REPORT REPRINT

Datacenter equipment maker Vertiv discovers its mojo as a stand-alone company

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After separating from Emerson Electric three years ago, Vertiv has remade itself and says it has been taking more share in a challenging but expanding datacenter market. Vertiv is positioned to be one of the successful consolidators if it can keep its product portfolio up to speed with technology shifts.

Introduction

In its third year as a stand-alone private enterprise, global datacenter equipment maker Vertiv (formerly Emerson Network Power) has remade itself for a datacenter market that demands a lean cost structure and rewards speed. It had found these characteristics difficult before the spinoff and they ultimately contributed to its divestiture by former parent Emerson Electric. In stark contrast to the more cloudy projections just a few years ago, the company is now gearing up to take advantage of its broad portfolio and global footprint to take more share in a challenging but expanding datacenter market.

451 TAKE

For a sector that is notorious for its glacial pace, the view of the datacenter landscape has changed dramatically in the space of a few years. Vertiv has gone through major restructurings to adapt and 451 Research believes the company is in better shape to succeed in this new faster-moving environment. Not only was the organization facing difficult organizational choices at the middle of the decade, but also a deteriorating business environment in which the future looked bleak for a global maker of datacenter equipment. It now looks like the opposite: as demand concentrates in the hands of a few hyperscale and international multi-tenant operators, so should more supply consolidate around major vendors over time as pressure to scale and drive costs out of the supply chain builds up. We think Vertiv successfully adjusted to this new era and is positioned to be one of the successful consolidators if it can keep its product portfolio up to speed with technology shifts.

Context

Vertiv is one of the largest vendors in the datacenter technologies segment, rivaled only by Schneider Electric. 451 Research estimates Vertiv's revenue for 2018 to be in the region of $4-4.2bn, which represents a growth of about 15% as a result of acquisitions coupled with strong organic performance. It leads the market for datacenter critical cooling and is also very strong in electrical equipment and datacenter services. It has about 19,500 employees, a large installed customer base globally, several strong brands, some 30 manufacturing facilities worldwide and entrenched supply-chain partners. Historically, about 60% of its business has been from datacenters, with telecommunications and industrial markets contributing about 20% each.

The company's headquarters are in Columbus, Ohio, and its owner is private equity firm Platinum Equity, which acquired Vertiv from Emerson Electric in an all-cash transaction valued at $4bn in late 2016. At Vertiv's helm is CEO Rob Johnson, formerly with Kleiner Perkins Caufield & Byers. Johnson also previously led APC, which Vertiv competitor Schneider Electric acquired for $6.1bn in 2006.

Vertiv has responded to the ongoing shift in capacity from enterprise-owned facilities to multi-tenant sites and cloud datacenters with two acquisitions: power distribution maker Geist and custom cooling specialist Energy Labs at the beginning of 2018. Platinum sold the automatic transfer switch unit ASCO, a highly profitable but niche specialty the new owners viewed as peripheral to the company's success in datacenters, to Schneider Electric, partly to finance investments in core areas.

Channeling speed and efficiency

Under private ownership, Vertiv has restructured to become leaner and nimbler via improved engineering and marketing coordination between regions. It has also improved margins via manufacturing efficiencies that had been trailing behind those of some rivals. Redundant engineering efforts hurt profits, slowed product development and made what was then Emerson Network Power look fragmented in the eyes of global operators, which had come to command a growing share of total market spending and to demand global standards from suppliers. These factors proved decisive in Emerson Electric's decision to spin off the business unit.

Some two years later, Vertiv has transformed under the new leadership installed by Platinum Equity. The company says almost all of its products are now globalized, which means research and development is owned and centralized by respective centers of excellence, with only final configuration and localization taking place in other regions. This is no easy task for any organization of Vertiv's size, but the company's fresh management team has demonstrated it is capable of reinvigorating the organization, taking on entrenched interests and resistance to change in order to improve margins and align the organization with market reality.

The Geist acquisition is a case in point. Vertiv snapped up Geist, a privately held maker of made-to-measure rack power distribution units (PDU), in early 2018 in a bid to buy a seat at the table with hyperscale and global datacenter operators. Geist's annual turnover was about $60-70m at the time, according to 451 Research's estimates, a drop in Vertiv's multi-billion-dollar bucket. Yet Vertiv has quickly established Geist as the internal standard for its rack PDU business; it has created a number of ready-made models from Geist's design library, which are then produced across Vertiv's manufacturing footprint for all markets.

Energy Labs, an operation of 900 people with annual revenue in the region of $100m at the time of the transaction, has also been integrated into Vertiv's much larger organization and acts as a center of excellence for large direct and indirect commercial and industrial air handlers, and some prefabricated modular datacenter projects for major US buyers. Like Geist, Energy Labs has honed an engineering and manufacturing operation that handles customization requests efficiently, which sits well with hyperscale and global datacenter operators that prefer to dictate specifications. Vertiv has brought Energy Labs designs to its European manufacturing and does localization for Asian markets.

Another major change to Vertiv's setup is in its relationship with the channel. Vertiv has traditionally been less engaged with resellers than Schneider Electric's datacenter business (owner of the APC brand) and did not enjoy the same reach. This is changing, with more of Vertiv's portfolio and business shifting toward the channel over time. In its campaign to sign up new reseller partners, Vertiv focuses on ease of doing business (also supported by standardized online product configurators), healthy margins and the fact that the market is not yet saturated with its products, which means partners will likely find there is a lower chance of competitive bids from another Vertiv reseller.

Outlook

With a leaner structure and snappier decision-making, Vertiv finds itself in a more favorable market environment compared with the time of its divestiture. By the middle of the decade it has become clear that hyperscale cloud operators would inevitably dictate market trends and absorb a growing share of datacenter capacity. What was not clear, a source of considerable anxiety, is what exactly this would do to overall demand and its composition, and how to participate in the hyperscale segment while maintaining margins. These concerns were not unfounded, as highlighted by the withdrawal of Swedish cooling specialist Munters from Europe, a vendor considered successful with some hyperscale operators but at the expense of margins.

However, the worst fears have not come to pass, to the relief of Vertiv and the wider datacenter industry. On balance, hyperscalers appear to add more net new capacity than they displace in the form of enterprise facilities. Hyperscalers' appetite for more capacity fuels the growth in multi-tenant datacenters, which in turn also attracts various service providers (smaller cloud players, hosting, managed services, content distribution and media, gaming) and ultimately enterprises too. Also, enterprises still spend good money on upgrading and refurbishing their core sites precisely because there is a mandate to consolidate footprint and decommission outdated or lower-quality locations – this segment is where Vertiv's traditional business has been strong. In emerging markets, enterprises are still adding capacity often for the lack of adequate supply of multi-tenant datacenter capacity.

There is more technology and market change coming still, and Vertiv has its work cut out for it. Examples include the rapid evolution of various battery chemistries and more rack integration of electrical infrastructure seen with hyperscalers; the potentially abrupt shift towards liquid cooling driven by escalating silicon power and the need to compress urban footprints; the elusive area of edge computing; and more sophisticated, AI-infused software that can optimize facility performance and efficiency and predict failures before they happen. Each of these is potentially disruptive to considerable parts of Vertiv's portfolio; nonetheless, the company appears to be in a much better shape to tackle these challenges – and capitalize on many of them – than it was only three years ago, while the market, contrary to fears, offers room for growth.

Competition

Vertiv's chief rival is Paris-based Schneider Electric, the only other company that can match its scale and portfolio in datacenters. In China and some emerging markets, Huawei also provides stiff competition. Electrical engineering giants ABB, Eaton and Siemens are major contenders in critical power systems and are also aggressively targeting major datacenter projects. DeltaTek is a competitor that is strong in the telecom segment. Vertiv may differentiate itself via more responsive and flexible designs matched by global prefabrication capacity.

More specifically, climatic systems (known as heating, ventilation and air-conditioning, or HVAC) is a tough market where Vertiv competes with some major vendors (such as Schneider, Munters in the United States, Nortek and STULZ), as well as a high number of established and startup specialists. Demand is shifting from enterprises to larger multi-tenant and cloud services datacenter operators that are in a stronger negotiating position, more technically apt and want high-efficiency cooling systems that are low maintenance.

Some fast-moving datacenter cooling startups that focus on free cooling, such as BladeRoom and Excool, have also reaped considerable commercial success, particularly in the UK where each have sold tens of megawatts of cooling capacity.

SWOT Analysis

STRENGTHS

Compared with most of its competition, Vertiv has a large installed base, a broad product portfolio and global reach, as well as strong product brand recognition for some major product lines in a risk-averse market. It's also in a strong financial position.

WEAKNESSES

Vertiv has been relatively less strong in marketing its products, technologies and services than others. Investments in software and distributed control have yet to be fully aligned with its equipment and services offerings. Product and monetization strategies for edge and next-generation cooling, including direct liquid, remains unclear.

OPPORTUNITIES

Multi-megawatt colocation and hyperscale sites offer ample opportunities to land large wins. On the other end of the scale, demand for smaller edge datacenters is expected to balloon as the number of connected machines grows in many vertical industries.

THREATS

As a major vendor, Vertiv is exposed to the shrinking enterprise datacenter segment, which is still a major part of its revenue. Telecom and industrial expenditures are also muted ahead of 5G rollouts and also due to cost pressures. Escalating geopolitical tensions might hurt Vertiv's prospects in China and in delayed investments by telecom customers.