

COMPANY UPDATE

New Oriental Education & Technology Group (EDU US)

Diverse Revenue Streams; Margin Improvement In Sight

We note that demand for after-school education remains resilient despite a weaker macro outlook as peer competition in China remains intense. To defend against potential uncertainties, EDU is cultivating a competitive moat by diversifying its revenue streams and investing in East Buy. Management guided 4QFY24 revenue growth of 28-31% yoy to US\$1,101.5m-1,127.3m while overall net margin should expand 2-3ppt yoy in FY24. Upgrade to BUY with a higher target price of US\$105.00 (HK\$82.00).

WHAT'S NEW

- Diversified revenue mix and investments in East Buy.** We believe New Oriental Education & Technology Group (EDU) remains in the initial stage of a multi-year scale expansion after the completion of business adjustments in FY23. Its offerings include: a) non-academic after-school tutoring (AST) services and smart learning devices for preschool to primary school students (FY23: 17% of total revenue; FY24E: 21% of total revenue), b) academic AST for high school students (FY23: 29%; FY24E: 25%), c) overseas test preparation and consulting services (FY23: 24%; FY24E: 22%), and d) other learning services (FY23: 8%; FY24E: 10%) such as domestic test preparation, adult language courses, and vocational training. Meanwhile, EDU owns 57% of East Buy Holding Ltd (East Buy) (FY23: 22% of total revenue; FY24: 22% of total revenue), a leading private label and live-streaming e-commerce platform that operates multiple accounts on major platforms like Douyin and Taobao.
- Capacity expansion to accelerate in FY25.** Revenue is guided to grow by 25-30% yoy in FY25. By segment, management expects overseas revenue to rise 20% yoy, bolstered by a 25% yoy growth in test preparation and 15% yoy growth in consulting. Revenue growth for domestic university, high school, new initiatives and others were guided to grow 30%/20%/30-40%/20%, respectively. In FY25, EDU plans to raise capacity expansion by 30%, on par with FY24. As of Feb 24, EDU had established 911 learning centres, including 81 schools across 74 cities.
- Comprehensive revamp to create economic moat.** EDU has been investing in the development of its private-label products including cultural trips, studied tours in China and overseas, and camp education, as part of its newly integrated tourism-related business line. Management has set the revenue target for newly-integrated tourism revenue at Rmb1.4b for FY25, up 3-4x from Rmb300m in FY24. The optimistic projections are supported by the number of registrations for the overseas summer study abroad programme which grew 50% from that of 2019. The company also operates the online platform "Koolearn" (新东方在线), which focuses on overseas studies, test preparation, and language learning. We believe EDU's competitive advantages include high-quality teachers, custom course materials and compliant operations.

KEY FINANCIALS

Year to 31 May (Rmbm)	2022	2023	2024F	2025F	2026F
Net turnover	3,105	2,998	4,295	5,515	6,637
EBITDA	(788)	313	501	713	1,023
Operating profit	(983)	190	383	571	854
Net profit (rep./act.)	(1,188)	177	336	551	741
Net profit (adj.)	(1,046)	259	414	665	845
EPS (Fen)	(61.7)	15.4	24.8	39.6	50.1
PE (x)	n.m.	529.8	328.6	205.4	162.5
P/B (x)	37.3	37.9	33.1	28.4	24.1
EV/EBITDA (x)	n.m.	36.3	22.7	15.9	11.1
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Net margin (%)	(38.2)	5.9	7.8	10.0	11.2
Net debt/(cash) to equity (%)	(26.4)	(41.8)	(57.8)	(74.1)	(84.5)
ROE (%)	n.a.	4.9	8.8	12.5	14.2
Consensus net profit	-	-	422	623	820
UOBKH/Consensus (x)	-	-	0.98	1.07	1.03

Source: New Oriental Education & Technology Group, Bloomberg, UOB Kay Hian
n.m. : not meaningful; negative P/E, EV/EBITDA reflected as "n.m."

BUY

(Upgraded)

Share Price	US\$81.38
Target Price	US\$105.00
Upside	+29.0%

COMPANY DESCRIPTION

New Oriental Education & Technology Group offers educational services including foreign language training, test preparation courses, K12 after school tutoring services and online courses in China.

STOCK DATA

GICS sector	Consumer Discretionary
Bloomberg ticker:	EDU US
Shares issued (m):	165.5
Market cap (US\$m):	13,468.5
Market cap (US\$m):	13,468.5
3-mth avg daily t'over (US\$m):	145.7

Price Performance (%)

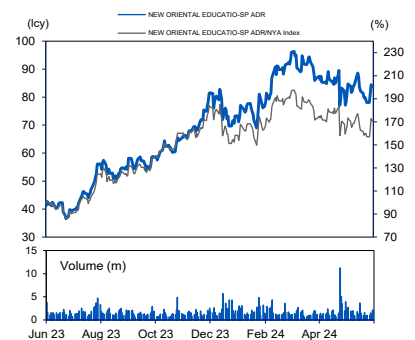
52-week high/low US\$96.31/US\$36.60

1mth	3mth	6mth	1yr	YTD
(1.1)	(13.0)	3.9	116.6	11.1

Major Shareholders

	%
Yu Minhong	15.1
Management Team	0.4
FY24 NAV/Share (US\$)	2.54
FY24 Net Cash/Share (US\$)	1.45

PRICE CHART



Source: Bloomberg

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STOCK IMPACT

- Glimpse of 3QFY24 results.** EDU's revenue grew 60% yoy to US\$1,207.3m in 3QFY24, mainly driven by the growth in net revenues from its educational new business initiatives and East Buy's private label products and livestreaming e-commerce business. EDU's overseas test preparation and overseas study consulting businesses continued its strong growth trajectory of 52.6% and 25.7% yoy, respectively. The revenue from domestic test preparation business targeting adults and university students ramped up 53.2% yoy while new educational business initiatives revenue surged 72.7% yoy in 3QFY24. Non-GAAP net profit was US\$105m, up 10% yoy, with net margin inching down 4ppt yoy to 9%, partially due to the investments in East Buy.
- East Buy's performance overview; poised for margin improvement.** In 1HFY24, East Buy's revenue rose 34% yoy to Rmb2.8b (22% of EDU's revenue), mainly driven by 19% yoy GMV growth. Non-GAAP net profit dropped 15% yoy, while net margin contracted 11ppt yoy to 18.2%. This is primarily attributed to: a) a comprehensive organisational structure, increasing professional talent, and app upgrades, b) stepped-up promotions of 1P private-label products, c) rising GMV and revenue contribution from 1P vs 3P, which dampened gross profit margin, and d) incremental investments in multi-platform strategy. Despite near-term margin pressure, we opine the viable execution of its strategic plans execution will result in both leverage and margin expansion.
- 4QFY24 guidance breakdown.** Management guided 4QFY24 revenue to come in at US\$1,101.5m-1,127.3m, representing 28-31% yoy growth. The sequentially moderating revenue growth in 4QFY24 is mainly dampened by weak seasonality and a normalised base in 4QFY23. By segment, the revenue contribution from overseas consulting is 15% and overseas preparation is 10%, domestic university 3%, high school 25%, new initiatives 21%. 4QFY24 net margin is forecasted to expand by 2-3ppt yoy to 6%, considering investment in newly developed platforms of East Buy. For FY24, overall net margin is guided to expand 2-3ppt yoy. The education segment's margin is guided to dip marginally yoy in 4QFY24, primarily attributed to heightened investments in East Buy and increased incentives for employees. For FY24, the operating margin of test preparation, consulting, domestic university, high school and new initiatives segments are guided at 20-25%, 15%, 5%, >20% and 20%, respectively.
- Shareholder returns.** As of 23 Apr 24, EDU had repurchased 6m ADS for US\$195.3m, representing US\$304.7m (2.4% of total market cap) remaining in the programme.

EARNINGS REVISION/RISK

- Risks include:** a) margin pressure stemming from heavy investment, b) uncertainties in policy changes, and c) US-China tensions impacting its overseas business.

VALUATION/RECOMMENDATION

- Upgrade to BUY with a target price of US\$105.00 (HK\$82.00)**, based on SOTP valuation. Our target price implies 26.5x FY25F PE and 0.7x PEG vs a three-year EPS CAGR of 35%. The company is currently trading at 20.7x forward PE.

SHARE PRICE CATALYST

- Increasing demand for overseas education, further market consolidation, growth in lower-tier cities' online penetration rates, rapid growth potential from East Buy.

SOTP VALUATION

Segment	CY25E Revenue US\$m	CY25E OP US\$m	CY25E OPM	CY25E NOPAT US\$m	CY25E Target EV/NOPAT	Value US\$m	Val/sh US\$
EDU core	5,104	718	14.1%	574	26x	14,952	89.3
Traditional K-12	1,373	236	17.2%	189	22x	4,155	24.8
Educational services and new initiatives	3,730	482	12.9%	386	28x	10,797	64.5
Other traditional businesses	1,723	140	8.1%	112	23x	2,595	15.5
New initiatives	2,007	342	17.0%	273	30x	8,202	49.0
East Buy	1,011	163	16.1%	131	18x	1,302	7.8
EDU total	6,115	881	14.4%	705	23x	16,254	97.1
Net cash (FY24/25E average, excluding deferred revenue)						3,337	19.9
Holdco. discount					10%	(1,959)	(11.7)
12-m target price (US\$)					20x	17,632	105.0
12-m target price (HK\$)						137,530	82.0

Source: New Oriental, UOB Kay Hian

PROFIT & LOSS

Year to 31 May (US\$m)	2023	2024F	2025F	2026F
Net turnover	2,998	4,295	5,515	6,637
EBITDA	313	501	713	1,023
Deprec. & amort.	123	118	142	169
EBIT	190	383	571	854
Total other non-operating income	118	131	151	163
Pre-tax profit	309	514	722	1,017
Tax	(66)	(124)	(165)	(225)
Minorities	0	0	0	0
Net profit	177	336	551	741
Net profit (adj.)	259	414	665	845

CASH FLOW

Year to 31 May (US\$m)	2023	2024F	2025F	2026F
Operating	971	1,035	1,404	1,511
Pre-tax profit	309	514	722	1,017
Tax	(66)	(124)	(165)	(225)
Deprec. & amort.	123	118	142	169
Working capital changes	(538)	(458)	(578)	(457)
Other operating cashflows	1,144	985	1,283	1,007
Investing	(37)	(189)	(231)	(264)
Capex (growth)	(143)	(189)	(231)	(264)
Proceeds from sale of assets	1	0	0	0
Others	104	0	0	0
Financing	(247)	0	0	0
Dividend payments	0	0	0	0
Issue of shares	13	0	0	0
Loan repayment	0	0	0	0
Others/interest paid	(260)	0	0	0
Net cash inflow (outflow)	687	846	1,173	1,247
Beginning cash & cash equivalent	1,149	1,774	2,617	3,791
Changes due to forex impact	(61)	(2)	0	0
Ending cash & cash equivalent	1,663	2,507	3,680	4,927

BALANCE SHEET

Year to 31 May (US\$m)	2023	2024F	2025F	2026F
Fixed assets	942	1,008	1,103	1,204
Other LT assets	1,037	1,126	1,126	1,126
LT debt	n.a.	n.a.	n.a.	n.a.
Cash/ST investment	1,663	2,507	3,680	4,927
Other current assets	2,751	2,889	3,031	3,143
Total assets	6,392	7,530	8,940	10,401
ST debt	156	156	156	156
Other current liabilities	2,095	2,748	3,468	4,038
Other LT liabilities	327	327	327	327
Shareholders' equity	3,604	4,068	4,758	5,649
Minority interest	210	227	227	227
Total liabilities & equity	6,392	7,530	8,940	10,401

KEY METRICS

Year to 31 May (%)	2023	2024F	2025F	2026F
Profitability				
EBITDA margin	10.4	11.7	12.9	15.4
Pre-tax margin	10.3	12.0	13.1	15.3
Net margin	5.9	7.8	10.0	11.2
ROA	2.9	4.8	6.7	7.7
ROE	4.9	8.8	12.5	14.2
Growth				
Turnover	(3.5)	43.3	28.4	20.4
EBITDA	n.a.	60.2	42.4	43.5
Pre-tax profit	n.a.	66.5	40.6	40.8
Net profit	n.a.	89.7	63.8	34.5
Net profit (adj.)	n.a.	59.8	60.8	27.0
EPS	n.a.	61.2	60.0	26.3
Leverage				
Debt to total capital	3.9	3.5	3.0	2.6
Debt to equity	4.3	3.8	3.3	2.8
Net debt/(cash) to equity	(41.8)	(57.8)	(74.1)	(84.5)

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