

Company Report

GSX education (GSX US)

GSX 3Q19 face growth but faster spending

■ 3Q19 revenue reached RMB557mn +462% yoy, with total full-priced enrolment at 820k +240% yoy.

■ Due to heavier marketing expenses, OPM trended down sequentially with 3Q19 at 1%, down from 16~17% in 4Q18 and 1Q19, and 9% in 2Q19.

■ Mgmt. guides earnings jump in 4Q19 and positive FY20 outlook driven by diversification and penetration into primary school segment

3Q19 revenue beat but bottom line pressured by selling exp.

3Q19 revenue increased by +462% yoy, above management guidance of 390%~411%. Marketing expenses increased significantly, nearly double the 2Q19 level, pressuring operating margin. Management guides 2Q and 3Q are important marketing seasons for online education to ensure strong enrolment in the autumn and spring quarters, and selling expenses should decline proportionally in 4Q and 1Q.

Diversifying offering to drive further growth

Management highlighted growth drivers for its strong 3Q19 revenue: 1) ASP boost from new critical thinking class, 2) strong growth in foreign language lessons, and 3) significant jump in revenue growth for its primary school segment. Overall, management continues to add more courses and teachers, to drive enrolment, as well as to help lower the percentage of revenue contribution from the company's top 10 teachers, who account for 35% of its 3Q19 revenue, vs. 46% last year.

Continued aggressive growth outlook for 4Q19 and FY20

On forward guidance, mgmt. guides 4Q19 revenue growth to reach 343%~354% yoy with Non-GAAP OPM to recover to 20%, comparable to 1Q19. For FY20 outlook, OPM should be largely in-line with that in FY19 while GPM should see some room for increase. Deferred revenue reached RMB778mn, about 40% larger than 3Q19 revenue, and increased substantially from RMB272mn in 2Q19. In other words, 4Q19 revenue growth is fairly secured unless significant refund occurs.

Continued aggressive growth and coverage read across

Based on Bloomberg consensus estimate, GSX currently trades at 99x FY19 and 36x FY20 P/E (implying c.180% earnings growth). We think execution will be key when GSX transits from a star-teacher model to a model that is more akin to the ones adopted by other tutoring companies, and when penetrating into primary school segment where closer parent/student contact is more important than star-teachers. Read-across: GSX guidance of lower online education selling expenses spending checks with our view of lower marketing expenses for TAL in current quarter, which should help drive a recovery in earnings.

Financials

Year ended 31 Dec (RMB mn)	FY17	FY18	9M18	9M19
Revenue	98	397	215	1,180
yoy%	n.a.	307%	n.a.	449%
Non-GAAP GP	73	255	130	850
Non-GAAP OP	-87	25	-3	85
Non-GAAP NP (after minority)	-120	-13	-31	68
Core EPS (RMB cents)	-1.30	-0.14	-0.34	0.59
Core ROE (%)	230%	50%	n.a.	5%

Sources: Company data, CMS (HK)

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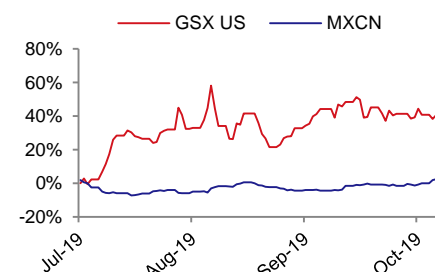
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NON-RATED

Price USD16.0

Price Performance



Source: Bigdata

%	1m	6m	12m
GSX US	9.0	n.a.	n.a.
HSI	7.2	(5.2)	6.0

Sector: Education

Hang Seng Index	27,683
HSCEI	10,878

Key Data

52-week range (USD)	8.5-17.5
Market cap (USD mn)	3,763
Avg. daily volume (mn)	2.1

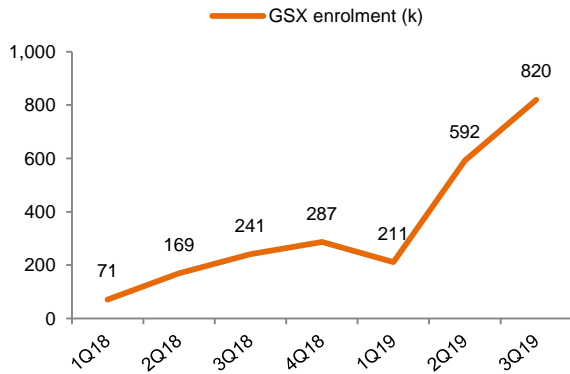
Shareholding Structure

Larry Xiangdong Chen	51.1%
No. of shares outstanding (mn)	125
Free float	48.9%

Source: Bloomberg

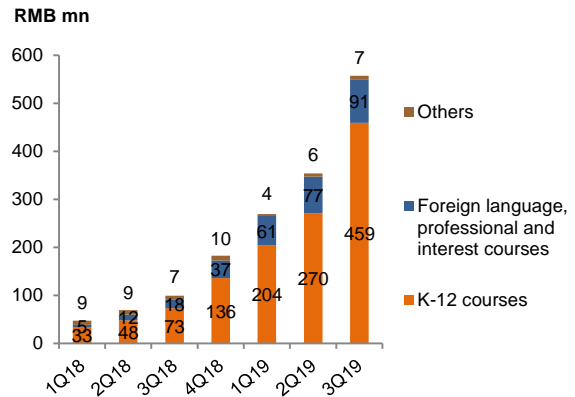
Focus charts

Figure 1: GSX education's quarterly enrolment



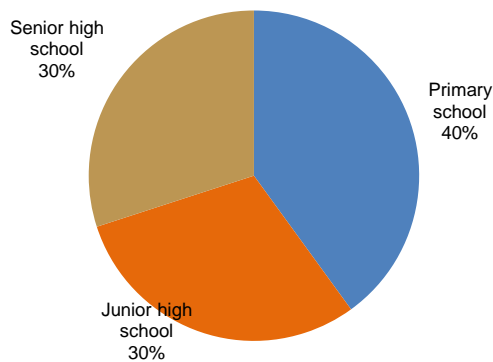
Sources: Company data, CMS (HK)

Figure 2: GSX education's revenue breakdown



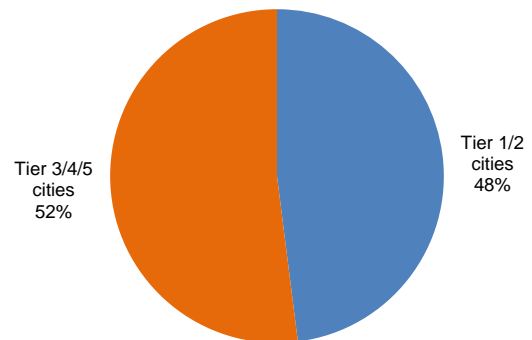
Sources: Company data, CMS (HK)

Figure 3: GSX's student distribution by ages



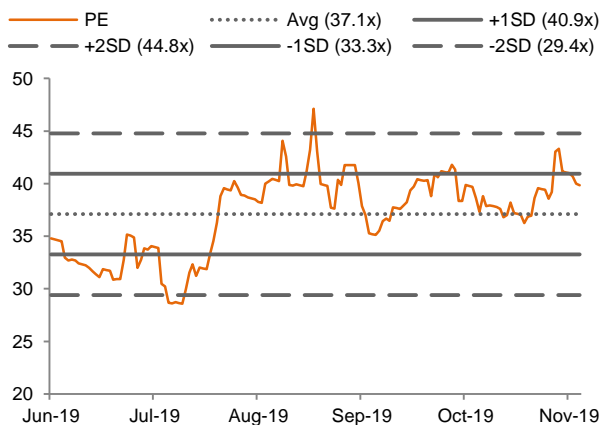
Sources: Company data, CMS (HK)

Figure 4: GSX's enrolment by city level



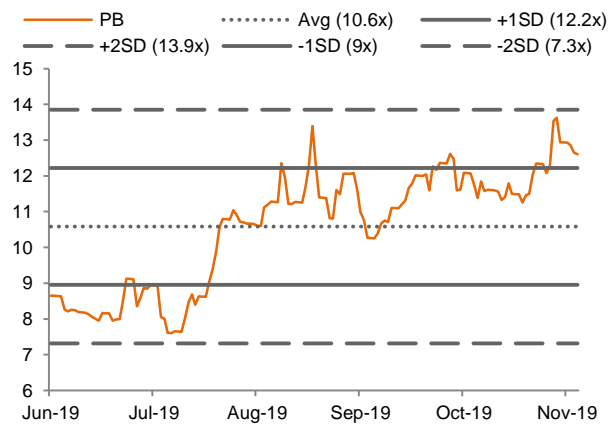
Sources: Company data, CMS (HK)

Figure 5: P/E range of GSX



Sources: Company data, Bloomberg, CMS (HK)

Figure 6: P/B range of GSX



Sources: Company data, Bloomberg, CMS (HK)

Figure 7: GSX 3Q19 results: revenue beat while Non-GAAP OPM narrowed due to heavier investment amid intense online competition

RMB '000	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	2Q19	3Q19	3Q19	Bloomberg Consensus	
As of	Mar 31	Jun 30	Sep 30	Dec 31	Mar 31	Jun 30	Sep 30	YoY%	YoY%	QoQ%	3Q19	% difference
Net revenues	46,911	68,886	99,244	182,265	269,155	353,679	556,994	413%	461%	57%	510,405	9.1%
COGS	(20,688)	(26,571)	(37,556)	(57,938)	(82,045)	(101,189)	(156,691)	281%	317%	55%		
Gross profit	26,223	42,315	61,688	124,327	187,110	252,490	400,303	497%	549%	59%		
Selling and marketing	(13,882)	(18,424)	(31,023)	(58,189)	(99,519)	(169,048)	(330,352)	818%	965%	95%		
R&D	(11,924)	(15,566)	(20,013)	(26,547)	(30,442)	(41,128)	(57,128)	164%	185%	39%		
G&A	(4,577)	(8,864)	(10,572)	(15,818)	(14,422)	(26,088)	(23,638)	194%	124%	-9%		
OP - as reported	(4,160)	(539)	80	23,773	42,727	16,226	(10,815)	n.a.	n.a.	-167%		
NP - as reported	(3,603)	(405)	684	22,974	33,891	16,374	1,902	n.a.	178%	-88%		
Non-GAAP Op income	(3,947)	170	442	28,406	46,549	31,087	7,424	18186%	1580%	-76%	(15,230)	n.a.
Non-GAAP Net income	(3,390)	304	1,046	27,607	37,713	31,235	20,141	10175%	1826%	-36%		
EPS - as reported (RMB)	(0.14)	(0.11)	(0.10)	n.a.	0.17	0.06	0.01	n.a.	n.a.	-81%		
Non-GAAP EPS (RMB)	(0.14)	(0.10)	(0.09)	n.a.	0.20	0.17	0.12	n.a.	n.a.	-30%	0.09	30.9%
Margins:												
GPM(%)	56%	61%	62%	68%	70%	71%	72%	10 ppt	9.7 ppt	0.5 ppt		
OPM(%)	-9%	-1%	0%	13%	16%	5%	-2%	5.4 ppt	-2 ppt	-6.5 ppt		
NPM(%)	-8%	-1%	1%	13%	13%	5%	0%	5.2 ppt	-0.3 ppt	-4.3 ppt		
Non-GAAP OPM(%)	-8%	0%	0%	16%	17%	9%	1%	8.5 ppt	0.9 ppt	-7.5 ppt		
Non-GAAP NPM(%)	-7%	0%	1%	15%	14%	9%	4%	8.4 ppt	2.6 ppt	-5.2 ppt		

Sources: Bloomberg, Company data, CMS (HK)

Figure 8: China tutoring education peers comparison

Company	中文名	Ticker	Price (local currency)	CMS			Mkt cap (US\$m)	3-mth avg t/o (US\$m)	P/E (x)			EPS CAGR (%)	PEG* (x)	P/B (x)	EV/EBITDA(X)
				Ratin g	TP(Local currency)	Up/(Dn) side (%)			FY19E	FY20E	FY21E	FY19-FY21E	FY19E	FY19E	FY19E
HSI			27,683						10.9	10.4	9.6	6.5	1.6	1.2	9.2
HSCEI			10,878						8.5	8.0	7.4	7.3	1.1	1.1	7.6
MXCN			81						12.6	11.3	10.0	12.4	0.9	1.6	11.2
Tutoring															
TAL	好未来	TAL US	43.3	BUY	49.0	13.1	25,640	102.9	70.2	50.8	36.1	39.5	1.3	10.5	51.3
NEW ORIENTAL	新东方	EDU US	122.2	BUY	140.0	14.6	19,352	122.9	47.3	34.5	26.0	34.9	1.0	8.2	27.5
GSX	跟谁学	GSX US	16.0	NR	n.a.	n.a.	3,764	16.1	99.0	36.0	23.6	104.7	0.3	15.9	103.8
KOOLEARN	新东方在线	1797 HK	17.6	NR	n.a.	n.a.	2,142	6.6	n.a.	2,281.5	117.4	n.a.	n.a.	6.2	n.a.
ONESMART	精锐	ONE US	7.1	NR	n.a.	n.a.	1,145	1.0	20.8	16.1	11.9	32.5	0.5	6.5	13.7
PUXIN	朴新	NEW US	9.8	NR	n.a.	n.a.	850	1.5	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
ONLY	昂立	600661 CH	18.5	NR	n.a.	n.a.	761	1.6	29.0	23.2	20.0	20.5	1.1	3.7	n.a.
SCHOLAR	思考乐	1769 HK	10.1	NR	n.a.	n.a.	709	2.0	48.3	33.1	26.7	34.6	1.0	6.5	n.a.
XUEDA	学大	000526 CH	34.9	NR	n.a.	n.a.	481	5.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
RISE	瑞思	REDU US	7.7	NR	n.a.	n.a.	437	0.2	17.8	15.8	13.1	16.6	1.0	5.0	10.5
SUNLANDS	尚德	STG US	2.5	NR	n.a.	n.a.	420	0.0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
BESTSTUDY	卓越	3978 HK	2.8	NR	n.a.	n.a.	307	0.2	16.9	11.2	8.9	37.8	0.3	2.7	7.7
51TALK	51TALK	COE US	7.0	NR	n.a.	n.a.	143	0.1	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
TARENA-ADR	达内	TEDU US	0.8	NR	n.a.	n.a.	44	0.1	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Average									43.7	278.0	31.5	40.1	0.8	7.2	35.7
Median									38.2	33.1	23.6	34.7	1.0	6.5	20.6
Education (US listed Non-China)															
ATGE US Equity		ATGE US	31.4	NR	n.a.	n.a.	1,693	23.9	12.0	10.2	n.a.	n.a.	n.a.	n.a.	9.0
CECO US Equity		CECO US	15.0	NR	n.a.	n.a.	1,054	10.8	12.1	11.1	n.a.	n.a.	n.a.	n.a.	9.4
LRN US Equity		LRN US	20.1	NR	n.a.	n.a.	824	9.0	23.1	20.2	n.a.	n.a.	n.a.	n.a.	5.0
HMHC US Equity		HMHC US	6.5	NR	n.a.	n.a.	812	3.8	n.a.	n.a.	n.a.	n.a.	n.a.	1.2	9.4
Average									15.7	13.8	n.a.	n.a.	1.2	8.2	7.8
Median									12.1	11.1	n.a.	n.a.	1.2	9.2	7.6

Sources: Company data, CMS (HK) estimates; share price as of 5 Nov 2019. Note: All information of Non-rated stocks was sourced from Bloomberg.

*PEG calculation: Based on FY20E P/E and FY19-21E EPS CAGR.

GSX (GSX US) financial summary

Balance Sheet

(RMB mn)	FY17	FY18	9M18	9M19
Cash and cash equivalents	19	33		32
Short-term investments	8	198		1,015
Total current assets	52	281		1,235
Total assets	103	338		2,624
Current liabilities	155	356		1,008
Total liabilities	156	365		1,160
Total mezzanine equity	427	466		0
Total shareholders' deficit	-479	-493		1,464
Total equity	-52	-26		1,464

Profit & Loss Statement

(RMB mn)	FY17	FY18	9M18	9M19
Net revenues	98	397	215	1,180
Gross profit	73	255	130	840
Selling expenses	-75	-122	-63	-599
R&D expenses	-52	-74	-48	-129
G&A expenses	-37	-40	-24	-64
Operating income	-92	19	-5	48
Pre-tax income	-91	21	-4	61
Net (loss) income	-87	20	-3	52
Net (loss) income after minority	-126	-19	-33	31
SBC	6	6	1	37
Non-GAAP items:				
Non-GAAP gross profit	73	255	130	850
Non-GAAP operating income	-87	25	-3	85
Non-GAAP net income	-81	26	-2	89
Non-GAAP net income after minority	-120	-13	-31	68

Sources: Company data, CMS (HK)

Financial ratios

	FY17	FY18	9M18	9M19
	31 Dec	31 Dec	31 Dec	31 Dec
YoY%				
Net revenues		307%		449%
Gross profit		251%		545%
Selling expenses		61%		846%
R&D expenses		41%		171%
G&A expenses		7%		167%
Operating income		n.a.		n.a.
Pre-tax income		n.a.		n.a.
Net (loss) income		n.a.		n.a.
Net (loss) income after minority		n.a.		n.a.
Non-GAAP items				
Non-GAAP gross profit		251%		552%
Non-GAAP operating income		n.a.		n.a.
Non-GAAP net income		n.a.		n.a.
Non-GAAP net income – after minority		n.a.		n.a.
Margins%				
Gross profit	74%	64%	61%	71%
Operating income	-95%	5%	-2%	4%
Pre-tax income	-94%	5%	-2%	5%
Net (loss) income	-89%	5%	-2%	4%
Net (loss) income after minority	-129%	-5%	-15%	3%
Non-GAAP items				
Non-GAAP gross profit	74%	64%	61%	72%
Non-GAAP operating income	-89%	6%	-2%	7%
Non-GAAP net income	-83%	6%	-1%	8%
Non-GAAP net income after minority	-123%	-3%	-15%	6%

Investment Ratings

Industry Rating	Definition
OVERWEIGHT	Expect sector to outperform the market over the next 12 months
NEUTRAL	Expect sector to perform in-line with the market over the next 12 months
UNDERWEIGHT	Expect sector to underperform the market over the next 12 months

Company Rating	Definition
BUY	Expect stock to generate 10%+ return over the next 12 months
NEUTRAL	Expect stock to generate +10% to -10% over the next 12 months
SELL	Expect stock to generate loss of 10%+ over the next 12 months

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