2	+2.8
Adj. diluted EPS (HK\$)	0.820	0.896	0.886	1.039	1.068
Adj. EPS growth (%)	+62.5	+9.3	-1.1	+17.2	+2.8
Change to previous EPS (%)			+4.9	+8.2	-3.2
Consensus EPS (HK\$)			0.951	1.073	1.229
ROE (%)	14.8	14.4	12.7	12.9	12.2
P/E (x)	8.8	8.0	8.1	6.9	6.7
P/B (x)	1.2	1.0	0.9	0.9	0.8
Yield (%)	5.6	5.6	4.9	5.8	5.9
DPS (HK\$)	0.399	0.403	0.355	0.415	0.427

Source: Bloomberg, OP Research

## Exhibit 2: Earnings review (Interim result ended Feb 2023)

(Ended Feb)	1H23	1H22	Yoy %		OP Comments
<b>Profitability Data (in RMB)</b>				% to the original forecasted FY23E result	
Revenue	2,775	2,351	+18.0%	48.9%	
Gross profit	1,593	1,394	+14.3%	47.7%	
Adjusted profit to shareholders	1,045	908	+15.1%	55.9%	The lower gross profit margin was offset by the lower tax expenses.
<b>Profitability Ratios (%)</b>				Our original forecast for FY23E	
GPM	57.4%	59.3%	-1.9p.p.	58.8%	We think this may due to the increase investment in teachers and teaching
NPM	37.7%	38.6%	-0.9p.p.	32.9%	
Effective tax rate	3.1%	1.8%	+1.3p.p.	10.0%	Effective tax rate remained at a very low level. CEG said Jiangxi School may complete the conversion into a for-profit school in the next FY, while other schools are waiting for policies for classified registration under the new private education law
<b>Operating ratio (% to revenue)</b>					
Selling & distribution	3.1%	3.1%	-	3.3%	
Administrative	13.9%	15.9%	-2.0p.p.	14.5%	

Source: OP Research

## Exhibit 3: Earnings revision

Year to Aug (RMB mn)	FY23E			FY24E			Reason for revision
	New	Old	% Chg	New	Old	% Chg	
Revenue	5,558	5,676	-2.1	6,393	6,476	-1.3	
Gross profit	3,198	3,339	-4.2	3,692	3,851	-4.1	
Gross margin	57.5%	58.8%	-1.3p.p.	57.8%	59.5%	-1.7p.p.	
Net Profit	1,970	1,869	+5.4	2,309	2,124	+8.7	This is mainly due to lower tax expenses, which offset the increase in finance costs and the lower profit margin. The conversion of CEG schools into for-profit schools may not come as early as we expected.
Diluted adj. EPS (HK\$)	0.886	0.845	+4.9	1.039	0.960	+8.2	

Source: OP Research

## Exhibit 4: Key assumptions revision

Student enrollments		Unit	SY22/23E	SY23/24E	SY24/25E
New		student	320,380	340,310	352,900
Old		student	320,380	340,310	352,900
Change (%)			-	-	-
<b>Student enrollments</b>					
(Exclude students enrolled in continuing education programs)					
New		student	246,680	266,610	280,700
Old		student	246,680	266,610	280,700
Change (%)			-	-	-
<b>Average revenue per student</b>			<b>FY23E</b>	<b>FY24E</b>	<b>FY25E</b>
New	RMB		17,348	18,785	20,106
Old	RMB		17,717	19,031	20,296
Change (%)			-2.1%	-1.3%	-0.9%

Source: OP Research

### Exhibit 5: Peer Group Comparison

								3-Yr								Sh px	
								EPS								Sh px	

\* Outliners and "N/A" entries are excl. from the calculation of averages

Source: Bloomberg, OP Research

### Exhibit 6: Positive catalysts and risks

Positives catalysts	Risks
<ul style="list-style-type: none"> <li>■ Solid track record in enhancing profitability of acquired schools</li> <li>■ Strong organic growth of students through capacity expansions</li> </ul>	<ul style="list-style-type: none"> <li>■ Higher than expected in effective tax rate after the full implementation of the new private education law.</li> <li>■ Policy uncertainty when implementing private education law</li> <li>■ Delay commencement of new campuses</li> </ul>

Source: OP research

## Financial Summary

Year to Aug	FY21	FY22	FY23E	FY24E	FY25E
<b>Income Statement (RMB mn)</b>					
Higher-education	2,759	3,931	4,679	5,408	6,069
Vocational education	703	636	643	668	726
Overseas education	220	189	236	317	370
<b>Turnover</b>	<b>3,682</b>	<b>4,756</b>	<b>5,558</b>	<b>6,393</b>	<b>7,165</b>
YoY%	+37.5	+29.2	+16.9	+15.0	+12.1
COGS	-1,507	-2,002	-2,360	-2,701	-3,007
<b>Gross profit</b>	<b>2,175</b>	<b>2,754</b>	<b>3,198</b>	<b>3,692</b>	<b>4,158</b>
Gross margin	59.1%	57.9%	57.5%	57.8%	58.0%
Other gain/losses	-47	57	228	254	254
Selling expenses	-168	-170	-175	-192	-213
Admin expenses	-474	-724	-767	-831	-896
Other expenses	0	0	0	0	0
<b>Total opex</b>	<b>-643</b>	<b>-894</b>	<b>-942</b>	<b>-1,023</b>	<b>-1,108</b>
<b>Operating profit (EBIT)</b>	<b>1,485</b>	<b>1,917</b>	<b>2,484</b>	<b>2,923</b>	<b>3,303</b>
Operating margin	40.3%	40.3%	44.7%	45.7%	46.1%
Interest Income	43	61	61	61	61
Change in FV of CB	145	299	0	0	0
Finance costs	-162	-308	-375	-365	-365
<b>Pre-tax profit</b>	<b>1,511</b>	<b>1,969</b>	<b>2,170</b>	<b>2,619</b>	<b>2,999</b>
Tax	-39	-33	-65	-131	-450
Minority interests	-28	-91	-135	-179	-175
<b>Net profit</b>	<b>1,444</b>	<b>1,845</b>	<b>1,970</b>	<b>2,309</b>	<b>2,374</b>
Net margin	39.2%	38.8%	35.4%	36.1%	33.1%
<b>Adj. net profit</b>	<b>1,606</b>	<b>1,800</b>	<b>1,970</b>	<b>2,309</b>	<b>2,374</b>
Adj. net margin	43.6%	37.8%	35.4%	36.1%	33.1%
YoY%	+63.2	+12.1	+9.4	+17.2	+2.8
<b>Adj. EBITDA</b>	<b>2,244</b>	<b>2,856</b>	<b>3,136</b>	<b>3,696</b>	<b>4,069</b>
EBITDA margin	60.9%	60.1%	56.4%	57.8%	56.8%
<b>Adj. diluted EPS (HK\$)</b>	<b>0.820</b>	<b>0.896</b>	<b>0.886</b>	<b>1.039</b>	<b>1.068</b>
YoY%	+62.5	+9.3	-1.1	+17.2	+2.8
<b>DPS (HK\$)</b>	<b>0.399</b>	<b>0.403</b>	<b>0.355</b>	<b>0.415</b>	<b>0.427</b>
Year to Aug	FY21	FY22	FY23E	FY24E	FY25E
<b>Cash Flow (RMB mn)</b>					
EBITDA	2,094	2,820	3,136	3,696	4,069
Chg in working cap	709	39	522	749	756
Others	-264	-87	0	0	0
<b>Operating cash</b>	<b>2,540</b>	<b>2,772</b>	<b>3,657</b>	<b>4,445</b>	<b>4,825</b>
Tax	-10	-19	-33	-65	-131
<b>Net cash from operations</b>	<b>2,530</b>	<b>2,753</b>	<b>3,624</b>	<b>4,380</b>	<b>4,694</b>
Capex	-2,841	-1,974	-2,000	-1,000	-1,000
Acquisitions	-477	-902	0	0	0
Other investment	-787	1,620	-2,296	0	0
Government grants	37	77	55	59	59
Div from assoc	0	0	0	0	0
Interests received	36	48	61	61	61
Others	-915	-613	0	0	0
<b>Investing cash</b>	<b>-4,947</b>	<b>-1,744</b>	<b>-4,180</b>	<b>-880</b>	<b>-880</b>
Issue of shares	1,696	981	1,406	0	0
Minority interests	-55	-336	-135	-179	-176
Dividends paid	-637	-395	-395	-788	-924
Interest paid	-301	-412	-375	-365	-365
Net change in bank loans and CB	2,300	704	0	0	0
Others	-643	-83	0	0	0
<b>Financing cash</b>	<b>2,360</b>	<b>459</b>	<b>501</b>	<b>-1,332</b>	<b>-1,464</b>
<b>Net change in cash</b>	<b>-57</b>	<b>1,468</b>	<b>-55</b>	<b>2,168</b>	<b>2,350</b>
Exchange rate or other Adj	-19	10	0	0	0
Opening cash	3,443	3,327	4,793	4,738	6,906
<b>Closing cash</b>	<b>3,327</b>	<b>4,793</b>	<b>4,738</b>	<b>6,906</b>	<b>9,256</b>
<b>CFPS(HK\$)</b>	<b>-0.029</b>	<b>0.730</b>	<b>-0.025</b>	<b>0.975</b>	<b>1.057</b>

Source: Company, OP Research

Year to Aug	FY21	FY22	FY23E	FY24E	FY25E
<b>Ratios</b>					
Gross margin (%) - blended	59.1	57.9	57.5	57.8	58.0
Operating margin (%)	40.3	40.3	44.7	45.7	46.1
Net margin (%)	39.2	38.8	35.4	36.1	33.1
Net adj. margin (%)	42.0	37.8	35.4	36.1	33.1
Selling exp/sales (%)	4.6	3.6	3.2	3.0	3.0
Admin exp/sales (%)	12.9	15.2	13.8	13.0	12.5
Payout ratio (%)	50.8	44.9	40.0	40.0	40.0
Effective tax (%)	2.8	1.7	3.0	5.0	15.0
Total debt/equity (%)	70.9	54.0	45.3	41.7	38.4
Net debt/equity (%)	42.6	25.1	21.3	9.6	Net cash
Net debt/EBITDA (x)	2.3	1.5	1.3	0.6	-0.1
Current ratio (x)	0.9	0.8	1.0	1.2	1.3
Quick ratio (x)	0.9	0.8	1.0	1.2	1.3
Inventory T/O (days)	0	0	0	0	0
AR T/O (days)	75	81	80	75	75
AP T/O (days)	7	10	10	10	10
Cash conversion cycle (days)	68	71	70	65	65
Asset turnover (x)	0.2	0.2	0.2	0.2	0.2
Financial leverage (x)	2.3	2.4	2.3	2.2	2.1
EBIT margin (%)	40.3	40.3	44.7	45.7	46.1
Interest burden (x)	1.0	1.0	0.9	0.9	0.9
Tax burden (x)	1.0	0.9	0.9	0.9	0.8
<b>Return on equity (%)</b>	<b>14.8</b>	<b>14.4</b>	<b>12.7</b>	<b>12.9</b>	<b>12.2</b>
Year to Aug	FY21	FY22	FY23E	FY24E	FY25E
<b>Balance Sheet (RMB mn)</b>					
Net PPE	12,126	15,700	17,118	17,413	17,717
Intangible assets	3,211	5,100	5,091	5,082	5,073
Goodwill	3,221	3,835	3,835	3,835	3,835
Deferred tax	13	13	13	13	13
Other non-current assets	2,300	2,753	2,753	2,753	2,753
<b>Non-current assets</b>	<b>20,870</b>	<b>27,401</b>	<b>28,810</b>	<b>29,096</b>	<b>29,391</b>
Inventories	0	0	0	0	0
Receivables, deposits and prepayments	754	1,058	1,218	1,314	1,472
Contract assets	74	68	68	68	68
Other current assets	1,721	256	2,556	2,556	2,556
Cash	3,327	4,793	4,738	6,906	9,256
<b>Current assets</b>	<b>5,876</b>	<b>6,175</b>	<b>8,580</b>	<b>10,844</b>	<b>13,352</b>
AP	27	56	65	74	82
Accruals & other payables	1,935	1,992	1,992	1,992	1,992
Tax	89	98	33	65	131
Bank loans & leases	1,473	1,831	1,831	1,831	1,831
Contract liabilities	2,266	3,178	3,836	4,657	5,563
Convertible bonds	2,244	0	0	0	0
Other current liabilities	459	458	458	458	458
<b>Current liabilities</b>	<b>8,492</b>	<b>7,613</b>	<b>8,214</b>	<b>9,077</b>	<b>10,058</b>
Bank loans	4,618	7,057	7,057	7,060	7,060
Convertible bonds	0	3	3	0	0
Other non-current liabilities	1,879	2,326	2,326	2,326	2,326
<b>Non-current liabilities</b>	<b>6,497</b>	<b>9,386</b>	<b>9,386</b>	<b>9,386</b>	<b>9,386</b>
<b>Total net assets</b>	<b>11,757</b>	<b>16,577</b>	<b>19,790</b>	<b>21,477</b>	<b>23,299</b>
<b>Total Equity</b>	<b>11,757</b>	<b>16,577</b>	<b>19,790</b>	<b>21,477</b>	<b>23,299</b>
<b>Shareholder's equity</b>	<b>10,920</b>	<b>14,008</b>	<b>17,086</b>	<b>18,594</b>	<b>20,240</b>
Share capital	0	0	0	0	0
Reserves	10,920	14,008	17,086	18,594	20,240
NCI	837	2,569	2,704	2,883	3,058
<b>BVPS (HK\$)</b>	<b>5.76</b>	<b>7.04</b>	<b>7.63</b>	<b>8.31</b>	<b>9.04</b>

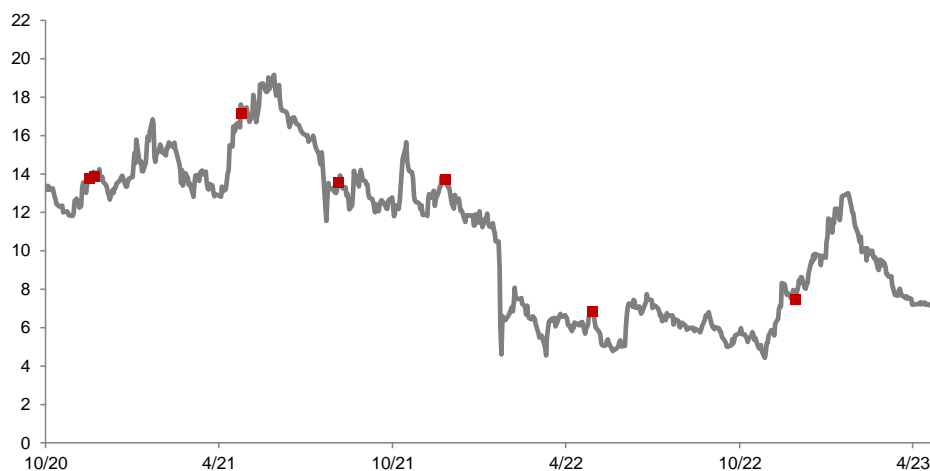
## Our recent reports

Date	Company / Sector	Ticker	Title	Rating	Analyst
04/05/2023	Edvantage Group	382	FY1H23 results showed the strong organic growth	BUY	John Siah
27/04/2023	New Higher Edu	2001	FY1H23 results in-line	BUY	John Siah
19/04/2023	361 Degrees	1361	2023Q1 sales bounced as expected	BUY	John Siah
24/03/2023	Micro Connect	-	Releasing the investment value of SMEs in China through technological innovation( <a href="#">中/ENG</a> )	NR	John Siah
02/03/2023	Xinyi Energy	3868	FY22 results miss, expecting a rebound for FY23E	BUY	John Siah
24/02/2023	Edvantage Group	382	FY23Q1 operations on track	BUY	John Siah
13/02/2023	Newborn Town	9911	More social apps expecting to begin bearing fruit	BUY	John Siah
02/02/2023	China Water Affairs	855	Tapping into opportunities in the direct drinking water market	BUY	John Siah
18/01/2023	361 Degrees	1361	The worst has likely passed	BUY	John Siah
05/12/2022	China Edu Group	839	Higher vocational education leads the growth	BUY	John Siah
05/12/2022	New Higher Edu	2001	FY22 results slightly beat, emphasis on quality education	BUY	John Siah
29/11/2022	Edvantage Group	382	FY22 earnings beat, moderate growth ahead	BUY	John Siah
20/10/2022	361 Degrees	1361	Lockdown may impact sales in Q4	BUY	John Siah
20/10/2022	Greentown Mgmt	9979	Impressive new contracts growth in Q3 under severe headwinds	BUY	John Siah
16/09/2022	EVA Holdings	838	Decent earnings outlook supported by strong order backlogs	BUY	John Siah
02/09/2022	Tian Lun Gas	1600	1H22 results missed, tough near-term outlook	HOLD	John Siah
02/09/2022	HK Tech Venture	1137	1H22 results beats amid better costs management	BUY	John Siah
31/08/2022	AAC Tech	2018	Headwinds likely to persist in 2H22E	HOLD	John Siah
31/08/2022	Truly Int'l	732	1H22 earnings decline as expected, negatives priced in	BUY	John Siah
26/08/2022	361 Degrees	1361	1H22 earnings beats, strong growth in e-commerce and kids' wear	BUY	John Siah

## Historical recommendations and target price: China Edu Group (839 HK)

(as of 05/04/2023)

(HK\$)



Date	Rating	TP	Close	Date	Rating	TP	Close
1 20 Nov 2020	BUY	HK\$19.10	HK\$14.90	6 4 May 2022	BUY	HK\$11.00	HK\$7.00
2 25 Nov 2020	BUY	HK\$20.00	HK\$15.08	7 5 Dec 2022	BUY	HK\$10.10	HK\$7.72
3 29 Apr 2021	BUY	HK\$21.80	HK\$18.46	8 5 May 2023	BUY	HK\$10.60	HK\$7.18
4 9 Aug 2021	BUY	HK\$20.00	HK\$14.42				
5 29 Nov 2021	BUY	HK\$18.70	HK\$14.62				

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