Client Id: 77

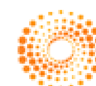
THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

GDS.O - Q2 2018 GDS Holdings Ltd Earnings Call

EVENT DATE/TIME: AUGUST 14, 2018 / 12:00PM GMT

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

CORPORATE PARTICIPANTS

Daniel Newman *GDS Holdings Limited - CFO*

Laura Chen

William Wei Huang *GDS Holdings Limited - Chairman & CEO*

CONFERENCE CALL PARTICIPANTS

Colby Alexander Synesael *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

Frank Garrett Louthan *Raymond James & Associates, Inc., Research Division - MD of Equity Research*

Gokul Hariharan *JP Morgan Chase & Co, Research Division - Head of Taiwan Equity Research and Senior Tech Analyst*

Jonathan Atkin *RBC Capital Markets, LLC, Research Division - MD and Senior Analyst*

Robert Ari Gutman *Guggenheim Securities, LLC, Research Division - Senior Analyst*

PRESENTATION

Operator

Hello, ladies and gentlemen. Thank you for standing by for GDS Holdings Limited Second Quarter 2018 Conference Call. (Operator Instructions) Today's conference call is being recorded. I will now turn the call over to your host, Ms. Laura Chen, Head of Investor Relations for the company. Please go ahead, Laura.

Laura Chen

Thank you. Hello, everyone. Welcome to 2Q '18 Earnings Conference Call of GDS Holdings Limited. The company's results were issued via Newswire services earlier today and are posted online. A summary presentation, which we will refer to during this conference call, can be viewed and downloaded from our IR website at investors.gds-services.com.

Leading today's call is Mr. William Huang, GDS Founder, Chairman and CEO, who will provide an overview of our business strategy and performance; Mr. Dan Newman, GDS CFO, will then review the financial and operating results.

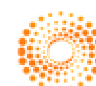
Before we continue, please note that today's discussion will contain forward-looking statements made under the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements involve inherent risks and uncertainties. As such, the company's results may be materially different from the views expressed today. Further information regarding these and other risks and uncertainties is included in the company's prospectus as filed with the U.S. SEC. The company does not assume any obligation to update any forward-looking statements, except as required under applicable law. Please also note that GDS earnings press release and this conference call include discussions of unaudited GAAP financial information as well as unaudited non-GAAP financial measures. GDS press release contains a reconciliation of the unaudited non-GAAP measures to the unaudited most directly comparable GAAP measures.

I will now turn the call over to GDS founder, Chairman and CEO, Mr. William Huang. Go ahead, William.

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Thank you, Laura. Hello, everyone. This is William. Thank you for joining us on today's call. 2Q '18 was a record quarter for GDS in terms of customer commitments, move-in, new projects and capital raising. Unfortunately, our outstanding performance has been overshadowed by the misinformed, if not invented, allegations published by a short seller who made no effort to contact us. Let me say again, these allegations are completely false.

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

During our call, in addition to walking you through our 2Q performance, we will respond to these false allegations throughout our commentary and put an end to this once and for all.

Now let's focus on our 2Q highlights. We achieved our highest ever level of new customer commitments at over 20,000 square meters. We achieved our highest average level of customer move-in, adding nearly 20,000 square meters to our revenue-generating area. Our total revenue grew by 89% and our adjusted EBITDA grew by 132% year-on-year. To keep up with demand, we initiated over 24,000 square meters of new projects, the largest ever in a single quarter. We successfully completed our largest ever capital raising, the $300 million convertible bond. In addition to what we achieved in China, it's great to see our strategic partners, CyrusOne and STT, winning significant new business from China's hyperscale customers in the U.S. and Singapore. While it benefited -- benefits them, it also benefits us in terms of strengthening our customer relationships.

Taking all of this together, our stronger revenue and EBITDA growth have put us ahead of expectations, leading to today's upward revision in our annual guidance.

Let me start with sales momentum on Slide 4. 2Q '18 was the third quarter in a row when our new commitments hit to the 20,000 square meter level. In the first half of 2018, we have done almost as much as we did in the whole of last year. Furthermore, as we look forward, our sales momentum is continuing and we target a similar level of new commitment in the second half of this year. How are we achieving this? To begin with, we are fortunate to operate in a market where the digital economy is booming. Demand for high-performance data centers capacity is accelerating, and it's challenging to generate new supply. It's obvious now that cloud adoption in China is taking off. The market leaders will report their result in the next few days, and we expect to see another quarter of hyper growth. The upside is huge.

The cloud market in China is still only 10% of the U.S. and less than 2% of the total IT spending.

China is at the forefront of AI technology. It's a major focus area for our largest customers, and it's already being deployed across their platforms. AI requires massive amounts of data to be collected, retaining -- retained and processed. AI-enabled applications are mission-critical and latency sensitive, driving demand for our high-performance data centers in Tier 1 market and close to users. China will be the forefront -- China will be at the forefront of 5G deployment next year. Our customers are gearing up in anticipation. 5G will result in a quantum increase in the amount of data created by devices and transmitted to data centers to feed real-time applications. AI plus 5G is a powerful combination.

The key to capturing this demand is to serve the right customers. Today, we have around an 80-20 split between cloud and the large Internet customers on the one hand, and financial services and the other large enterprise customers on the other. We believe that our cloud and the large Internet customers account for a very large part of total market demand. That's why 80% to 90% of our new business is coming from existing customers. We are getting follow-on orders from them quarter-after-quarter.

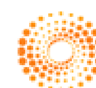
During this recent period, they have reached out to us to show their support and trust and also to give indication for new business going forward. Today, our top 2 customers are roughly equal in size, each accounting for around 30% of our total area committed. They have a presence in around 15 different GDS data centers. Beyond our top 2, we have significant sales pipeline from our other hyperscale customers, with great potential from players, such as Huawei and other global cloud player. We target adding to our base of highly strategic cloud and the large Internet customers.

In 2Q '18, we had a major breakthrough, winning our first order from NetEase, the fifth largest Chinese Internet company by market capitalization. In the second half of 2018, we expect to make several more breakthroughs with major Chinese and the U.S. customers.

Our strategy is to build the home of the cloud. We believe that the cloud POPs in our data centers will attract new enterprise customers and increase customers' stickiness. In 2Q '18, we, again, add about 25% year-on-year to our large enterprise customer count. We now have nearly 100 enterprise customers using our software-defined network or SDN hub to connect to major cloud platforms inside our data centers. Our customers remain firmly committed to data center outsourcing in Tier 1 markets and we are very confident that this trend will continue.

Technology developments are making our data centers more and more valuable. Our largest customers have high visibility for their future requirements. They are looking to us to fulfill them -- whenever and wherever. We realized some time ago that resource supply is a critical success factor. We stepped up our all sourcing efforts and, despite the challenges, I'm pleased to report significant progress in sourcing new projects.

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

Let's turn to Slide 5. We started this quarter with 40,000 square meters under construction. In 2Q '18, we initiated 24,000 square meters of new projects. Just as importantly, we brought the same amount of capacity into service on time and within budget. Since the end of 2Q '18, we have initiated another 16,000 square meters of new projects. As of today, we have about 56,000 square meters under construction. It's by far the largest development pipeline in the market and underpins our confidence in maintaining sales momentum.

Outside of Tier 1 markets, our largest customers locate part of their capacity in lower cost areas for data storage, machine learning and other applications, which are nonreal time or latency sensitive. This capacity complements the capacity we provided in Tier 1 markets. Historically, our customers have developed this kind of the remote data center themselves. However, we are starting to see a trend towards outsourcing. Last year, we committed to build 3 data centers on a campus in Hebei province for one of our largest customers. We completed these projects in less than 9 months and they are now all in service. You can see a photo on Slide 7.

We gained a lot of the experience from doing these projects and the outcome has been very successful for us. There are a lot of more opportunities like this, but they require a different approach to project management and financing. We are in ongoing discussions with various partners about innovative ways of addressing these opportunities.

Turning to Slide 7. We entered Hong Kong market over 3 years ago, relying on capacity in third-party data centers to provide service to a few of our largest Chinese financial institution customers. As you know, we have over 300 financial institution customers in China and most of them have a presence in Hong Kong. Our China cloud and the large Internet customers also use Hong Kong as launch point for their international services. It has long been our ambition to upgrade our presence in Hong Kong, but it's very difficult to secure suitable buildings and power supply. I'm, therefore, very excited to report that we have taken a significant first step to solving this problem with the acquisition of a site for redevelopment in Kwai Chung, Hong Kong's premier data center hub. Based on the plot ratio and our initial plan, we aim for around 7,000 square meters of high-quality resource. We are very confident of the demand which we can attract in Hong Kong and this project opens up a new avenue of growth. The site acquisition will close in a couple of months, and we will share more details with you in due course.

Beyond Hong Kong, we also see increasing demand in another emerging Tier 1 markets in China. We expect that by the end of 2018, we will enter at least one more new market. As our business has scaled up rapidly, we have successfully maintained a balance between customer commitments and capacity. Our commitment rate for area in service is now at a record high level of 95.6% and, despite the significant new projects initiated in the past few months, our pre-commitment rate is over 50%. We entered second half of the year with strong forward momentum, which reflects the company's unmatched ability to develop and operate high-performance data centers on behalf of the most demanding, cloud, Internet and enterprise customers in China. We have such an exciting opportunity in front of us and are so well positioned. We look forward to giving this our full attention.

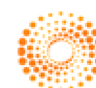
With that, I will hand over to Dan for the financial and operating review. Thank you.

Daniel Newman - *GDS Holdings Limited - CFO*

Thank you, William. Before I get into the numbers, I'd like to make some comments about our business model and how we add value. GDS develops and operates high-performance data centers. We begin by securing long-term tenure of entire buildings in shell state. We either build these shells ourselves, work with property partners who build for us or convert existing buildings. We invest in structural works and all the critical systems needed to turn the building into a data center. To give some idea of proportion, our investment is typically multiples of what the real estate alone would cost. We provide move-in ready data center capacity, configured to suit the needs of individual customers. Essentially, we have 2 types of customers: cloud and large Internet, who order in high volume and high-power density; and, large enterprises with small to medium order size, lower power density, but high redundancy. We operate the whole of every one of our self-developed data centers as a service for our customers.

Our customer contracts always specify numerous service-level parameters, which we commit to deliver. Our operating track record is as important to our customers as the quality of our facilities. Our customers install their IT equipment in our data centers, deal directly with the telecom carriers for connectivity and manage their own IT operations or, if they wish, outsource to us. For the avoidance of doubt, our customers do not operate any part of our data centers. Our customers are not tenants and our service contracts are not leases.

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

Getting back to 2Q '18 results. Starting on Slide 12, where we strip out the contribution from equipment sales and the effect of Forex changes. On a quarter-on-quarter basis, our service revenue grew by 13.6%, our underlying adjusted NOI grew by 15.9%, and our underlying adjusted EBITDA grew by 21.3%. Our underlying adjusted EBITDA margin increased by 2.3 percentage points to 35.3%.

Turning to Slide 13. The main driver of revenue growth in 2Q '18 was the 20,000 square meter increase in area utilized. We define area utilized as the net floor area of data centers in services, which is revenue generating, pursuant to customer agreements in effect. Area utilized is usually occupied by customers, but our ability to recognize revenue, bill and collect is not dependent on physical occupancy.

There have been some reports recently about short-term slowdown in server demand. I cannot comment on the validity of those reports. All I can say is that what we are seeing in terms of move-in by hyperscale customers is acceleration, across data centers in all our markets. Monthly service revenue or MSR per square meter in 2Q '18 was within the range which we have seen over multiple quarters. On a per square meter basis, selling prices are stable and, as the backlog is delivered, we expect MSR per square meter to stay within the established rate.

As shown on Slide 14, profit margins are on an upward trend. The growth drag at the adjusted NOI level which we saw in the past few quarters has now reversed, and we continue to realize operating leverage on the corporate cost base. As shown on Slide 15, our data center area in service is now 48% stabilized, 52% ramping up. The proportion which is stabilized is actually lower than in 1Q '18, mainly due to 3 new projects or phases of projects coming into service. However, the utilization rate of the ramping up portion is much higher at nearly 45% compared with 31% last quarter. The commitment rate is 98% for stabilized and 93% for ramping up. These are truly remarkable commitment rates by anyone's standards.

As an aside, please note that our Guangzhou 1, GZ1 data center is now 100% committed and 100% utilized. Almost 80% is taken by one of our largest customers.

At the corporate level, on Slide 16, SG&A is now down to 11.2% of service revenue. If we factor in full delivery of the backlog, the current level of SG&A represents around 6% to 7% of service revenue.

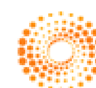
Turning to our CapEx on Slide 17. In 2Q '18, our CapEx paid increased to CNY 1.2 billion, including payments of CNY 231 million as front-end consideration for the equity of the Guangzhou 3 and Shanghai 11 acquired entities. The table of data centers under construction shows that we have around 36,000 square meters of capacity not yet committed. At our current sales run rate, its equivalent to around 2 quarters new customer commitments.

Turning to Slide 18. After completion of the convertible bond offering in June, our cash position has risen to nearly CNY 4.5 billion or $673 million. When we raise capital out of GDS Holdings, we receive proceeds in US dollars off-shore. We use these proceeds mainly to capitalize our data center projects companies onshore with equity. At the initiation of each new project, in our internal records, we allocate cash as the project equity. This ensures that we always have enough funds to capitalize our committed projects through to completion. Depending on the progress of projects and the requirement to fund CapEx, we inject cash into the project companies onshore and spend it. Cross-border cash transfers require various Chinese regulatory approvals and must have a specific qualifying purpose. We cannot transfer cash onshore for general purposes and leave it idle. We cannot convert it into renminbi without producing CapEx contracts and supplier invoices. Furthermore, once cash has been injected into project companies, it is not easy to move to our other onshore subsidiaries as a result of restrictions in our finance agreements and regulatory prohibitions or intra-group cash transfers.

Our effective interest cost on borrowings for 2Q '18 was 6.2%, excluding the CB. Our interest coverage based on adjusted EBITDA over reported interest was 1.7x, excluding capitalized interest cost or 1.4x including it. During 2Q '18, our net debt increased by CNY 4.6 billion to CNY 7.2 billion. CNY 1.3 billion of the increase was due to capital leases associated with the GZ3 acquisition and additional resources we secured in Beijing, some of which are categorized as held for future development.

Mainly as a result of these capital leases, our net debt to last quarter adjusted EBITDA ratio increased to 7.8x. Over time, we aim to bring our net debt-to-EBITDA ratio down to conventional levels. However, given our current rate of growth and scale of development, we feel that this metric does not give a good sense of our balance sheet strength. On the one hand, we have stabilized projects which are leveraged at less than 3x. On the other hand, we have incurred debt to finance projects which are ramping up or under construction with little or no EBITDA. Yet this debt is to

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

a large degree covered by customer contracts, a substantial majority with investment grade counterparties. Such customer contract tenors are longer than most of our loans and the total contract value is far in excess of the amount of outstanding loans. I'm often asked how much capacity we can develop with our existing financial resources.

On Slide 19, we show an illustrative indication. Assuming that we are able to leverage capital injected into projects 1:1 with project debt, we currently have sufficient capital to finance around CNY 9 billion, that's $1.4 billion of new investments. On the commitment side, the cost to complete all data centers currently in service and under construction is CNY 2.2 billion, $333 million. Adding to this the cost to complete projects initiated during the current quarter, the remaining amounts payable for acquisitions, including the maximum amount payable under contingent performance obligations and the cost of the Hong Kong site, we would require a grand total of CNY 5.5 billion, $830 million to complete every data center in service or under construction as of today.

The total capacity of such data center portfolio would be around 192,000 square meters. Based on this illustrative indication, we have potentially CNY 3.5 billion available for further new commitments.

Turning to Slide 20. We have an excellent track record in managing receivables. Day sales outstanding at 70 days is well up to the highest industry standards. We have not had a bad debt since 2015. In other words, we have collected 100% of what we have recognized as revenue in the past 3 years. Any company which recognizes revenue as service is rendered and bills in arrears, which is standard operation practice in ours and many sectors, will have unbilled receivables. Prime examples of companies, such as AT&T and PG&E. Unbilled receivables is not a mandatory disclosure under U.S. GAAP, but we have chosen to disclose it because it provides transparency to the length of our billing cycle. In the past few years, the proportion of our revenues coming from cloud and large Internet customers has increased significantly. We bill these customers quarterly in arrears. Nonetheless, we have managed to maintain an acceptable DSO. Over 80% of our unbilled receivables at the end of 2Q '18 relate to revenue recognized during the quarter. Unbilled receivables are easy to audit as they are tied to contracts in force and are part of a repeating quarterly billing cycle.

For days payable outstanding, we look at the OpEx cycle and the CapEx cycle. Both are reasonable. You can look at them on a combined basis if you prefer, but to exclude total CapEx purchases from the denominator as some have done, yields a completely meaningless ratio.

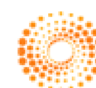
During the past quarter, we had 2 acquisitions which closed, Guangzhou 3 and Shanghai 11. I'd like to take this opportunity to provide some commentary on our acquisition strategy and the deals which we have done. Faced with strong demand from our customers, we started a few years ago to look for data centers which we could acquire to enhance our resource supply. As shown on Slide 21, between May 2016 and the present, we have completed 7 acquisitions. Two of them, Beijing 4 and Beijing 5, are categorized as acquisitions, but were really just a mechanism for acquiring new project companies with agreements in place relating to property and power capacity. Net of those 2, it's 5 acquisitions in the usual sense of the word.

We've been highly selective in the data centers which we have acquired. They must fit our profile in terms of asset quality and suitability for serving our target customer segments. We have also been very careful in the way that we structure the acquisitions, deferring as much consideration as possible and linking it to the achievement of project milestones. This is referred to as contingent performance obligations.

Out of the total equity consideration for the 5 real acquisitions of CNY 1.3 billion. CNY 752 million have been paid and CNY 506 million is contingent. We've involved legal advisers and financial advisers in due diligence. We have always bought 100%, paid in cash, and done so at single-digit multiples of projected stabilized cash EBITDA. The outcome has been highly successful. Every acquired data center has met or exceeded our expectations. For example, we were able to obtain additional power capacity and upsize the area of Shenzhen 5 by 53% post acquisition. Over 96% of the committed area of the acquired data centers is taken by our top 10 customers.

Our first acquisition was of the Guangzhou 1, GZ1 data center. As you can see on Slide 22, it is one of the 3 data centers, which we now own in the same location. We have acquired GZ1, GZ2 and GZ3 in 3 separate transactions, only moving forward when our acquisition criteria could be satisfied. It should not surprise you, given the integrated nature of the Guangzhou development that while each data center was owned by a different set of selling shareholders, the lead investor was the same. Based on our satisfactory experience of GZ1, we also acquired Shenzhen 5, SZ5 from a different set of shareholders with the same lead investor from the Guangzhou cluster.

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



Client Id: 77

If you examine the corporate records of the acquired companies for GZ1, GZ2, GZ3 and Shenzhen 5, you will find that prior to our acquisition, they share some directors contact details, et cetera, for the simple and obvious reason that they have the same lead investor. You will also find that at the time when we acquired these companies, we replaced the seller appointed directors and other personnel with our appointees at our earliest opportunity. I will illustrate this by going through the example of the Shenzhen 5, SZ5 acquisition on Slide 23.

Data center services is a restricted industry in China. It requires a value-added telecom service license. There is a foreign ownership restriction for licensees. In order to comply with this regulation, we have set up a group of PRC companies, which hold the relevant licenses and over which we had total control by contractual relationships known as variable interest entity or VIE. The structure has been very common in China for the past 20 years, and moreover, companies with several trillion dollars of market cap listed in the U.S. utilize this structure.

Optimally, for each data center project, we put the provision of services and commercial contracts into a license co, which is part of our VIE group, and the data center operating assets into an asset co that is under an intermediate holding company in Hong Kong. This ensures regulatory compliance and facilitates financing. It is not always possible. Sometimes the operating assets are in the license co, but wherever it is possible, this is the most efficient model and the one we use.

When we acquire projects, we sometimes find that they are already structured in this way. As you can see on Slides 23 and 24, this was the case with the SZ5, Guangzhou 2 and Guangzhou 3 acquisitions. In order to implement the acquisitions, we first took over the respective holding company in Hong Kong. In the case of Shenzhen 5, it is called RDTJ. RDTJ had a wholly owned PRC subsidiary, in essence, the asset co for Shenzhen 5. I will refer to this subsidiary as WGYL. The acquisition of RDTJ was completed on the 24th of May, 2017, as evidenced by the publicly available annual return filed with the Companies Registry, Hong Kong, which shows that we also replaced the seller appointed director on the same date.

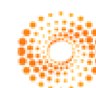
At that point in time, we had effective control over the entire SZ5 target group by virtue of ownership and contractual relationships. The second step in the transaction is the acquisition of the license co. In the case of SZ5, it is called Shenzhen Yaode. The acquirer, Beijing Wanguo is not a subsidiary of GDS. It is part of our VIE group. Due to the longer time required to complete change of company ownership in China, the Shenzhen Yaode acquisition completed on the 29th of June, 2017. We replaced it seller appointed directors and other representatives on the same date. On the prior day, we replaced the seller appointed directors and other representatives of WGYL. In China, it is a requirement to file with the State Administration for Industry and Commerce, or SAIC, for change of ownership, change of directors, et cetera. Accordingly, we filed with SAIC for the change of ownership and directors of Shenzhen Yaode and for the change of directors of WGYL. However, the change of ownership of WGYL was indirect and did not require an SAIC filing at that time.

In our 2016 20F, we referred to the pending acquisition of the data center in Shenzhen, i.e. Shenzhen 5 and specifically state that it involves agreements for the simultaneous acquisition of a Hong Kong company and a PRC company. In our 2017 20F, we referred to the acquisition of Shenzhen 5 and the acquisition of a target group, in other words, a group of companies, plural. In describing the financing arrangements in the 20F, we disclose the names of the 3 companies at the heart of the Shenzhen 5 transaction, RDTJ, WGYL and Shenzhen Yaode. Allegations have been made stating that the Shenzhen 5, Guangzhou 2 and Guangzhou 3 acquisitions were undisclosed related-party transactions. Given the facts that the acquired data centers had the same lead investor, the acquisitions involved a target group as disclosed in our SEC filings, WGYL was a central part of the Shenzhen 5 acquisition, SAIC filings for WGYL show its owner to be RDTJ, annual returns for RDTJ are publicly available in Hong Kong showing its change of ownership and directors, it is clear that the allegations are baseless.

By failing to accurately describe these facts, the short seller made, in our opinion, an egregious error. To compound this failing by making defamatory allegations of fraud and self-dealing, is in our view, totally unacceptable. We encourage our investors and the legitimate analysts who cover us to base their conclusions on objective facts and not on what we view to be obvious and self-interested distortions or misstatements of those facts.

Because we have always been 100% committed to transparency. I also want to address the transaction structures for the Guangzhou 2 and Guangzhou 3 transactions, which is shown on Slide 24. Once again, each acquisition involved a target group, 2 transactions: one onshore, one offshore, and the filings show that the seller appointed directors, et cetera were replaced by our representatives when the acquisitions completed. The composition of the GZ2 target group is disclosed in our 2017 20F. GZ3 was completed this year, and we've not yet filed our 2018 20F.

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

If you go back to Slide 21, where we show the equity consideration, it should be obvious by now that disclosure in an SAIC filing of consideration paid for the onshore acquisition does not include the consideration paid for the offshore acquisition. There is one more point, which I need to address. One of the prior shareholders of Guangzhou 2 made a disclosure required by domestic stock market regulations in China, which included references to the revenue and property and equipment of GZ2. The disclosed revenue under PRC GAAP did not include power income, which we are required to book as revenue under U.S. GAAP in our financial statements. The disclosed property and equipment under PRC GAAP did not include leases, which under U.S. GAAP, we are required capitalize in our financial statements. Once again, we believe that the mischaracterization of these facts reflects, at a minimum, obvious and elementary errors.

Turning to Slide 25. At the end of 2Q '18, our backlog had increased again slightly to nearly 57,000 square meters, which is equivalent to 65% of our area utilized at the same date. Finally, on Page 26, our 2Q '18 results clearly show that we are tracking ahead of expectations in terms of revenue and adjusted EBITDA growth. The accelerated move-in has brought forward new service revenue that we expected to commence later in the year. Given where we are today, we are raising our original guidance ranges for revenue and adjusted EBITDA by approximately 3%. This means that the bottom end of the new range is nearly in line with the high end of the original range.

We have also had accelerate CapEx and new project initiation in order to keep up with the sales demand. Accordingly, we are raising our CapEx guidance for the full year to around CNY 4 billion, just over $600 million. This includes CNY 662 million or USD 100 million, which we expect to pay for the Hong Kong site acquisition. In the future, we may sell and leaseback this site, but for now, it is included in our CapEx.

With that, I will end the formal part of my presentation. We'd now like to open the call to questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Frank Louthan from Raymond James.

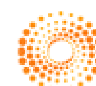
Frank Garrett Louthan - *Raymond James & Associates, Inc., Research Division - MD of Equity Research*

I appreciate all the additional disclosure. One quick question on sort of the quarter and the outlook and then a follow-up. Can you talk about the pricing with the new projects, what are we seeing there? Is there anything to do with the mix of hyperscale there? And then one other issue that's come up with some investors is some of the common phone numbers and so forth in some of the filings. I assume that just relates to the related parties, but are the -- the various, you're sharing the directors and so forth and just timing of when you made the acquisitions. Can you walk through why those show up in the filings and that would be great?

Daniel Newman - *GDS Holdings Limited - CFO*

There are a couple I'll address. Thank you for thanking us for the additional disclosures, but I would actually point out that almost my entire explanation was based on what is already publicly available either in our SEC filings, SAIC filings or Hong Kong Companies Registry. It's just a question of looking at it carefully and coming to the correct conclusions. As regards to the common phone numbers, what I was saying is that in effect, we did 2 acquisitions. One was of a cluster of 3 data centers in Guangzhou and the other one was a very large data center in Shenzhen 5. So those 2 acquisitions had the same lead investor, and in fact, each one, the other shareholders were a different group. So the presence of a lead investor, who in effect is the lead developer or promoter of those projects, meant that the directors and other representatives of those companies were the same because they're all part of the lead investor's team. What I hope I made clear in my explanation is that if you look at those filings, you will find that in every single case as soon as we completed the acquisition of these target companies, we replaced all of the lead investor's appointed directors and other personnel with our own appointees. It's simple. William, do you want to talk about pricing?

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Yes. I mean, to talk about the pricing, we didn't see any change compared with the last couple of quarters. As we've mentioned again and again, in the Tier 1 markets where we are, demand and supply -- there's still a gap. So the price dynamic still didn't change a lot. So, I think that we can keep this pricing level in the next couple of quarters.

Frank Garrett Louthan - *Raymond James & Associates, Inc., Research Division - MD of Equity Research*

Okay. Great. And if we look out a year, what we'll -- what do you expect the customer concentration to look like based on your current backlog? And can you comment on any successes you've had with the partnership with CyrusOne as far as being able to get to new logos?

Daniel Newman - *GDS Holdings Limited - CFO*

Okay, Frank, on the customer concentration, we don't set any limits. We don't have any quota for customers. We have established a group of very strategic customers. We think having the relations we have is absolutely key. I don't know how you can build a successful franchise in this business without those relationships. We started off with the very top 3, 4, 5, 6 names. We identified, at least, another 10 or even 20 names who we considered to be highly strategic, either because of the scale or because of the kind of data which they have, and the ecosystems which revolve around that. It takes time to break through to these accounts. But we're doing it gradually. Last year, we added Ctrip. First half of this year, we've added NetEase. I think it's fairly obvious to people who know the China cloud and Internet landscape who the next set of targets that we target are. I think if we're successful in doing that the customer concentration will diminish, but that's not to say that we have an issue with it.

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Yes, agreed.

Daniel Newman - *GDS Holdings Limited - CFO*

CyrusOne he asked about.

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

CyrusOne, I mean, sorry, what's the question?

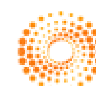
Daniel Newman - *GDS Holdings Limited - CFO*

What we benefit (multiple speakers).

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Yes. And first of all, we take the revenue from the -- take the margin from the CyrusOne referred deal from China to U.S. and also to our Singapore business partner, STT. So this is number one. Number two is I think with CyrusOne, we are working on couple of deals. I think we are very close to close that deal soon, which is based on the U.S. The momentum is happening right now. This is a long-term relationship. We just started. We think it is a great cooperation and teamwork when working with the 2 sides and the larger customers.

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

Operator

Our next question comes from the line of Robert Gutman from Guggenheim Partners.

Robert Ari Gutman - *Guggenheim Securities, LLC, Research Division - Senior Analyst*

And again, thank you for the thoughtful update and information addressing all those accusations. Could you tell us the sqm and use added of almost 20,000 in the quarter was a big number. Can you just review the composition of that by facility? And secondly, in the context of accelerating pace of CapEx and demand, can you just talk about your forward views on the balance sheet and on net leverage?

Daniel Newman - *GDS Holdings Limited - CFO*

Yes. Robert, it's Dan here. First of all, let me say I'm sorry that you got dragged into this short attack. I guess, you know more about Chinese regulations than you probably wanted to now. Well, I think you certainly know more than somebody I know. Yes. The 20,000 square meter net add was tremendous, and it's something that started in the first quarter and I commented on before, and it's carried on. And it's actually across multiple facilities. You can look at the individual data centers disclosures and you'll see this everywhere. And we brought a lot of capacity into service in the fourth quarter of last year and in the first quarter of this year. And so the momentum of move-in of that capacity has really started to accelerate. In addition, those 3 data centers, which we built in Hebei, built to suit for a particular customer, that customer has started to deploy very rapidly in those data centers. So I think, it's really a combination of those factors. Yes, on the balance sheet, I think, you want me to add, right. I gave that illustration. First of all, we have got to look at it in terms of what is our capacity, what financial resources do we have to invest. I gave those numbers during the prepared remarks. You're asking specifically about the net debt-to-EBITDA multiple. I think around the current level is more or less, as high as it will go. I said more or less, but with the caveat of what I said on in the prepared remarks, which is the comment that the metric only has limited meaning. We have a lot of data centers, which are under construction and ramping up, which are 100%, or near 100%, contracted to investment grade customers: quite often with 8- to 10-year contracts, quite often with no right of early termination. The cash flow from those contracts, net of the CapEx and OpEx, is still far in excess of the amount of debt.

Operator

Our next question comes from the line of Jonathan Atkin from RBC.

Jonathan Atkin - *RBC Capital Markets, LLC, Research Division - MD and Senior Analyst*

So I was interested in the Hong Kong acquisition and the expectation that you would have as to when power might be available to that site?

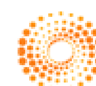
Daniel Newman - *GDS Holdings Limited - CFO*

Jon, I think, we've just entered into a -- what you call a provisional sale and purchase agreement for the site. And we would -- we make a disclosure today because its material. But we would prefer to wait until probably, late September early October when the acquisition closes and then we will make more detailed disclosure about the projects. Do you have another question?

Jonathan Atkin - *RBC Capital Markets, LLC, Research Division - MD and Senior Analyst*

So I was interested also in just the level of -- you mean, you talked about -- William talked about supply and demand that there is still a gap, and as you look at the data center development going on in China, obviously, by yourself you raised the CapEx guidance, but I'm just interested in most of the other development happening from independent developers or the public companies. Can you maybe talk a little bit about who else is developing capacity to meet that need?

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Yes, Jon, as we've always talked, first of all, in the different markets we have different competitors, and the data center is hot right now in China. A lot of the new project players and new capital is jumping into the market. But I think in terms of the competition, GDS is already in a very good position, no matter if it is from the reputation point of view from our customer, stickiness point of view and also our operational excellence point of view. So we're not afraid of any competition. But on the other hand, we are targeting the Tier 1 markets. Now we are sitting on around a 35% to 40% market share. We are not here to say that we want to have the 100% market. So this gives a lot of market space to leave to the other players.

Daniel Newman - *GDS Holdings Limited - CFO*

Sorry, Jon, something just occurred to me about the question you asked before. One of the reasons why power is difficult to obtain in Hong Kong is because most of the substations are at capacity -- full capacity or near to full capacity. One solution to that is to build your own substation. The problem is there are very few existing buildings you can find, which are suitable for putting a power substation inside. But the site that we are acquiring is a site where there's an existing 50-year old building, which we will pull down. And so we will build a new building on that site and incorporate into our plan a substation in that building. That will be something which is not available, or is not an option, I think, in 99.9% of existing industrial buildings.

Jonathan Atkin - *RBC Capital Markets, LLC, Research Division - MD and Senior Analyst*

That's a good point. And then lastly, in terms of expansions, are there anything -- are there any thoughts being given to additional remote hub markets besides the one in Hebei province? And then you mentioned in the script that you would be entering one additional Tier 1 market. What are the types of criteria that you look at and you'll evaluate opening up a new Tier 1 presence?

Daniel Newman - *GDS Holdings Limited - CFO*

Yes. For the remote projects, when you say evaluate, so it's really -- it's built to suit, so it's all about the counterparty. It's all about how the contract is structured and the economics. Yes, we are talking to 3 big customers about remote projects. If we can get the project management and the financing right, it is potentially, a large opportunity. It's there for the taking. That's why we are investing in quite a lot of time and effort to try to get the approach right.

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Yes, but Jon, I would like to add my opinion. We will still stay with our strategy, targeting the Tier 1 markets. We are trying to focus on solving the supply issue in the future, because we see that the next couple of years, the demand is tremendous. So we are still working on how to solve the hyperscale demand in the Tier 1 market. In the meanwhile, obviously, the remote market is a new market, and we already have some experience working on that. For us, it's nice to have, but not a must have. We will try to find some smart and very innovative way to achieve the capital to serve this kind of demand.

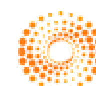
Operator

Our next question comes from the line of Colby Synesael from Cowen.

Colby Alexander Synesael - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

Just a follow-up on that last question regarding expansion in new markets. You mentioned on your prepared remarks, you're expecting to add or enter at least one new market, I think, by year-end. How many markets do you think that you could enter over time within China, just to kind of

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

give us a sense? And what is the velocity you would intend to expand into new markets perhaps over the next few years? Second question, there's obviously, a lot of talk in the news about trade wars, particularly between China and the U.S. Does that you think create risk that some of the U.S.-based cloud companies may not deploy in China as quickly as what we've seen maybe in the last year? And then, I guess, vice versa, perhaps more from a CyrusOne perspective. Is there a risk there that some of these domestic Chinese cloud companies don't actually deploy in the U.S. as quickly as perhaps we're all thinking right now?

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Okay. To answer a couple of questions. First of all, it's a new market, right? Our strategy is to follow our customers; that's our strategy. Once customers require us to get into some new market, we will see the market, is it sizable and is it strategic for GDS. So now what we are seeing is that there are a couple of the new markets are getting more mature and qualified for GDS to get into. That's why I say in our pipeline, we are keep watching a couple of cities, which may include Chongqing, include Wuhan, include other cities. We are seriously seeking some opportunity to get into at least one more market in China. This is the first question.

Daniel Newman - *GDS Holdings Limited - CFO*

Yes. Colby asked how many? How fast?

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

How many and how fast. I think this year we would target at least one.

Daniel Newman - *GDS Holdings Limited - CFO*

Next year?

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Yes. Maybe next year, let's see, we will add one more, maybe. But I would emphasize that our strategy is to keep our leading position in our existing market, and get more market share in our existing market. On the other hand, we are very seriously and carefully watching what's the next one in China. So after a couple of years evaluation, we will make some decisions soon.

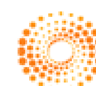
Colby Alexander Synesael - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

And then I had the other question with the trade wars?

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Trade war, yes. First of all, GDS is focused on the domestic customer, this is number one. In our total area commitment, I think our backlog, I think 90% is generated by the local domestic customer; only 10% is multinational. And there's another 100% from U.S., and we have the customer from Japan. We have the customer from Europe. So it's quite diversified. This is number one. The second one is, I mean, the trade war is more effective to the traditional industry like manufacturing, like other export and import, this kind of business. So it's not [affected] high-tech Internet and cloud business in China. On the other hand, I think, what we're seeing is recently, is very active topic is Facebook and Google are getting into China. In China, the [central] media, last week just -- in [China type of] tweets said, welcoming Facebook and Google. This looks like it's quite open for U.S.-based cloud players getting into China. On the other hand, we see that the China government has already announced to open the market for the financial institutions. Please remember, GDS has almost 300 financial institution. So this is very, very good news for us. If more and more foreign

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

financial players get into China, I think that GDS, obviously, will be the #1 choice for them. So in this view, I think, trade war doesn't impact all our business. In some way, maybe it's good for us.

Operator

Our next question comes from the line of Gokul Hariharan from JPMorgan.

Gokul Hariharan - *JP Morgan Chase & Co, Research Division - Head of Taiwan Equity Research and Senior Tech Analyst*

I think one question. First of all, thanks a lot for putting all those data together and the clarifications. First question, could you talk a little bit about when the Hebei project for one of the largest customers comes online, it looks like it's coming online in fact quickly. Could you talk a little bit about how it affects the average selling price, and how does it affect your EBITDA conversion, et cetera, given that the -- that seems to be something that will be ramping up in a very quick fashion over the next 12 to 18 months? That's first question. Second, could you talk a little bit about what does mean the kind of -- you did talk about some market share dynamics of 35% to 40% in Tier 1 markets. Could you talk a little bit about for your biggest 2 customers, how has been the decision points in terms of self-build versus outsourced? As well as, I think, traditionally they've also used a fair number of telco carriers' data centers also. How has that dynamic been changing over the last year or so, now that you are signing even bigger size deals with your top 2 customers?

Daniel Newman - *GDS Holdings Limited - CFO*

Okay. Gokul, I'll answer the question of Hebei. William, you answer about decision-making and relationship with the top 2 customers. So yes, Gokul, the first of the 3 data centers in Hebei came into service in April. And then the second and third came into service just the beginning of July. So that's why we say they're all in service now. And then you're asking about how it impacts our financial metric. It does have an impact, but because it's just 15,000 square meters, it's just over 10% of our total capacity. And unless we do a lot more of these projects, my approach was just to let it be part of the blended average. It does have a slight drag effect on our revenue per square meter. On the other hand, it's quite high margin. I don't want to get into disclosing remote projects as a separate data center category. I think that just overcomplicates things for now. William?

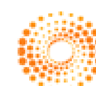
William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Yes, about the customer relationship. Number one, I think the GDS strategy is to build the home of the cloud. That's our strategy. Because we believe the cloud is the leading driver to drive the next 5 or even 10 years growth. So we have already started to build relationships with our customers for a couple of years. So now I think as everybody knows, we announced we are the preferred data center vendor to our 2 largest customers. We're working very closely with their tech team, network team, procurement team and even business team. We shared our resource plan. We also shared their 3-year rolling forecast demand. So we are working very close with all their demand forecasts. So this is our advantage. On the other hand, our tech team is very close with their design and architecture team as well. So we also take another advantage to know their technology trend. So this our big advantage compared with other competitors.

Gokul Hariharan - *JP Morgan Chase & Co, Research Division - Head of Taiwan Equity Research and Senior Tech Analyst*

Okay. And William could you talk a little bit about, I think, you mentioned that even some of the remote projects are moving from self-build to outsourced. Could you talk about what you are seeing in terms of visibility, especially for the larger customers who used to be a lot more self-built in some of these remote locations as well? Is that something that is consistent across most of the customers that you talk to?

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.



THOMSON REUTERS

Client Id: 77

William Wei Huang - *GDS Holdings Limited - Chairman & CEO*

Yes, our target, our strategy is the Tier 1 market, right? In Tier 1 market, I can confidently say that they are 100% outsourcing, no change. This is number one. Remote sites originally they built by themselves, but from what we see in the last 2 years, the trend is changing to 100% outsourcing. We cannot tell what the trend will be like after the next couple of years. But I still believe that their major business is to grow their main business. Data center is not their core competence. In this way, I think outsourcing still will be their key strategy.

Operator

As there are no further questions, I'd like to now turn the call back over to the company for closing remarks.

Laura Chen

Thank you, all, once again for joining us today. If you have further questions, please feel free to contact GDS Investor Relations through the contact information on our website or the Piacente Group Investor Relations. Thank you.

Operator

This concludes this conference call. You may now disconnect your line. Thank you.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2018, Thomson Reuters. All Rights Reserved.

©2018 Thomson Reuters. All rights reserved. Republication or redistribution of Thomson Reuters content, including by framing or similar means, is prohibited without the prior written consent of Thomson Reuters. 'Thomson Reuters' and the Thomson Reuters logo are registered trademarks of Thomson Reuters and its affiliated companies.

THOMSON REUTERS