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Western Digital (WDC.N)

Management Callback Takeaways

CITI'S TAKE

We spoke with WDC mgmt post Sept-Q earnings and recap our key takeaways below.

Demand & Customer Visibility – Management emphasized that demand remains strong and is not the constraint on growth. Top 7 customers are providing visibility through 2030-2031, and management noted aggregated demand signals support 25+% long-term exabyte CAGR. Revenue and exabyte shipments continue to be primarily constrained by Western Digital's ability to supply drives rather than end-market demand, with near term constraints as they undergo transitions. Existing supply-demand gap was not expected to disappear in the near term

Exabyte Growth Outlook – Management reaffirmed visibility to 25%+ long-term exabyte demand growth. Future exabyte acceleration will depend on both Western Digital's execution and customer adoption of higher-capacity products.

CapEx & Manufacturing Investments – CapEx is expected to remain modestly above the historical 4%-6% of revenue range for roughly the next two years. Management emphasized that elevated CapEx is not intended to add HDD unit capacity. Instead, spending is focused on head wafers, media capacity, glass substrates, and HAMR-related manufacturing requirements as well as automation to improve yields. Additional investment is also needed to support increasing platter counts per drive and future technologies such as high-bandwidth drives and dual-pivot architectures.

Continued...

EPS (US$)	Q1	Q2	Q3	Q4	FY	FC Cons
2026A	1.78A	2.13A	2.72A	3.56A	10.22A	10.22A
2027E	**4.26E**	**4.84E**	**5.98E**	**7.04E**	**22.09E**	**21.03E**
Previous	4.26E	4.84E	5.98E	7.04E	22.09E	na
2028E	**8.13E**	**8.91E**	**9.46E**	**10.57E**	**37.02E**	**34.16E**
Previous	8.13E	8.91E	9.46E	10.57E	37.02E	na
2029E	**na**	**na**	**na**	**na**	**48.39E**	**44.54E**
Previous	na	na	na	na	48.39E	na

Source: Company Reports and dataCentral, Citi Research. FC Cons: First Call Consensus.

Buy

Price (22 Oct 26 16:00)	US$353.80
Target price	US$740.00
Expected share price return	109.2%
Expected dividend yield	0.2%
Expected total return	109.3%
Market Cap	US$132,168M

Price Performance
(RIC: WDC.N, BB: WDC US)



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Pricing & Long-Term Agreements – Pricing remains favorable. Existing LTAs contain a mix of fixed pricing, premium pricing for incremental volumes, and annual escalators. While demand visibility extends through 2030-2031, commercial terms for those years have not yet been finalized. For the December quarter, management noted that the vast majority of revenue is already under contract with pricing locked in and indicated ASP-per-terabyte growth should exceed the prior quarter's 28% increase.

Product Roadmap: ePMR and HAMR – The latest ePMR platform offers capacity of up to 40 TB and had begun volume production, with customer adoption progressing ahead of prior product transitions. Management expected it to account for close to 30% of nearline shipments in fiscal Q2 2027 and 50% in fiscal Q3 2027. The latest ePMR platform offers capacity of up to 40 TB and had begun volume production, with customer adoption progressing ahead of prior product transitions. Management expected it to account for close to 30% of nearline shipments in fiscal Q2 2027 and 50% in fiscal Q3 2027. For first-generation HAMR, management expected to complete qualifications with two hyperscale customers in calendar Q1 2027 and begin volume shipments in the first half of calendar 2027. For first-generation HAMR, management expected to complete qualifications with two hyperscale customers in calendar Q1 2027 and begin volume shipments in the first half of calendar 2027.Management reiterated that first-generation HAMR drives, expected in 1H27, will average roughly 4TB per platter, while second-generation HAMR products targeted for qualification in 2H27 are expected to average about 5TB per platter. The company expects HAMR margins to be at least comparable to, and potentially better than, current ePMR margins once volume production is reached. Product transitions from current 32TB drives to 40TB drives and subsequently to HAMR are expected to drive higher exabyte output and improved cost-per-terabyte economics.

Cost Per Terabyte – Management noted cost-per-terabyte reductions have temporarily slowed due to product transitions and recently-emerging input-cost headwinds. Value-engineering initiatives are underway to offset these pressures, although implementation and customer qualification will take several quarters. Longer term, management remains confident in returning to roughly 10% annual cost-per-terabyte reductions.

Inventory – Inventory increased sequentially as the company prepares for accelerating exabyte shipments. Management said inventory is being built primarily in components, and not finished goods, to support future demand in a tight supply-chain environment. Mgmt emphasized that any additional available exabytes could be shipped immediately.

Platter Count Expansion – Current flagship products use 11 platters, with a roadmap to 12- and eventually 14-platter drives. Total platter counts are increasing at a low-teens percentage rate year over year with higher platters up more significantly. Management also highlighted opportunities to increase exabyte output by migrating customers from lower-capacity drives to newer high-capacity products.

AI, Hyperscalers & Neoclouds – Management continues to view hyperscalers as its core strategic customers but highlighted growing demand from AI frontier labs and neocloud providers. Mgmt noted this reinforces the view that AI is fundamentally a data and storage challenge, not solely a compute opportunity. Demand from these newer customer groups is being incorporated into forecasts and investment plans.

On neoclouds specifically, management emphasized it is highly selective, evaluating customers based on business viability, balance-sheet strength, and end-customer quality, while structuring commercial agreements to mitigate credit risk.

Margin Outlook – Despite temporary cost headwinds, management remains confident in the margin profile of the business. Gross margins next quarter are guided to be 60-61% range, with further improvement supported by favorable pricing, continued transition to higher-capacity drives, successful product technology transitions, and continued cost-per-terabyte reductions.

Capital Allocation – Management reaffirmed its commitment to returning excess free cash flow to shareholders after funding growth investments. The company continues to target free-cash-flow margins above 30% on a trailing annual basis. Western Digital recently repurchased approximately $1 billion of stock, increased its dividend, and noted that 83% of trailing twelve-month free cash flow has been returned to shareholders through dividends and buybacks.

Western Digital

Company description

Western Digital Corporation is a global data storage supplier of hard disk drives (HDDs). The company offers mobile drives for the notebook, PC, and gaming markets; serial attached small computer system interface drives; home video recorders; home network storage devices; and portable, desktop, and personal cloud storage. Western Digital was founded in 1970 and is headquartered in San Jose, CA.

Investment strategy

We have a Buy rating on Western Digital given our view of a cyclical recovery in the storage market, which, coupled with our view of AI-driven storage demand growth and rational capacity additions, should enable the company to sustain higher revenue and earnings growth ahead.

Valuation

Our target price for WDC is $740 valued at 20x FY28 EPS estimates, in line with its market peer multiple given strong recent execution, demand visibility confidence, and continued outlook of solid and durable HDD supply/demand dynamics supportive of pricing and margins.

Risks

Downside risks that could impede the stock price from reaching our target price include:
1) returning weakness in cloud/enterprise demand from macro-induced factors could curtail storage spending, and upset the current balance in supply-demand dynamics and causing significant charges;
2) a decrease in SSD prices due to faster-than-expected HDD cannibalization by SSDs;
3) continued challenges in improving cost structure vs. the 10-15% historically; and
4) HAMR development roadmap stalls, allowing competitive threats to WDCs enterprise business from Seagate's earlier established HAMR high-capacity drives.

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Appendix A-1

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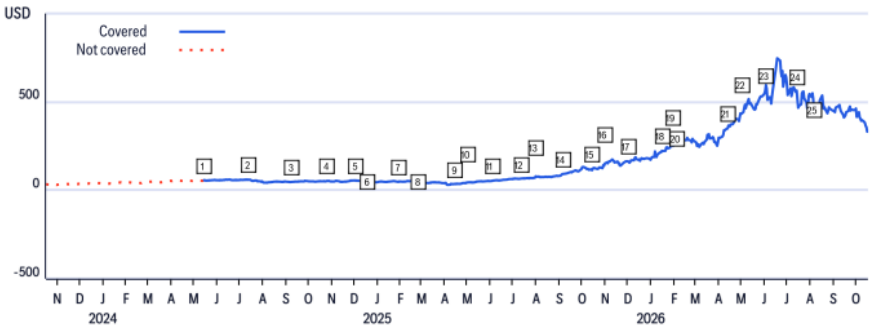
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Western Digital (WDC)

Ratings and Target Price History
Fundamental Research

Analyst: Asiya Merchant, CFA



	Date	Rating	Target Price	Closing Price
1	14-May-24 03:30:00	*1	*68.01	55.65
2	12-Jul-24 03:00:00	1	*71.79	59.61
3	09-Sep-24 19:32:14	1	*64.23	47.34
4	25-Oct-24 04:08:51	1	*65.74	52.48
5	02-Dec-24 18:28:07	1	*64.23	55.51
6	19-Dec-24 06:30:00	1	*61.96	45.06
7	30-Jan-25 01:59:33	1	*60.45	49.73
8	24-Feb-25 17:12:10	1	*64.00	48.97
9	14-Apr-25 05:00:00	1	*48.00	35.81
10	30-Apr-25 21:49:48	1	*56.00	43.88
11	03-Jun-25 16:41:58	1	*62.00	53.75
12	11-Jul-25 04:00:00	1	*78.00	66.13
13	31-Jul-25 02:57:56	1	*88.00	78.66
14	07-Sep-25 21:24:48	1	*110.00	92.05
15	13-Oct-25 00:10:56	1	*135.00	118.88
16	31-Oct-25 05:43:04	1	*180.00	150.26
17	01-Dec-25 23:07:43	1	*200.00	163.58
18	19-Jan-26 19:00:00	1	*280.00	221.52
19	30-Jan-26 03:14:41	1	*325.00	250.11
20	03-Feb-26 21:23:12	1	*335.00	290.34
21	13-Apr-26 03:59:36	1	*405.00	350.18
22	01-May-26 02:42:15	1	*500.00	431.62
23	02-Jun-26 06:01:17	1	*685.00	563.14
24	13-Jul-26 03:42:28	1	*800.00	555.30
25	06-Aug-26 04:18:42	1	*740.00	450.90

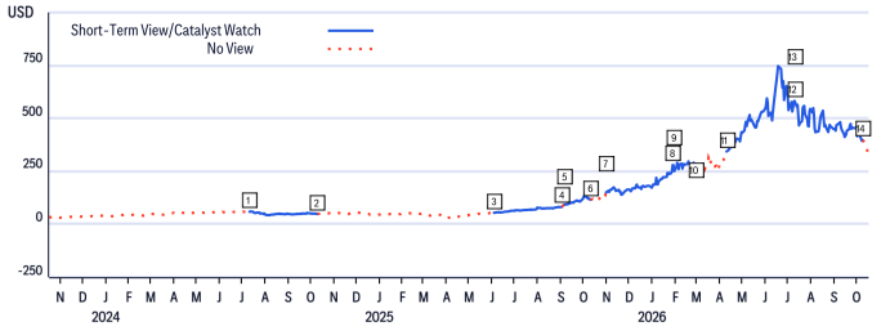
*Indicates Change

Rating/target price changes above reflect Eastern Time

Western Digital (WDC)

Short-Term View/Catalyst Watch Research

Analyst: Asiya Merchant, CFA



	Date	Action	Expected Direction	Duration	Closing Price
1	11-Jul-24 23:00:00	Add STV	Upside	90 Days	58.85
2	10-Oct-24 08:26:14	Remove STV	Upside	90 Days	48.38
3	03-Jun-25 12:41:58	Add STV	Upside	90 Days	53.75
4	02-Sep-25 08:16:05	Remove STV	Upside	90 Days	81.91
5	07-Sep-25 17:24:48	Add STV	Upside	90 Days	92.05
6	12-Oct-25 20:10:56	Remove STV	Upside	90 Days	115.37
7	31-Oct-25 01:43:04	Add STV	Upside	90 Days	150.26
8	29-Jan-26 06:11:50	Remove STV	Upside	90 Days	278.45
9	29-Jan-26 22:14:41	Add STV	Upside	30 Days	278.45
10	27-Feb-26 12:28:10	Remove STV	Upside	30 Days	279.65
11	12-Apr-26 23:59:36	Add STV	Upside	90 Days	343.49
12	10-Jul-26 14:21:17	Remove STV	Upside	90 Days	582.34
13	12-Jul-26 23:42:28	Add STV	Upside	90 Days	582.34
14	09-Oct-26 14:04:36	Remove STV	Upside	90 Days	397.21

CW - Catalyst Watch , STV - Short-Term View

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% of companies in each rating category that are investment banking clients	39%	43%	30%	42%	38%	36%

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