

# Keppel DC REIT

## Uncollected rents impact DPU



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### SINGAPORE | REAL ESTATE (REIT) | FY23 UPDATE

09 February 2023

- FY23 DPU of 9.383 Singapore cents (-8.1% YoY) fell short of our expectations at 94.7% of our FY23e forecast, mainly due to the uncollected rental and coupon income of c.5.5 months amounting to S\$10.5mn at the Guangdong DCs.
- To date, Guangdong Bluesea Data Development (Bluesea), the tenant at Guangdong Data Centre (GDC) 1, 2 & 3, has only settled RMB0.5mn of the RMB48.3mn in arrears. Therefore, we think that Bluesea will likely be unable to meet its rental obligations, and KDCREIT will have to eventually replace the tenant.
- Downgrade from BUY to ACCUMULATE with a lower DDM-derived target price of S\$1.86 from S\$2.26. FY24e, FY25e, and FY26e DPU estimates are cut by 14%, 11%, and 8%, respectively, after we factor in the default and eventual replacement of Bluesea. Organic growth will stem from renewals in FY24e (27.5% of leases expire in 2024); we expect portfolio rental reversions of c.4% for FY24e. Potential catalysts include accretive acquisitions and the collection of rental in arrears from Bluesea. The current share price implies FY24e/25e DPU yields of 5.4%/5.8%.

#### Results at a glance

(SGD mn)	2H23	2H22	YoY	FY23	FY22	YoY	Comments
Gross revenue	140.7	141.8	-0.7%	281.2	277.3	1.4%	Stable due to contributions from acquisitions made in FY22, positive reversions and income escalations; offset by lower contributions from some of Singapore colocation assets arising from higher facilities expenses.
Net property inc.	117.6	129.3	-9.1%	245	253	-3.0%	Higher property expenses due to loss allowance for uncollected rental income from Guangdong DCs.
Finance costs	(25.8)	(18.0)	43.5%	(48.5)	(31.1)	56.1%	
Distributable inc.	76.4	93.7	-18.5%	167.7	184.9	-9.3%	Lower DI also due to higher finance costs and less favourable forex hedges, partially offset by tax savings.
DPU (cents)	4.33	5.17	-16.1%	9.38	10.21	-8.1%	Loss allowance in relation to uncollected rental and coupon income of 5.5 months impacted FY23 DPU by 0.649 cents.

Source: Company, PSR

#### The Positives

**+ Maintained high portfolio occupancy of 98.3% (unchanged QoQ)**, with a portfolio WALE of 7.6 years. 27.5% of leases by rental income will expire in 2024. Leases signed in FY23 were at positive rental reversions. Additionally, some of the leases signed were restructured into power pass-through leases, which should improve NPI margins.

**+ Prudent capital management**, with 74% of debt on a fixed rate. The average cost of debt increased 0.1ppts QoQ to 3.6% in 4Q23, and ICR remains healthy at 4.7x. Only 4% of debt is up for refinancing in 2024 with the majority of debt expiring from 2026 and beyond. Gearing increased 20bps QoQ to 37.4%, still below KDCREIT's internal cap of 40%. Forecast foreign-sourced income is also substantially hedged till Dec 2024.

**+ Stable portfolio valuations (+0.4% yoy), with no write-down for China assets yet.** In local currency terms, higher valuations were achieved in Singapore, Australia, Ireland, Italy, and the Netherlands. KDCREIT has not written-down valuations for the China assets, but we see a risk of impairment should they be unable to recover the rental arrears.

#### ACCUMULATE (Downgraded)

LAST CLOSE PRICE	SGD 1.650
FORECAST DIV	SGD 0.094
TARGET PRICE	SGD 1.860
TOTAL RETURN	18.4%

#### COMPANY DATA

BLOOMBERG CODE:	KDCREIT SP
O/S SHARES (MN) :	1,723
MARKET CAP (USD mn / SGD mn) :	2128 / 2860
52 - WK HI/LO (SGD) :	2.3 / 1.6
3M Average Daily T/O (mn) :	8.18

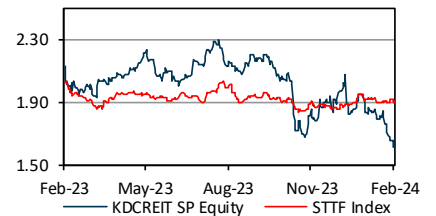
#### MAJOR SHAREHOLDERS (%)

KEPPEL CORP LTD	20.2%
BLACKROCK INC	6.8%
VANGUARD GROUP INC	3.0%

#### PRICE PERFORMANCE (%)

	1MTH	3MTH	YTD
COMPANY	(9.1)	(10.1)	(14.2)
STTF RETURN	(1.4)	(0.8)	(3.0)

#### PRICE VS. STTF



Source: Bloomberg, PSR

#### KEY FINANCIALS

Y/E Dec	FY22	FY23	FY24e	FY25e
Gross Rev. (SGD mn)	277	281	300	312
NPI (SGD mn)	253	245	251	261
Dist. Inc. (SGD mn)	185	168	161	173
P/NAV (x)	1.17	1.23	1.22	1.22
DPU, adj (cents)	10.21	9.38	8.87	9.53
Dist. Yield	6.2%	5.7%	5.4%	5.8%

Source: Company Data, PSR

#### VALUATION METHOD

DDM (Cost of Equity: 7%; Terminal g: 1.75%)

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**+ Positive outcome for DXC litigation**, as the high court ruled in favour of KDCREIT on its interpretation of contractual rights. KDCREIT is claiming S\$3mn from DXC as the sum outstanding from Apr 21 to Dec 21, as well as loss suffered as a result of DXC's refusal to pay for the space it unilaterally gave up from Apr 21 to Mar 25. The dispute is set for trial in February 24 to determine the actual quantum to be paid by DXC to KDCREIT.

#### The Negatives

- **Rentals owed by master lessee at Guangdong DCs.** To date, Bluesea has only settled RMB0.5mn of the RMB48.3mn in arrears, and that excludes the top-up of RMB32.2mn of security deposits that KDCREIT requested. We therefore expect further loss provisions in FY24e. Management is working with Bluesea on a recovery roadmap and is also reserving its rights to terminate the acquisition of GDC 3. There is currently a RMB100mn deposit on GDC 3.

#### Outlook

The global demand for data center space is expected to continue growing due to factors like cloud computing, digital transformation, artificial intelligence, big data, and the Internet of Things. This should benefit KDCREIT, which has a diversified portfolio of data centers in key markets. Inorganic growth opportunities could be the sponsor's Keppel DC Singapore 7 (KDC SGP 7) asset situated at Genting Lane, which is currently being fitted out by the tenant after its completion in 2Q23.

#### **Downgrade from BUY to ACCUMULATE with a lower DDM TP of S\$1.86 from S\$2.26**

KDCREIT's long WALE of 7.6 years is still superior to other asset classes. Its largest tenants are some of the biggest internet enterprises in the world, with its largest contributing 35% of rental income. Catalysts include more accretive acquisitions and the collection of rental in arrears from Bluesea. The current share price implies FY24e/25e DPU yields of 5.4%/5.8%.

## Financials

### Statement of Total Return and Distribution Statement

Y/E Dec, SGD mn	FY21	FY22	FY23	FY24e	FY25e
<b>Gross revenue</b>	<b>271</b>	<b>277</b>	<b>281</b>	<b>300</b>	<b>312</b>
Property expenses	(23)	(25)	(36)	(49)	(51)
<b>Net property income</b>	<b>248</b>	<b>253</b>	<b>245</b>	<b>251</b>	<b>261</b>
Net Finance (Expense)/Inc	(21)	(22)	(38)	(41)	(39)
Manager's fees	(24)	(26)	(27)	(27)	(28)
Other items	(3)	1	(7)	(8)	(8)
FV change, Inv. Properties	151	68	(28)	-	-
<b>Total Return Before Tax</b>	<b>351</b>	<b>265</b>	<b>138</b>	<b>175</b>	<b>187</b>
Taxation	(29)	(31)	(16)	(9)	(9)
<b>Total Return After Tax</b>	<b>322</b>	<b>234</b>	<b>122</b>	<b>166</b>	<b>178</b>
Unitholders	314	231	119	162	174
Non-controlling interest	8	3	4	4	4
Distribution adjustments	(142)	(46)	49	(1)	(1)
<b>Income available for distribution</b>	<b>172</b>	<b>185</b>	<b>168</b>	<b>161</b>	<b>173</b>

### Per unit data

Y/E Dec	FY21	FY22	FY23	FY24e	FY25e
NAV (\$\$)	1.34	1.40	1.34	1.36	1.36
DPU (cents)	9.85	10.21	9.38	8.87	9.53

### Cash Flow

Y/E Dec, SGD mn	FY21	FY22	FY23	FY24e	FY25e
<b>CFO</b>					
<b>Total Return After Tax</b>	<b>322</b>	<b>234</b>	<b>122</b>	<b>166</b>	<b>178</b>
Adjustments	(102)	(2)	111	57	55
WC changes	(22)	(4)	(14)	13	1
<b>Cash generated from ops</b>	<b>198</b>	<b>228</b>	<b>220</b>	<b>236</b>	<b>234</b>
Others	(8)	(10)	(9)	(9)	(9)
<b>Cashflow from ops</b>	<b>190</b>	<b>218</b>	<b>211</b>	<b>228</b>	<b>225</b>

### CFI

Purchase of Inv. propty., net	(196)	(247)	-	-	-
Capex, net	(113)	(48)	(26)	(29)	(29)
Others	(66)	(4)	11	11	11
<b>Cashflow from investments</b>	<b>(374)</b>	<b>(299)</b>	<b>(15)</b>	<b>(18)</b>	<b>(18)</b>

### CFF

Share issuance, net	204	-	-	-	-
Net borrowings	551	518	265	60	100
Distributions	(205)	(178)	(226)	(208)	(206)
Others	(416)	(256)	(275)	(63)	(110)
<b>Cashflow from financing</b>	<b>135</b>	<b>84</b>	<b>(236)</b>	<b>(211)</b>	<b>(216)</b>
<b>Net change in cash</b>	<b>(49)</b>	<b>3</b>	<b>(41)</b>	<b>(2)</b>	<b>(10)</b>
Effects of exchange rate	(1)	(9)	0	-	-
<b>Ending cash</b>	<b>196</b>	<b>190</b>	<b>150</b>	<b>148</b>	<b>138</b>

Source: Company, Phillip Securities Research (Singapore) estimates

### Balance Sheet

Y/E Dec, SGD mn	FY21	FY22	FY23	FY24e	FY25e
<b>ASSETS</b>					
Investment properties	3,401	3,639	3,656	3,685	3,715
Inv. Propty. Under Devmnt.	-	-	-	-	-
Others	117	206	141	138	120
<b>Total non-current assets</b>	<b>3,518</b>	<b>3,845</b>	<b>3,797</b>	<b>3,823</b>	<b>3,835</b>
Cash	196	190	150	148	138
Trade receivables	50	61	54	63	66
Others	16	11	6	6	6
<b>Total current assets</b>	<b>262</b>	<b>263</b>	<b>209</b>	<b>217</b>	<b>210</b>
<b>Total Assets</b>	<b>3,780</b>	<b>4,108</b>	<b>4,007</b>	<b>4,040</b>	<b>4,045</b>
<b>LIABILITIES</b>					
Borrowings	163	175	72	111	287
Trade payables	50	63	70	93	97
Others	7	7	6	6	6
<b>Total current liabilities</b>	<b>221</b>	<b>245</b>	<b>149</b>	<b>210</b>	<b>389</b>
Borrowings	1,136	1,300	1,408	1,357	1,171
Others	-	106	96	89	89
<b>Total non-current liabilities</b>	<b>1,136</b>	<b>1,406</b>	<b>1,504</b>	<b>1,446</b>	<b>1,261</b>
<b>Total Liabilities</b>	<b>1,357</b>	<b>1,651</b>	<b>1,653</b>	<b>1,656</b>	<b>1,650</b>
<b>Net assets</b>	<b>2,423</b>	<b>2,457</b>	<b>2,354</b>	<b>2,384</b>	<b>2,395</b>
<b>Represented by:</b>					
<b>Unitholders' funds</b>	<b>2,293</b>	<b>2,414</b>	<b>2,311</b>	<b>2,339</b>	<b>2,347</b>
Non-controlling interest	42	43	43	46	48

### Valuation Ratios

Y/E Dec	FY21	FY22	FY23	FY24e	FY25e
P/NAV (x)	1.23	1.17	1.23	1.22	1.22
Distribution Yield	6.0%	6.2%	5.7%	5.4%	5.8%
NPI yield	7.7%	7.2%	6.7%	6.8%	7.1%

### Growth & Margins (%)

Growth					
Revenue	2.1%	2.3%	1.4%	6.6%	4.0%
Net property income (NPI)	1.6%	1.8%	-3.0%	2.4%	4.0%
Distributable income	9.4%	7.7%	-9.3%	-3.9%	7.4%
DPU	7.4%	3.7%	-8.1%	-5.4%	7.3%
Investment Property	13.2%	7.0%	0.5%	0.8%	0.8%
Margins					
NPI margin	91.5%	91.1%	87.1%	83.7%	83.7%
Key Ratios					
Gearing (%)	34.4%	35.9%	37.0%	36.3%	36.0%

<b>KDC</b>	<b>ESG Rating</b>	Jan 2024	<b>A-</b>
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SGX: AJBU | Keppel DC REIT



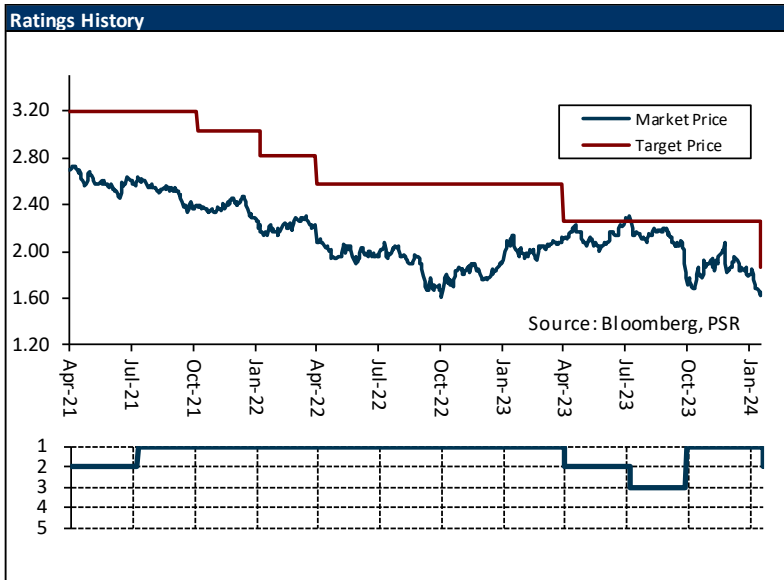
**Company ESG Risk Rating Report**



Objective 1 Managing ESG Risks (Positive input)	Objective 2 Mitigating Negative Externalities (Positive influence)	Objective 3 Measuring Positive Change and Impact (Positive impact)
<b>5.81</b>	<b>5.52</b>	<b>4.46</b>

**Quarterly Update**

- Adjustments to ESG Rating: Objective 2 decreased from 5.85 to 5.52 as decarbonisation and renewables efforts focus only on Dublin and carbon intensity is more than 3 times higher than peer average<sup>1</sup>
- Top 3 ESG indicators that influence our rating. There has been no action or significant change in the following:
  1. Financial impacts of physical climate risks.
  2. Increased use and new sources of renewable energy.
  3. Net Zero target by 2050.



### 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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