

Keppel DC REIT

In anticipation of acquisitions



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SINGAPORE | REAL ESTATE(REIT) | 3Q20 UPDATE

26 October 2020

- 9M20 DPU of 6.73 cents in line, forming 71.3% of our FY20e DPU estimate.
- Portfolio metrics healthy: long WALE of 7.2 years, portfolio occupancy of 96.7% and interest coverage ratio of 12.7x. AEI and rental escalations to provide organic growth.
- Reiterate NEUTRAL with a higher DDM-based target price of S\$2.91 from S\$2.57 after incorporating S\$500mn of acquisitions for 1Q21e. Despite strong metrics and future-ready asset classes, reiterate Neutral as we believe the market has priced in potential catalysts from acquisitions and STI inclusion. Prefer Ascendas REIT (AREIT SP, Accumulate, TP: S\$3.63) in the sector.

Results at a glance

(SGD mn)	3Q20	3Q19	YoY	9M20	9M19	YoY	Comments
Gross revenue	67.7	46.4	46.0%	192	142	35.1%	Mainly due to contribution from KDC SGP 4 (acquired 31 Oct 19), DC1 (acquired 21 Nov 2019) and Kelsterbach (acquired 1 May 2020)
Net property income	62.4	42.3	47.6%	177	129	37.1%	
Distributable income	40.5	27.4	47.6%	115.5	81.8	41.2%	
DPU (cents)	2.36	1.93	22.1%	6.73	5.78	16.5%	

Source: Company, PSR

The Positives

- 3Q20 DPU grew +22.1% YoY.** This was mainly driven by its acquisitions of KDC SG 4 and DC1 in 4Q19 and Kelsterbach DC in March 2020, tax savings from attainment of tax transparency for KDC SG 4 and higher rents charged on the conversion of non-DC space to DC at KDC SG 5. DPU was up 16.5% YoY in 9M20. KDC has several AEIs underway (Figure 1), which should continue to drive revenue.
- Strong leasing quarter, occupancy inched up from 96.1% to 96.7%.** KDC Dub 1's Asset Enhancement Initiative (AEI) was completed despite a 2-month delay to bring more power onsite. Occupancy increased from 63.3% to 81.1% upon the power upgrade. The space has been leased to a new telco tenant. Despite large take-up of 12,125 sq ft, no discounts were offered. Client expansion at KDC SG 1 is expected to lift occupancy from 89.2% to 91.0% (1,975 sq ft) and from 93.5% to 98.2% (1,809 sq ft) at KDC SG 2, both of which commenced on 1 October 2020. KDC also managed to secure an early lease renewal for its iSeek Data Centre in Australia, terming out its iSeek's WALE from six years to 10.7 years.

The Negatives

- AEIs and development completions pushed to 1H21; intermittent disruptions.** Most of KDC's AEIs was disrupted by construction delays due to COVID-19 lockdowns in 1H20. Client fit-out at DC 1 has also been delayed to 1H21. While construction has resumed, delays in certain supplies and manpower scheduling have resulted in intermittent disruptions.

Outlook

Still awaiting acquisitions. KDC is still negotiating several third-party deals with cap rates of 4-7%, some in advance stages. However, its deal process has been stalled by travel restrictions. Management shared that the number of deals and size have increased. While demand for data centres has compressed cap rates, asking prices for deals under negotiation are unchanged.

NEUTRAL (Maintained)

LAST CLOSE PRICE	SGD 3.000
FORECAST DIV	SGD 0.094
TARGET PRICE	SGD 2.910
TOTAL RETURN	0.1%

COMPANY DATA

BLOOMBERG CODE:	KDCREITSP
O/S SHARES (MN):	1,633
MARKET CAP (USD mn / SGD mn):	3610 / 4899
52 - WK HI/LO (SGD):	3.16 / 1.74
3M Average Daily T/O (mn):	5.95

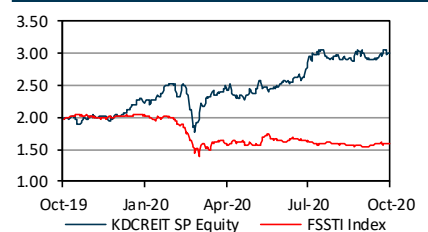
MAJOR SHAREHOLDERS (%)

KEPPEL CORP LTD	23.4%
SUMITOMO MITSUI ASSET MGMT CO	7.8%
COHEN & Steers inc	5.1%

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	1.0	10.4	53.1
STI RETURN	1.6	(2.8)	(16.1)

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec	FY18	FY19	FY20e	FY21e
Gross Rev. (SGD mn)	176	195	260	315
NPI (SGD mn)	158	177	229	270
Dist. Inc. (SGD mn)	96	113	154	189
P/NAV (x)	2.80	2.57	2.55	2.29
DPU, adj (cents)	7.32	7.61	9.44	10.79
Dist. Yield	2.4%	2.5%	3.1%	3.6%

Source: Company Data, PSR

VALUATION METHOD

DDM (Cost of Equity: 5.75%; Terminal g: 2.0%)

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*Keppel DC REIT was included in the Straits Times Index on 19 October 2020

Demand-supply gap to lift market rents. Demand-supply gaps exist in many markets due to government restrictions on the supply of data centres. Globally, demand for data centres is being driven by big data, 5G and cloud adoption. Singapore has attracted Chinese tech companies looking to set up headquarters and operations here to perform big data analytics. We understand, however, that the Chinese tech players were unsuccessful in securing land from the government for data-centre development. Given the moratoriums on data centres in Singapore, we expect market rents to be bid up in the coming two years. While KDC's high portfolio occupancy of 96.7% and long WALE of 7.2 years translate to low expiries in 2021/22 and leave little opportunity for positive rental reversions, many of its existing leases and co-location arrangements have built-in periodic rental escalations averaging 2-4% p.a.

Figure 1: Ongoing AEs and developments

Est. Completion	Asset	Cost	Details
1H21	KDC Dub 2	€12m	Converting additional space to data hall
1H21	Intellicentre 3 (Aust)	A\$26- A\$36m	Development of S&C DC, fully committed
1H21 2H20	KDC SG 5	S\$29.9m	Convert vacant non-DC space, 15.8% of NLA
1H21 3Q20	DC1	S\$56.6m	Convert from 2 floors of S&C space to FF

Source: Company, PSR

Note: S&C and FF stand for Shell & Core and Fully Fitted respectively

Maintain NEUTRAL with higher target price of S\$2.91, from S\$2.57.

Our DDM-based TP has been raised from S\$2.57 to S\$2.91 following our assumption of S\$500mn of acquisitions with an NPI yield of 6% and LTV of 30% for 1Q21e. This translates to DPU accretion of 5.0%/ 5.8% for FY21e/FY22e and gearing of 35% in FY21e. Despite strong portfolio metrics and future-ready asset classes, we reiterate our Neutral view as we believe the market has priced in potential catalysts from acquisitions and STI inclusion. KDC is trading at an all-time high and DPU yield of 3.1%/3.6% for FY20e/21e is not compelling. Prefer Ascendas REIT (AREIT SP, Accumulate, TP: S\$3.63) in the sector.

Financials

Statement of Total Return and Distribution Statement

Y/E Dec, SGD mn	FY17	FY18	FY19	FY20e	FY21e
Gross revenue	139	176	195	260	315
Property expenses	(14)	(18)	(18)	(31)	(45)
Net property income	125	158	177	229	270
Net Finance (Expense)/Inc	(13)	(16)	(15)	(17)	(17)
Manager's fees	(11)	(14)	(16)	(22)	(25)
Other items	(14)	(9)	(6)	(10)	(9)
FV change, Inv. Properties	(9)	33	(16)	-	-
Total Return Before Tax	78	151	124	181	218
Taxation	(7)	(5)	(13)	(9)	(8)
Total Return After Tax	70	146	111	172	211
Unitholders	65	142	107	167	206
Non-controlling interest	5	4	5	5	5
Distribution adjustments	17	(46)	7	(13)	(17)
Income available for distribution	82	96	113	154	189

Per unit data

Y/E Dec	FY17	FY18	FY19	FY20e	FY21e
NAV (S\$)	0.97	1.07	1.17	1.17	1.31
DPU (cents)	7.12	7.32	7.61	9.44	10.79

Cash Flow

Y/E Dec, SGD mn	FY17	FY18	FY19	FY20e	FY21e
CFO					
Total Return After Tax	70	146	111	172	211
Adjustments	51	(2)	41	30	26
WC changes	1	(30)	19	(14)	(10)
Cash generated from ops	123	114	171	189	226
Others	(5)	(2)	(16)	(9)	(8)
Cashflow from ops	118	112	155	179	219

CFI

Purchase of Inv. propty., net	(293)	(413)	(586)	(173)	(500)
Capex, net	(12)	(34)	(57)	(83)	(57)
Others	-	(1)	(27)	-	-
Cashflow from investments	(305)	(448)	(669)	(256)	(557)

CFF

Share issuance, net	-	303	478	-	350
Net borrowings	357	231	383	273	310
Distributions	(74)	(85)	(129)	(157)	(191)
Others	(273)	(102)	(189)	(79)	(147)
Cashflow from financing	10	347	543	36	321

Net change in cash	(178)	11	29	(40)	(17)
Effects of exchange rate	(0)	1	(2)	-	-
Ending cash	116	128	156	116	99

Source: Company, Phillip Securities Research (Singapore) estimates

Balance Sheet

Y/E Dec, SGD mn	FY17	FY18	FY19	FY20e	FY21e
ASSETS					
Investment properties	1,570	2,029	2,637	2,893	3,450
Inv. Propty. Under Devmnt.	-	-	-	-	-
Others	15	4	11	8	8
Total non-current assets	1,585	2,033	2,648	2,900	3,457
Cash	118	128	156	116	99
Trade receivables	56	86	96	132	160
Others	4	6	28	28	28
Total current assets	178	220	280	276	287
Total Assets	1,763	2,253	2,928	3,176	3,744
LIABILITIES					
Borrowings	4	134	40	108	165
Trade payables	48	36	60	82	100
Others	1	17	8	8	8
Total current liabilities	53	187	108	198	272
Borrowings	576	573	880	1,023	1,146
Others	18	-	37	37	37
Total non-current liabilities	594	573	917	1,060	1,183
Total Liabilities	647	760	1,025	1,258	1,455
Net assets	1,117	1,493	1,903	1,918	2,289
Represented by:					
Unitholders' funds	1,090	1,445	1,868	1,882	2,250
Non-controlling interest	27	31	35	36	38

Valuation Ratios

Y/E Dec	FY17	FY18	FY19	FY20e	FY21e
P/NAV (x)	3.09	2.80	2.57	2.55	2.29
Distribution Yield	2.4%	2.4%	2.5%	3.1%	3.6%
NPI yield	8.9%	8.8%	7.6%	8.3%	8.5%

Growth & Margins (%)

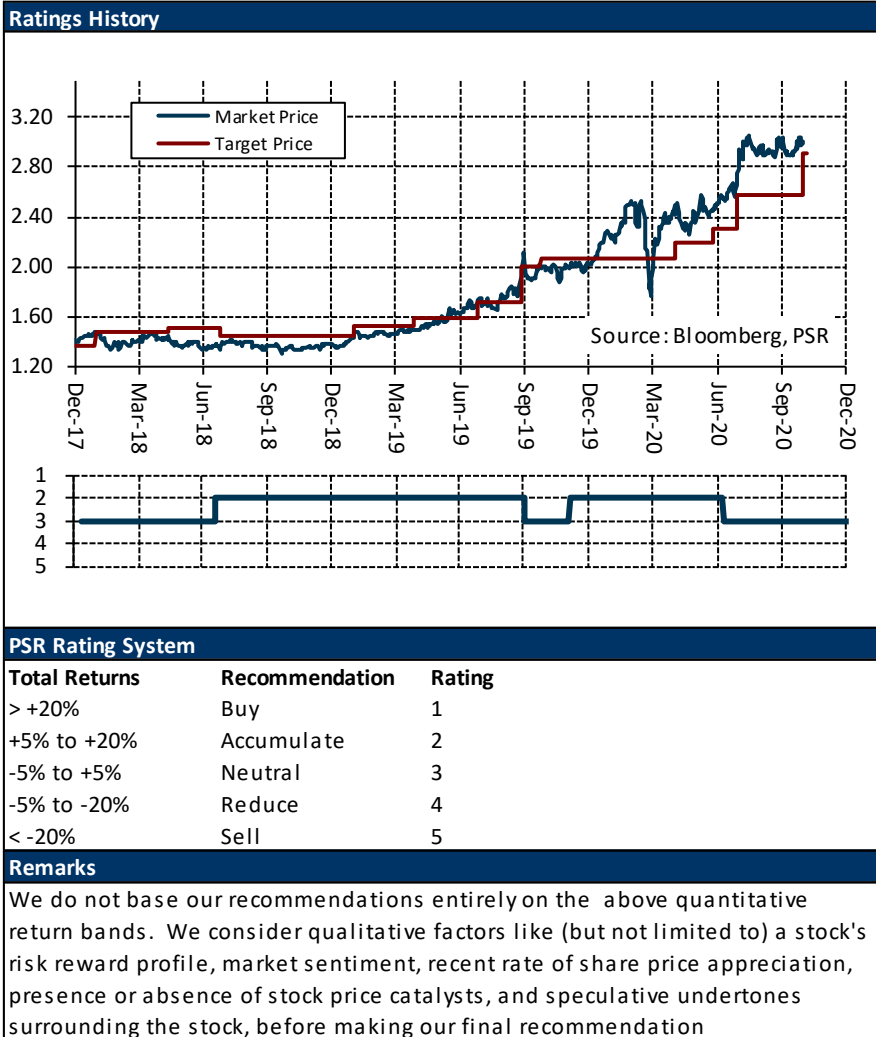
Growth					
Revenue	29.1%	26.2%	11.0%	33.6%	21.0%
Net property income (NPI)	37.0%	26.0%	12.4%	29.3%	17.9%
Distributable income	36.3%	16.7%	17.8%	36.2%	22.4%
DPU	4.1%	2.8%	4.0%	24.1%	14.3%
Investment Property	28.1%	29.2%	30.0%	9.7%	19.3%

Margins

NPI margin	90.0%	89.8%	91.0%	88.0%	85.8%
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Key Ratios

Gearing (%)	32.9%	31.4%	31.4%	35.6%	35.0%
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