



# Keppel DC REIT

## (KDCREIT SP)

### 2Q19 results update; Near term catalysts looked to be priced in

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- **2Q19 results largely within expectations.** Keppel DC REIT (KDC) reported 2Q19 gross revenue of S\$47.5mn (+13.2% YoY), and distributable income of S\$27.2mn (+18.1% YoY).
- **Next in line for benchmark inclusion.** Based on free float market cap, KDC looks to be next in line amongst industrial peers for benchmark inclusion.
- **Third party acquisition likely nearer within the acquisition timeline.** Third party acquisition could see a DPU accretion of c. 7.8% - 10.3% given the debt headroom of S\$298mn and asking cap rate of between 6.0% - 7.0%.
- **Downgrade to NEUTRAL.** We downgrade our recommendation to NEUTRAL as the near term catalysts look to be priced in.

**1H19 revenue makes up 48% of our full year forecast.** 1H19 revenue of S\$95.5mn makes up 48% of our previous FY19 revenue forecast of S\$199.8mn. Our revenue forecast for FY19 increased marginally to S\$200.0mn due to a slight occupancy uplift in KDC Dublin 1. The delay in completion of ICDC 3 East (AU), targeted at 2H20, will not affect our revenue forecast for FY20 at S\$212.8mn.

**Upside from retrofitting works expected in 2H19.** As a recap, KDC3 (SG) and KDC Dublin 2 (IE) are currently undergoing retrofitting and upgrading works to cater to the expansion of existing clients. KDC Dublin 2 will see occupancy increase from 91% to full occupancy after the expansion in 2H19, while KDC3 (SG), which was previously at full occupancy, could see an upside in rental reversions.

**Operating statistics looks largely unchanged.** Basis Bay DC and KDC Dublin remains to be the two low hanging fruits within KDC's portfolio, at occupancy rates of 63% and 62% respectively. KDC Dublin 1 is currently undergoing AEI works, with completion targeted at 2020. A full occupancy rate for KDC Dublin 1 could translate to an additional S\$9mn in annual rent. Capital management remains prudent with a leverage ratio of 31.9%. Debt headroom is currently at S\$298mn based on KDC's internal gearing limit of 40%. We anticipate a marginal increase in KDC's average cost of debt after the refinancing of their SGD denominated loans which makes up 17.1% of total borrowings.

**KDC4 (SG) has yet to stabilise despite favorable supply and demand factors.** Management guided that acquisition of KDC4 (SG) could potentially go through this year, but the data centre has yet to stabilise despite stable demand in Singapore (CAGR of 9.4% between 2018 and 2022). We suspect that a third party acquisition for a foreign data centre could possibly be nearer within the acquisition timeline, given the current debt headroom and an asking cap rate of between 6.0% - 7.0%. An acquisition of that size

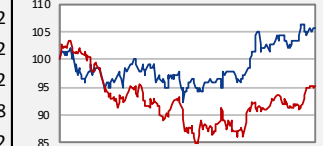
#### Neutral (Downgrade)

Price as of 17 Jul 19 (SGD)	1.71	<b>Performance (Absolute)</b>	
12M TP (S\$)	1.71	1 Month (%)	5.6
Previous TP (S\$)	1.62	3 Month (%)	14.8
Upside, incl div (%)	4.6%	12 Month (%)	30.7

#### Trading data

Mkt Cap (\$mn)	2,312
Issued Shares (mn)	1,352
Vol - 3M Daily avg (mn)	4.2
Val - 3M Daily avg (\$mn)	6.8
Free Float (%)	74.52

#### Perf. vs STI Index (Red)



#### Major Shareholders

Keppel Corp Ltd	25.4%
Sumitomo Mitsui	4.8%
TMB Asset Management	2.6%

#### Previous Recommendations

18-Apr-19	BUY S\$1.62
5-Apr-19	BUY S\$1.62

#### Financials & Key Operating Statistics

YE Dec SGD mn	2017	2018	2019F	2020F	2021F
Gross revenue	139.1	175.5	200.0	212.8	221.4
Net property income	125.1	157.7	180.0	191.5	199.2
Distributable income	82.3	96.1	116.1	120.5	127.5
DPS (SGD cents)	7.1	7.3	7.7	8.0	8.5
DPS growth (%)	16.0	2.8	5.6	3.7	5.9
Div Yield (%)	5.0	5.4	4.5	4.7	5.0
P/NAV (x)	1.0	1.1	1.1	1.1	1.1
Price / Book (x)	1.5	1.3	1.6	1.6	1.5
NPI Margin (%)	90.0	89.8	90.0	90.0	90.0
Net Margin (%)	50.5	83.2	66.1	64.7	65.2
Gearing (%)	31.0	29.9	31.8	31.5	31.0
ROE (%)	6.4	10.1	9.0	9.3	9.5

Source: Company Data, KGI Research

could see a DPU accretion of c. 7.8% - 10.3% based on conservative assumptions. Nonetheless, we think that this is likely priced in by the market at the current trading price.

**Likely next in line for benchmark inclusion.** KDC looks to be next in line, amongst industrial peers, for the inclusion within the FTSE EPRA Nareit Developed Index. Frasers Logistics and Industrial Trust was the latest to be included in Mar 2019. Given the current free float market cap, another acquisition will probably catalyse KDC's inclusion into this benchmark and further improve the REITs visibility to global investors.

#### Valuation & Action:

**Downgrade to NEUTRAL with TP of S\$1.71.** KDC is currently trading at a historical high P/B of 1.6x, and has far outperformed the industrial peer average P/B of 1.2x. We prefer a more conservative price for accumulation and await a catalyst for near term re-rating. We increase our TP from S\$1.62 to S\$1.71 after lowering our cost of equity from 6.7% to 6.5% to reflect a lower risk free rate.

#### Risks:

Continued underperformance of Basis Bay DC (MY); AUD, Euro and pound to continue remaining weak against the SGD

## Financials

INCOME STATEMENT (SGD mn)	2017A	2018A	2019F	2020F	2021F
<b>Gross revenue</b>	<b>139.1</b>	<b>175.5</b>	<b>200.0</b>	<b>212.8</b>	<b>221.4</b>
Property expenses	(13.9)	(17.9)	(20.0)	(21.3)	(22.1)
<b>Net property income</b>	<b>125.1</b>	<b>157.7</b>	<b>180.0</b>	<b>191.5</b>	<b>199.2</b>
REIT Manager's fees	(11.3)	(14.0)	(14.1)	(14.3)	(14.3)
REIT Trustee's fees	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Net interest expense	(13.3)	(15.8)	(15.3)	(15.2)	(15.3)
Other expenses	(15.1)	(9.2)	(10.5)	(16.1)	(16.6)
<b>Net profit/(loss)</b>	<b>85.2</b>	<b>118.4</b>	<b>139.8</b>	<b>145.6</b>	<b>152.8</b>
Change in fair value - investment ppty	(7.6)	32.6	0.0	0.0	0.0
<b>Total return before tax</b>	<b>77.6</b>	<b>151.0</b>	<b>139.8</b>	<b>145.6</b>	<b>152.8</b>
Income tax	(7.3)	(5.0)	(7.7)	(8.0)	(8.4)
Total return after tax	70.3	146.0	132.1	137.6	144.4
<b>Distributable income for the period</b>	<b>82.3</b>	<b>96.1</b>	<b>116.1</b>	<b>120.5</b>	<b>127.5</b>
BALANCE SHEET (SGD mn)	2017A	2018A	2019F	2020F	2021F
Cash and cash equivalents	118.2	128.4	154.7	138.0	171.6
Trade and other receivables	56.2	85.7	97.7	103.9	108.1
Other current assets	3.7	6.1	6.1	6.1	6.1
<b>Total current assets</b>	<b>178.1</b>	<b>220.2</b>	<b>258.5</b>	<b>248.0</b>	<b>285.8</b>
Investment properties	1,570.1	2,028.7	2,048.0	2,076.5	2,078.5
Intangibles, others	15.1	4.0	0.8	0.8	0.8
<b>Total assets</b>	<b>1,763.3</b>	<b>2,252.9</b>	<b>2,307.3</b>	<b>2,325.3</b>	<b>2,365.1</b>
Trade and other payables	48.2	53.2	59.6	63.4	66.0
Other current liabilities	0.0	0.0	0.0	0.0	0.0
<b>Total current liabilities</b>	<b>48.2</b>	<b>53.2</b>	<b>59.6</b>	<b>63.4</b>	<b>66.0</b>
LT Borrowings	546.9	673.1	733.3	733.3	733.3
Other non-current liabilities	51.7	50.6	50.6	50.6	50.6
<b>Total liabilities</b>	<b>646.8</b>	<b>776.9</b>	<b>843.5</b>	<b>847.3</b>	<b>849.8</b>
Unitholders' funds and reserves	1,116.5	1,476.0	1,463.8	1,478.0	1,515.3
<b>Total liabilities and equity</b>	<b>1,763.3</b>	<b>2,252.9</b>	<b>2,307.3</b>	<b>2,325.3</b>	<b>2,365.1</b>
CASH FLOW STATEMENT (SGD mn)	2017A	2018A	2019F	2020F	2021F
<b>Total return before tax</b>	<b>70.3</b>	<b>146.0</b>	<b>132.1</b>	<b>137.6</b>	<b>144.4</b>
Depreciation & Amortisation	7.3	5.0	7.7	8.0	8.4
Other non-cash adjustments	43.8	(7.5)	22.7	22.5	22.6
Changes in working capital	1.1	(29.9)	(5.6)	(2.4)	(1.6)
Taxes paid	(4.7)	(1.7)	(1.7)	(1.7)	(1.7)
<b>Cash flows from operations</b>	<b>117.8</b>	<b>111.9</b>	<b>155.2</b>	<b>164.0</b>	<b>172.1</b>
Capital expenditure	(305.1)	(447.1)	(30.0)	(76.2)	(30.0)
Acquisition of investment properties	0.0	0.0	0.0	0.0	0.0
Other investing cashflow	0.0	(0.8)	0.0	0.0	0.0
<b>Cash flows from investing</b>	<b>(305.1)</b>	<b>(447.9)</b>	<b>(30.0)</b>	<b>(76.2)</b>	<b>(30.0)</b>
Borrowings raised / (repaid)	84.9	129.3	0.0	0.0	0.0
Equity raised / (bought back)	(0.9)	302.7	0.0	0.0	0.0
Dividends paid	(74.3)	(84.8)	(98.9)	(104.5)	(108.4)
Other financing cashflow	-	-	0.0	0.0	0.0
<b>Cash flows from financing</b>	<b>9.7</b>	<b>347.2</b>	<b>(98.9)</b>	<b>(104.5)</b>	<b>(108.4)</b>
FX Effects, Others	(0.2)	1.1	0.0	0.0	0.0
<b>Net increase in cash</b>	<b>(177.9)</b>	<b>12.3</b>	<b>26.3</b>	<b>(16.7)</b>	<b>33.6</b>
Beginning Cash	294.0	116.1	128.4	154.7	138.0
<b>Ending cash</b>	<b>116.1</b>	<b>128.4</b>	<b>154.7</b>	<b>138.0</b>	<b>171.6</b>
KEY RATIOS	2017A	2018A	2019F	2020F	2021F
DPS (SGD cents)	7.1	7.3	7.7	8.0	8.5
Dividend yield (%)	4.98	5.42	4.52	4.69	4.97
NAV per share (SGD cents)	1.0	1.1	1.1	1.1	1.1
Price/NAV (x)	1.5	1.3	1.6	1.6	1.5
<b>Profitability (%)</b>					
NPI Margin	90.0	89.8	90.0	90.0	90.0
Net Margin	50.5	83.2	66.1	64.7	65.2
ROE	6.4	10.1	9.0	9.3	9.5
ROA	4.0	6.5	5.7	5.9	6.1
<b>Financial Structure</b>					
Interest Coverage (x)	6.8	8.1	9.7	10.0	10.5
Gearing (%)	31.0	29.9	31.8	31.5	31.0

Source: Company Data, KGI Research

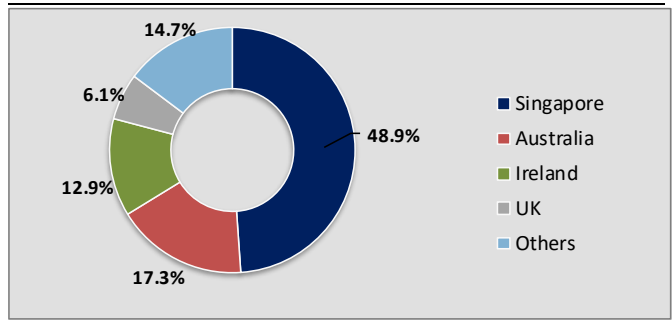
## Company Snapshot

**Figure 1: Company profile**

Keppel Data Centre Real Estate Investment Trust (KDCREIT) is a Singapore real estate investment trust (REIT) listed on Singapore Exchange Securities Trading Limited (the SGX-ST) since 10 December 2014. Its investment strategy is principally to invest in a portfolio of income-producing data centres globally. The REIT is managed by Keppel DC REIT Management Pte. Ltd., (the Manager) which is partly owned by the Sponsor, Keppel Telecommunications & Transportation Ltd (Keppel T&T), part of the Keppel Group.

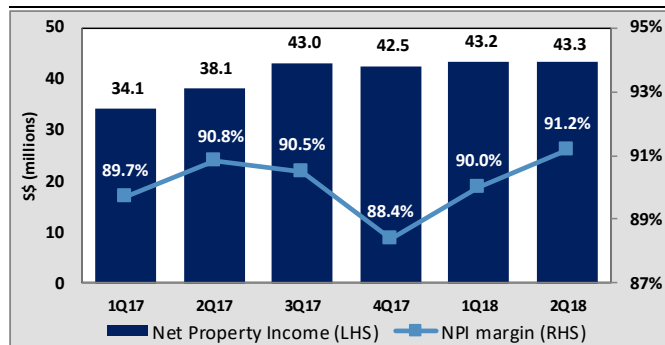
Source: Company

**Figure 2: Portfolio breakdown by NLA**



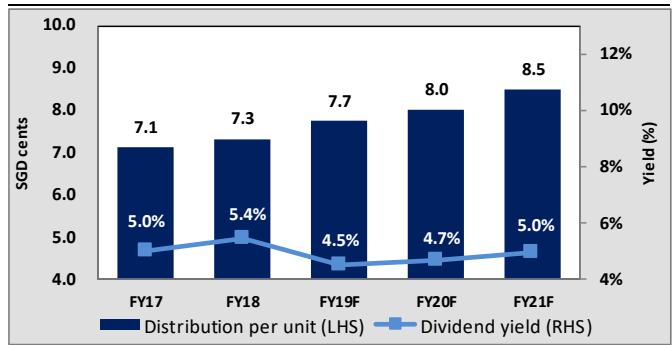
Source: Company Data, KGI Research

**Figure 3: NPI vs NPI margins**



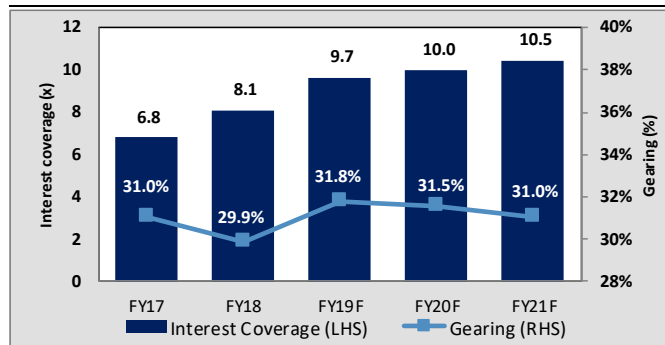
Source: Company Data, KGI Research

**Figure 4: DPU and Dividend yield**



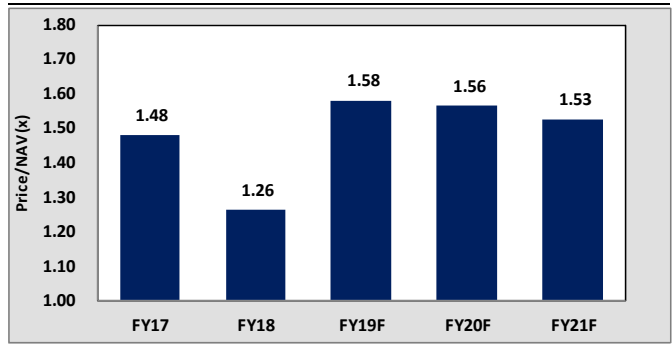
Source: Company Data, KGI Research

**Figure 5: Interest coverage and gearing**



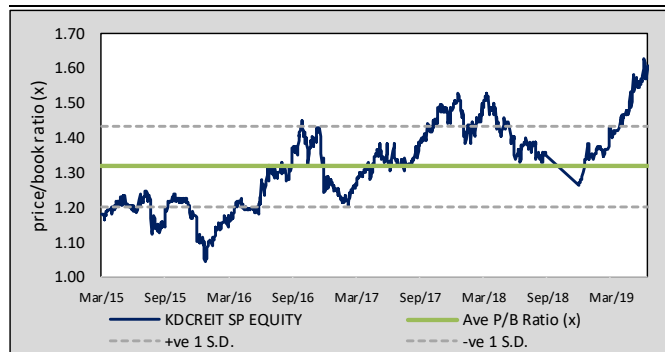
Source: Company Data, KGI Research

**Figure 6: Price/NAV**



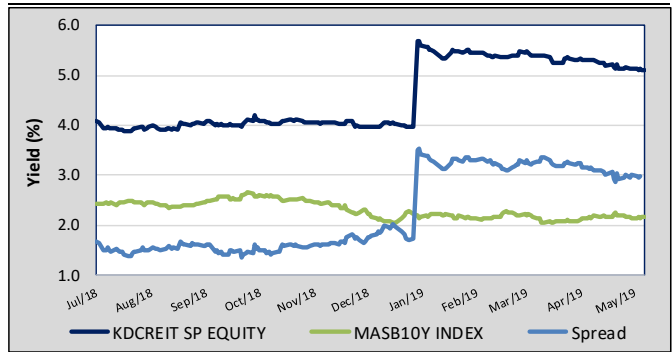
Source: Company Data, KGI Research

**Figure 7: Historical P/B band since IPO**



Source: Bloomberg, KGI Research

**Figure 8: Yield Spread above 10Y Government Bond**



Source: Bloomberg, KGI Research

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<b>Outperform (OP)</b>	We take a positive view on the stock. The stock is expected to outperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
<b>Neutral (N)</b>	We take a neutral view on the stock. The stock is expected to perform in line with the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
<b>Underperform (U)</b>	We take a negative view on the stock. The stock is expected to underperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
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