

Equity Research | Greater China | Education Services 25 July 2016

Acquisition of Lucrum in Singapore

- CMLE announced to acquire Lucrum Development (Lucrum) today at a consideration of SGD68mn (HKD388mn), or P/B of c.3.3x.
- Lucrum's principal asset is a school property in Singapore, which is currently leased to an independent 3rd-party K-12 school operator with lease to be expired in Oct 2017. CMLE targets to turn it into its first bilingual international school for K12 education overseas.
- The acquisition is expected to be completed on 1 Sept 2016, and CMLE will regard it as an investment property under the current lease team. We project EPS accretive of 3.4% for FY17E base on the rental income. We have revised up our DCF-based PT to HKD7.4 (prev: HKD7.1), but downgraded our rating to HOLD on rich valuation. It currently trades at 46.5/38.0x PER for FY16/17E.

Acquisition financed by internal funding and bank borrowings. The acquisition can be more than covered by CMLE internally, given our estimated net cash position of RMB1bn and zero bank borrowings in FY16E.

The school property. The property is located in 11 Hillside Drive, Singapore, with a site area/GFA of 7,568.6/4,343.46sq.m.. It has 30 classrooms, with an estimated annual capacity of c.600 students. As at 30 Jun 2016, the unaudited book value of the property was c.HKD338mn, whereas the total unaudited net asset and total asset value of Lucrum were HKD119/424mn. It is currently leased to Hillside World Academy Pte. Ltd, an independent 3rd party K-12 school operator, with lease expiring on 31 Oct 2017, subject to two consecutive renewal options for a further term of 3 years in each renewal (max. 6 years) to Oct 2023. The monthly rental is SGD200k, hence gross rental yield for CMLE is 3.5%.

EPS accretive of c.3.4% from rental income in FY17E. CMLE intends to run its first bilingual international school for K12 education overseas with the acquisition of Lucrum. However, as the lease is still subject to a maximum of 6 years' term, it will be treated as an investment property for the time being. With the acquisition due to be completed on 1 Sept 2016, we expect EPS enhancement of c.3.4% for FY17E.

Downgraded to HOLD. We have tweaked our earnings estimates slightly downwards by 0.4% in FY16E, given the additional capex and interest expenses but adjusted it upwards by 3.4% for FY17E. Thus, we have revised up our PT to HKD7.40 (prev: HKD7.10). CMLE currently trades at 46.5x/38.0x PER for FY17/18E. Valuation is stretched given the recent share price gains. Its peers listed in the US market trades at an average of 33.5x/25.4x FY17/18E (see Figure 2).

China Maple Leaf Educational (CMLE) (1317 HK)

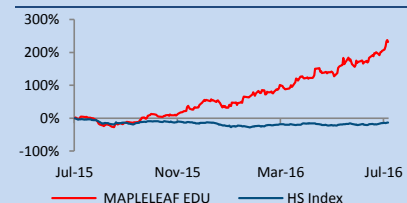
Hold

(Downgrade)

Price Target	HK\$7.4	
(Revision)	(+4.2%)	
(downside)	(-8.6%)	
EPS revision	2016E (-0.4%)	2017E (+3.4%)
Close price	HKD8.16	
Market cap.	HKD7,941mn	
Free float	42.23%	
52-week range	HKD1.68 – 8.41	
3-mth ave. T/O	HKD32.8mn	

Price as of 22 July 2016

Stock rel. HSI performance (%)



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Valuation. The expected rental income from Lucrum will be booked as other income and will book in FY17E, and hence we have maintained our revenue forecast but tweaked our earnings estimates slightly downwards by 0.4% in FY16E, given the additional capex and interest expenses but adjusted it upwards by 3.4% for FY17E with the expectation of rental income. As such, our PT is adjusted upwards by 4.2% to HKD7.40. Valuation is stretched given the recent share price gains. Its peers listed in the US market trades at an average of 33.5x/25.4x FY17/18E. We downgraded our rating to HOLD from BUY.

Figure 1: Revised DCF valuation

Assumptions		Benchmark basis	
Beta	1.2	CMLE's historical beta	
Market premium (rm-rf)	9.93%	Forward Equity Risk Premium: implied market discount rate of 10.01%	
Risk free rate (rf)	0.08%	Hong Kong Generic 3 month government bills	
Cost of equity (re)	11.5%		
Cost of debt (rd)	5.2%	Reference to historical cost of debt	
MV (equity) (HK\$m)	\$11,095		
MV (MI)			
MV (preference share)			
Debt	-		
Total	\$11,095		
E/ (D+E+MI+P)	70%		
MI/ (D+E+MI+P)	0%		
P/(D+E+MI+P)	0%		
D/ (D+E+MI+P)	30%		
Country risk premium	0%		
Terminal growth (g)	1%		
WACC	9.3%		

DCF	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
WACC @ 9.3%										
FCF (RMB mn)	(105.3)	13.2	263.5	315.2	328.0	399.9	422.4	465.5	489.2	513.6
Discount Factor	0.91	0.84	0.77	0.70	0.64	0.59	0.54	0.49	0.45	0.41
Discounted FCF (RMB mn)	(96.3)	11.1	201.6	220.6	209.9	234.0	226.1	227.9	219.1	210.3
Present value of estimated FCF (RMB mn)	1,454									
Terminal Value (RMB mn)	6,222									
Enterprise Value (RMB mn)	7,676									
+ Cash & Cash Equivalent	1,030									
- Debt	-									
- Minority Interest	-									
Equity Value	8,706									
Total shares outstanding	1,360									
Equity Value per share (RMB)	6.4									
Equity Value per share (HKD)	7.4									

Source: CSCI research estimates, (RMB/HKD: 1.1575, as of 25 July 2016)

Figure 2: Peers valuation

Name	Rating	PT	Ticker	Curre ncy	FYE	Mkt Cap		EV/		PBR (x)	ROIC (%)	ROA (%)	D yield (%)	
						Last Price	(bn HKD)	1-yr fwd PER (x)	2-yr fwd PER (x)					EBITDA (X)
HK-listed														
CMLE	HOLD	7.9	1317 HK	HKD	08/2015	7.1	10.0	46.3	37.7	28.4	5.4	11.2	8.5	0.8
Virscend Edu.	NR	N/A	1565 HK	HKD	12/2015	4.7	12.5	42.8	34.4	33.2	N/A	11.5	4.2	0.0
<i>HK-Average</i>							11.2	44.6	36.1	30.8	5.4	11.4	6.4	0.4
US-listed														
Tal Edu.	NR	N/A	xrs us equity	USD	02/2016	63.6	5.1	42.6	29.6	33.7	11.8	10.2	11.2	-
New Oriental Edu.	NR	N/A	edu us equity	USD	05/2016	44.4	7.0	24.6	20.0	17.8	5.0	12.5	10.4	0.0
Nord Anglia	NR	N/A	nord us equity	USD	08/2015	21.6	11.6	33.4	26.5	15.8	4.9	6.4	1.7	0.0
<i>US-Average</i>							7.9	33.5	25.4	22.4	7.2	9.7	7.8	-
Average of All - excluding China Maple Leaf							9.0	35.8	27.6	25.1	7.2	10.2	6.9	-

Source: CSCI research, Bloomberg.

Income statement (RMBm)

Year end: Aug	2014	2015	2016E	2017E	2018E
Revenue	540	653	857	1,022	1,229
COGS	(305)	(354)	(447)	(536)	(648)
Gross profit	235	299	410	486	581
Marketing expenses	(22)	(22)	(30)	(36)	(43)
Administrative expenses	(74.5)	(102)	(118)	(141)	(169)
Other expenses	(24.1)	(8)	(11)	(13)	(15)
Investment and other gains/ (losses)	4.1	14.0	10.3	26.0	28.5
EBITDA	158	227	323	394	466
Depreciation & Amortization	39	46	61	71	84
EBIT	119	181	262	323	381
Net interest expenses/ (income)	14	(4)	(10)	(10)	(11)
Non-recurring items	(87)	20	-	-	-
JVs and associates	-	-	-	-	-
Pretax profit	48	217	272	333	392
Taxation	(8)	(11)	(22)	(27)	(31)
Minority interests	-	-	-	-	-
Net profit	40	206	250	306	361
Net profit (*adjusted)	127	186	250	306	361
Basic EPS (RMB)	0.05	0.17	0.18	0.23	0.27
Basic EPS (RMB) - (adjusted)	0.17	0.15	0.18	0.23	0.27
Diluted EPS (RMB)	0.05	0.16	0.18	0.21	0.25
Diluted EPS (RMB) - (adjusted)	0.16	0.15	0.18	0.21	0.25
DPS (RMB)	-	0.10	0.05	0.06	0.08

Cash flow statement (RMBm)

Year end: Aug	2014	2015	2016E	2017E	2018E
EBIT	119	181	262	323	381
Depreciation & amortisation	(39)	(46)	(61)	(71)	(84)
Net interest expenses/ (income)	(14)	4	10	10	11
Taxes paid	(8)	(11)	(22)	(27)	(31)
Changes in working capital	220	131	(6)	46	29
Others	27	127	141	152	178
Cash flow from operations	304	385	325	432	483
Capex	(114)	(212)	(400)	(400)	(200)
Acquisitions	(158)	(27)	158	-	-
Disposals	-	-	-	-	-
Others	-	-	-	-	-
Cash flow from investing	(272)	(239)	(242)	(400)	(200)
Dividends	-	(27)	(75)	(92)	(108)
Issue of shares	-	750	-	-	-
Change in debt	(52)	(224)	-	-	-
Others	(10)	(4)	-	-	-
Cash flow from financing	(61)	496	(75)	(92)	(108)
Change in cash	(29)	642	8	(59)	175
Cash and cash equivalents at Beg. of the year	409	380	1,022	1,030	971
Cash and cash equivalents at End of the ye	380	1,022	1,030	971	1,146
Free cash flow	256	134	(105)	13	263

Balance sheet (RMBm)

Year end: Aug	2014	2015	2016E	2017E	2018E
Cash	380	1,022	1,030	971	1,146
Short term investments	162	158	-	-	-
Accounts receivables	25	32	35	41	50
Inventory	-	1	1	1	1
Other current assets	4	-	-	-	-
Total current assets	571	1,214	1,065	1,013	1,197
PP&E	1,237	1,415	1,757	2,088	2,206
Intangible Assets	-	1	(2)	(5)	(7)
Associates and JVs	-	-	-	-	-
Other long term assets	200	187	230	252	303
Total long term assets	1,437	1,602	1,985	2,335	2,502
TOTAL ASSETS	2,008	2,816	3,051	3,348	3,699
Short term debt	224	-	-	-	-
Accounts payables	218	295	310	373	451
Other current liabilities	517	687	712	723	734
Total current liabilities	959	982	1,022	1,096	1,185
Long term debt	-	-	-	-	-
Deferred tax	19	22	41	51	60
Convertible bonds	-	-	-	-	-
Other long term liabilities	562	-	-	-	-
Total long term liabilities	582	22	41	51	60
TOTAL LIABILITIES	1,540	1,004	1,063	1,147	1,245
Shareholders' funds	467	1,812	1,987	2,202	2,454
Minority interests	-	-	-	-	-
TOTAL LIAB AND EQUITY	2,008	2,816	3,051	3,348	3,699
Net cash / (debt)	157	1,022	1,030	971	1,146

Key ratios

Year end: Aug	2014	2015	2016E	2017E	2018E
Operating ratios					
Gross margin	43.5	45.7	47.9	47.6	47.3
EBIT margin (%)	29.2	34.7	37.6	38.5	37.9
Effective tax rate (%)	17.3	5.2	8.0	8.0	8.0
Revenue growth (%)	14.7	20.9	31.3	19.2	20.2
Net income growth (%)	20.7	413.4	21.8	22.3	17.9
Net income (adjusted) growth (%)	20.9	45.9	34.7	22.3	17.9
Basic EPS growth adj (%)	20.9	(6.5)	19.1	22.3	17.9
DPS growth (%)	N/A	N/A	(44.5)	22.3	17.9
Efficiency ratios					
ROE (%)	27.3	10.3	12.6	13.9	14.7
ROCE (%)	11.3	9.8	12.9	14.3	15.2
Asset turnover (x)	0.3	0.2	0.3	0.3	0.3
Op cash / EBIT (x)	2.6	2.1	1.2	1.3	1.3
Depreciation / CAPEX (x)	(0.3)	(0.2)	(0.2)	(0.2)	(0.4)
Inventory turnover days	-	0.7	0.7	0.7	0.7
Accounts receivable days	13.8	15.8	14.8	14.8	14.8
Accounts payable days	243.3	264.4	253.8	253.8	253.8
Leverage ratios					
Net cash/ equity (%)	(33.6)	(56.4)	(51.8)	(44.1)	(46.7)
Net debt / EBITDA (x)	N/A	N/A	N/A	N/A	N/A
Interest cover (x)	N/A	N/A	N/A	N/A	N/A
Current ratio (x)	0.6	1.2	1.0	0.9	1.0
Valuation					
PER (x)	49.4	52.8	44.3	36.2	30.8
PER (x) - fully-diluted and adj. EPS	50.3	55.7	46.5	38.0	32.2
EV/EBITDA (x)	38.8	38.7	31.2	25.7	21.4
PBR (x)	13.5	5.4	5.6	5.0	4.5
Dividend yield (x)	-	1.2	0.6	0.8	0.9

Source: Company data, CSCI research estimates (*Remarks: Adjusted net profit excludes changes in fair value on redeemable convertible shares, fair value of warrants, gain on cancellation of warrants and listing expenses.)



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Company Rating Definition

The Benchmark: Hong Kong Hang Seng Index; Time Horizon: 12 months

Buy	12-month absolute total return: >=10%
Hold	12-month absolute total return: >-10% but <10%
Sell	12-month absolute total return: <=-10%

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