

# Keppel DC REIT

Strengthening its presence in Europe

SINGAPORE | REAL ESTATE (REIT) | UPDATE

12 October 2016

- Acquisition of Data Centre in Cardiff, Wales, United Kingdom
- Strengthens position in Europe, diversifies across five cities in Europe
- Fully funded by debt and immediately DPU accretive

## What is the news?

Keppel DC REIT (KDCREIT) announced the acquisition of a shell and core building of a data centre in Cardiff, Wales, United Kingdom. The data centre is located within the Celtic Gateway Business Park and comprises a two-storey data centre that is connected to a three-storey office block. The site is on c.26,000 sqm (279,864 sqft) of freehold land and the buildings have a total lettable area of c.7,380sqm (79,439 sqft). The purchase consideration is for GBP 34.0mn (c.S\$59.7mn). The acquisition of the data centre has been fully-funded by debt and aggregate leverage has increased from 29.1% to c.32.5%.

## How do we view this?

### REIT Manager demonstrates ability to acquire from outside of the ROFR

This is the fourth acquisition by the Manager; and the third from outside of the Right of First Refusal (ROFR) portfolio. The first two from outside of the ROFR portfolio are the forward purchase of maincubes Data Centre (Frankfurt) and the Milan Data Centre which is pending transaction completion.

### Geographical diversification, but increases exposure to GBP amidst Brexit

This will be the fifth city in Europe in addition to the existing locations of London, Dublin, Amsterdam and Milan. KDCREIT would strengthen its position in Europe, balancing out the contribution from Asia Pacific. Rental income contribution from Europe increases to 28.5% from 24.7%. However, we note that the GBP has depreciated c.20% relative to SGD over the last twelve months, and could depress further with the ensuing uncertainty over Brexit. FY17e exposure to the GBP would be c.7.4% by Gross revenue in SGD-terms without the acquisition, and c.12% with-acquisition, by our estimates.

### Income stability from a fully-fitted lease, reducing exposure to co-location leases

The data centre is on a triple-net lease to one of the largest global cloud service providers. Publicly available information suggests that the data centre is known as BT Cardiff Bay Data Centre and is located on Watkiss Way. The client is well-established and creditworthy. The lease is for 15 years commencing 24 June 2016. Consequently, the portion of income from master lease will be increased to 35.0% from 31.6%, and portfolio weight average lease expiry (WALE) extends to 9.5 years by lettable area from 8.7 years.

### Immediately accretive, but Unitholder dilution could come in the future

The acquisition was fully funded by GBP debt, thus providing a natural hedge and at the same time making it immediately accretive. Leverage has increased from 29.1% to c.32.5%. On an illustrative pro-forma basis, the Manger expects the acquisition to be 0.28 cents accretive to distribution per unit (DPU); but our analysis suggests that it will be closer to 0.20~0.24 cents. We think that the balance sheet can be further utilised to make two or three more acquisitions, before any equity fund raising is required to bring the gearing back to the Manager's long-term target of 30%.

### Maintain "Accumulate" rating with new higher target price of S\$1.29 (previous: S\$1.26)

Key downside risk to our target price is the capital structure for the acquisition of Keppel DC Singapore 3 (formerly known as T27) and dilutive effect arising from the associated equity fund raising (EFR). Our FY18e DPU is already lower than FY17e DPU because we have assumed an EFR for the acquisition of mainCubes data centre, which will increase the Unitholder base by c.10%.

*Note: KDCREIT will be announcing 3QFY16 financial results on 17 October, after trading hours.*

## Accumulate (Maintained)

LAST CLOSE PRICE	SGD 1.225
FORECAST DIV	SGD 0.070
TARGET PRICE	SGD 1.290
<b>TOTAL RETURN</b>	<b>11.0%</b>

### COMPANY DATA

O/S SHARES (MN):	883
MARKET CAP (USD mn / SGD mn):	771 / 1064
52 - WK HI/LO (SGD):	124 / 0.96
3M Average Daily T/O (mn):	187

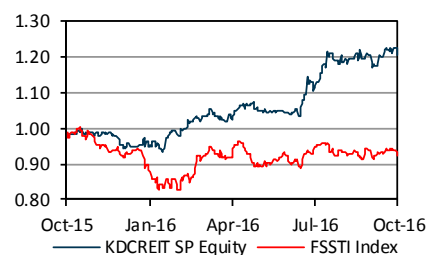
### MAJOR SHAREHOLDERS (%)

KEPPEL CORLLTD	35.0%
COHEN & STEERS CAPITAL MANAGEMENT	3.6%
MORGAN STANLEY	3.4%

### PRICE PERFORMANCE (%)

	1M TH	3M TH	1YR
COMPANY	17	110	24.6
STIRETURN	(0.6)	10	(10)

### PRICE VS. STI



Source: Bloomberg, PSR

### KEY FINANCIALS

Y/E Dec	FY15	FY16e	FY17e	FY18e
Gross Rev. (SGD mn)	107.7	102.3	111.3	113.9
NPI (SGD mn)	91.3	89.2	96.3	98.6
Dist. Inc. (SGD mn)	60.4	60.6	65.7	67.1
P/NAV (x)	1.10	1.32	1.31	1.29
DPU, adj (cents)	6.84	6.96	7.45	7.26
Distribution Yield (%)	6.74	5.68	6.08	5.93

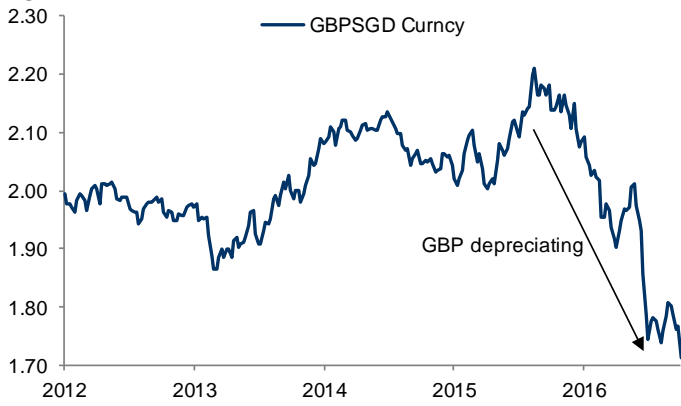
Source: Company Data, PSR est.

### VALUATION METHOD

DDM (Cost of Equity: 6.7%; Terminal g: 10%)

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**Figure 1. Price of 1 GBP in SGD**



Source: Bloomberg, Phillip Securities Research (Singapore)

GBP has depreciated c.20% relative to SGD over the last 12 months.

**Peer relative valuation**

KDCREIT is trading at a premium to Australia Stock Exchange (ASX)-listed peer Asia Pacific Data Centre in terms of P/NAV multiple and with a lower 12M-trailing yield.

**Peer comparison (arranged by Mkt. Cap.)**

	Currency	Price (LCY\$)	Mkt. Cap. (S\$ mn)	Mkt. Cap. (US\$ mn)	Trailing P/NAV (x)	12M-trailing yield (%)
Keppel DC REIT	SGD	1.205	1,064	770	1.31	5.5
Asia Pacific Data Centre	AUD	1.56	188	136	1.09	6.2

Source: Bloomberg (Updated: 12 October 2016), Phillip Securities Research (Singapore)

## Financials

FY15 = 12 December 2014 to 31 December 2015

### Statement of Total Return and Distribution Statement

Y/E Dec, SGD mn	FY15	FY16e	FY17e	FY18e
<b>Gross rental income</b>	<b>105.9</b>	<b>101.3</b>	<b>110.2</b>	<b>112.9</b>
Other income	1.7	1.0	1.1	1.0
<b>Gross revenue</b>	<b>107.7</b>	<b>102.3</b>	<b>111.3</b>	<b>113.9</b>
Property expenses	(16.4)	(13.1)	(15.0)	(15.4)
<b>Net property income</b>	<b>91.3</b>	<b>89.2</b>	<b>96.3</b>	<b>98.6</b>
Net Finance (Expense)/Inc	(12.1)	(11.4)	(15.2)	(15.5)
Manager's fees	(8.7)	(8.9)	(9.5)	(9.9)
Other items	(1.8)	1.2	1.2	1.2
Exceptional items	-	-	-	-
FV change, Invmnt. properties	41.1	-	-	-
<b>Total Return Before Tax</b>	<b>109.8</b>	<b>70.1</b>	<b>72.8</b>	<b>74.3</b>
Taxation	(5.6)	(4.2)	(4.3)	(4.4)
<b>Total Return After Tax</b>	<b>104.2</b>	<b>65.9</b>	<b>68.5</b>	<b>69.9</b>
Unitholders	104.2	65.8	68.5	69.8
Non-controlling interest	0.04	0.03	0.03	0.03
Distribution adjustments	(43.8)	(5.3)	(2.9)	(2.9)
<b>Income available for distribution</b>	<b>60.4</b>	<b>60.6</b>	<b>65.6</b>	<b>66.9</b>
<b>Income distributed</b>	<b>60.4</b>	<b>61.5</b>	<b>65.6</b>	<b>67.0</b>

### Per share data

Y/E Dec	FY15	FY16e	FY17e	FY18e
NAV (\$\$)	0.92	0.93	0.93	0.95
EPU (Cents)	11.80	7.46	7.75	7.63
DPU (Cents)	6.84	6.96	7.42	7.23

\*Forward EPU does not include change in Fair Value of Investment Properties

### Cash Flow

Y/E Dec, SGD mn	FY15	FY16e	FY17e	FY18e
<b>CFO</b>				
Total return	104.2	65.9	68.5	69.9
Adjustments	(23.4)	15.7	19.5	20.0
WC changes	(24.4)	1.5	(3.0)	(0.9)
Cash generated from ops	56.4	83.1	85.0	88.9
Others	(0.2)	(4.2)	(4.3)	(4.4)
<b>Cashflow from ops</b>	<b>56.3</b>	<b>78.9</b>	<b>80.7</b>	<b>84.5</b>
<b>CFI</b>				
CAPEX, net	(8.8)	(4.0)	(2.0)	(2.0)
Purchase of Inv. Propty.	(477)	(120)	-	(117)
Others	(47.6)	-	-	-
<b>Cashflow from investments</b>	<b>(533)</b>	<b>(124)</b>	<b>(2)</b>	<b>(119)</b>
<b>CFF</b>				
Share issuance, net	507	-	-	91
Loans, net of repayments	364	119.7	-	27
Dividends	(57.5)	(61.0)	(63.5)	(65.9)
Others	(306)	(11)	(15)	(16)
<b>Cashflow from financing</b>	<b>507</b>	<b>47</b>	<b>(79)</b>	<b>37</b>
<b>Net change in cash</b>	<b>30.3</b>	<b>2.0</b>	<b>(0.0)</b>	<b>2.4</b>
Effects of exchange rate	(1)	-	-	-
<b>Ending cash</b>	<b>37.2</b>	<b>39.1</b>	<b>39.1</b>	<b>41.5</b>

Source: Company, Phillip Securities Research (Singapore) Estimates

\*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.

### Balance Sheet

Y/E Dec, SGD mn	FY15	FY16e	FY17e	FY18e
<b>ASSETS</b>				
Investment properties	1,103	1,227	1,229	1,361
Inv. Propty. Under Devmnt.	-	-	-	-
Others	17.3	17.3	17.3	4.5
<b>Total non-current assets</b>	<b>1,120</b>	<b>1,244</b>	<b>1,246</b>	<b>1,365</b>
Cash	37.2	39.1	39.1	41.5
Trade receivables	53.1	50.8	55.2	56.5
Others	1.0	1.0	1.0	1.0
<b>Total current assets</b>	<b>91.2</b>	<b>90.9</b>	<b>95.3</b>	<b>99.1</b>
<b>Total Assets</b>	<b>1,211</b>	<b>1,335</b>	<b>1,341</b>	<b>1,464</b>
<b>LIABILITIES</b>				
Trade payables	17.8	17.0	18.5	19.0
Borrowings	33.6	3.5	156.5	133.5
Others	0.1	0.1	0.1	0.1
<b>Total current liabilities</b>	<b>51.6</b>	<b>20.7</b>	<b>175.2</b>	<b>152.6</b>
Borrowings	338.3	488.1	335.1	385.4
Others	7.8	7.8	7.8	7.8
<b>Total non-current liabilities</b>	<b>346.1</b>	<b>495.9</b>	<b>342.9</b>	<b>393.2</b>
<b>Total Liabilities</b>	<b>397.7</b>	<b>516.6</b>	<b>518.1</b>	<b>545.9</b>
<b>Net assets</b>	<b>813.5</b>	<b>818.4</b>	<b>823.4</b>	<b>918.3</b>
<b>Represented by:</b>				
<b>Unitholders' funds</b>	<b>813.1</b>	<b>818.0</b>	<b>823.0</b>	<b>918.0</b>
Non-controlling interest	0.37	0.38	0.38	0.38

### Valuation Ratios

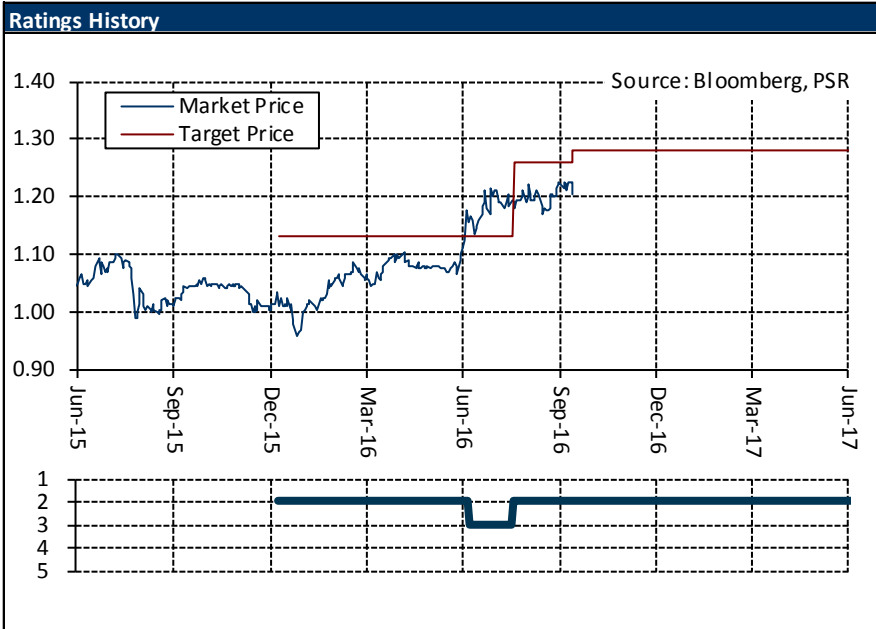
Y/E Dec	FY15	FY16e	FY17e	FY18e
P/NAV (x)	1.10	1.32	1.31	1.29
P/DPU (x)	14.8	17.6	16.5	16.9
Distribution Yield (%)	6.74	5.68	6.06	5.90
NPI yield (%)	8.28	7.66	7.85	7.61

### Growth & Margins (%)

Growth				
Revenue		-5.0%	8.8%	2.3%
Net property income (NPI)		-2.3%	8.0%	2.3%
Distributable income		0.3%	8.3%	2.0%
DPU		1.8%	6.6%	-2.6%
Margins				
NPI margin	84.8%	87.2%	86.5%	86.5%

### Key Ratios

Net Debt or (Net Cash)	334.8	452.5	452.5	477.5
Gearing (%)	30.7%	36.8%	36.7%	35.4%



**PSR Rating System**

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

**Remarks**

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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