Research Report

MINNEAPOLIS-ST. PAUL DATA CENTER

2016 Review | 2017 Forecast

Colliers INTERNATIONAL

Accelerating success.

Colo, Clouds and Data Center Investment Point to Future of Industry

LOCAL COLOCATION ABSORPTION

LOCAL COLOCATION PRICING

CLOUD MIGRATION

SALE/ LEASEBACK CAP RATES

Colocation Data Center Leases Have Active Year

Colocation data center deals were on the rise in the Minneapolis/ St. Paul market in 2016. The U.S. Bank/Stream data center build-to-suit with Stream, located in Chaska and announced in December, rounded out the year. Colocation deals completed at providers such as Cologix and Databank, continued to help absorb approximately 5.5. mW of existing turnkey inventory and helped to justify expansion into new space. While more national searches considered the Minneapolis market in 2016, most activity still came from local companies looking for local solutions. By end of year, some enterprise requirements continued to "explore their options" and others decided to renew in existing locations. The general consensus was local third-party service providers offer the most competitive options for outsourcing data center operations.

Industry Sales Transactions

Industry-wide data center acquisitions totaled just under $2 billion dollars in 2016 leading to a very active year. Large giants like Verizon and Centurylink both found buyers for their data center assets expecting to close in 2017. This activity could lead total acquisition dollar values for 2017 to triple. In 2016, other investors and operators such as Equinix, Digital Realty, GI Partners and OTS all made large acquisitions. In February, colocation operator Cologix was acquired by private equity firm, Stonepeak. Additionally, Databank was acquired by Data Bridge with an expansion plan that will move them into new markets.

Locally, data center sales transactions were minimal; instead many enterprise data users continue to evaluate data center sale-leaseback or partial leaseback scenarios.

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Future Trends

› More Clouds on the Horizon

More workloads went to the Cloud in 2016 with the trend expected to continue into 2017. In 2016, large Cloud providers such as AWS and Microsoft teamed up with colocation facility operators to enable both providers to offer a local connection to Cloud enabled services and hybrid solutions at one location. What remains to be seen is the way companies reconcile the total cost of operation once users determine the best mix of network, storage and computing outsourcing vs. the optionality and elasticity the Cloud offers.

› Future Accounting Rules will affect Data Center Decisions today

Starting in late 2018, new accounting rules issued by the Financial Accounting Standards Board will require companies to report operating leases on their balance sheet. The rule will affect real estate and equipment leases for data centers on leases that are longer than one year. Historically, data center costs have been steered toward operating costs (leases) as a way to manage financial reporting that does not negatively affect a company's balance sheet and credit rating.

› Buy vs. Lease

With leasing now being added to the balance sheet, future commitments of space and power will cause data centers to take a fresh look at buying vs. leasing. From a financial liability perspective, owning data centers could be considered similar to leasing when it comes to the importance of operational expertise and company. Structuring lease deals that will not penalize a company for booking unused capacity commitments will allow for less impact on the balance sheet. This scenario could tip financial preference back to leasing.

Aligned Data Centers has written an informative whitepaper on the subject. It offers more in-depth insights on the rule should you consider a renewal or new agreement with a data center services provider.

Data Center REITs Find Footing

Shares in Data Center Real Estate Investment Trusts (Data Center REITS) can be bought and sold like stocks of other companies that own income producing real estate. REITS are offered in asset classes such as office, industrial, and retail properties. More specialized categories like health care and self-storage REITS give investors the ability to focus on niches within commercial real estate. Data center REITs have emerged as a niche REIT with established asset class staying power.

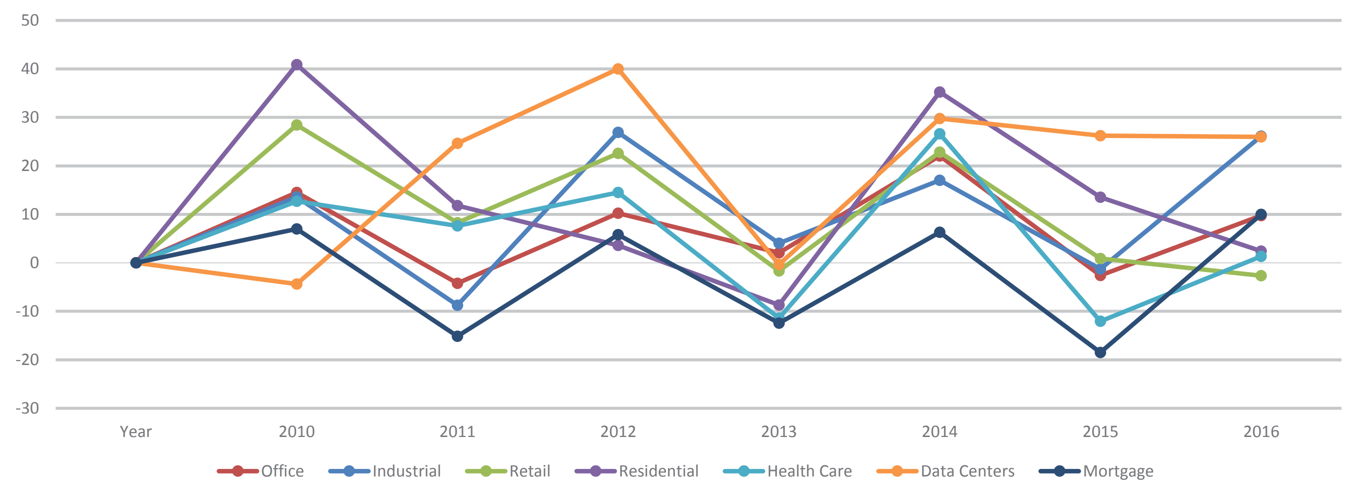
The six publicly traded Data Center REITs are diverse and different in their strategies, profiles and locations. Some REITs focus on large-scale deployments in large wholesale data center markets and others provide smaller leases in multiple markets. Many have pivoted toward hybrid and cloud offerings to incorporate more services and address more client needs.

Long-Term Stability

The data center REITs have been solid performers in their short history when valuing performance of these stocks in comparison to other product segment REITs. After finding their legs in the early existence of the segment, the data center REITs performance has mirrored performance of health care, office, industrial, retail and mortgage REITs over the last three years. Certain stocks, such as CoreSite (COR) has outperformed on a year over year increase percentage better than the other five currently available –CyrusOne, Digital Realty, Dupont Fabros, Equinix and QTS.

Looking ahead, factors affecting all REITS (dividend yield, maintenance costs and price change) may factor more heavily in data centers because of their expensive infrastructure operations but ultimately we believe the Data Center REITS will be seen as a stable investment category for the long term.

Historical Stock Performance



Colliers Minneapolis-St. Paul Technology Services maintains a proprietary database of available data center space. For additional information and to access this data please contact:

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