

Hong Kong

**ADD** (no change)

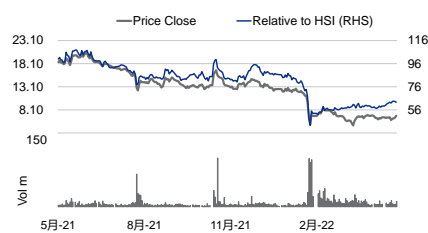
Consensus ratings\*: Buy 23 Hold 3 Sell 0

Current price:	HK\$6.81
Target price:	HK\$23.20
Previous target:	HK\$23.50
Up/downside:	240.7%
CGI / Consensus:	36.6%
Reuters:	0839.HK
Bloomberg:	839 HK
Market cap:	US\$2,074m
	HK\$16,271m
Average daily turnover:	US\$10.41m
	HK\$81.35m
Current shares o/s:	2,220m
Free float:	25.0%

\*Source: Bloomberg

**Key changes in this note**

- FY22F EPS decreased by 1.7%.
- FY23F EPS decreased by 1.4%.
- FY24F EPS decreased by 1.6%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	-0.7	-3	-63.1
Relative (%)	3.1	7.5	-35.1

**Major shareholders**

	% held
Mr. Yu Guo	37.5
Mr. Xie Ketao	37.5

**Analysts**

**Hang Xu**

T (852) 3698 6308  
E xuhang@chinastock.com.hk

**Lei Yang**

T (86) 21 6162 9676  
E yanglei@chinastock.com.hk

# China Education Group

## Results in line, with a promising enrolment outlook

- China Education Group (CEG) reported 1H FY8/22 revenue of Rmb2,351m, up 28.9% yoy, and adjusted net profit of Rmb909m, up 20.1% yoy, in line with our expectations.
- We expect FY8/22F full-year revenue growth of 28% yoy and adjusted net profit growth of 20% yoy, with about 14–18% organic yoy growth in the adjusted net profit.
- CEG has received preliminary approval for its 22/23 school year new student intake quotas and tuition increases for several of its programs, with 7–100% quota increases and 7–20% tuition increases.
- Reiterate Add with new DCF-based TP of HK\$23.2.

## Results in line, with strong growth in higher vocational education

1H FY8/22 revenue growth in the higher vocational education segment was 44.2% yoy, but this was offset by a 7.8% and 35.7% yoy revenue drop in the secondary vocational education and global education segments, because the pandemic control measures affected the student recruitment process for these two segments. The student recruitment for these two segments is market-oriented recruitment instead of national unified enrolment, which is used for higher vocational education. Excluding the consolidation of Jincheng College (in Sep 2021), the organic revenue growth in 1H FY8/22 was 16% yoy, with 27% yoy organic revenue growth in the higher vocational education segment. Its gross margin was flat yoy, and its operating margin expanded by 4.5% pts yoy to 58.0%, because of a decline in the selling expenses to total revenue ratio, reflecting fewer student recruitment campaigns amid the pandemic. CEG announced a share repurchase plan instead of an interim dividend. The total amount of the share repurchases will be no more than Rmb500m. CEG will resume its dividend payout when market conditions improve. We expect FY8/22F full-year revenue growth of 28% yoy and adjusted net profit growth of 20% yoy, with 14–18% organic yoy growth in adjusted net profit.

## Promising enrolment outlook and overseas market releases

CEG has received preliminary approval for the 22/23 school year new student intake quotas and tuition increases for several of its programs, with 7–100% quota increases and 7–20% tuition increases. Owing to the pandemic, the global education segment depends mainly on on-shore students in 1H FY8/22, since the overseas student number has fallen considerably. But the Australian government reopened its border for foreign students in Feb 2022, and the global education segment recovered strongly in Mar. In Mar 2022, CEG saw new student applications increase by 63% yoy and 75% vs the same period in 2019 for its Australia school, which is expected to drive flat yoy and 90% hoh segment profit growth in 2H FY8/22F. CEG paused its M&A plan, given the weaker stock market. The recent primary market valuation of private universities still stands at 10–20x P/E.

## Government policy still in favour of higher vocational education

Recently, the new Vocational Education Law was announced by the National Congress, promoting vocational education with measures including welcoming private capital, integrating industry and education, and providing more autonomy to schools. CEG will choose the for-profit business model for all of its schools, and the process is under way in some provinces. Although the MoE is encouraging an acceleration of the process, different provinces are at different stages, based on their actual situation. In Shanghai, six private higher-education schools have started the process. One Shanghai higher-education school owned by a HK-listed company has already been approved by the education department to convert to a for-profit school and has seen a continuous increase in student enrolment and tuition. We expect the for-profit conversions to be completed by as early as end-2022.

**Financial Summary**

	Aug-20A	Aug-21A	Aug-22F	Aug-23F	Aug-24F
Revenue (Rmbm)	2,678	3,682	4,681	5,330	6,109
Operating EBITDA (Rmbm)	667	1,912	2,220	2,541	2,894
Net Profit (Rmbm)	633	1,444	1,694	1,976	2,287
Normalised EPS (Rmb)	0.52	0.71	0.85	0.98	1.12
Normalised EPS Growth	23.3%	35.2%	20.3%	14.9%	14.3%
FD Normalised P/E (x)	11.00	8.74	6.62	5.76	5.04
DPS (Rmb)	0.24	0.23	0.42	0.48	0.55
Dividend Yield	4.21%	3.96%	7.25%	8.36%	9.58%
EV/EBITDA (x)	12.41	9.09	7.60	6.60	5.70
P/FCFE (x)	NA	NA	11.05	8.83	7.33
Net Gearing	18.7%	42.6%	38.3%	33.0%	27.2%
P/BV (x)	1.35	1.16	1.09	1.02	0.94
ROE	14.0%	16.2%	16.8%	18.0%	19.1%
% Change In Normalised EPS Estimates			(1.69%)	(1.41%)	(1.59%)
Normalised EPS/consensus EPS (x)			1.12	1.14	1.18

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

# Results in line, with a promising enrolment outlook

## Reiterate Add with new DCF-based TP of HK\$23.2

We raised our revenue forecasts, given strong expected student enrolment and tuition increases, but cut our adjusted earnings forecasts for FY8/22–24F by 1.7%, 1.4% and 1.6%, respectively, as its margin is expected to be lower than our previous forecasts given a share-based payment rebate in FY8/21. We like China Education Group because of its 1) strong organic growth capability, and 2) likely future M&A. The main risk is negative government policies for the education sector.

**Figure 1: CEG results review**

FYE Aug (Rmb m)	1H FY8/21	1H FY8/22	yoy
<b>Revenue</b>	<b>1,823.4</b>	<b>2,350.6</b>	<b>28.9%</b>
Cost of revenue	-745.9	-957.4	28.3%
<b>Gross profit</b>	<b>1,077.5</b>	<b>1,393.2</b>	<b>29.3%</b>
<b>Gross margin</b>	<b>59.1%</b>	<b>59.3%</b>	<b>0.2% pts</b>
Selling expenses	-85.7	-73.2	-14.6%
Administrative expenses	-208.3	-372.7	78.9%
Others	135.6	210.7	55.4%
<b>Operating profit</b>	<b>975.9</b>	<b>1,362.9</b>	<b>39.7%</b>
<b>Operating margin</b>	<b>53.5%</b>	<b>58.0%</b>	<b>4.5% pts</b>
Net finance income	-93.3	-134.7	44.3%
<b>Profit before taxation</b>	<b>882.5</b>	<b>1,228.2</b>	<b>39.2%</b>
Taxation	-30.3	-21.9	-27.9%
Non-controlling interests	20.8	37.9	82.2%
<b>Profit attributable to shareholders</b>	<b>831.4</b>	<b>1,168.5</b>	<b>40.5%</b>
Extraordinary items	0.0	0.0	N/A
<b>Adjusted net profit</b>	<b>756.7</b>	<b>908.6</b>	<b>20.1%</b>

SOURCES: CGIS RESEARCH, COMPANY REPORTS

**Figure 2: Revision to forecasts**

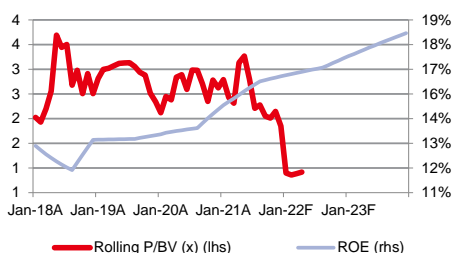
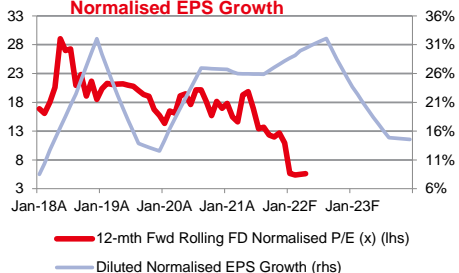
FYE Aug (Rmb m)	FY22F			FY23F			FY24F		
	Old	New	% change	Old	New	% change	Old	New	% change
Revenue	4,352.6	4,694.4	7.9%	5,005.5	5,378.4	7.5%	5,749.6	6,167.2	7.3%
Gross margin	59.2%	59.2%	0.0% pts	59.2%	59.2%	0.0% pts	59.2%	59.2%	0.0% pts
Operating margin	47.1%	43.1%	-4.0% pts	46.7%	43.2%	-3.5% pts	46.4%	43.0%	-3.4% pts
Adjusted net profit	1,926.6	1,898.9	-1.4%	2,206.7	2,194.2	-0.6%	2,527.5	2,509.8	-0.7%

SOURCES: CGIS RESEARCH, COMPANY REPORTS

**Figure 3: China Education DCF valuation**

FCF computation (Rmb m)	FY8/22F	FY8/23F	FY8/24F	FY8/25F	FY8/26F	FY8/27F	FY8/28F	FY8/29F	FY8/30F	FY8/31F	FY8/32F	FY8/33F
<b>EBIT</b>	<b>2,022.2</b>	<b>2,325.4</b>	<b>2,649.4</b>	<b>2,861.4</b>	<b>3,090.3</b>	<b>3,337.5</b>	<b>3,604.5</b>	<b>3,892.9</b>	<b>4,204.3</b>	<b>4,540.6</b>	<b>4,903.9</b>	<b>5,296.2</b>
Taxes	-46.6	-54.5	-62.9	-67.9	-73.3	-79.2	-85.5	-92.4	-99.8	-107.7	-116.4	-125.7
<b>NOPAT</b>	<b>1,975.6</b>	<b>2,270.9</b>	<b>2,586.5</b>	<b>2,793.5</b>	<b>3,016.9</b>	<b>3,258.3</b>	<b>3,519.0</b>	<b>3,800.5</b>	<b>4,104.5</b>	<b>4,432.9</b>	<b>4,787.5</b>	<b>5,170.5</b>
<i>NOPAT growth</i>	<i>17.2%</i>	<i>14.9%</i>	<i>13.9%</i>	<i>8.0%</i>	<i>8.0%</i>	<i>8.0%</i>	<i>8.0%</i>	<i>8.0%</i>	<i>8.0%</i>	<i>8.0%</i>	<i>8.0%</i>	<i>8.0%</i>
D&A	462.6	495.2	527.7	559.4	593.0	628.6	666.3	706.2	748.6	793.5	841.2	891.6
<b>Funds from operation</b>	<b>2,438.2</b>	<b>2,766.1</b>	<b>3,114.3</b>	<b>3,352.9</b>	<b>3,609.9</b>	<b>3,886.9</b>	<b>4,185.2</b>	<b>4,506.7</b>	<b>4,853.1</b>	<b>5,226.4</b>	<b>5,628.7</b>	<b>6,062.1</b>
Change in net working Capital	184.8	167.7	104.7	107.9	111.1	114.5	117.9	121.4	125.1	128.8	132.7	136.7
<b>Cash flow from operation</b>	<b>2,623.1</b>	<b>2,933.8</b>	<b>3,219.0</b>	<b>3,460.8</b>	<b>3,721.0</b>	<b>4,001.3</b>	<b>4,303.1</b>	<b>4,628.2</b>	<b>4,978.2</b>	<b>5,355.2</b>	<b>5,761.4</b>	<b>6,198.8</b>
Capex	-1,000.0	-1,000.0	-1,000.0	-1,010.0	-1,020.1	-1,030.3	-1,040.6	-1,051.0	-1,061.5	-1,072.1	-1,082.9	-1,093.7
<b>Free cash flow from operation</b>	<b>1,623.1</b>	<b>1,933.8</b>	<b>2,219.0</b>	<b>2,450.8</b>	<b>2,700.9</b>	<b>2,971.0</b>	<b>3,262.5</b>	<b>3,577.1</b>	<b>3,916.7</b>	<b>4,283.1</b>	<b>4,678.5</b>	<b>5,105.1</b>
<i>FCF growth</i>	<i>-1882.5%</i>	<i>19.1%</i>	<i>14.7%</i>	<i>10.4%</i>	<i>10.2%</i>	<i>10.0%</i>	<i>9.8%</i>	<i>9.6%</i>	<i>9.5%</i>	<i>9.4%</i>	<i>9.2%</i>	<i>9.1%</i>
Terminal free cash flow	65,381.0	<b>Assumptions</b>										
Total discounted free cash flow	22,188.4	<b>Cost of equity</b> 8.8%										
Present value of terminal free cash flow	25,841.4	Risk free rate 2.5%										
		Market Risk Premium 7.0%										
<b>Total present value of forecasted free cash flows</b>	<b>48,029.8</b>	Beta 0.90										
Less: Net Debt	4,785.7	<b>Cost of debt (after tax)</b> 3.8%										
<b>Equity Value</b>	<b>43,244.2</b>	<b>Target Debt / (Debt + Equity)</b> 15.0%										
No. Shares (millions)	2,220.4	<b>WACC</b> 8.0%										
<b>Per Share Equity Value (Rmb)</b>	<b>19.5</b>	<b>Terminal growth rate</b> 3.0%										
Exchange rate	0.8											
<b>Target price (HK\$)</b>	<b>23.5</b>											

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

**BY THE NUMBERS**
**P/BV vs ROE**

**12-mth Fwd FD Normalised P/E vs FD Normalised EPS Growth**

**Profit & Loss**

(Rmbm)	Aug-20A	Aug-21A	Aug-22F	Aug-23F	Aug-24F
<b>Total Net Revenues</b>	<b>2,678</b>	<b>3,682</b>	<b>4,681</b>	<b>5,330</b>	<b>6,109</b>
<b>Gross Profit</b>	<b>1,601</b>	<b>2,175</b>	<b>2,771</b>	<b>3,155</b>	<b>3,616</b>
<b>Operating EBITDA</b>	<b>667</b>	<b>1,912</b>	<b>2,220</b>	<b>2,541</b>	<b>2,894</b>
Depreciation And Amortisation	-273	-370	-463	-495	-528
<b>Operating EBIT</b>	<b>394</b>	<b>1,542</b>	<b>1,757</b>	<b>2,046</b>	<b>2,366</b>
Financial Income/(Expense)	-93	-162	-167	-167	-167
Pretax Income/(Loss) from Assoc.	0	0	0	0	0
Non-Operating Income/(Expense)	0	0	0	0	0
<b>Profit Before Tax (pre-EI)</b>	<b>730</b>	<b>1,511</b>	<b>1,790</b>	<b>2,080</b>	<b>2,399</b>
Exceptional Items					
<b>Pre-tax Profit</b>	<b>302</b>	<b>1,380</b>	<b>1,590</b>	<b>1,880</b>	<b>2,199</b>
Taxation	-19	-39	-46	-54	-62
Exceptional Income - post-tax					
<b>Profit After Tax</b>	<b>282</b>	<b>1,341</b>	<b>1,544</b>	<b>1,826</b>	<b>2,137</b>
Minority Interests	-77	-28	-50	-50	-50
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax	428	131	200	200	200
Preference Dividends (Australia)					
<b>Net Profit</b>	<b>633</b>	<b>1,444</b>	<b>1,694</b>	<b>1,976</b>	<b>2,287</b>
Normalised Net Profit	710	1,472	1,744	2,026	2,337
<b>Fully Diluted Normalised Profit</b>	<b>1,061</b>	<b>1,574</b>	<b>1,894</b>	<b>2,176</b>	<b>2,487</b>

**Cash Flow**

(Rmbm)	Aug-20A	Aug-21A	Aug-22F	Aug-23F	Aug-24F
<b>EBITDA</b>	<b>667</b>	<b>1,912</b>	<b>2,220</b>	<b>2,541</b>	<b>2,894</b>
Cash Flow from Invt. & Assoc.	0	-29	0	0	0
Change In Working Capital	-549	709	178	148	96
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense	709	326	463	495	528
Other Operating Cashflow	196	-216	-146	-178	-211
Net Interest (Paid)/Received	-93	-162	-167	-167	-167
Tax Paid	-20	-10	-46	-54	-62
<b>Cashflow From Operations</b>	<b>911</b>	<b>2,530</b>	<b>2,501</b>	<b>2,786</b>	<b>3,078</b>
Capex	-844	-2,841	-1,000	-1,000	-1,000
Disposals Of FAs/subsidiaries	983	7,551	0	0	0
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	-2,677	-9,646	-200	-200	-200
<b>Cash Flow From Investing</b>	<b>-2,539</b>	<b>-4,936</b>	<b>-1,200</b>	<b>-1,200</b>	<b>-1,200</b>
Debt Raised/(repaid)	347	1,238	-167	-167	-167
Proceeds From Issue Of Shares	1,799	1,686	0	0	0
Shares Repurchased					
Dividends Paid	-411	-637	-922	-1,063	-1,219
Preferred Dividends					
Other Financing Cashflow	-105	73	0	0	0
<b>Cash Flow From Financing</b>	<b>1,630</b>	<b>2,360</b>	<b>-1,089</b>	<b>-1,229</b>	<b>-1,385</b>
Total Cash Generated	3	-45	213	356	492
<b>Free Cashflow To Equity</b>	<b>-1,280</b>	<b>-1,167</b>	<b>1,135</b>	<b>1,419</b>	<b>1,711</b>
<b>Free Cashflow To Firm</b>	<b>-1,535</b>	<b>-2,243</b>	<b>1,468</b>	<b>1,753</b>	<b>2,044</b>

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

**BY THE NUMBERS... cont'd**

<b>Balance Sheet</b>					
<b>(Rmbm)</b>	<b>Aug-20A</b>	<b>Aug-21A</b>	<b>Aug-22F</b>	<b>Aug-23F</b>	<b>Aug-24F</b>
Total Cash And Equivalents	3,443	3,327	3,540	3,896	4,389
Total Debtors	594	752	977	1,271	1,652
Inventories					
Total Other Current Assets	1,004	1,797	1,797	1,797	1,797
<b>Total Current Assets</b>	<b>5,041</b>	<b>5,876</b>	<b>6,314</b>	<b>6,964</b>	<b>7,837</b>
Fixed Assets	3,259	5,851	6,847	12,126	12,664
Total Investments	0	0	0	0	0
Intangible Assets	4,091	6,432	6,432	6,432	6,432
Total Other Non-Current Assets	5,584	8,588	8,330	3,755	3,890
<b>Total Non-current Assets</b>	<b>12,934</b>	<b>20,871</b>	<b>21,609</b>	<b>22,313</b>	<b>22,986</b>
Short-term Debt	292	1,473	1,473	1,473	1,473
Current Portion of Long-Term Debt					
Total Creditors	1,742	2,340	878	1,053	1,210
Other Current Liabilities	1,345	2,435	4,302	4,568	4,888
<b>Total Current Liabilities</b>	<b>3,379</b>	<b>6,249</b>	<b>6,653</b>	<b>7,094</b>	<b>7,572</b>
Total Long-term Debt	4,815	6,862	6,862	6,862	6,862
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	874	1,880	1,880	1,880	1,880
<b>Total Non-current Liabilities</b>	<b>5,689</b>	<b>8,741</b>	<b>8,741</b>	<b>8,741</b>	<b>8,741</b>
Total Provisions	0	0	0	0	0
<b>Total Liabilities</b>	<b>9,067</b>	<b>14,990</b>	<b>15,394</b>	<b>15,836</b>	<b>16,313</b>
Shareholders' Equity	8,573	10,919	11,641	12,504	13,523
Minority Interests	334	837	887	937	987
<b>Total Equity</b>	<b>8,907</b>	<b>11,757</b>	<b>12,529</b>	<b>13,442</b>	<b>14,510</b>

<b>Key Ratios</b>					
	<b>Aug-20A</b>	<b>Aug-21A</b>	<b>Aug-22F</b>	<b>Aug-23F</b>	<b>Aug-24F</b>
Revenue Growth	37.0%	37.5%	27.1%	13.9%	14.6%
Operating EBITDA Growth	12.4%	86.6%	18.5%	13.3%	12.9%
Operating EBITDA Margin	40.9%	55.5%	51.7%	51.4%	50.6%
Net Cash Per Share (Rmb)	-0.82	-2.26	-2.16	-2.00	-1.78
BVPS (Rmb)	4.24	4.92	5.24	5.63	6.09
Gross Interest Cover	8.88	10.32	11.74	13.47	15.39
Effective Tax Rate	6.38%	2.84%	2.92%	2.87%	2.83%
Net Dividend Payout Ratio	46.0%	32.0%	48.7%	48.9%	49.0%
Accounts Receivables Days	79.57	66.68	67.42	76.98	87.55
Inventory Days	-	-	-	-	-
Accounts Payables Days	9.66	7.30	5.92	6.76	7.69
ROIC (%)	9.8%	14.6%	10.5%	11.7%	13.0%
ROCE (%)	6.5%	9.8%	9.6%	10.5%	11.5%
Return On Average Assets	7.39%	7.89%	7.72%	8.36%	9.00%

<b>Key Drivers</b>					
	<b>Aug-20A</b>	<b>Aug-21A</b>	<b>Aug-22F</b>	<b>Aug-23F</b>	<b>Aug-24F</b>
Overall student enrolment growth (%)	15.9%	25.7%	8.8%	2.6%	2.9%
Blended ASP growth (%)	15.4%	7.7%	15.6%	11.0%	11.3%

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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CGS-CIMB Securities (USA) Inc. neither expects to receive nor intends to seek compensation for investment banking services from any of the company mentioned within the next 3 months.

As of the end of the month immediately preceding the date of publication of this report, CGS-CIMB Securities (USA) Inc. beneficially owns 1% or more of any class of common equity securities of .

**Other jurisdictions:** In any other jurisdictions, except if otherwise restricted by laws or regulations, this report is only for distribution to professional, institutional or sophisticated investors as defined in the laws and regulations of such jurisdictions.

Distribution of stock ratings and investment banking clients for quarter ended on 31 Dec 2021		
619 companies under coverage for quarter ended on 31 Dec 2021		
	Rating Distribution (%)	Investment Banking clients (%)
Add	71.1%	1.5%
Hold	21.8%	0.0%
Reduce	7.1%	0.0%

**Spitzer Chart for stock being researched ( 2 year data )**

**China Education Group (839 HK)**

## RECOMMENDATION FRAMEWORK

### Stock Ratings Definition:

Add	The stock's total return is expected to reach 15% or higher over the next 12 months.
Hold	The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
Reduce	The stock's total return is expected to fall below negative 10% over the next 12 months.

*The total expected return of a stock is defined as the sum of the:(i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.*

### Sector Ratings Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

### Country Ratings Definition:

Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.

## Analyst Certification

The analyst who is primarily responsible for the content of this report, in whole or in part, certifies that with respect to the securities or issuer covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject, securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by the analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the securities covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the securities covered in this research report three business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong-listed companies covered in this report; and (4) have any financial interests in the Hong Kong-listed companies covered in this report.

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