

China Software & IT Services

Lockdowns add uncertainty to cloud recovery timeline

We think China IaaS/ PaaS 1H22 growth could slow to +10-20% YoY as enterprise IT spending and hybrid cloud delivery schedule could be affected by Omicron spread. However, market share reshuffle will be more significant as Huawei/ China Telcos have become aggressive in cloud. Given lower visibility in cloud recovery, IDCs are turning conservative in expansion. Among the cloud plays, we prefer 1) SaaS with high earnings/ cash flow visibility - Glodon (002410 CH) and 2) Huawei Cloud IT service provider - Chinasoft (354 HK).

- **IaaS/ PaaS 1H22 growth could slow to +10-20% YoY due to the spread of Omicron and lockdowns.** We [expected](#) China IaaS/ PaaS market growth of 30-40% YoY in 2022E and that the cloud demand will be driven by enterprise cloud migration instead of internet applications. However, IaaS/ PaaS demand could be more back-end loaded this year as Omicron has induced new rounds of lockdowns in China recently. As macro uncertainties linger, we are worried that enterprises may scale back on cloud spending temporarily. Meanwhile, hybrid cloud project delivery could face delays. We believe 1H22 cloud market growth could be slowed to +15-20% YoY.
- **Huawei/ China Telcos cloud market share gain to accelerate.** In 2021, we observed that non-internet cloud service providers have delivered impressive growth. Huawei/ China Telecom/ China Mobile cloud businesses achieved revenue growth of +34%/+102%/+114% YoY respectively, compared to AliCloud of +30% YoY. We think the market share reshuffle will become more significant in 2022. In particular, China Telecom/ China Mobile have laid out concrete targets in cloud/ IDC business. China Telecom plans to raise cloud/IDC capex by +62% YoY in 2022 (adding 160k cloud servers). China Mobile targets >660k cloud servers by end of 2022E (server scale similar to Huawei Cloud, based on our channel checks).
- **IDC becomes conservative in expansion.** The three US-listed IDCs (GDS/ 21Vianet/ ChinData) have guided a softer 2022E outlook with slower revenue growth (+26% YoY in 2022 vs. +36% YoY in 2021), decline in adj. EBITDA margin (due to higher utility cost since China liberalized power tariff in Oct 2021) and lower capex spending (+3% YoY in 2022 vs. +33% YoY in 2021). We think lockdowns have added uncertainty to their 2022 growth plans as capacity move-in could face delays.
- **Cloud market recovery could be delayed.** We think recovery in IaaS/ PaaS/ IDC may be slower than expected if Omicron spread/ lockdowns continue. Among the cloud plays, we now prefer SaaS given higher earnings and cash flow visibility. Our top picks in cloud are Glodon (SaaS with high cash flow visibility) and Chinasoft (Huawei cloud share gain, announced up to HK\$1bn share repurchase plan on 11 Apr).

Valuation Table

Company	Ticker	Rating	Price (LC)	TP (LC)	EV/sales FY22E	P/E FY22E	ROE FY21	Sales CAGR FY21-24E
GDS	GDS US	BUY	33.57	52.28	7.3	N/A	N/A	19%
GDS	9698 HK	BUY	31.80	50.63	7.2	N/A	N/A	19%
Chinasoft	354 HK	BUY	5.94	10.52	0.5	15.2	11.1	19%
Kingsoft Cloud	KC US	BUY	5.14	7.87	0.4	N/A	N/A	13%
Glodon	002410 CH	BUY	46.81	82.75	8.2	56.4	10.8	17%

Source: Bloomberg, CMBIGM estimates

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Focus Charts - IaaS/ PaaS

Figure 1: Non-internet cloud service providers delivered robust growth in 2021

Cloud revenue (RMB bn)	2020	2021	YoY
Alibaba	55.8	72.4	30%
China Telecom	13.8	27.9	102%
China Mobile	11.3	24.2	114%
Huawei	15.0	20.1	34%
China Unicom	11.1	16.3	46%
Baidu	9.2	15.1	64%
Kingsoft Cloud	6.6	9.1	38%
UCloud	2.5	2.9	18%
Total	125.3	187.9	50%

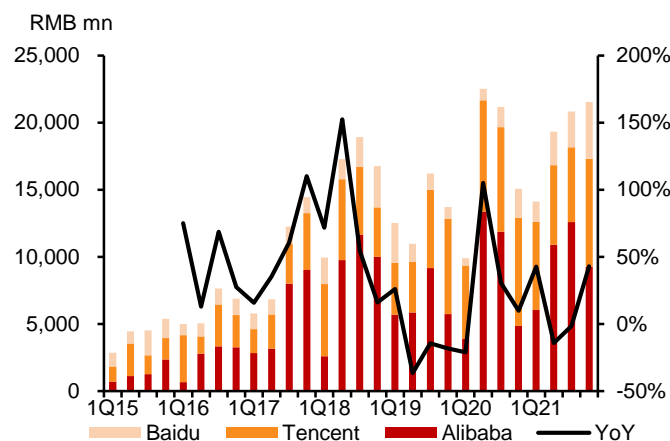
Source: Company data, CMBIGM

Figure 2: China Telecom/ China Mobile are increasing cloud/ IDC capex

Cloud-related capex (RMB bn)	2021	YoY	2022E	YoY	Remarks to 2022E targets
China Telecom	17.3	30%	27.9	62%	
- IDC			6.5		• To add 45k cabinets. Cumulative cabinets to reach 515k.
- Cloud servers			14.0		• To add 160k cloud servers.
China Mobile			48.0		• Cumulative >450k IDC cabinets will be available for external use. • Cumulative >660k cloud servers will be commissioned.

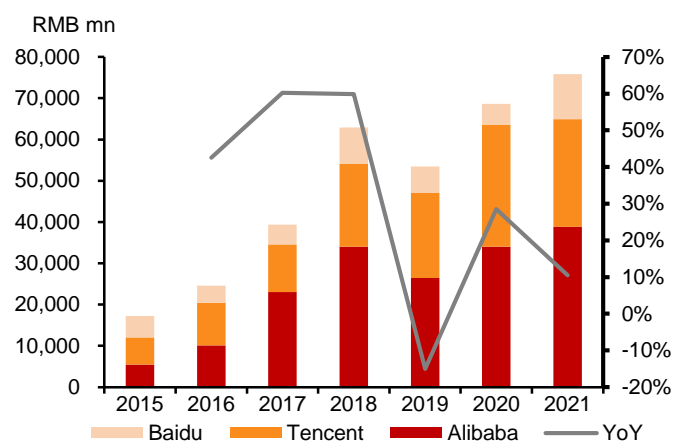
Source: IDC, CMBIGM

Figure 3: BAT operating capex (quarterly)



Source: Company data, CMBIGM

Figure 4: BAT operating capex (yearly)



Source: Company data, CMBIGM

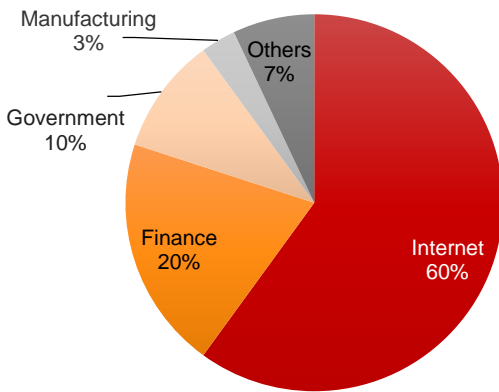
Focus Charts - IDC

Figure 5: IDCs generally guided a softer FY22E outlook with slower revenue growth, decline in adj. EBITDA margin and a more conservative capex plan

RMB bn	FY21			FY22E Guidance *		
	Revenue	Adj. EBITDA	Capex	Revenue	Adj. EBITDA margin	Capex
GDS	7.82 (+36% YoY)	3.70 (margin: 47.4%)	13.69	9.5 (+22% YoY)	46.0% (-1.4 pts YoY)	-12.4% YoY
21Vianet	6.19 (+28% YoY)	1.75 (margin: 28.3%)	3.99	7.6 (+23% YoY)	27.0% (-1.4 pts YoY)	+12.8% YoY
ChinData	2.85 (+56% YoY)	1.42 (margin: 49.7%)	3.77	4.12 (+44% YoY)	50.5% (+0.7 pts YoY)	+46.0% YoY

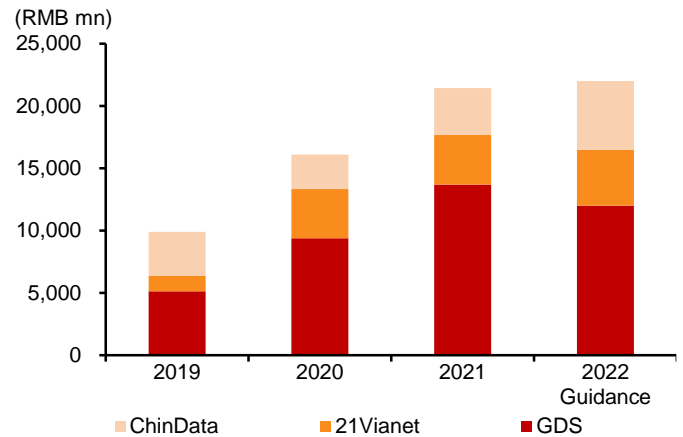
Source: Company data, CMBIGM *reflects mid-point of guidance

Figure 6: IDCs downstream customers are mainly internet cloud service providers



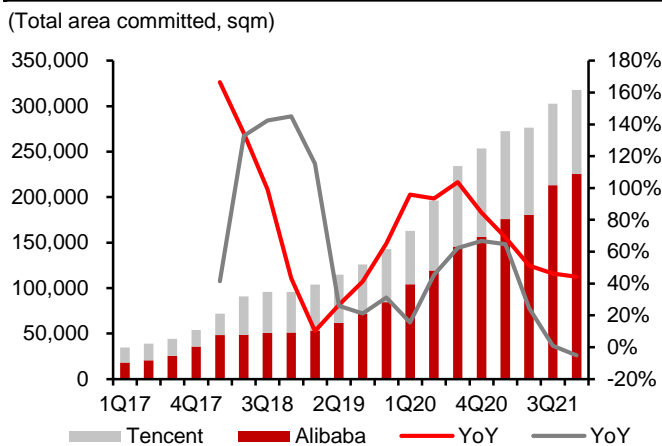
Source: iResearch (2019), CMBIGM

Figure 7: IDCs are turning conservative in expansion in 2022E



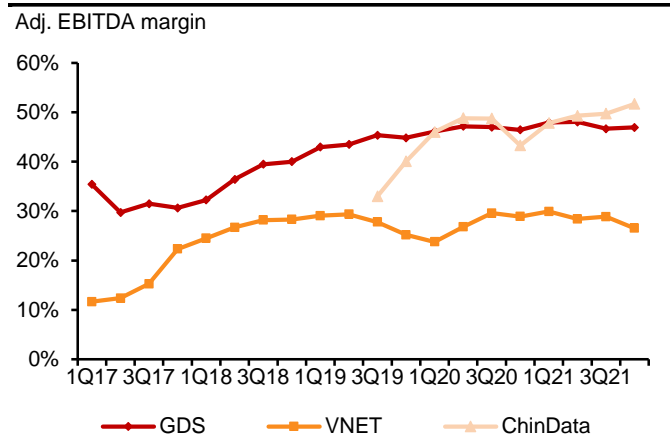
Source: Company data, CMBIGM

Figure 8: Tencent total committed area to GDS continued to decline although Alibaba's demand remained resilient



Source: Company data, CMBIGM

Figure 9: GDS and VNET are guiding a decline in adj. EBITDA margin in 2022E due to higher power tariff (not all utility costs can be passed through)



Source: Company data, CMBIGM

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