



Rating
Sell

Asia
China

Technology
Software & Services

Company
**Wangsu
Technology**

Reuters 300017.SZ Bloomberg 300017 CS Exchange SHZ Ticker 300017

Date
29 August 2017

Forecast Change

Price at 28 Aug 2017 (CNY)	11.47
Price target - 12mth (CNY)	8.90
52-week range (CNY)	23.78 - 9.60
Shenzhen Index	2,026

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Turnaround not yet in sight

Sailing against the wind

While Wangsu's 1H17 result was broadly in line with its profit guidance, this was helped by an exceptionally low tax rate. The 2Q result suggests a worsening trend: revenue excluding the CDNetworks acquisition fell 5% QoQ, gross margin fell 3ppts QoQ and operating costs rose sharply such that gross operating profit fell 56% YoY. With the company continuing to be buffeted by competitive headwinds from large cloud operators, we see limited signs of a turnaround in the near term; retaining Sell.

Conference call feedback

Highlights of the results conference call held on 23 August included: 1) the July gross margin continued to slide but the trend improved slightly from 2Q; 2) the company seems to be shifting its focus to IDC businesses, which are lower in return and higher in capex intensity; 3) CDNetworks contributed RMB150m in revenue in 2Q and a 1ppt improvement in gross margin (hence worsening the underlying gross margin trend); and 4) the company believes that it is holding on to its market share (by volume), with bandwidth usage growing 30% YoY.

Potential upside scenarios?

While Wangsu's participation in China Unicom's mixed ownership is a confidence booster, operationally we see limited competitive benefits, given that its largest competitors are playing more important roles in the same reform process. M&A also offers potential upside, but with Wangsu still trading at 34x FY17E EPS, we believe that valuation is not sufficiently appealing as yet.

Earnings, valuation and risks

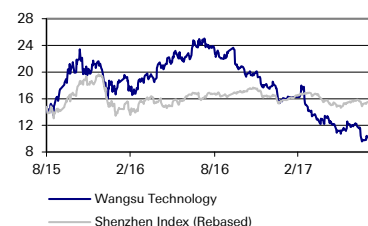
We reduced earnings forecasts by 16-20% to reflect the weak 1H17 underlying results and reduced our target price accordingly. We value Wangsu at the mid-point between our peer-based P/E valuation and DCF (WACC 7.5%, TGR 1%). Risks relate to market share, tax rate, regulation and margins (details on Pg 6).

Key changes

TP	10.20 to 8.90	↓	-12.7%
Sales (FYE)	5,095 to 5,201	↑	2.1%
Op prof margin (FYE)	18.5 to 13.7	↓	-25.8%
Net profit (FYE)	973.1 to 812.8	↓	-16.5%

Source: Deutsche Bank

Price/price relative



Performance (%)	1m	3m	12m
Absolute	12.3	2.8	-52.1
Shenzhen Index	3.7	7.0	-4.3

Source: Deutsche Bank

Forecasts And Ratios

Year End Dec 31	2015A	2016A	2017E	2018E	2019E
Sales (CNYm)	2,931.7	4,446.4	5,200.7	6,215.3	7,682.8
EBITDA (CNYm)	889.5	1,268.6	1,000.3	1,277.0	1,555.9
Reported NPAT (CNYm)	831.3	1,249.9	812.8	815.6	941.5
DB EPS FD(CNY)	1.16	1.60	0.34	0.34	0.39
% Change	0.0%	0.0%	-16.7%	-20.5%	-20.9%
DB EPS growth (%)	-22.1	38.0	-79.0	0.1	15.0
PER (x)	14.0	12.9	34.1	34.1	29.7
EV/EBITDA (x)	11.7	10.0	24.5	18.6	14.8
DPS (net) (CNY)	0.20	0.25	0.05	0.06	0.07
Yield (net) (%)	1.2	1.2	0.5	0.5	0.6

Source: Deutsche Bank estimates, company data

¹ DB EPS is fully diluted and excludes non-recurring items

² Multiples and yields calculations use average historical prices for past years and spot prices for current and future years, except P/B which uses



Model updated: 29 August 2017

Running the numbers

Asia

China

Software & Services

Wangsu Technology

Reuters: 300017.SZ

Bloomberg: 300017 CS

Sell

Price (28 Aug 17) CNY 11.47

Target Price CNY 8.90

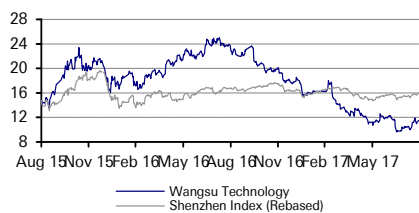
52 Week range CNY 9.60 - 23.78

Market Cap (m) CNYm 27,697
USDm 4,170

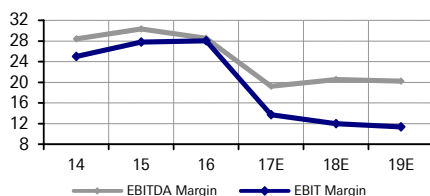
Company Profile

Wangsu is a leading CDN and internet service platform provider in China. It provides solutions including content distribution and acceleration, server hosting and rental, and network optimization solutions. It has a variety of enterprise customers ranging across industries such as media, gaming, e-commerce, internet portals, public sector and consumer brands.

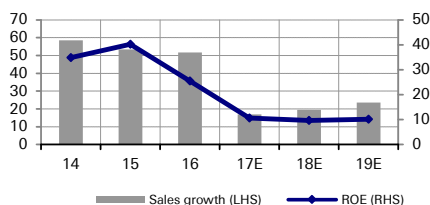
Price Performance



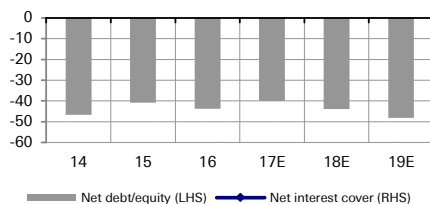
Margin Trends



Growth & Profitability



Solvency



Fiscal year end 31-Dec

Financial Summary

	2014	2015	2016	2017E	2018E	2019E
DB EPS (CNY)	1.49	1.16	1.60	0.34	0.34	0.39
Reported EPS (CNY)	1.49	1.16	1.60	0.34	0.34	0.39
DPS (CNY)	0.15	0.20	0.25	0.05	0.06	0.07
BVPS (CNY)	5.2	3.6	9.5	3.3	3.7	4.0
Weighted average shares (m)	314	700	773	2,415	2,420	2,430
Average market cap (CNYm)	2,548	11,401	15,919	27,697	27,697	27,697
Enterprise value (CNYm)	1,785	10,372	12,699	24,488	23,813	22,988

Valuation Metrics

P/E (DB) (x)	5.4	14.0	12.9	34.1	34.1	29.7
P/E (Reported) (x)	5.4	14.0	12.9	34.1	34.1	29.7
P/BV (x)	1.39	5.55	1.88	3.45	3.14	2.85
FCF Yield (%)	14.7	3.0	2.8	nm	3.2	3.8
Dividend Yield (%)	1.8	1.2	1.2	0.5	0.5	0.6
EV/Sales (x)	0.9	3.5	2.9	4.7	3.8	3.0
EV/EBITDA (x)	3.3	11.7	10.0	24.5	18.6	14.8
EV/EBIT (x)	3.7	12.7	10.2	34.3	31.9	26.3

Income Statement (CNYm)

Sales revenue	1,911	2,932	4,446	5,201	6,215	7,683
Gross profit	833	1,312	1,866	1,714	1,941	2,359
EBITDA	543	889	1,269	1,000	1,277	1,556
Depreciation	80	98	148	300	440	546
Amortisation	-15	-23	-126	-15	90	135
EBIT	477	815	1,247	715	747	874
Net interest income/(expense)	17	15	98	81	86	103
Associates/affiliates	0	2	2	2	2	2
Exceptionals/extraordinary	0	0	0	0	0	0
Other pre-tax income/(expense)	7	48	-19	42	38	51
Profit before tax	501	878	1,326	837	871	1,028
Income tax expense	18	49	78	26	57	88
Minorities	0	0	0	0	0	0
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	484	831	1,250	813	816	941
DB adjustments (including dilution)	0	0	0	0	0	0
DB Net profit	484	831	1,250	813	816	941

Cash Flow (CNYm)

Cash flow from operations	522	718	1,480	1,118	1,823	2,219
Net Capex	-147	-380	-1,029	-1,130	-932	-1,152
Free cash flow	375	338	451	-12	890	1,066
Equity raised/(bought back)	29	51	3,661	1	0	0
Dividends paid	-31	-48	-160	-205	-130	-139
Net inc/(dec) in borrowings	-4	556	261	218	0	0
Other investing/financing cash flows	-481	-693	-4,026	453	-86	-103
Net cash flow	-113	205	187	455	674	825
Change in working capital	0	0	0	0	0	0

Balance Sheet (CNYm)

Cash and other liquid assets	762	1,050	3,221	3,437	4,111	4,936
Tangible fixed assets	306	466	762	1,595	1,794	2,037
Goodwill/intangible assets	61	84	132	1,278	1,371	1,472
Associates/investments	0	15	36	36	36	36
Other assets	848	1,890	4,512	3,486	3,660	3,903
Total assets	1,978	3,506	8,663	9,831	10,972	12,384
Interest bearing debt	0	26	0	214	214	214
Other liabilities	342	966	1,306	1,542	1,872	2,346
Total liabilities	342	992	1,306	1,756	2,086	2,559
Shareholders' equity	1,636	2,503	7,320	8,025	8,836	9,774
Minorities	0	11	36	51	51	51
Total shareholders' equity	1,636	2,514	7,356	8,076	8,887	9,825
Net debt	-762	-1,025	-3,221	-3,223	-3,898	-4,722

Key Company Metrics

Sales growth (%)	58.6	53.4	51.7	17.0	19.5	23.6
DB EPS growth (%)	0.9	-22.1	38.0	-79.0	0.1	15.0
EBITDA Margin (%)	28.4	30.3	28.5	19.2	20.5	20.3
EBIT Margin (%)	25.0	27.8	28.0	13.7	12.0	11.4
Payout ratio (%)	9.7	16.8	15.5	16.0	17.0	18.0
ROE (%)	34.9	40.2	25.4	10.6	9.7	10.1
Capex/sales (%)	7.7	13.0	23.2	21.7	15.0	15.0
Capex/depreciation (x)	1.5	3.1	5.6	2.8	1.5	1.4
Net debt/equity (%)	-46.6	-40.8	-43.8	-39.9	-43.9	-48.1
Net interest cover (x)	nm	nm	nm	nm	nm	nm

Source: Company data, Deutsche Bank estimates

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Figure 1: Half yearly P&L summary

Wangsu Technology	300017.SZ	Analyst	James Wang +852 2203 6145	james-z.wang@db.com				
Capitalization Summary								
Share Price (\$)	11.47							
Target price (\$)	8.90	Shares o/s	2,410					
Upside	-22%	Mkt Cap (RMBm)	27,639					
Horizon	12 months	EV (RMBm)	25,699					
Rationale	DCF & SoTP							
Income Statement (Y.E. Dec) RMBm								
	2016	2017F	2018F	2019F	1H16	2H16	1H17	2H17F
Revenue	4,446	5,201	6,215	7,683	2,056	2,390	2,442	2,759
Change	51.7%	17.0%	19.5%	23.6%	66.2%	41.0%	18.8%	15.4%
of which: CDN	4,038	4,701	5,641	7,051	1,863	2,175	2,199	2,502
Change	58.9%	16.4%	20.0%	25.0%	76.0%	46.7%	18.1%	15.0%
Gross profit	1,866	1,714	1,941	2,359	897	970	831	883
Gross profit margin	42%	33%	31%	31%	44%	41%	34%	32%
Opex	(3,178)	(4,200)	(4,938)	(6,127)	(1,440)	(1,738)	(2,014)	(2,186)
Change	55.6%	32.2%	17.6%	24.1%	68.6%	46.2%	39.9%	25.8%
EBITDA	1,269	1,000	1,277	1,556	616	652	428	572
Change	42.6%	-21.2%	27.7%	21.8%	60.9%	28.8%	-30.6%	-12.3%
EBITDA margin	29%	19%	21%	20%	30%	27%	18%	21%
Other operating income	142	165	148	178	76	66	107	73
D&A	(183)	(408)	(640)	(808)	(81)	(102)	(154)	(254)
EBIT	1,228	757	785	925	612	617	381	391
Change	42%	-38%	4%	18%	72.3%	21.4%	-37.7%	-36.6%
EBIT margin	28%	15%	13%	12%	30%	26%	16%	14%
Net interest expense	98	81	86	103	13	85	38	42
Profit before tax	1,326	837	871	1,028	624	702	419	433
Tax	(78)	(26)	(57)	(88)	(39)	(39)	(4)	(22)
Tax rate	6%	3%	7%	9%	6%	5%	1%	5%
Profit after tax	1,248	811	814	940	585	663	415	411
Non-controlling interests	2	2	2	2	1	1	1	1
Net profit	1,250	813	816	941	586	665	416	412
Change	50%	-35%	0%	15%	81.8%	30.5%	-29.0%	-37.9%
EPS	1.60	0.34	0.34	0.39	0.77	0.83	0.17	0.17
DPS	0.25	0.05	0.06	0.07	0.00	0.25	0.00	0.05
Payout ratio	16%	16%	17%	18%				
Balance Sheet								
	2016	2017F	2018F	2019F				
Cash	5,656	4,356	5,030	5,855				
Gross debt	-	214	214	214				
Net debt	(5,656)	(4,142)	(4,817)	(5,641)				
Net debt to EBITDA	-4.5	-4.1	-3.8	-3.6				
Total assets	8,663	9,831	10,972	12,384				
Shareholders' equity	7,320	8,025	8,836	9,774				
Return Information								
	2016	2017F	2018F	2019F				
ROIC	17.1%	9.9%	9.0%	9.4%				
ROA	14.4%	8.3%	7.4%	7.6%				
ROTE	17.4%	12.0%	10.9%	11.3%				
ROE	17.1%	10.1%	9.2%	9.6%				
Capex/revenue	23%	22%	15%	15%				
Cashflow								
	2016	2017F	2018F	2019F				
Operating cash flow	1,480	1,118	1,823	2,219				
Capex	-1,029	-1,130	-932	-1,152				
Free cash flow (post capex)	451	-12	890	1,066				
FCF yield	4.9%	0.0%	3.2%	3.8%				
Valuation & Leverage Metrics								
	2016	2017F	2018F	2019F				
P/E	22.1	34.1	34.1	29.7				
FCF yield		0.0%	3.2%	3.8%				
DY		0.5%	0.5%	0.6%				
EV/EBITDA		23.5	18.0	14.3				
P/BV		3.45	3.15	2.86				
Payout ratio	16%	16%	17%	18%				
Net debt/equity	-77%	-52%	-55%	-58%				
Net debt/EBITDA	-4.5	-4.1	-3.8	-3.6				

Source: Deutsche Bank estimates, Company data



Earnings changes

We have made the following adjustments to our earnings forecasts:

- Reduced our gross margin forecasts to reflect continuing competitive pressure;
- Increased opex forecasts to reflect increases in personnel and sales and marketing expenses; and
- Increased D&A to reflect a higher-than-expected contribution from the CDNetworks acquisition.

Figure 2: Earnings changes

	Earnings (RMB m)			Diluted EPS (RMB)			DPS (RMB)		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
FY16	1,250	1,250	0.0%	1.60	1.60	0.0%	0.25	0.25	0.0%
FY17F	973	813	-16.5%	0.40	0.34	-16.7%	0.06	0.05	-16.6%
FY18F	1,023	816	-20.3%	0.42	0.34	-20.5%	0.07	0.06	-20.4%
FY19F	1,187	941	-20.7%	0.49	0.39	-20.9%	0.09	0.07	-20.8%

Source: Deutsche Bank estimates, Company Data

The key drivers are summarized below. The remainder of FY17 will continue to cycle high comparables, which could mean more headline shocks. We already allow for revenue growth to pick up in FY18 and FY19 to reflect growth from its international business (including contribution from the CDNetworks acquisition) and some improvement in the domestic business.

Figure 3: Key drivers

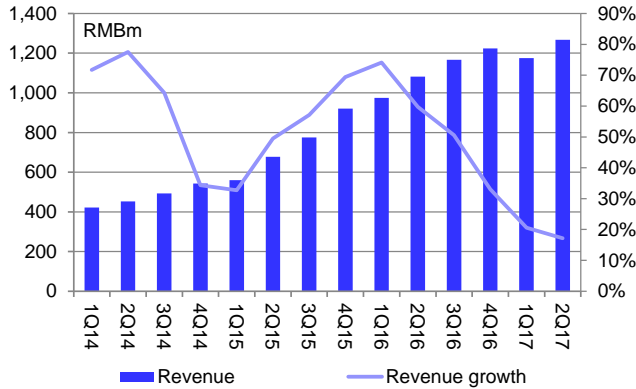
	FY16	1H17	2H17F	FY17F	FY18F	FY19F
Revenue						
CDN growth	59%	18%	15%	16%	20%	25%
Overall growth	52%	19%	15%	17%	20%	24%
Cost						
COGS growth	59%	39%	32%	35%	23%	25%
Opex growth	41%	44%	-2%	19%	-7%	21%
Gross margin	42%	34%	32%	33%	31%	31%
Opex as % of revenue	13%	17%	11%	14%	11%	10%
Profitability						
EBITDA growth	43%	-31%	-12%	-21%	28%	22%
EBITDA margin	29%	18%	21%	19%	21%	20%
Net profit growth	50%	-29%	-38%	-35%	0%	15%
Net profit margin	28%	17%	15%	16%	13%	12%
Balance sheet						
Capex as % of revenue	12%			43%	15%	15%
Free cash flow in RMBbn	451			-12	890	1,066
Returns						
DPS (RMB)	0.20			0.05	0.06	0.07
ROE	25.4%			10.6%	9.7%	10.1%

Source: Deutsche Bank estimates, Company Data



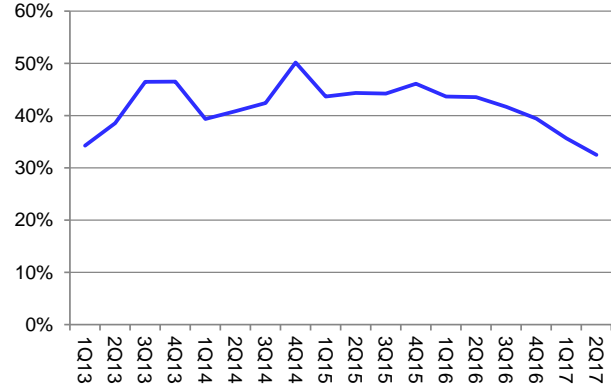
Quarterly trends

Figure 4: Revenue helped by CDNetworks acquisition



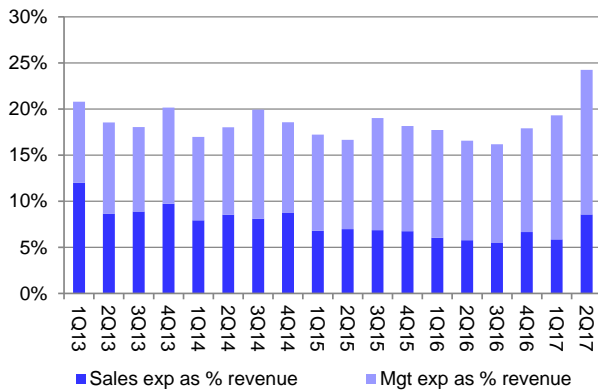
Source: Deutsche Bank, Company data

Figure 5: Gross profit margin still under pressure



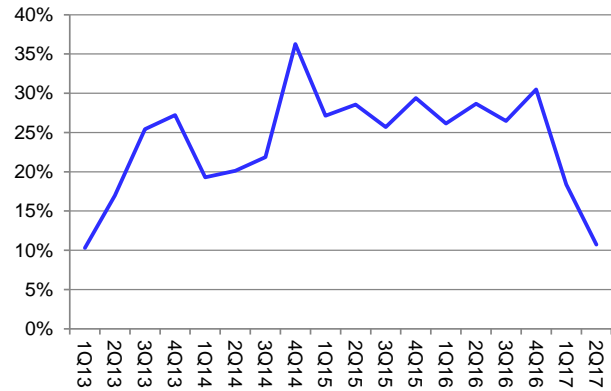
Source: Deutsche Bank, Company data

Figure 6: Sales and management expense trends



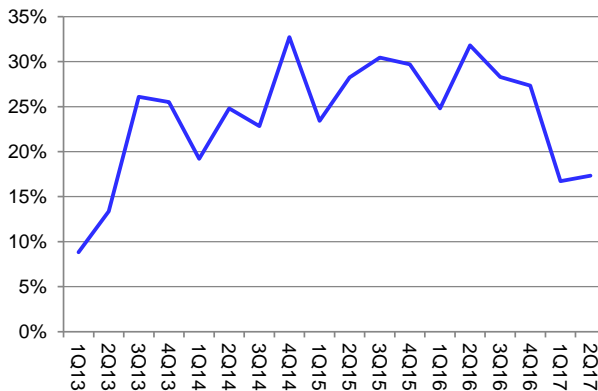
Source: Deutsche Bank, Company data

Figure 7: Operating profit margin



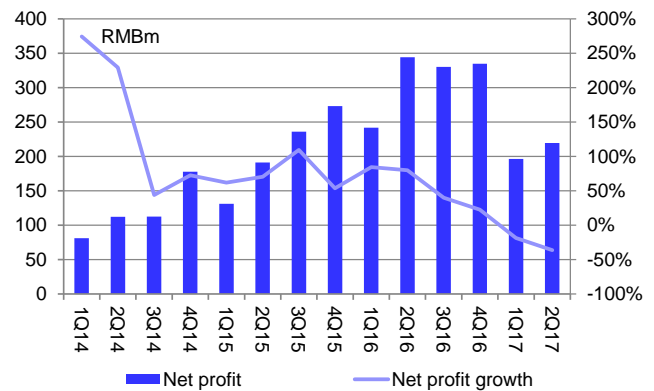
Source: Deutsche Bank, Company data

Figure 8: Net profit margin



Source: Deutsche Bank, Company data

Figure 9: Net profit growth



Source: Deutsche Bank, Company data



Valuation and risks

Reducing target price to RMB8.90

We have reduced our target price from RMB10.20 to RMB8.90, reflecting the weaker-than-expected 1H17 results.

Figure 10: Revised target price

(RMB)	Combined valuation	Implied FY17 PE
Peer-based P/E valuation	9.70	28.8
DCF valuation	8.00	23.9
Target price	8.90	26.3

Source: Deutsche Bank estimates, Company data

We value Wangsu at the mid-point between our DCF and peer-based P/E valuations. Our DCF valuation is RMB8/share, based on the assumptions in Figure 11. TGR is 1%, reflecting long-term share and margin erosion as a result of new entrants.

Figure 11: Key DCF assumptions

Debt %	10.0%
Equity %	90.0%
Cost of debt (after tax)	3.4%
Risk-free rate	3.0%
Beta	0.90
Risk premium	5.5%
Cost of equity	8.0%
WACC	7.5%
Terminal growth	1.0%

Source: Deutsche Bank estimates

Our peer-based P/E valuation is RMB9.70/share. We take the average of BAT's (Baidu, Alibaba and Tencent) FY17E PER as the base, discounted 20%, as we believe that, over the longer term, Wangsu's P/E should trade at a discount to BAT, which has stronger competitive "moats" than CDN operators (on par with Akamai's discount to large US internet companies).

Figure 12: Peer-based P/E valuation

	FY17 PE
Alibaba	33.8
Tencent	41.5
Baidu	32.5
Average	36.0
20% PER discount	7.2
Adopted multiple	28.8
Wangsu FY17 EPS forecast (RMB)	0.34
Value per share (RMB)	9.70

Source: Bloomberg Finance LP, Deutsche Bank estimates



Risks

Key upside risks:

- Improvement in competitive dynamics resulting in price stabilization;
- Better-than-expected market share gains;
- Significantly stronger-than-expected profit contribution from the cloud business; and
- Better-than-expected contributions from new acquisitions.



Appendix 1

Important Disclosures

*Other information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
Wangsu Technology	300017.SZ	11.47 (CNY) 28 Aug 17	NA

Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Other information is sourced from Deutsche Bank, subject companies, and other sources. For disclosures pertaining to recommendations or estimates made on securities other than the primary subject of this research, please see the most recently published company report or visit our global disclosure look-up page on our website at <http://gm.db.com/ger/disclosure/DisclosureDirectory.eqsr>. Aside from within this report, important conflict disclosures can also be found at <https://gm.db.com/equities> under the "Disclosures Lookup" and "Legal" tabs. Investors are strongly encouraged to review this information before investing.

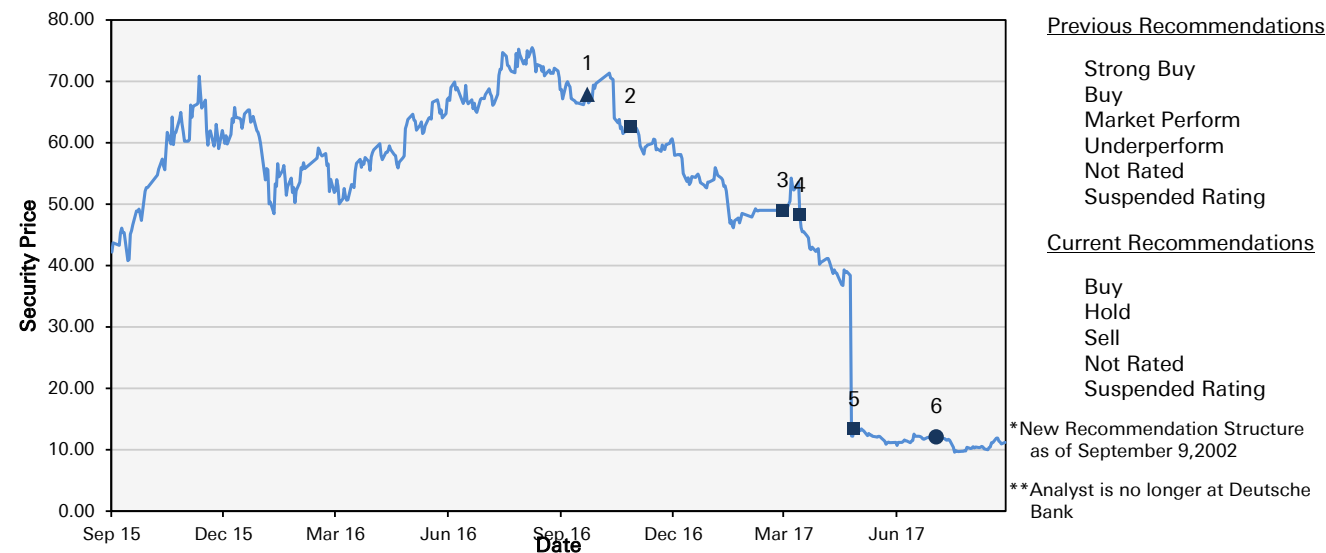
For disclosures pertaining to recommendations or estimates made on securities other than the primary subject of this research, please see the most recently published company report or visit our global disclosure look-up page on our website at <http://gm.db.com/ger/disclosure/Disclosure.eqsr?ricCode=300017.SZ>

Analyst Certification

The views expressed in this report accurately reflect the personal views of the undersigned lead analyst(s) about the subject issuer and the securities of the issuer. In addition, the undersigned lead analyst(s) has not and will not receive any compensation for providing a specific recommendation or view in this report. James Wang

Historical recommendations and target price: Wangsu Technology (300017.SZ)

(as of 8/28/2017)



1. 22/09/2016:	Upgrade to Hold, Target Price Change CNY70.00	4. 14/03/2017:	Hold, Target Price Change CNY45.00	James Wang
2. 27/10/2016:	Hold, Target Price Change CNY67.00	5. 27/04/2017:	Hold, Target Price Change CNY12.00	James Wang
3. 28/02/2017:	Hold, Target Price Change CNY57.00	6. 03/07/2017:	Downgrade to Sell, Target Price Change CNY10.20	James Wang



Equity rating key

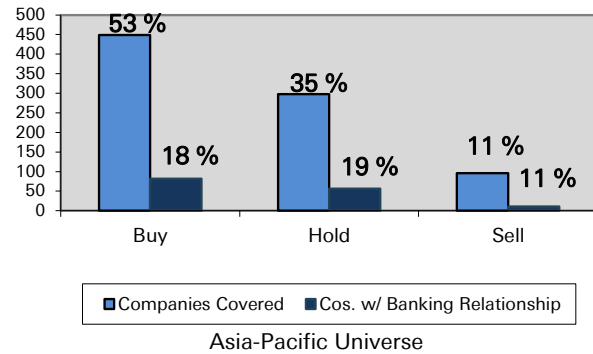
Buy: Based on a current 12-month view of total share-holder return (TSR = percentage change in share price from current price to projected target price plus projected dividend yield), we recommend that investors buy the stock.

Sell: Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock

Hold: We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.

Newly issued research recommendations and target prices supersede previously published research.

Equity rating dispersion and banking relationships



Asia-Pacific Universe



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