Kingsoft Cloud (KC US)

China cloud service pure play

NOT RATED

Current Price US$60.74

LEADING VIDEO PUBLIC CLOUD VENDOR Kingsoft Cloud (KC) had 5.4% share in 2019 China IaaS + PaaS market with ByteDance being top customer. KC delivered strong growth (Rev +78% YoY in 2019), thanks to 1) internet customers adopting multi-cloud strategy, 2) increasing number of premium customers (+58% YoY to 243 in 2019) and 3) higher ASP per premium customer (+16% YoY to RMB15.9mn) on product cross-selling. Lower revenue from Kingsoft Group and continuous margin expansion are re-rating catalysts.

- **Robust growth as internet customers adopting multi-cloud strategy.** Kingsoft Cloud (KC) is a leading cloud service provider in China with 5.4% market share in 2019 (IaaS + PaaS). KC is well-positioned to capture the growing cloud market (28.3% CAGR in 2019-2024 to reach a size of RMB563.3bn in China). Although Alibaba is a leader in China public cloud market, KC is able to achieve robust growth (79% revenue CAGR in 2017-2019) as internet companies (e.g. game/ video verticals) are adopting multi-cloud strategy to lower reliance on single cloud provider. Among KC's new customers, around 80% are deployed on multi-cloud. According to Frost & Sullivan, 26% of enterprises with over 1,000 employees in China are using cloud adopted multi-cloud strategy, compared with 85% in the US.
- **Improving customer mix with less dependence on Kingsoft Group.** KC is gradually reducing dependency on Kingsoft Group, and revenue from related parties (Kingsoft Group + Xiaomi + Cheetah Group) declined from 34% in 2017 to only 12% in 1H20. This proves KC's cloud technology and R&D capabilities to attract new customers. KC has 1,150 R&D engineers and spent 15% of revenue (RMB595mn) on R&D in 2019.
- **Continuous margin expansion with scale benefits.** KC delivered continuous margin expansion on larger scale, higher efficiency and bandwidth utilization. Cost of revenue mainly consists of IDC costs (bandwidth + rack) and depreciation of servers. IDC costs as % of revenue was at 66% in 3Q20 (vs. 71% in 3Q19) while that of depreciation was at 10% (vs. 16% in 3Q19). KC gross margin turned positive since 3Q19 and reached 6.5% in 3Q20. Management expects gross margin to improve at +5 pct pts YoY in 2021E.
- **Rare independent IaaS provider.** KC is a rare IaaS pure play in the market and is trading at 9.2x consensus FY21E P/S. Along the cloud service supply chain, companies with IaaS exposure are trading at 7.3x but with lower growth (avg. FY19-22E sales CAGR 24% vs. 61% for KC) while capex-light SaaS + PaaS companies are trading at 30x FY21E P/S.

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19A	FY20E	FY21E
Revenue (RMB mn)	1,236	2,218	3,956	6,567	10,468
YoY growth (%)	n.a.	79%	78%	66%	59%
Adj. EBITDA (RMB mn)	(338)	(520)	(418)	(227)	248
YoY growth (%)	n.a.	n.a.	n.a.	n.a.	n.a.
Net income (RMB)	(1,320)	(1,749)	(1,161)	(942)	(728)
EPS (RMB)	(1.66)	(2.20)	(1.31)	(3.98)	(2.88)
YoY growth (%)	n.a.	n.a.	n.a.	n.a.	n.a.
P/S (x)	77.4	43.1	24.2	14.6	9.1
ROE (%)	n.a.	-43%	-33%	-17%	-12%
Net gearing (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, Bloomberg consensus

China Software & IT services

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Stock Data

Mkt Cap (US$ mn)	14,875
Avg 3 mths t/o (US$ mn)	88.73
52w High/Low (US$)	74.67/ 17.01
Total Issued Shares (mn)	218

Source: Bloomberg

Shareholding Structure

Kingsoft Group (3888 HK)	43.6%
Xiaomi (1810 HK)	13.8%
Mr. Jun LEI	13.8%

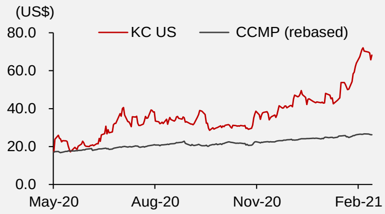
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	49.5%	45.8%
3-mth	90.7%	63.0%
6-mth	99.2%	62.4%

Source: Bloomberg

12-mth Price Performance

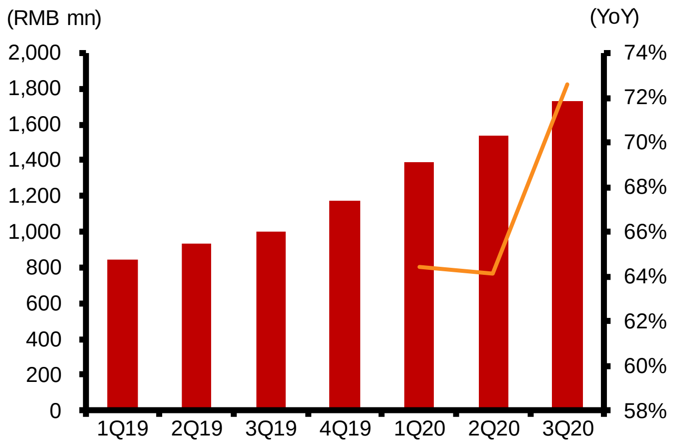


Source: Bloomberg

Auditor: Ernst & Young Hua Ming

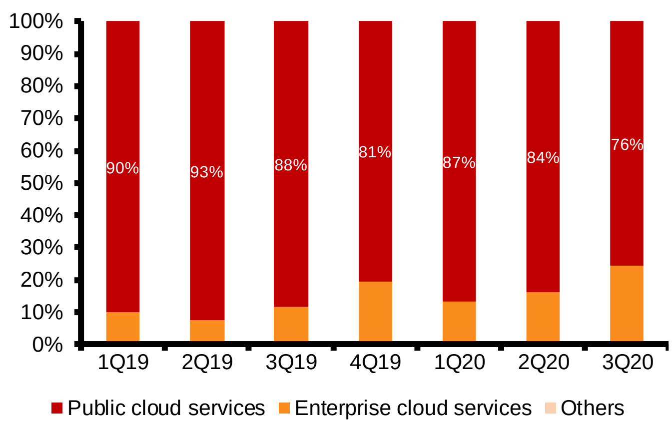
Focus Charts

Figure 1: Revenue and YoY



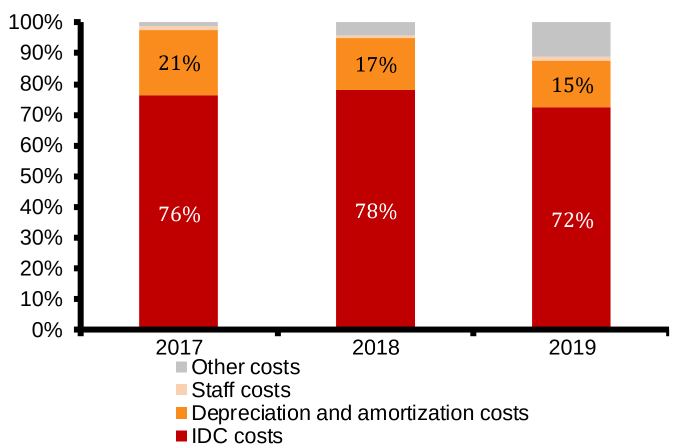
Source: Company data

Figure 2: Revenue mix



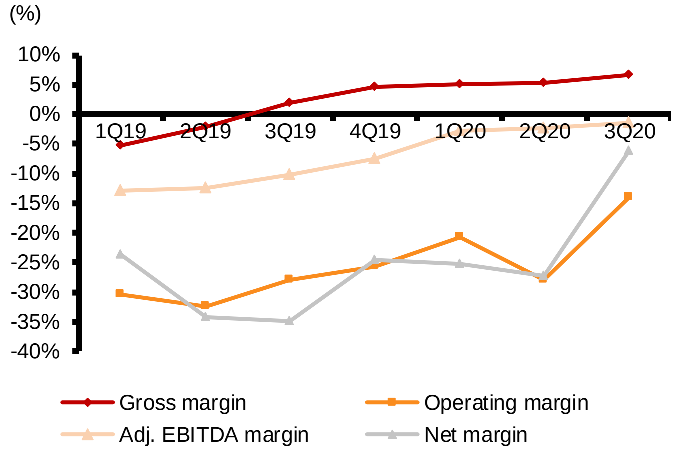
Source: Company data

Figure 3: Cost of sales



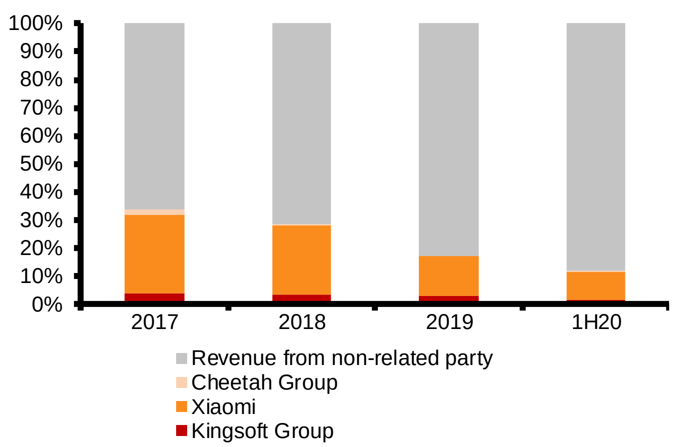
Source: Company data

Figure 4: Margins



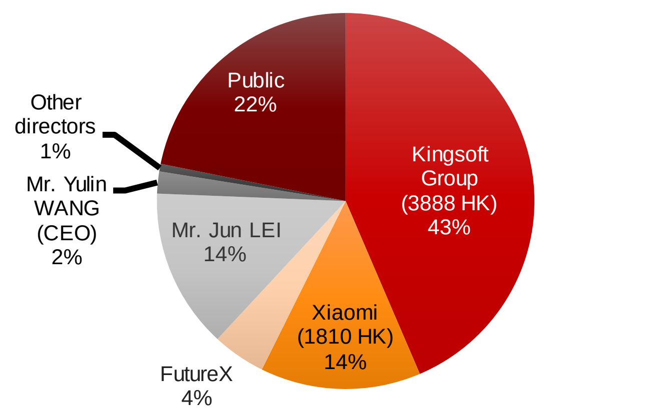
Source: Company data

Figure 5: Related party transaction (revenue)



Source: Company data

Figure 6: Shareholding structure



Source: Company data

Company overview

Kingsoft Cloud (KC), founded in 2012 and listed on Nasdaq in May 2020, is a leading cloud service provider in China. It had 5.4% market share from IaaS and PaaS public cloud services in 2019, according to Frost & Sullivan. As of 31 Dec 2019, KC had a data center and CDN node network with >73,000 servers throughout China and in six other countries.

In 2019, KC derived RMB3.5bn revenue from Public Cloud Services with 175 premium customers (paying >RMB700k annually). Net dollar retention rate is high at 155%. In 2017, KC started to provide private cloud solutions for financial, public service and healthcare industries. Number of premium customers grew from only 2 in 2017 to 67 in 2019 with average revenue per premium customer of RMB7.2mn.

Figure 7: Kingsoft Cloud key businesses

RMB mn	Public Cloud Services	Enterprise Cloud Services
Verticals served	Game, video, AI, e-commerce, education and mobile internet	Financial service, public service and healthcare business
Pricing model	1) Monthly billing based on utilization and duration or 2) subscription	Project based
2019		
No. of premium customers*	175 (+25% YoY)	67 (+294% YoY)
Avg. revenue per premium customer	19.2 (+32% YoY)	7.2 (31% YoY)
Net dollar retention rate of premium customer	155%	-
Revenue	3,459	486
as % of total	87%	12%
YoY	64%	415%

Source: Company data *premium customer: annual revenue to Kingsoft Cloud >RMB700,000*

Figure 8: Kingsoft Cloud key customers

Source: Company data

Financials

Figure 9: Kingsoft Cloud operating model

RMB mn	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20	2017	2018	2019
Revenue breakdown										
Public cloud services	763	866	885	945	1,209	1,287	1,310	1,202	2,111	3,459
Enterprise cloud services	83	68	114	220	182	246	409	15	94	486
Others	-	0	3	8	1	2	10	18	13	11
Total	**846**	**935**	**1,002**	**1,174**	**1,391**	**1,535**	**1,729**	**1,236**	**2,218**	**3,956**
Revenue mix										
Public cloud services	90%	93%	88%	81%	87%	84%	76%	97%	95%	87%
Enterprise cloud services	10%	7%	11%	19%	13%	16%	24%	1%	4%	12%
Others	0%	0%	0%	1%	0%	0%	1%	1%	1%	0%
Revenue YoY										
Public cloud services					58%	49%	48%		76%	64%
Enterprise cloud services					119%	259%	257%		518%	415%
Others						397%	256%		-27%	-16%
Total					64%	64%	73%		79%	78%
Key operating metrics										
Public cloud										
No. of premium customers*								112	139	175
YoY									24%	26%
Net dollar retention rate of premium customer								0%	161%	155%
Avg. revenue per premium customer								10.2	14.5	19.2
YoY									42%	32%
Computing								356	663	1,018
Storage								220	289	298
Delivery								629	1,161	2,137
Enterprise cloud										
No. of premium customers*								2	17	67
Avg. revenue per premium customer								-	5.5	7.2
Cost of sales breakdown										
IDC costs	676	744	701	735	920	978	1,060	1,033	1,890	2,857
Depreciation and amortization costs	135	137	154	173	205	218	157	290	407	599
Staff costs								17	24	52
Other costs								14	98	440
Total	**891**	**955**	**983**	**1,119**	**1,320**	**1,454**	**1,616**	**1,354**	**2,419**	**3,949**
Cost of sales mix										
IDC costs	76%	78%	71%	66%	70%	67%	66%	76%	78%	72%
Depreciation and amortization costs	15%	14%	16%	15%	16%	15%	10%	21%	17%	15%
Staff costs								1%	1%	1%
Other costs								1%	4%	11%

Source: Company data, **premium customer: annual revenue to Kingsoft Cloud >RMB700,000*

Figure 10: Kingsoft Cloud income statement

RMB mn	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20	2017	2018	2019
Revenues	846	935	1,002	1,174	1,391	1,535	1,729	1,236	2,218	3,956
Cost of sales	(891)	(955)	(983)	(1,119)	(1,320)	(1,454)	(1,616)	(1,354)	(2,419)	(3,949)
Gross Profit	**(45)**	**(20)**	**19**	**54**	**71**	**81**	**113**	**(118)**	**(200)**	**8**
Gross margin	*-5.3%*	*-2.2%*	*1.9%*	*4.6%*	*5.1%*	*5.3%*	*6.5%*	*-9.6%*	*-9.0%*	*0.2%*
R&D	(124)	(143)	(156)	(171)	(196)	(231)	(168)	(399)	(441)	(595)
SG&A	(88)	(140)	(143)	(186)	(164)	(280)	(188)	(210)	(339)	(556)
Operating Income	**(257)**	**(304)**	**(280)**	**(303)**	**(289)**	**(430)**	**(243)**	**(727)**	**(979)**	**(1,144)**
Operating margin	*-30.4%*	*-32.5%*	*-27.9%*	*-25.8%*	*-20.8%*	*-28.0%*	*-14.0%*	*-58.8%*	*-44.2%*	*-28.9%*
Adj. EBITDA	**(109)**	**(118)**	**(102)**	**(89)**	**(39)**	**(36)**	**(26)**	**(338)**	**(520)**	**(418)**
Adj. EBITDA margin	*-12.9%*	*-12.6%*	*-10.2%*	*-7.6%*	*-2.8%*	*-2.3%*	*-1.5%*	*-27.4%*	*-23.4%*	*-10.6%*
Non-Operating Income	59	(14)	(68)	65	(37)	12	142	13	(17)	41
Profit Before Tax	(199)	(318)	(348)	(237)	(326)	(418)	(101)	(714)	(997)	(1,102)
Income tax (expense) gain	(3)	(2)	(2)	(2)	(6)	(2)	(4)	(1)	(10)	(9)
Minorities	-	-	-	-	(0)	0	0	2	2	2
Accretion to redemption value of convertible preferred shares	-	-	-	(50)	(20)	-	-	-	-	-
Net Income to Shareholders	**(201)**	**(320)**	**(351)**	**(289)**	**(352)**	**(420)**	**(105)**	**(1,320)**	**(1,749)**	**(1,161)**
Net margin	*-24%*	*-34%*	*-35%*	*-25%*	*-25%*	*-27%*	*-6%*	*-107%*	*-79%*	*-29%*

Source: Company data

Valuation

Figure 9: Peers' valuation

Company	Ticker	Rating	Market Cap (US$ mn)	Price (LC)	P/S FY20E	P/S FY21E	EV/sales FY20E	EV/sales FY21E	Sales CAGR FY19-22E	EBITDA margin FY19
Companies with IaaS business										
Kingsoft Cloud	**KC US**	**NR**	**14,875**	**68.23**	**14.7**	**9.2**	**13.7**	**8.6**	**61%**	**-14%**
Ucloud	688158 CH	NR	2,927	44.80	8.0	5.5	7.1	4.9	48%	21%
Alibaba	BABA US	NR	713,537	263.59	9.2	6.5	8.3	5.9	35%	25%
Tencent	700 HK	NR	882,917	713.50	11.9	9.6	12.1	9.8	24%	41%
Baidu	BIDU US	NR	115,935	339.91	7.0	6.0	6.3	5.4	10%	26%
Amazon	AMZN US	NR	1,636,535	3249.90	4.3	3.5	4.4	3.5	26%	14%
Microsoft	MSFT US	NR	1,817,448	240.97	12.8	11.1	12.5	10.8	13%	45%
Google	GOOG US	NR	1,412,465	2101.14	9.6	7.3	8.8	6.7	12%	30%
				Mean	**9.7**	**7.3**	**9.2**	**7.0**	**31%**	**23%**
China SaaS + PaaS										
Agora	API US	NR	9,989	98.08	76.4	58.4	71.5	54.7	57%	-7%
Glodon	002410 CH	BUY	14,025	76.50	22.1	17.9	21.3	17.3	20%	11%
Yonyou	600588 CH	NR	20,546	40.63	14.8	12.5	14.7	12.4	17%	18%
Kingsoft Office	688111 CH	NR	26,656	374.00	69.5	46.7	66.7	44.8	48%	25%
Kingdee	268 HK	NR	14,848	33.20	28.5	22.9	27.8	22.4	17%	27%
MYC	909 HK	HOLD	12,564	50.55	46.7	33.2	46.2	32.9	39%	21%
Youzan	8083 HK	NR	8,459	3.80	29.9	19.2	29.5	18.9	53%	-65%
Weimob	2013 HK	NR	7,895	26.90	22.8	15.0	22.7	14.9	48%	8%
				Mean	**38.8**	**28.2**	**37.6**	**27.3**	**37%**	**5%**
US SaaS + PaaS										
Adobe	ADBE US	NR	229,355	479.12	17.9	15.1	17.8	15.0	16%	36%
Atlassian	TEAM US	NR	64,618	258.41	33.3	28.3	40.0	32.9	24%	1%
Autodesk	ADSK US	NR	67,154	305.40	20.6	17.9	20.7	18.0	19%	3%
Datadog	DDOG US	NR	31,991	105.05	54.3	38.4	52.8	37.4	45%	2%
Docusign	DOCU US	NR	49,467	265.16	51.2	34.6	51.3	34.7	39%	-55%
Intuit	INTU US	NR	108,080	411.35	14.6	12.1	14.1	11.8	15%	31%
Salesforce	CRM US	NR	226,277	246.56	13.3	10.7	13.1	10.6	24%	14%
SAP	SAP US	NR	155,799	126.82	4.8	4.8	5.1	5.1	1%	23%
ServiceNow	NOW US	NR	111,920	570.73	25.0	19.5	24.8	19.4	27%	10%
Shopify	SHOP US	NR	175,780	1435.01	44.1	33.3	59.4	42.7	50%	-6%
Snowflake	SNOW US	NR	82,099	290.00	n.a.	141.6	n.a.	133.7	125%	-187%
Twilio	TWLO US	NR	64,241	425.55	38.5	26.5	37.0	25.5	41%	-20%
Veeva System	VEEV US	NR	47,533	313.82	43.6	32.8	42.2	31.8	26%	27%
Workday	WDAY US	NR	66,322	276.34	15.4	13.2	18.1	15.3	21%	-7%
Zoom	ZM US	NR	121,768	417.26	47.2	34.5	196.5	46.5	120%	4%
				Mean	**30.3**	**30.9**	**42.4**	**32.0**	**39%**	**-8%**

Source: Bloomberg, CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19A
Revenue	**1,236**	**2,218**	**3,956**
Cost of sales	(1,354)	(2,419)	(3,949)
Gross Profit	**(118)**	**(200)**	**8**
Selling And Distribution Expenses	(116)	(192)	(317)
Administrative Expenses	(94)	(147)	(239)
Research And Development Expenses	(399)	(441)	(595)
Operating Profit/(Loss)	**(727)**	**(979)**	**(1,144)**
Adj. EBITDA	**(338)**	**(520)**	**(418)**
Interest income	26	24	17
Interest expense	(3)	(2)	-
Other non-operating income	505	640	778
Profit Before Tax	**(199)**	**(318)**	**(348)**
Income Tax Expense	(1)	(10)	(9)
Profit After Tax	**(714)**	**(1,006)**	**(1,111)**
Non-controlling Interest	-	-	-
Accretion to redemption value of redeemable convertible preferred shares	(606)	(742)	(50)
Attributable To Owners Of The Parent	**(1,320)**	**(1,749)**	**(1,161)**

Cash flow summary

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19A
Net Income	**(714)**	**(1,006)**	**(1,111)**
Depreciation and Amortization	298	412	605
Net Change In Working Capital	220	68	(113)
Others	62	143	181
Net cash from operating activities	**(135)**	**(383)**	**(439)**
Capital Expenditures	(346)	(1,095)	(1,000)
Purchases of short-term investments	(1,902)	(2,867)	(1,112)
Other Investing Activities	427	2,788	2,995
Net cash from investing activities	**(1,821)**	**(1,174)**	**883**
Proceeds from redeem. conv. pref. shares	1,723	2,852	349
Change of debts	16	(80)	(81)
Dividend paid	0	0	0
Others	123	(336)	(204)
Net cash from financing activities	**1,861**	**2,436**	**65**
Net change in cash	**(94)**	**879**	**509**
Cash at the beginning of the year	706	573	1,507
Exchange difference and others	(39)	54	8
Cash at the end of the year	573	1,507	2,023

Balance sheet

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19A
Non-current assets	n.a.	**1,125**	**1,882**
PPE - Net	n.a.	1,043	1,721
Other Intangible Assets	n.a.	10	7
Other noncurrent assets	n.a.	71	154
Current assets	n.a.	**4,734**	**4,150**
Cash and Equivalents	n.a.	1,507	2,023
Accounts Receivable - Trade	n.a.	542	1,347
Other current assets	n.a.	2,686	779
Current liabilities	n.a.	**1,437**	**2,420**
Borrowings	n.a.	81	100
Accounts Payable - Trade	n.a.	721	1,255
Accrued Expenses	n.a.	424	949
Other non-current liabilities	n.a.	212	116
Non-current liabilities	n.a.	**320**	**75**
Borrowings	n.a.	174	74
Amounts due to related parties	n.a.	145	-
Others	n.a.	0	0
Total mezzanine equity	n.a.	**7,346**	**7,735**
Share capital	n.a.	5	6
Capital surplus	n.a.	-	92
Retained earnings	n.a.	-	-
Others	n.a.	543	608
Total equity	n.a.	**(3,243)**	**(4,197)**

Key ratios

YE 31 Dec	FY17A	FY18A	FY19A
Key operating metrics			
Public cloud - # of premium customer	112	139	175
Net dollar retention rate of prem. customer	0%	161%	155%
Avg. revenue per premium customer	10	15	19
Enterprise cloud - # of premium customer	2	17	67
Growth (YoY)			
Revenue	n.a.	79%	78%
Gross profit	n.a.	n.a.	n.a.
Adj. EBITDA	n.a.	n.a.	n.a.
Net profit	n.a.	n.a.	n.a.
Margins			
Gross margin	-10%	-9%	0%
Operating margin	-59%	-44%	-29%
Adj. EBITDA margin	-27%	-23%	-11%
Balance sheet ratio			
Net debt / equity ratio (%)	n.a.	net cash	net cash
Current ratio	n.a.	3.3	1.7
Returns (%)			
ROE	n.a.	n.a.	n.a.
ROA	n.a.	n.a.	n.a.
Per share			
EPS (RMB)	(1.66)	(2.20)	(1.31)
BVPS (RMB)	n.a.	(4.1)	(4.7)

Source: Company data

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