

# GDS (GDS US)

## Power price hike, slower move-in weighed on 3Q21

GDS reported in-line FY3Q21 revenue/ adj. EBITDA growth of +35%/ +34% YoY. Although hyperscalers slowing capex and power outage were well-anticipated negative factors, magnitude of GPM erosion (-1.5 pct pts QoQ) due to higher utility price was larger than expected. Meanwhile, we are positive to see new customer win (Meituan), M&A progress (raised FY21 capex guidance) and SEA market expansion. Maintain BUY.

- 3Q21 adj. EBITDA in-line but GPM missed. FY21 guided down.** GDS 3Q21 revenue was at RMB2,061mn (+35% YoY). Adj. EBITDA was at RMB962mn (+34% YoY) but net loss widened further to RMB337mn. GPM deteriorated to 22.1% (-1.5 pct pts QoQ) mainly on higher utility costs. Adding on slower move-in rate in 2H21, GDS revised down FY21 targets. Mid-point of new guidance implied +35.5% YoY in revenue (prior +36.8% YoY) and +37.8% YoY in adj. EBITDA (prior +39.2% YoY) in FY21.
- Utility price hike will continue to affect margin in 4Q21.** We think the magnitude of GPM erosion was higher than expected. Utility cost accounted for 37% of 3Q21 revenue and rose +18% QoQ. Because of power outage, GDS has spent RMB19mn on back-up power in 3Q21 and unit price was 3x higher than traditional grid power price. Half of the utility price hike can be passed through to customers. Looking into 4Q21, although power supply is gradually going back to normal, mgmt. expects unit power cost price to remain high due to higher power tariff related to surging coal price and that utility cost as % of revenue will be similar to 3Q21 level at 28.8% (vs. 26.9% in 2Q21).
- Capacity move-in slower than expected starting from 3Q21.** GDS customers delayed capacity move-in schedule by few thousands sqm in 3Q21. Mgmt. attributed the weaker ramp up to factors including 1) market structural change that traditional hyperscalers are slowing capex, 2) server shortage and 3) power outage. Meanwhile, GDS has secured a new hyperscaler customer (Meituan) in 3Q. The Company also raised FY21 capex for M&A (+33% to RMB16bn) and announced new expansion plans in Indonesia/ Singapore as GDS remains confident in the secular growth of cloud computing.
- Secular growth trend of cloud computing remains unchanged.** We maintain our FY21-23E estimates. Retain BUY with unchanged target price of US\$73.01, based on 25x FY22E EV/EBITDA, in-line with 3 year mean.

### Earnings Summary

(YE 31 Dec)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue (RMB mn)	4,122	5,739	7,871	10,096	12,113
YoY growth (%)	48%	39%	37%	28%	20%
Adj. EBITDA (RMB mn)	1,824	2,681	3,724	4,632	5,613
YoY growth (%)	74%	47%	39%	24%	21%
Consensus EBITDA (RMB)	1,824	2,681	3,659	4,937	6,384
Net income (RMB mn)	(442)	(669)	(885)	(869)	(767)
EPS (RMB)	-0.45	-0.59	-0.69	-0.68	-0.61
YoY growth (%)	n.a.	n.a.	n.a.	n.a.	n.a.
EV/EBITDA	43.2	28.0	24.2	21.4	19.2
Yield (%)	n.a.	n.a.	n.a.	n.a.	n.a.
ROE (%)	n.a.	n.a.	n.a.	n.a.	n.a.

Source: Company data, Bloomberg, CMBIS estimates

### BUY (Maintain)

Target Price	US\$73.01
(Previous TP)	US\$73.01)
Up/Downside	+23.9%
Current Price	US\$58.92

### China software & IT services

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#### Stock Data

Mkt Cap (US\$ mn)	11,012
Avg 3 mths t/o (mn)	77.85
52w High/Low (US\$)	116.76/ 49.16
Total Issued Shares (mn)	178

Source: Bloomberg

#### Shareholding Structure

STT GDC	32.1%
William Huang - Chairman	5.4%
Ping An	2.3%

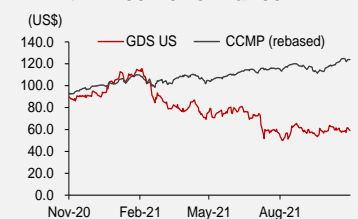
Source: Bloomberg

#### Share Performance

	Absolute	Relative
1-mth	1.5%	-4.6%
3-mth	1.8%	-4.9%
6-mth	-20.9%	-33.0%

Source: Bloomberg

#### 12-mth Price Performance



Source: Bloomberg

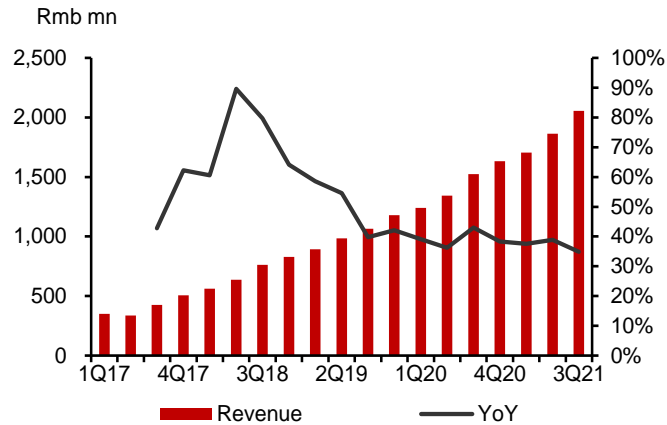
#### Auditor: KPMG

#### Related Reports

- China Software & IT Services – China cloud outlook mixed – 4 Nov 2021
- China Software & IT Services – Implications of setting up state-owned cloud - 30 Aug 2021

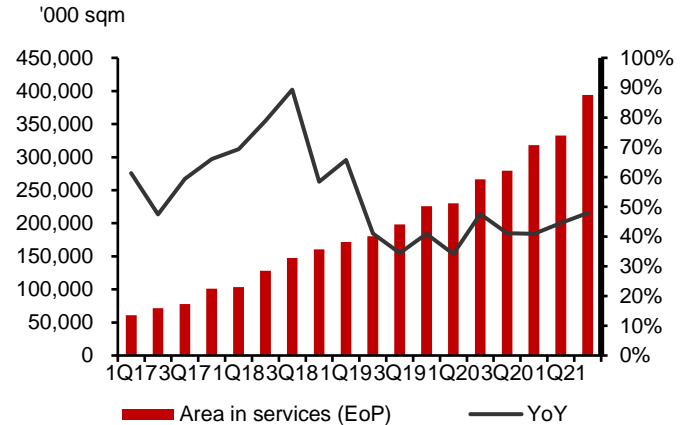
**Focus charts**

**Figure 1: Revenue and YoY growth**



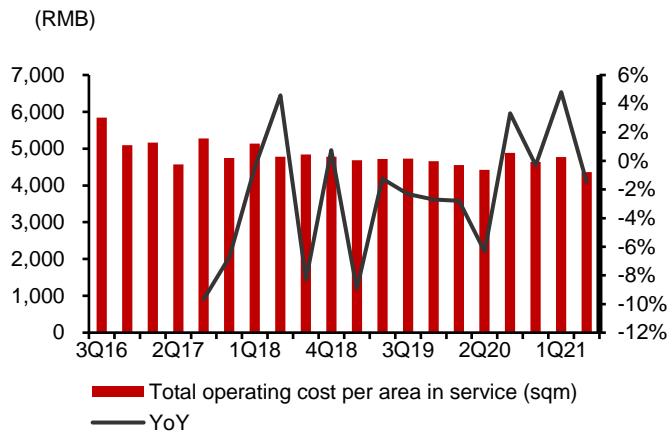
Source: Company data, CMBIS

**Figure 2: Area in services and YoY**



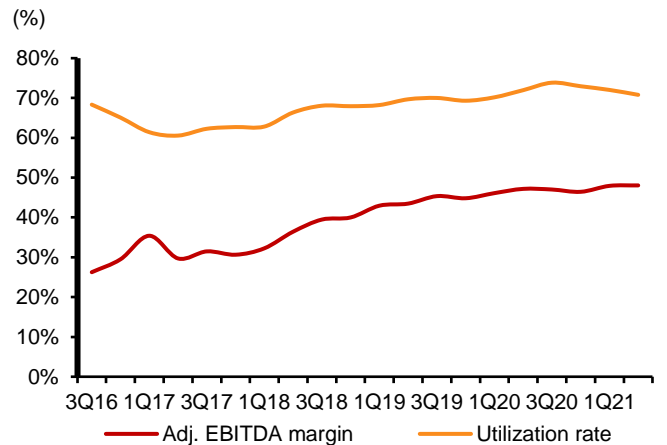
Source: Company data, CMBIS

**Figure 3: Total operating cost per area in service**



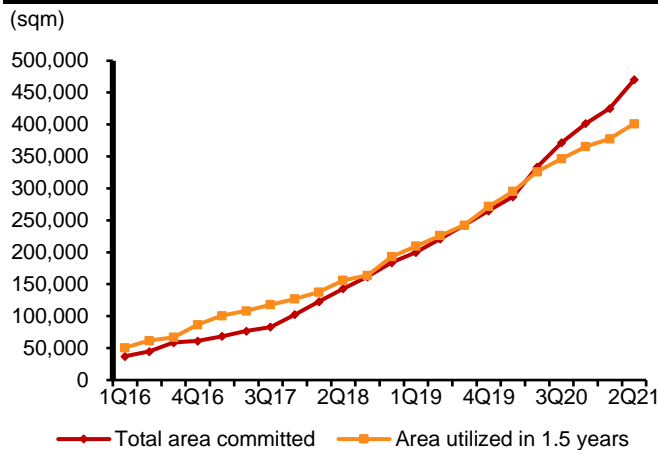
Source: Company data, CMBIS

**Figure 4: EBITDA margin vs. utilization**



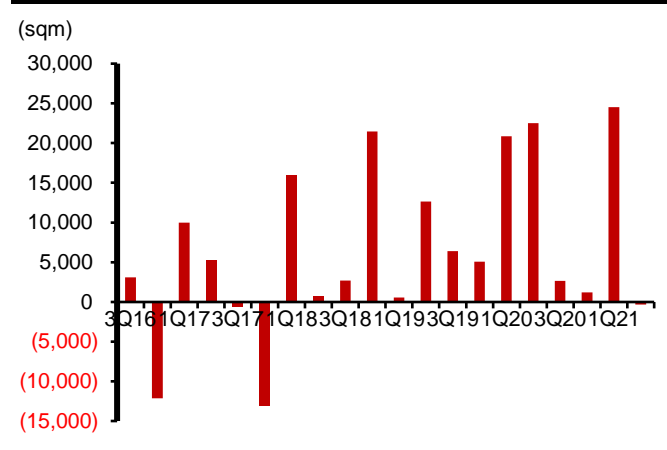
Source: Company data, CMBIS

**Figure 5: Total area committed vs. fwd area utilized**



Source: Company data, CMBIS

**Figure 6: Net adds in area under construction**



Source: Company data, CMBIS

## 3Q21 earnings review

### 3Q21 results review

- **Revenue** was at RMB2,061mn (+35% YoY, +11% QoQ), **in-line** with our and consensus estimates.
- **Gross profit** was at RMB455mn (+11% YoY, +4% QoQ), **below** our estimate by 17% and consensus by 29%.
- **Gross margin** was at 22.1% (-4.7 pct pts YoY, -1.5 pct pts QoQ), **below** our estimates by 4.6 pct pts and consensus by 9.2 pct pts.
- **Adj. EBITDA** was at RMB962mn (+34% YoY, +7% QoQ), **in-line** with our and consensus estimates.
- **Adj. EBITDA margin** was at 46.7% (-0.4 pct pts YoY, -1.4 pct pts QoQ), **missed** our estimates by 0.5 pct pts but **slightly above** consensus by 0.1 pct pts.
- **Net loss** widened to RMB337mn, missed both our and consensus estimates

### FY21E guidance slightly revised down

- **Revenue** will be in the range of RMB7,700-7,850mn (implying +34.2% to +36.8% YoY). Mid-point of revenue guidance is revised down by 1.9% from RMB7,850mn to RMB7,775mn.
- **Adj. EBITDA** will be in the range of RMB3,660-3,730mn (implying +36.5% to +39.1% YoY). Mid-point of adj. EBITDA guidance is revised down by 0.9% from RMB3,730mn to RMB3,695mn.
- **Capex** is revised up by 33% to RMB16bn (+71% YoY), vs. prior guidance of +28% YoY to RMB12bn.

Figure 7: 3Q21 results review

	Sep-20 3Q20	Jun-21 2Q21	Sep-21 3Q21			Sep-21 3Q21	versus	Sep-21 3Q21	versus
RMB mn	actual	actual	actual	YoY	QoQ	CMBI	CMBI	consensus	consensus
Revenue	1,525	1,864	2,061	35%	11%	2,057	0%	2,067	0%
Gross profit	409	440	455	11%	4%	549	-17%	646	-29%
Gross margin	26.8%	23.6%	22.1%	-4.7 pct pts	-1.5 pct pts	26.7%	-4.6 pct pts	31.2%	-9.2 pct pts
Operating profit	159	147	150	-6%	2%	233	-36%	230	-35%
Operating margin	10.4%	7.9%	7.3%	-3.2 pct pts	-0.6 pct pts	11.3%	-4.1 pct pts	11.2%	-3.9 pct pts
Adj. EBITDA	717	896	962	34%	7%	971	-1%	962	0%
Adj. EBITDA margin	47.0%	48.1%	46.7%	-0.4 pct pts	-1.4 pct pts	47.2%	-0.5 pct pts	46.6%	0.1 pct pts
Net non-op	-329	-394	-381			-401		-446	
PBT	-170	-247	-231	-37%	6%	-167	-38%	-216	-7%
Net income	-224	-325	-337	-51%	-4%	-211	-60%	-248	-36%
Net margin	-14.7%	-17.4%	-16.4%	-1.7 pct pts	1.1 pct pts	-10.3%	-6.1 pct pts	-12.0%	-4.4 pct pts
EPS RMB	-0.18	-0.22	-0.23	-30%	-3%	-0.15	-59%	-0.31	25%

Source: Company data, CMBIS

**Figure 8: Operating model**

RMB mn	2019	2020	2021E	2022E	2023E
<b>Revenues</b>	<b>4,122</b>	<b>5,739</b>	<b>7,871</b>	<b>10,096</b>	<b>12,113</b>
Service Revenue	4,095	5,717	7,856	10,079	12,095
Equipment Revenue	28	22	15	17	18
Cost of sales	-3,080	-4,189	-5,819	-7,355	-8,679
<b>Gross Profit</b>	<b>1,043</b>	<b>1,550</b>	<b>2,052</b>	<b>2,741</b>	<b>3,433</b>
<i>Gross margin</i>	<i>25.3%</i>	<i>27.0%</i>	<i>26.1%</i>	<i>27.1%</i>	<i>28.3%</i>
R&D	-22	-40	-41	-65	-71
SG&A	-541	-837	-1,192	-1,405	-1,586
Operating Income	480	673	819	1,271	1,777
<b>Adj. EBITDA</b>	<b>1,824</b>	<b>2,681</b>	<b>3,724</b>	<b>4,632</b>	<b>5,613</b>
<i>Adj. EBITDA margin</i>	<i>44.2%</i>	<i>46.7%</i>	<i>47.3%</i>	<i>45.9%</i>	<i>46.3%</i>
Interest Expense	-969	-1,287	-1,634	-2,065	-2,494
Net other income (exp)	62	66	70	70	70
Profit Before Income Taxes	-426	-548	-745	-724	-648
Income Tax Expense	-16	-121	-140	-146	-119
<b>Net profit (loss)</b>	<b>-500</b>	<b>-738</b>	<b>-989</b>	<b>-977</b>	<b>-875</b>
<i>Net margin</i>	<i>-10.7%</i>	<i>-11.7%</i>	<i>-11.2%</i>	<i>-8.6%</i>	<i>-6.3%</i>
EPS (RMB)	-0.45	-0.59	-0.69	-0.68	-0.61
<b>Key assumptions</b>					
Total area in service (EoP)	225,963	318,272	466,694	583,368	740,877
Total area utilized (EoP)	156,020	226,212	326,043	401,306	501,991
Utilization rate (area utilized/ area in service)	69%	72%	70%	69%	68%
Average MSR (Rmb / Sqm / Month)	2,532	2,403	2,306	2,253	2,169
Depreciation	1,142	1,638	2,353	2,932	3,459
<b>Growth (YoY)</b>					
Revenues	48%	39%	37%	28%	20%
Gross Profit	68%	49%	32%	34%	25%
Adj. EBITDA	74%	47%	39%	24%	21%
Net profit (loss)	3%	51%	32%	-2%	-12%

Source: Company data, CMBIS

## Valuation

### Maintain BUY with target price of US\$73.01

We maintain our BUY recommendation on GDS with unchanged target price of US\$73.01, based on 25x FY22E adj. EV/EBITDA, in-line with its 3-year mean. We think the long term trend that China is increasing cloud investment remains unchanged but the stock lacks near term catalyst.

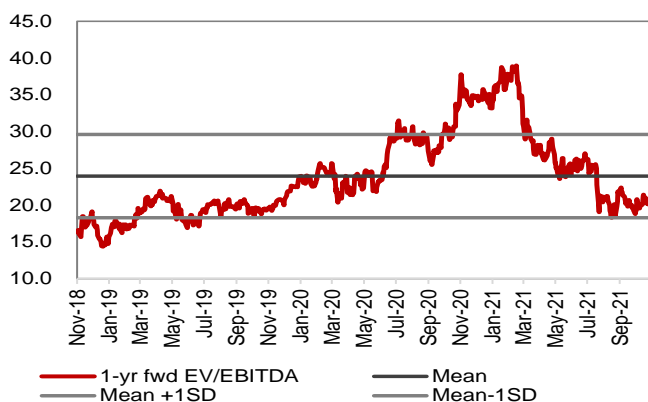
We use EV/EBITDA as the valuation methodology as it better reflects IDC operating profitability than P/E given high depreciation expense during ramp-up stage and large interest expense gap between peers if capital structure is different.

**Figure 9: Peers' valuation**

Company	Ticker	Rating	Market Cap (US\$ mn)	Price (LC)	TP (LC)	EV/EBITDA (x)		EBITDA margin (%)		Revenue FY20-23E CAGR
						FY21E	FY22E	FY21E	FY22E	
GDS	GDS US	BUY	11,503	58.92	73.01	24.3	21.5	47%	47%	36%
21Vianet	VNET US	NR	2,431	17.38	N/A	9.4	6.9	28%	30%	25%
Sinnet	300383 CH	NR	3,527	14.61	N/A	14.0	12.1	22%	23%	14%
Baosight	600845 CH	NR	14,751	73.63	N/A	40.8	30.5	18%	18%	31%
AtHub	603881 CH	NR	1,757	34.15	N/A	20.0	14.7	61%	61%	33%
ChinData	CD US	NR	3,762	10.30	N/A	16.5	11.4	49%	49%	79%
Equinix	EQIX US	NR	72,009	799.73	N/A	26.9	25.0	47%	47%	11%
Digital Realty Trust	DLR US	NR	47,131	162.05	N/A	25.8	24.6	54%	54%	17%
					<b>Mean</b>	<b>22.2</b>	<b>17.9</b>	<b>41%</b>	<b>41%</b>	<b>31%</b>
					<b>Median</b>	<b>22.3</b>	<b>16.5</b>	<b>47%</b>	<b>47%</b>	<b>28%</b>

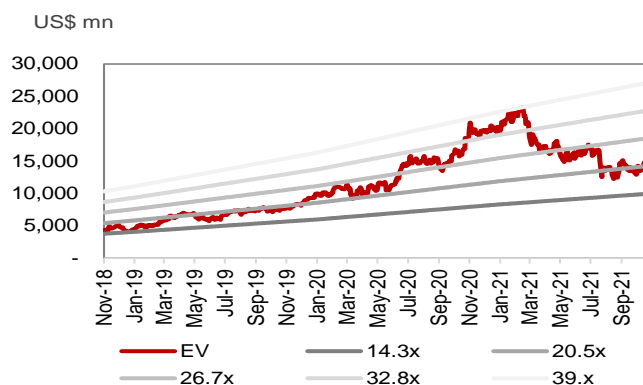
Source: Bloomberg, CMBIS

**Figure 10: 12M forward EV/EBITDA chart**



Source: Company data, CMBIS

**Figure 11: 12M forward EV/EBITDA band**



Source: Company data, CMBIS

## Financial Summary

Income statement						Cash flow summary					
YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E	YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Revenues</b>						<b>Net Income</b>	(442)	(669)	(885)	(869)	(767)
Service Revenue	4,095	5,717	7,856	10,079	12,095	Depreciation & Amortization	1,142	1,638	2,353	2,932	3,459
Equipment Revenue	28	22	15	17	18	Net change in WC	<b>(653)</b>	<b>(1,023)</b>	<b>(890)</b>	<b>778</b>	<b>411</b>
<b>Total Revenue</b>	<b>4,122</b>	<b>5,739</b>	<b>7,871</b>	<b>10,096</b>	<b>12,113</b>	Others	247	375	322	0	0
Cost of sales	(3,080)	(4,189)	(5,819)	(7,355)	(8,679)	<b>Net cash from operating</b>	<b>293</b>	<b>321</b>	<b>899</b>	<b>2,841</b>	<b>3,103</b>
<b>Gross Profit</b>	<b>1,043</b>	<b>1,550</b>	<b>2,052</b>	<b>2,741</b>	<b>3,433</b>	Capital Expenditures	(4,553)	(8,021)	(10,169)	(7,294)	(7,207)
R&D Expenditures	(22)	(40)	(41)	(65)	(71)	Acquisition of Business	(579)	(1,357)	(1,795)	(1,287)	(1,272)
Sales/Marketing/Ad Exp.	(130)	(135)	(164)	(189)	(242)	Other Investing Activities	0	0	(1,936)	(3,485)	(3,136)
G&A Expenses	(411)	(703)	(1,028)	(1,216)	(1,344)	<b>Net cash from investing</b>	<b>(5,131)</b>	<b>(9,378)</b>	<b>(13,900)</b>	<b>(12,067)</b>	<b>(11,615)</b>
<b>Operating Income</b>	<b>480</b>	<b>673</b>	<b>819</b>	<b>1,271</b>	<b>1,777</b>	Equity raised	4,934	12,724	0	0	0
<b>Adj. EBITDA</b>	<b>1,824</b>	<b>2,681</b>	<b>3,724</b>	<b>4,632</b>	<b>5,613</b>	Change of debts	3,730	790	5,447	6,226	7,357
Interest Expense	(969)	(1,287)	(1,634)	(2,065)	(2,494)	Dividend paid	(25)	0	0	0	0
Other non-oper. income	62	66	70	70	70	Others	<b>(277)</b>	<b>6,630</b>	<b>(1,382)</b>	<b>0</b>	<b>113</b>
<b>Profit Before Income Taxes</b>	<b>(426)</b>	<b>(548)</b>	<b>(745)</b>	<b>(724)</b>	<b>(648)</b>	<b>Net cash from financing</b>	<b>8,362</b>	<b>20,144</b>	<b>4,065</b>	<b>6,226</b>	<b>7,470</b>
Income Tax Expense	(16)	(121)	(140)	(146)	(119)	<b>Net change in cash</b>	<b>3,524</b>	<b>11,087</b>	<b>(8,935)</b>	<b>(2,999)</b>	<b>(1,042)</b>
<b>Net Profit (loss)</b>	<b>(442)</b>	<b>(669)</b>	<b>(885)</b>	<b>(869)</b>	<b>(767)</b>	Cash at beg. of the year	2,162	5,811	16,259	7,312	4,312
Non-controlling interests	(58)	(69)	(104)	(108)	(109)	Ex. difference and others	125	(638)	(13)	0	0
<b>Net Profit (loss) to shr holders</b>	<b>(500)</b>	<b>(738)</b>	<b>(989)</b>	<b>(977)</b>	<b>(875)</b>	<b>Cash at the end of the year</b>	<b>5,811</b>	<b>16,259</b>	<b>7,312</b>	<b>4,312</b>	<b>3,270</b>

Balance sheet						Key ratios					
YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E	YE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Non-current assets</b>	24,408	38,940	52,915	62,049	70,206	<b>Key operating ratios</b>					
PPE - Net	19,185	29,596	41,097	48,944	55,829	Total area in service ('000 sqm)	226	318	467	583	741
Other Intangible Assets	<b>2,300</b>	<b>3,382</b>	<b>5,000</b>	<b>6,287</b>	<b>7,559</b>	Avg. UTR	69%	72%	70%	69%	68%
Other noncurrent assets	2,923	5,962	6,818	6,818	6,818	Avg. MSR (RMB/ sqm/ Month)	2,532	2,403	2,306	2,253	2,169
<b>Current assets</b>	<b>7,085</b>	<b>18,319</b>	<b>10,559</b>	<b>8,143</b>	<b>7,739</b>	<b>Growth (YoY)</b>					
Cash and Equivalents	5,811	16,259	7,312	4,312	3,270	Revenue	47.6%	39.2%	37.1%	28.3%	20.0%
A/R - Trade	880	1,480	2,206	2,666	3,212	Gross profit	67.5%	48.7%	32.3%	33.6%	25.3%
Other current assets	394	579	1,042	1,164	1,257	EBITDA	74.3%	47.0%	38.9%	24.4%	21.2%
<b>Current liabilities</b>	<b>4,000</b>	<b>7,644</b>	<b>8,810</b>	<b>11,018</b>	<b>13,069</b>	Net profit	n.a.	n.a.	n.a.	n.a.	n.a.
Borrowings	1,138	2,153	2,472	3,319	4,320	<b>Margins</b>					
AP - Trade	1,676	3,657	4,116	5,037	5,760	Gross margin	25.3%	27.0%	26.1%	27.1%	28.3%
Accrued Expenses	818	1,493	1,749	2,190	2,512	Operating margin	11.6%	11.7%	10.4%	12.6%	14.7%
Other non-current liab.	<b>368</b>	<b>341</b>	<b>473</b>	<b>473</b>	<b>478</b>	EBITDA margin	44.2%	46.7%	47.3%	45.9%	46.3%
<b>Non-current liabilities</b>	16,137	22,947	28,577	33,956	40,425	<b>Balance sheet ratio</b>					
Borrowings	<b>8,028</b>	<b>10,567</b>	<b>15,696</b>	<b>21,075</b>	<b>27,431</b>	Net debt / equity ratio (%)	0.5	net cash	0.5	0.9	1.3
Convertible bonds	2,050	1,928	1,915	1,915	1,915	Current ratio	1.8	2.4	1.2	0.7	0.6
Others	<b>6,059</b>	<b>10,452</b>	<b>10,966</b>	<b>10,966</b>	<b>11,079</b>	<b>Returns (%)</b>					
<b>Total mezzanine equity</b>	1,062	1,102	1,283	1,283	1,283	ROE	n.a.	n.a.	n.a.	n.a.	n.a.
Share capital	0	1	1	1	1	ROA	n.a.	n.a.	n.a.	n.a.	n.a.
Capital surplus	<b>12,403</b>	<b>28,729</b>	<b>28,892</b>	<b>28,892</b>	<b>28,892</b>	<b>Per share</b>					
Retained earnings	(2,057)	(2,724)	(3,605)	(4,474)	(5,241)	EPS (RMB)	-0.45	-0.59	-0.69	-0.68	-0.61
Other reserves	<b>(53)</b>	<b>(440)</b>	<b>(543)</b>	<b>(543)</b>	<b>(543)</b>	BVPS (RMB)	9.3	20.4	19.8	19.1	18.5
<b>Total equity</b>	<b>10,294</b>	<b>25,566</b>	<b>24,803</b>	<b>23,934</b>	<b>23,167</b>						

Source: Company data, CMBIS estimates



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