Market Insight Report Reprint

Datacenter REITs spending more on capex, with guidance suggesting further increases

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Datacenter operators have inherently elevated capex requirements. Our expectations for intensifying investment were generally confirmed by recent quarterly results and forward guidance from the five US datacenter REITs, which reported first-quarter results that were in-line with or better than Wall Street expectations.

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Introduction

All five datacenter REITs trading publicly in the US reported first quarter results that were generally in line with or better than Wall Street expectations. Sequential growth rates were impressive, even on a year-over-year basis, since this quarter's results lap the last partially pre-COVID quarter (1Q 2020) used for comparison.

Digital Realty saw its core FFO increase 9% year-over-year, and Equinix saw its 1Q AFFO best the fourth quarter of 2020 by more than 20%. CoreSite experienced 8.5% year-over-year growth in FFO, and 4.5% higher levels compared to the fourth quarter. QTS reported operating FFO that was 27.5% higher than the comparable quarter of 2020, and CyrusOne reported normalized FFO up 8% versus 1Q 2020 (but only 3% on a diluted per-share basis).

We take a particular interest in what these operators are spending on capital expenditures, and what they communicate to shareholders on an expectational basis. Here, we dive into some of the details as reported or released by the REITs in their earnings announcements and quarterly filings.

THE 451 TAKE

As the world in 2020 grappled with the pandemic, enterprises shifted their processes and infrastructure toward digitalization at rates not previously seen. This resulted in strong demand for datacenter space from cloud and IT service providers. The momentum in business strength witnessed by many datacenter operators in 2020 seems to be persisting, as indicated in recent earnings results posted by publicly traded US datacenter REITs. However, accelerating growth in the industry requires operators to successfully grow, evolve and maintain their IT infrastructure, all of which requires significant capital outlays. We have been monitoring such capital allocations as they rise organically through the process of digital transformation (even prior to the global pandemic), but the increased demand is driving capex higher. We will continue to follow these numbers as a leading indicator of new builds and expansions to come.

Equinix

Equinix spent $564m on capex during the first quarter of 2021, with $235m allocated to EMEA, $205m to the Americas, and $123m to APAC. This compares to $2.3bn spent on capex in all of 2020, with $867m going to the Americas, $888m going to EMEA, and $527m to APAC. Annualizing the latest quarterly figures produces an estimate that is already in line with 2020 levels: $2.3bn across all geographic segments; $940m EMEA, $820m Americas, $492m APAC. The vast majority of capital spend during the first quarter was nonrecurring capex, at $544m, with the remaining $20m accruing to recurring capex.

In total, these funds were responsible for adding 7,400 retail colocation cabinets across eight new projects. The company also acquired brownfield sites for redevelopment in both Montreal and Mexico City. On its earnings call, the company's CFO seemed to imply that analysts should net out capex against its hyperscale xScale investments, due to the fact that it anticipates recovering those amounts in the future. Excluding xScale-related outlays, nonrecurring capex is expected to range from $2.125bn to $2.315bn for full-year 2021 (with expected recurring capex between $175m and $185m). Guidance inclusive of these capital outlays calls for 2021 capex of between $2.725bn and $2.975bn.

Digital Realty

Digital Realty spent 35% more on capex in the first quarter of 2021 ($479m) over the same period in 2020 ($355m). Most of this was development costs (up 37% on their own, with $158m of the total $440m accruing to Interxion), with only $40m recurring. In its earnings call, the company's CEO noted the organization currently has 44 development projects totaling more than 300MW to be delivered over the next 18 months.

CoreSite

CoreSite spent $29.7m on capital expenditures during the first quarter of 2021. Approximately $20m went to datacenter expansion activity, another $4.2m went to recurring capex for its colocation facilities, and another $2.8m was spent on tenant improvements. Of the $20m that went to fund datacenter expansions, $5.4m was used in Chicago ($4.7m of which funded the purchase of a parking lot adjacent to the company's CH2 facility, presumably for expansion purposes). CoreSite's LA3 and NY2 (Secaucus) facilities were also top recipients of capex.

Annualizing the quarterly $29.7m of capex produces a value of $119m, well below the company's 2021 capex guidance provided in its supplemental materials (range of $185m to $225m with a midpoint of $205m). Presumably, an acceleration in capex spend is planned in order for the company to hit this target by year end.

QTS

In the first quarter of 2020, QTS has spent less than a quarter of the amount it spent during the same quarter last year on acquisitions ($1.8m vs $0.4m). However, development capex was up 28% year-over-year. Maintenance capex and what the company buckets into 'other capital expenditures' (which includes capitalized interest, commissions, personal property, overhead costs, and corporate fixed assets such as corporate offices, leasehold improvements and product-related assets) were up 2.5% and 8.8% y/y, respectively.

QTS expects further development capital expenditures (excluding acquisitions) in 2021 to come in between $660m and $760m, but notes a significant chunk of this spend is discretionary and may ultimately not come to fruition.

CyrusOne

The one outlier to the bunch is CyrusOne, which actually saw a decline in capex spend in the first quarter of 2021 relative to the first quarter of 2020, coming in at $175.4m (versus $196.5m one year ago). Of the $175.4m, $172.8m was related to the development and construction of datacenters.

The money was primarily spent on land acquisitions and development activities in Dublin, Frankfurt, London, New York, Northern Virginia, Paris, Phoenix and San Antonio, Texas. (While Dublin, New York, Paris and San Antonio are new mentions, projects in Amsterdam, Austin, Dallas and Raleigh-Durham, North Carolina, are no longer on the list as areas of primary focus). In February, CyrusOne began developing a new 18MW (130,000 square foot) facility in London, which it will lease for 20 years.

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