

## VNET Group Inc

Bloomberg: VNET US Equity | Reuters: VNET.O

Refer to important disclosures at the end of this report

DBS Group Research . Equity

31 Mar 2022

### BUY

Last Traded Price (30 Mar 2022): US\$7.12 (NASDAQ : 14,442)  
Price Target 12-mth: US\$13.60 (91% upside) (Prev US\$15.30)

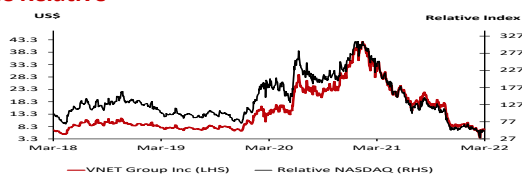
#### Analyst

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#### What's New

- Adjusted EBITDA grew by 18.8% y-o-y to Rmb463m in 4Q21, in line
- FY22 adjusted EBITDA guidance is Rmb1,975m-Rmb2,125m, below market expectations
- FY22 expansion target revised down from 25k to 14.4k-17.4k due to macro uncertainties
- Maintain BUY with a lower TP of US\$13.6, given the lower expansion target in FY22

#### Price Relative



#### Forecasts and Valuation

FY Dec (RMBm)	2020A	2021A	2022F	2023F
Turnover	4,829	6,190	7,605	8,941
EBITDA	1,106	1,289	1,922	2,380
Pre-tax Profit	(2,571)	627	(170)	(288)
Net Profit	(3,180)	500	(310)	(453)
Net Profit Gth (Pre-ex) (%)	(248.8)	48.2	5.9	(46.1)
EPS (RMB)	(26.61)	3.47	(1.79)	(2.27)
EPS (US\$)	(4.19)	0.55	(0.28)	(0.36)
EPS Gth (%)	(1,527.5)	N/A	N/A	(27.1)
Diluted EPS (US\$)	(0.84)	(0.34)	(0.28)	(0.36)
DPS (US\$)	0.00	0.00	0.00	0.00
BV Per Share (US\$)	7.27	7.91	6.32	5.15
PE (X)	nm	13.0	nm	nm
P/Cash Flow (X)	7.6	4.7	23.3	8.1
P/Free CF (X)	nm	nm	nm	nm
EV/EBITDA (X)	5.8	6.0	6.1	6.7
Net Div Yield (%)	0.0	0.0	0.0	0.0
P/Book Value (X)	1.0	0.9	1.1	1.4
Net Debt/Equity (X)	CASH	0.1	0.5	1.0
ROAE (%)	(60.7)	7.8	(4.4)	(6.7)
Adi EBITDA	1,324	1,754	2,042	2,500
Adi EBITDA Gth (%)	26.0	32.4	16.5	22.4
EV/Adi EBITDA	8.9	6.7	5.7	4.7
Adi EBITDA Rev (%)			(10.0)	(12.4)
Consensus EPS (RMB)			(1.76)	(1.31)
Other Broker Recs:		B:15	S:1	H:0

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

### Transformation to bear fruit

#### Investment Thesis

Riding on growing demand for data centre services from various industries. VNET has a diversified retail customer base across various industries, and demand for data centre services has been strong as these companies embark on their digital transformation.

**Strong capacity expansion to support growth.** Despite macro uncertainties, VNET aims to expand its capacity by 14.4k-17.4k cabinets in FY22 to meet rising demand, representing 18%-22% growth. It targets to maintain a healthy utilisation rate of c.60% despite the increase in capacity.

**Expect to secure more wholesale contracts,** given the existing retail relationships with internet and cloud customers, as well as strong capacity growth. VNET currently has 252MW wholesale capacity in service or under MOU.

#### Valuation:

Our TP of US\$13.6 is based on 12x FY22F EV/adjusted EBITDA, slightly higher than its historical average for its wholesale transformation.

#### Where we differ:

**Expect expansion into wholesale market to trigger re-rating.** The market is concerned about VNET's growth outlook due to its retail business model which has lower visibility. We believe the company will successfully expand into the wholesale market, supported by existing retail relationships with wholesale customers and a strong project pipeline.

#### Key Risks to Our View:

**Excess DC supply.** Excess DC capacity could result in pricing pressures for the whole industry.

**Slowdown in DC demand.** The slowdown in demand for DC could lead to overcapacity and pricing pressure.

#### At A Glance

Issued Capital (m shrs)	136
Mkt Cap (US\$m)	968
Major Shareholders (%)	
Tus-Holdings Co., Ltd.	11.3
TT International Asset Management Ltd	9.3
GIC Private Limited	9.0
Blackstone Tactical Opportunities Advisors L.L.C.	7.4
Majara Investment Ltd	6.4
Free Float (%)	56.6
3m Avg. Daily Val. (US\$m)	24.46
GICS Industry: Information Technology / Software & Services	



Watchlist the stock on Insights Direct to receive prompt updates



## WHAT'S NEW

### FY22 guidance below market expectations with a lower expansion target

#### 4Q21 result highlights

Revenue increased by 29.4% y-o-y to Rmb1,745m in 4Q21, slightly below the low-end of management guidance of Rmb1,750m-Rmb1,770m.

Total cabinets in service increased by 46.7% y-o-y to 78.5k, with net additions of 13.3k cabinets in 4Q21. Total net additions was 25k in FY21, in line with its expansion target. Utilised cabinets increased by 49.6% y-o-y to 48.4k. Utilisation rate expanded 1.2ppts y-o-y to 61.6%.

Adjusted cash gross profit increased by 22.7% to Rmb714m in 4Q21, with adjusted cash gross margin contracting 2.3ppts y-o-y to 40.9%, due to massive delivery of new cabinets in 4Q21.

Adjusted EBITDA increased by 18.8% y-o-y to Rmb463m in 4Q21, in line with management guidance of Rmb450-Rmb470m, with adjusted EBITDA margin contracting 2.4ppts y-o-y to 26.5%. Net loss narrowed by 97.3% y-o-y to Rmb27m in 4Q21, mainly attributable to increase in the fair value of convertible promissory notes.

#### Outlook

The company's guidance for FY22 revenue and adjusted EBITDA are Rmb7,450m-Rmb7,750m and Rmb1,975m-Rmb2,125m, with midpoints implying 22.8% and 16.9% y-o-y growth respectively, both are below market expectations. The company also has a capex budget of Rmb4bn-Rmb5bn in FY22.

The midpoint of guidance implies an adjusted EBITDA margin of 27% in FY22, down by 1.3ppts from FY21, due to massive delivery of new cabinets in 4Q21, higher electricity cost and expansion of non-IDC business. The higher electricity cost would have c.1% impact on the margin. Currently, a large portion of the contracts are bundled with electricity costs due to low portion of existing wholesale cabinets. With the ramp-up of wholesale customers in FY22 and roll-over of retail contracts, management expects non-bundled contracts to reach c.30%.

Management has revised down its expansion target in FY22 from 25k to 14.4k-17.4k due to the macro uncertainties, and 60% of the expansion will be wholesale

cabinets. The company continues to expand its wholesale capacity. The company currently has 252MW wholesale capacity, with 30MW under construction. The company won pre-committed wholesale orders of c.7MW in 4Q21 and c.11MW in 1Q22 respectively from an existing internet customer, along with other three recent contracts totaling c.5MW.

Management has kept the utilisation rate target at 60% for FY22. Retail monthly recurring revenues (MRR) increased 1.9% y-o-y to Rmb9,301 in 4Q21, similar to 3Q21. Management expects MRR to be stable at around Rmb9,000, taking into account of quarterly fluctuations.

VNET plans to apply for a secondary listing in Hong Kong, while the schedule is subject to market conditions and regulatory approval. The listing in Hong Kong market could help ease market concern on the funding channels and delisting risk from the US market.

We have cut our adjusted EBITDA forecasts by 10% and 12.4% for FY22 and FY23 respectively, due to a lower expansion target in FY22. We project adjusted EBITDA to grow by 16.5% and 22.4% in FY22 and FY23 respectively. We maintain our BUY call on VNET for its steady capacity expansion amid macro uncertainties, as well as strong demand for data centre services in China. Our TP of US\$13.6 is based on 12x FY22 EV/Adjusted EBITDA (unchanged), lower than the average of its wholesale peers.

#### Company Background

VNET is one of the leading and fast-growing carrier-neutral data centre (DC) operators in China. The business, which is based in Beijing, was founded by Sheng Chen and Jun Zhang in 1999 and started the first carrier-neutral DC in China. It operates 78k cabinets in more than 20 cities throughout China, servicing a diversified base of 1,400+ IDC customers.

### Quarterly Results

Rmb '000	4Q20	1Q21	2Q21	3Q21	4Q21	y-o-y %chg	q-o-q %chg
<b>Total net revenues</b>	<b>1,348,367</b>	<b>1,386,923</b>	<b>1,496,978</b>	<b>1,560,460</b>	<b>1,745,440</b>	<b>29.4%</b>	<b>11.9%</b>
Total cost of revenues	(1,053,942)	(1,063,611)	(1,137,463)	(1,185,225)	(1,365,472)	29.6%	15.2%
Gross profit	294,425	323,312	359,515	375,235	379,968	29.1%	1.3%
Total operating expenses	(369,244)	(243,180)	(262,471)	(261,333)	(649,741)	76.0%	148.6%
<b>Operating (loss) profit</b>	<b>(74,819)</b>	<b>80,132</b>	<b>97,044</b>	<b>113,902</b>	<b>(269,773)</b>	<b>260.6%</b>	<b>-336.8%</b>
Interest income	4,176	5,709	8,103	9,148	8,937	114.0%	-2.3%
Interest expense	(79,243)	(84,479)	(87,095)	(88,013)	(75,363)	-4.9%	-14.4%
Other income and expenses	(817,829)	(43,737)	495,524	166,200	328,926	-140.2%	97.9%
(Loss) income before income taxes and gain (loss) from equity method investments	(967,715)	(42,375)	513,576	201,237	(7,273)	-99.2%	-103.6%
Income tax benefits (expenses)	(41,210)	(37,299)	(29,499)	(29,060)	(15,549)	-62.3%	-46.5%
Gain (loss) from equity method investments	15,194	(1,305)	(23,605)	(12,027)	(1,729)	-111.4%	-85.6%
Net (loss) profit	(993,731)	(80,979)	460,472	160,150	(24,542)	-97.5%	-115.3%
-Net loss (income) attributable to noncontrolling interest and redeemable noncontrolling interest	(21,647)	(3,680)	(4,620)	(3,967)	(2,736)	-87.4%	-31.0%
Net profit (loss) attributable to the Company's ordinary shareholders	(1,015,378)	(84,659)	455,852	156,183	(27,278)	-97.3%	-117.5%
Operating (loss) profit	(74,819)	80,132	97,044	113,902	(269,764)	260.6%	-336.8%
Plus: depreciation and amortisation	300,917	300,105	297,739	316,951	352,783	17.2%	11.3%
Plus: share-based compensation expenses	82,034	34,855	27,507	4,608	253,040	208.5%	5391.3%
Other adjustments	81,619	-	2,816	14,959	126,902	55.5%	748.3%
<b>Adjusted EBITDA</b>	<b>389,751</b>	<b>415,092</b>	<b>425,106</b>	<b>450,420</b>	<b>462,961</b>	<b>18.8%</b>	<b>2.8%</b>

Source: Company, DBS HK

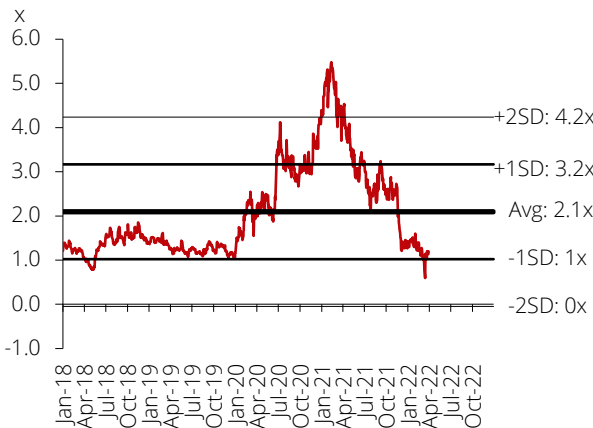
VNET Group Inc

Historical PE and PB band

Forward EV/adjusted EBITDA band (x)



PB band (x)



Source: Thomson Reuters, DBS HK

## VNET Group Inc

### Key Assumptions

FY Dec	2019A	2020A	2021A	2022F	2023F
IDC MRR per cabinet (Rmb /month /cabinet)	8,127.0	8,955.2	8,633.5	8,719.8	8,894.2
Total number of cabinets	36,291.0	53,553.0	78,540.0	94,440.0	114,440.0
Overall utilisation rate of cabinets (%)	66.0	60.4	61.6	60.0	60.6

Source: Company, DBS HK

### Segmental Breakdown (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
<b>Revenues (RMB m)</b>					
Revenue from IDC services	2,223	3,025	4,182	5,496	6,727
Revenue from cloud services & VPN services	1,566	1,804	2,008	2,108	2,214
<b>Total</b>	<b>3,789</b>	<b>4,829</b>	<b>6,190</b>	<b>7,605</b>	<b>8,941</b>

Source: Company, DBS HK

### Income Statement (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	3,789	4,829	6,190	7,605	8,941
Cost of Goods Sold	(2,850)	(3,753)	(4,752)	(5,856)	(6,884)
<b>Gross Profit</b>	<b>939</b>	<b>1,076</b>	<b>1,438</b>	<b>1,749</b>	<b>2,056</b>
Other Opng (Exp)/Inc	(757)	(959)	(1,417)	(1,392)	(1,591)
<b>Operating Profit</b>	<b>182</b>	<b>117</b>	<b>21</b>	<b>357</b>	<b>465</b>
Other Non Opng (Exp)/Inc	(67)	206	79	0	0
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(291)	(349)	(303)	(527)	(752)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	(2,544)	829	0	0
<b>Pre-tax Profit</b>	<b>(176)</b>	<b>(2,571)</b>	<b>627</b>	<b>(170)</b>	<b>(288)</b>
Tax	(5)	(109)	(111)	(125)	(150)
Minority Interest	(1)	(29)	(15)	(15)	(15)
Preference Dividend	0	(471)	0	0	0
<b>Net Profit</b>	<b>(182)</b>	<b>(3,180)</b>	<b>500</b>	<b>(310)</b>	<b>(453)</b>
Net Profit before Except.	(182)	(636)	(329)	(310)	(453)
EBITDA	954	1,106	1,289	1,922	2,380
<b>Growth</b>					
Revenue Gth (%)	11.4	27.4	28.2	22.9	17.6
EBITDA Gth (%)	9.4	15.8	16.6	49.1	23.8
Opg Profit Gth (%)	(23.3)	(36.0)	(81.7)	1,576.9	30.1
Net Profit Gth (%)	11.1	(1,644.4)	N/A	N/A	(46.1)
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	24.8	22.3	23.2	23.0	23.0
Opg Profit Margin (%)	4.8	2.4	0.3	4.7	5.2
Net Profit Margin (%)	(4.8)	(65.9)	8.1	(4.1)	(5.1)
ROAE (%)	(3.6)	(60.7)	7.8	(4.4)	(6.7)
ROA (%)	(1.4)	(18.9)	2.4	(1.2)	(1.6)
ROCE (%)	1.8	0.9	0.1	1.7	1.9
Div Payout Ratio (%)	N/A	N/A	0.0	N/A	N/A
Net Interest Cover (x)	0.6	0.3	0.1	0.7	0.6

Source: Company, DBS HK

**VNET Group Inc**
**Interim Income Statement (RMB m)**

<b>FY Dec</b>	<b>2H2019</b>	<b>1H2020</b>	<b>2H2020</b>	<b>1H2021</b>	<b>2H2021</b>
Revenue	2,029	2,235	2,594	2,884	3,306
Cost of Goods Sold	(1,559)	(1,728)	(2,025)	(2,201)	(2,551)
<b>Gross Profit</b>	<b>470</b>	<b>506</b>	<b>570</b>	<b>683</b>	<b>755</b>
Other Oper. (Exp)/Inc	(402)	(391)	(569)	(506)	(911)
<b>Operating Profit</b>	<b>69</b>	<b>116</b>	<b>1</b>	<b>177</b>	<b>(156)</b>
Other Non Opg (Exp)/Inc	(17)	(63)	269	11	68
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(155)	(184)	(165)	(158)	(145)
Exceptional Gain/(Loss)	0	(1,612)	(932)	415	414
<b>Pre-tax Profit</b>	<b>(103)</b>	<b>(1,743)</b>	<b>(828)</b>	<b>446</b>	<b>180</b>
Tax	15	(43)	(66)	(67)	(45)
Minority Interest	3	(5)	(24)	(8)	(7)
<b>Net Profit</b>	<b>(86)</b>	<b>(2,262)</b>	<b>(918)</b>	<b>371</b>	<b>129</b>
Net profit bef Except.	(86)	(650)	14	(44)	(285)
<b>Growth</b>					
Revenue Gth (%)	14.5	27.0	27.8	29.0	27.4
Opg Profit Gth (%)	(46.8)	2.0	(98.5)	53.3	(14,929.9)
Net Profit Gth (%)	40.2	(2,245.7)	(969.3)	N/A	N/A
<b>Margins</b>					
Gross Margins (%)	23.2	22.7	22.0	23.7	22.8
Opg Profit Margins (%)	3.4	5.2	0.0	6.1	(4.7)
Net Profit Margins (%)	(4.2)	(101.2)	(35.4)	12.9	3.9

Source: Company, DBS HK

## VNET Group Inc

**Balance Sheet (RMB m)**

FY Dec	2019A	2020A	2021A	2022F	2023F
Net Fixed Assets	5,444	8,106	10,092	13,352	15,502
Invt in Associates & JVs	0	0	0	0	0
Other LT Assets	3,532	5,076	7,670	7,710	7,764
Cash & ST Invt	2,721	3,402	1,708	2,011	1,984
Inventory	0	0	0	0	0
Debtors	657	847	1,406	1,979	2,327
Other Current Assets	1,920	1,942	2,218	2,320	2,428
<b>Total Assets</b>	<b>14,274</b>	<b>19,374</b>	<b>23,095</b>	<b>27,373</b>	<b>30,005</b>
ST Debt	1,178	2,158	384	384	384
Creditors	303	289	494	481	566
Other Current Liab	2,988	3,675	4,302	4,302	4,302
LT Debt	2,140	887	2,215	5,215	8,215
Other LT Liabilities	2,433	5,467	8,099	9,699	9,699
Shareholder's Equity	4,953	6,565	7,242	6,947	6,510
Minority Interests	279	333	359	344	329
<b>Total Cap. &amp; Liab.</b>	<b>14,274</b>	<b>19,374</b>	<b>23,095</b>	<b>27,373</b>	<b>30,005</b>
Non-Cash Wkg. Capital	(714)	(1,175)	(1,172)	(484)	(113)
Net Cash/(Debt)	(597)	357	(891)	(3,588)	(6,615)
Debtors Turn (avg days)	56.9	56.9	66.4	81.2	87.9
Creditors Turn (avg days)	60.9	39.1	41.0	41.5	38.5
Inventory Turn (avg days)	0.2	N/A	N/A	N/A	N/A
Asset Turnover (x)	0.3	0.3	0.3	0.3	0.3
Current Ratio (x)	1.2	1.0	1.0	1.2	1.3
Quick Ratio (x)	0.8	0.7	0.6	0.8	0.8
Net Debt/Equity (X)	0.1	CASH	0.1	0.5	1.0
Net Debt/Equity ex MI (X)	0.1	CASH	0.1	0.5	1.0
Capex to Debt (%)	39.1	82.2	105.2	82.5	47.9
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

**Cash Flow Statement (RMB m)**

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Profit	(176)	(2,571)	627	(170)	(288)
Dep. & Amort.	772	989	1,268	1,565	1,915
Tax Paid	(42)	(102)	(111)	(125)	(150)
Assoc. & JV Inc/(loss)	0	0	0	0	0
(Pft)/ Loss on disposal of FAs	(23)	6	0	0	0
Chg in Wkg.Cap.	(121)	(510)	33	(688)	(371)
Other Operating CF	392	2,902	(428)	(246)	0
<b>Net Operating CF</b>	<b>803</b>	<b>714</b>	<b>1,388</b>	<b>336</b>	<b>1,107</b>
Capital Exp.(net)	(1,297)	(2,502)	(2,734)	(4,619)	(4,119)
Other Invt.(net)	(115)	71	(757)	0	0
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(200)	(1,459)	(282)	0	0
<b>Net Investing CF</b>	<b>(1,612)</b>	<b>(3,889)</b>	<b>(3,773)</b>	<b>(4,619)</b>	<b>(4,119)</b>
Div Paid	0	0	0	0	0
Chg in Gross Debt	832	(554)	3,266	3,000	3,000
Capital Issues	(22)	(130)	(1,702)	0	0
Other Financing CF	(349)	4,848	(597)	1,585	(15)
<b>Net Financing CF</b>	<b>462</b>	<b>4,163</b>	<b>968</b>	<b>4,585</b>	<b>2,985</b>
Currency Adjustments	44	(229)	9	0	0
Chg in Cash	(304)	759	(1,408)	302	(27)
Opg CFPS (RMB)	8.29	10.24	9.39	5.92	7.43
Free CFPS (RMB)	(4.44)	(14.96)	(9.33)	(24.75)	(15.13)

Source: Company, DBS HK

**VNET Group Inc**

**Target Price & Ratings History**



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	26-May-21	US\$21.22	US\$47.50	Buy
2:	25-Aug-21	US\$18.20	US\$27.00	Buy
3:	19-Nov-21	US\$18.86	US\$27.00	Buy
4:	20-Jan-22	US\$9.31	US\$15.30	Buy

Source: DBS HK

Analyst: Tsz Wang Tam  
Harry Zhuang



DBS HK recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**FULLY VALUED** (negative total return, i.e., > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

\*Share price appreciation + dividends

Completed Date: 31 Mar 2022 14:20:38 (HKT)

Dissemination Date: 31 Mar 2022 15:02:25 (HKT)

Sources for all charts and tables are DBS HK unless otherwise specified.

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