

## COMPANY RESULTS

### Digital Core REIT (DCREIT SP)

2H22: Business And Share Price Turning Around

DCREIT's 2H22 results were in line with expectations with its 10 data centres maintaining occupancy of 98%. It has completed the acquisition of a 25% interest in a freehold data centre in Frankfurt for US\$150m in Dec 22, which is accretive to DPU by 2.0%. Demand for data centre capacity could rise due to increased usage of artificial intelligence. DCREIT provides a distribution yield of 5.7% for 2023F (KDCREIT: 4.9% and MINT: 5.6%). Maintain BUY. Target price: US\$0.97.

#### 2H22 RESULTS

Year to 31 Dec (US\$m)	1H22 Actual	Forecast*	Variance (%)
Gross Revenue	54.9	53.0	+3.6
Net Property Income	34.0	33.4	+1.6
Distributable Income	21.5	23.8	-9.4
DPU (US cents)	1.92	2.09	-8.1

Source: DCREIT, UOB Kay Hian \*Derived based on full year forecast for 2022 as disclosed in DCREIT's IPO prospectus divided by two.

#### RESULTS

- Digital Core REIT (DCREIT) reported DPU of 3.98 US cents for 2022, which is 4.8% below forecast disclosed in the IPO prospectus but in line with our expectations.
- Stability from long WALE.** DCREIT maintained portfolio occupancy at 98%. Portfolio weighted average lease expiry (WALE) is long at 4.5 years. All its leases contain cash rental escalation of 1-3% (weighted average: 2%).
- Completed maiden acquisition in Dec 22.** DCREIT has completed the acquisition of a 25% interest in a state-of-the-art freehold data centre in Frankfurt for US\$150m in Dec 22. Frankfurt is the second largest data centre market in Europe. Capitalisation rate is 4.5% for the Frankfurt facility. The Frankfurt facility's occupancy is 91.3% as of Jun 22 (vacancy: 8.7%). The acquisition will add nine new customers, bringing DCREIT's total number of customers to 25 post-acquisition. Yield improves from 4.5% to 5.0% when the vacant spaces are leased-up and backfilled. The data centre has in-place contractual rental escalation averaging 1.6%. The deal is expected to be accretive to DPU by 2.0%.
- Creating value by buying back units.** DCREIT repurchased 10.7m units under its unit buyback mandate at a 30% discount to NAV with an average price of US\$0.585, which were initially held as treasury units and subsequently cancelled in Jan 23. The buyback of units delivered 1% DPU accretion but only added 0.4ppt to its aggregate leverage.
- NAV per unit dropped 4.6% to US\$0.83.** Portfolio valuation declined about 1.1% due to capitalisation rate expansion of 25bp to 4.5%, which was partially offset by increase in valuation for data centres in Northern Virginia due to market rent growth.

#### KEY FINANCIALS

Year to 31 Dec (US\$m)	2021	2022	2023F	2024F	2025F
Net turnover	n.a.	115	111	111	112
EBITDA	n.a.	72	72	72	73
Operating profit	n.a.	72	72	72	73
Net profit (rep./act.)	n.a.	13	43	43	43
Net profit (adj.)	n.a.	42	44	43	42
EPU (US\$ cent)	n.a.	3.7	3.9	3.8	3.7
DPU (US\$ cent)	n.a.	4.0	3.9	4.0	4.0
PE (x)	n.a.	18.2	17.4	18.1	18.4
P/B (x)	n.a.	0.8	0.8	0.8	0.9
DPU Yld (%)	n.a.	5.9	5.7	5.9	6.0
Net margin (%)	n.a.	11.7	38.6	38.5	38.0
Net debt/(cash) to equity (%)	n.a.	50.3	52.9	55.5	58.4
Interest cover (x)	n.a.	6.7	3.3	3.0	3.0
ROE (%)	n.a.	n.a.	4.6	4.7	4.7
Consensus DPU (US\$ cent)	n.a.	n.a.	3.9	4.0	n.a.
UOBKH/Consensus (x)	-	-	0.99	1.00	-

Source: Digital Core REIT, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	US\$0.68
Target Price	US\$0.97
Upside	+42.6%
(Previous TP)	US\$0.90)

#### COMPANY DESCRIPTION

DCREIT is a pure-play data centre REIT. Its portfolio comprises 10 freehold data centres concentrated within top-tier markets in the US (North Virginia, Silicon Valley and Los Angeles) and Canada (Toronto) with an appraised valuation of US\$1.4b. Its sponsor Digital Realty is the world's largest data centre owner and operator.

#### STOCK DATA

GICS sector	Real Estate
Bloomberg ticker:	DCREIT SP
Shares issued (m):	1,123.3
Market cap (US\$m):	763.9
Market cap (US\$m):	763.9
3-mth avg daily t'over (US\$m):	1.5

#### Price Performance (%)

52-week high/low		US\$1.16/US\$0.50		
1mth	3mth	6mth	1yr	YTD
23.6	29.5	(19.5)	(41.4)	23.6

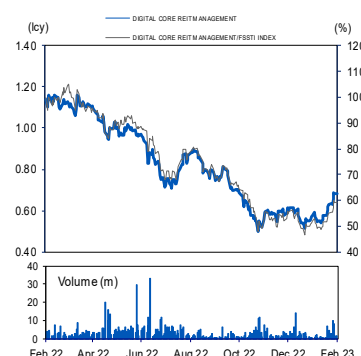
#### Major Shareholders

Digital Realty Trust	35.0
Sumitomo Mitsui Fin	7.0

FY23 NAV/Share (US\$) 0.82

FY23 Net Debt/Share (US\$) 0.43

#### PRICE CHART



Source: Bloomberg

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- **Balance sheet flexibility is preserved** with aggregate leverage at 34.0% post acquisition of 25% interest in Frankfurt data centre (Sep 22: 26.2%). Weighted average cost of debt deteriorated from 3.1% to 3.9%. The proportion of interest rate exposure increased from 50% to 75%.

### STOCK IMPACT

- **Data centre fundamentals continue to strengthen.** According to datacenterHawk, market vacancy is in the low- to mid-single digits across DCREIT's five core markets. Northern Virginia, which accounts for 35% of rental income, remains supply constrained and vacancy is very tight at 1%.
- **Growth from data centre as infrastructure of new economy.** Demand for data centres is not directly linked to head count of technology companies, who are encountering short-term headwinds. Companies will continue to expand their digital infrastructure, which leads to increased demand for data centres. Demand for data centre capacity could also rise due to increased usage of artificial intelligence.
- **Able to scale up due to sizeable sponsor pipeline.** Sponsor Digital Realty has a network of 291 data centres with net rentable square feet (NRSF) of 35.8m sf across 47 metropolises in 24 countries on six continents. DCREIT is the exclusive S-REIT vehicle of Digital Realty. The sponsor has granted DCREIT a global right of first refusal (ROFR) on its growing data centre pipeline worth over US\$15b (existing: US\$10b, under construction: US\$5b).
- **Secured replacement tenant.** One of DCREIT's customers who occupied 37,000nrsf in Toronto filed for bankruptcy protection in Apr 22. The customer has vacated the data centre on 1 Jan 23. DCREIT has executed a short-term lease agreement with an investment grade cloud service provider covering half the bankrupt customer's rental obligation. It is working closely with the sponsor's sales team to backfill the remaining vacant space.

### EARNINGS REVISION/RISK

- We trimmed our 2023 DPU forecast by 0.8% after factoring in higher interest rates and cancellation of 10.7m treasury units.

### VALUATION/RECOMMENDATION

- **Maintain BUY.** Our target price of US\$0.97 is based on DDM (cost of equity: 6.75%, terminal growth: 2.8%).
- **Pure play on data centres.** DCREIT provides a distribution yield of 5.7% for 2023F (KDCREIT: 4.9% and MINT: 5.6%). It deserves to trade at a premium as it is a pure play on data centres with acquisition-led growth supported by Digital Realty.

### SHARE PRICE CATALYST

- Organic growth from cash rental escalation of 1-3% (weighted average: 2%).
- Yield accretive acquisitions tapping on sponsor's large and growing data centre pipeline.

### KEY OPERATING METRICS – DCREIT

	1Q22	2Q22	3Q22	4Q22	yoy % Chg	qoq % Chg
DPU (US cents)	n.a.	2.06	n.a.	1.92	n.a.	-6.8%
Occupancy	100.0%	100.0%	100.0%	98.0%	-2ppt	-2ppt
Aggregate Leverage	26.0%	25.7%	26.2%	34.0%	7ppt	7.8ppt
Average Cost of Debt	2.1%	2.3%	3.1%	3.9%	2.7ppt	0.8ppt
WALE by Annualised Rents (years)	5.5	5.2	5.0	4.5	-1.7yrs	-0.5yrs
Weighted Average Debt Maturity (years)	4.7	4.4	4.2	3.6	-1.1yrs	-0.6yrs
% of Borrowings in Fixed Rates	50%	50%	50%	75%	75ppt	25ppt

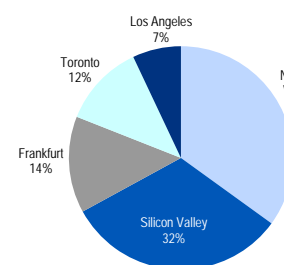
Source: DCREIT, UOB Kay Hian \* hoh % chg for DPU

### FRANKFURT FACILITY



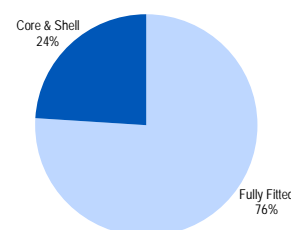
Source: DCREIT

### RENTAL INCOME BY CORE MARKET (DEC 22)



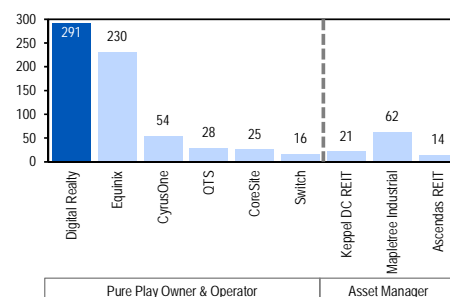
Source: DCREIT

### RENTAL INCOME BY PROPERTY TYPE (DEC 22)



Source: DCREIT

### NUMBER OF DATA CENTRES



Source: DCREIT

**PROFIT & LOSS**

Year to 31 Dec (US\$m)	2022	2023F	2024F	2025F
Net turnover	115.0	110.7	111.4	112.2
EBITDA	71.8	71.5	72.0	72.6
Deprec. & amort.	0.0	0.0	0.0	0.0
EBIT	71.8	71.5	72.0	72.6
Associate contributions	(0.5)	6.3	6.4	6.5
Net interest income/(expense)	(10.6)	(21.8)	(23.7)	(24.5)
Pre-tax profit	31.9	54.9	55.1	55.0
Tax	(13.1)	(6.6)	(6.4)	(6.4)
Minorities	(5.3)	(5.5)	(5.7)	(5.9)
Net profit	13.4	42.8	42.9	42.6
Net profit (adj.)	42.2	43.8	42.5	42.2

**BALANCE SHEET**

Year to 31 Dec (US\$m)	2022	2023F	2024F	2025F
Fixed assets	1,423.8	1,426.3	1,428.8	1,431.3
Other LT assets	154.2	154.2	154.2	154.2
ST debt	n.a.	n.a.	n.a.	n.a.
Cash/ST investment	25.2	31.7	30.8	33.2
Other current assets	9.3	8.2	8.3	8.3
<b>Total assets</b>	<b>1,612.6</b>	<b>1,620.5</b>	<b>1,622.1</b>	<b>1,627.0</b>
Other current liabilities	25.9	20.5	20.6	20.7
LT debt	495.0	520.0	535.0	555.0
Other LT liabilities	14.6	14.6	14.6	14.6
Shareholders' equity	934.9	922.7	909.0	893.6
Minority interest	142.1	142.6	142.9	143.1
<b>Total liabilities &amp; equity</b>	<b>1,612.6</b>	<b>1,620.5</b>	<b>1,622.1</b>	<b>1,627.0</b>

**CASH FLOW**

Year to 31 Dec (US\$m)	2022	2023F	2024F	2025F
Operating	77.6	49.1	55.3	54.7
Pre-tax profit	1.5	31.1	31.2	30.8
Tax	(2.5)	(2.5)	(2.5)	(1.5)
Working capital changes	14.5	(4.3)	0.1	0.1
Non-cash items	(17.8)	10.0	10.1	10.1
Other operating cashflows	81.9	14.8	16.4	15.2
Investing	(1,452.3)	(2.5)	(2.5)	(2.5)
Capex (growth)	(1,294.7)	0.0	0.0	0.0
Capex (maintenance)	(2.6)	(2.5)	(2.5)	(2.5)
Investments	(68.9)	0.0	0.0	0.0
Others	(86.1)	0.0	0.0	0.0
Financing	1,400.0	(40.1)	(53.7)	(49.8)
Distribution to unitholders	(26.7)	(43.3)	(45.0)	(46.2)
Issue of shares	977.4	0.0	0.0	1.0
Proceeds from borrowings	497.5	25.0	15.0	20.0
Others/interest paid	(48.2)	(21.8)	(23.7)	(24.5)
Net cash inflow (outflow)	25.2	6.5	(1.0)	2.4
Beginning cash & cash equivalent	0.0	25.2	31.7	30.8
Ending cash & cash equivalent	25.2	31.7	30.8	33.2

**KEY METRICS**

Year to 31 Dec (%)	2022	2023F	2024F	2025F
<b>Profitability</b>				
EBITDA margin	62.5	64.6	64.7	64.7
Pre-tax margin	27.8	49.6	49.4	49.0
Net margin	11.7	38.6	38.5	38.0
ROA	n.a.	2.6	2.6	2.6
ROE	n.a.	4.6	4.7	4.7
<b>Growth</b>				
Turnover	n.a.	(3.7)	0.7	0.7
EBITDA	n.a.	(0.4)	0.7	0.7
Pre-tax profit	n.a.	72.1	0.4	(0.3)
Net profit	n.a.	218.6	0.5	(0.7)
Net profit (adj.)	n.a.	3.7	(2.9)	(0.7)
EPU	n.a.	4.5	(3.5)	(1.8)
<b>Leverage</b>				
Debt to total capital	31.5	32.8	33.7	34.9
Debt to equity	53.0	56.4	58.9	62.1
Net debt/(cash) to equity	50.3	52.9	55.5	58.4
Interest cover (x)	6.7	3.3	3.0	3.0

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