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New capacity in the pipeline

The Star, Malaysia



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THE data centre industry globally is seeing a major boost in new builds driven by demand from digitalisation, geopolitics and expectations for the potential artificial intelligence (AI) could present.

Asean has already received proposals for 1.5 gigawatt (GW) of new builds, which would more than double the region's current 1.2GW capacity, including some 1,146.2 megawatt (MW) of proposed new data centre capacity in Malaysia.

More new capacity is in the pipeline, especially in Johor and the Klang Valley.

Microsoft's Satya Nadella was Santa Clause-like in his recent three-nation tour to Malaysia, Indonesia and Thailand, promising billions in investments by the hyperscaler including some US\$2.2bil of investments in cloud computing and AI in Malaysia over the next four years.

Not surprisingly, the data centre thematic has seen the stock prices of companies like YTL Power International Bhd, YTL Corp Bhd, Sunway Construction Group Bhd, VSTECs Bhd and SNS Network Technology Bhd, among others, rally over the past year, driven by bullish expectations.

"The stock prices of many of the companies have run way

ahead of their fundamentals. Many investors seem prepared to invest in the future by paying a premium now. Market action is predictable in some sense.

"You only have to look back to the Covid-19 pandemic period to recall that there were analysts forecasting the share prices of glove makers like Top Glove Corp Bhd could rise above RM50 a share including one forecast of RM110 – we know how that turned out," warned an analyst with a local brokerage.

YTL Power's share price is up some 350% to hit a historic high of RM5.04 while parent YTL Corp is up 400% at RM3.41. VSTECs, meanwhile, is up 165% year-on-year at RM3.45 after hitting a historic high of RM3.88 on being named an Amazon Web Services (AWS) distributor in Malaysia.

SNS' share price has doubled in the past year as, like VSETCS, it is seen as a potential supplier of server hardware to the new build data centres. Analysts say other names linked to the thematic include Natiogate Holdings Bhd, Telekom Malaysia Bhd, MN Holdings Bhd, Critical Holdings Bhd and HE Group Bhd, among many more.

Rakuten Trade head of equity sales Vincent Lau remains bullish on the belief the rise in the data centre thematic stocks could be sustainable.

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TNB will benefit from power demand

"Covid-19 was a one-off event but technology is here to stay and drive change in the economy and lives of people.

"Although the data centres may present one-off investments, they will nevertheless offer income opportunities to the various listed companies for power, equipment and services," he tells *StarBizWeek*.

This would come in the form of construction contracts, demand for power, server spend, network spend and storage spend, in particular

From a valuation perspective and despite having risen substantially, YTL Power is now trading at 12 times its trailing price-earnings (PE) multiple and well below peers in the power sector like Tenaga Nasional Bhd (TNB) at 25 times PE, which means the former could still advance further, backed by an improving outlook for its utilities business locally and abroad (Wessex Water).

An analyst at HLIB Research

expects YTL Power's data centre business, with its new build capacity set to be commissioned this year, to become the main earnings driver for the company, and in extension YTL Corp's, in the financial years ahead.

The research house now has a target price of RM5.55 a share on YTL Power but a revision could be on the cards if the data centre business earnings hit RM1bil by the financial year ending June 30, 2026.

Nvidia and YTL Power are investing US\$4.3bil in AI, cloud computing and supercomputer infrastructure in Malaysia. The first phase of the project is expected to be operational by mid-2024.

That said, JP Morgan, in a report on the data centre gold rush in the region, said the new builds could transition to destruction in value for data centre investors.

"In our view, heavy builds and capital deployment are likely to

erode economic returns for the data centre industry. Many markets could see an expansion in already high vacancy rates. Data centre operators with undifferentiated services will be susceptible to price competition and compression in rental rates," the international investment bank said.

The bank noted that Kuala Lumpur has a 17% colocation vacancy rate at present and the new builds with an undifferentiated service will face downside risks to rental rates and internal rate of returns from price competition, more so when hyperscalers turn from customers to competitors by building their own data centres.

The intense competition in an already crowded field could see certain data centres face obsolescence. It highlighted geopolitics, however, could create new technology hubs and distort current market demand forecasts, and

warned that while AI could be a driver of future demand, there is limited evidence of significant AI adoption.

JP Morgan, however, added that demand for interconnection between data centres can create network effects. Interconnection results in higher performance and lower costs, driving demand from customers.

As customers for interconnected data centres grow, it could bring incremental demand from their ecosystem partners as co-locations can result in better performance and lower costs.

That said, for a lower risk exposure to the data centre thematic, JP Morgan believes companies like TNB will benefit from power demand while Gamuda Bhd could win contracts to construct the proposed data centre facilities.

Contract up for grabs include the RM9bil (300MW) facility by EdgeConneX, RM3bil (65MW) by

NextDC and RM13bil (256MW) by Vantage DC.

TNB has signed 635MW electricity supply agreements for nine new data centre projects, with another 2,300MW potential demand in the pipeline.

The data centre thematic is providing many companies with land in the right locations to unlock value.

Only this week, Paragon Globe Bhd for instance has inked a sale and purchase agreement with Bridge Data Centres Malaysia IV Sdn Bhd for a proposed disposal of a 19.36-hectare land in Plentong, Johor, for RM238.32mil, booking a gain of RM68.47mil on flipping the land that was acquired last November for RM71.5mil

Bridge Data Centre has plans to invest RM2.5bil over the next five years to expand its data centre capacity across Malaysia.

Crescendo Corp Bhd is another company that sold land parcels in Johor to Microsoft Malaysia for some RM448mil in the past few months.