Securitized Products Special Topics

Data Centers: Takeaways from 2023-Vintage Deals

No Longer Niche, Data Center Deals Offer Diverse Exposures

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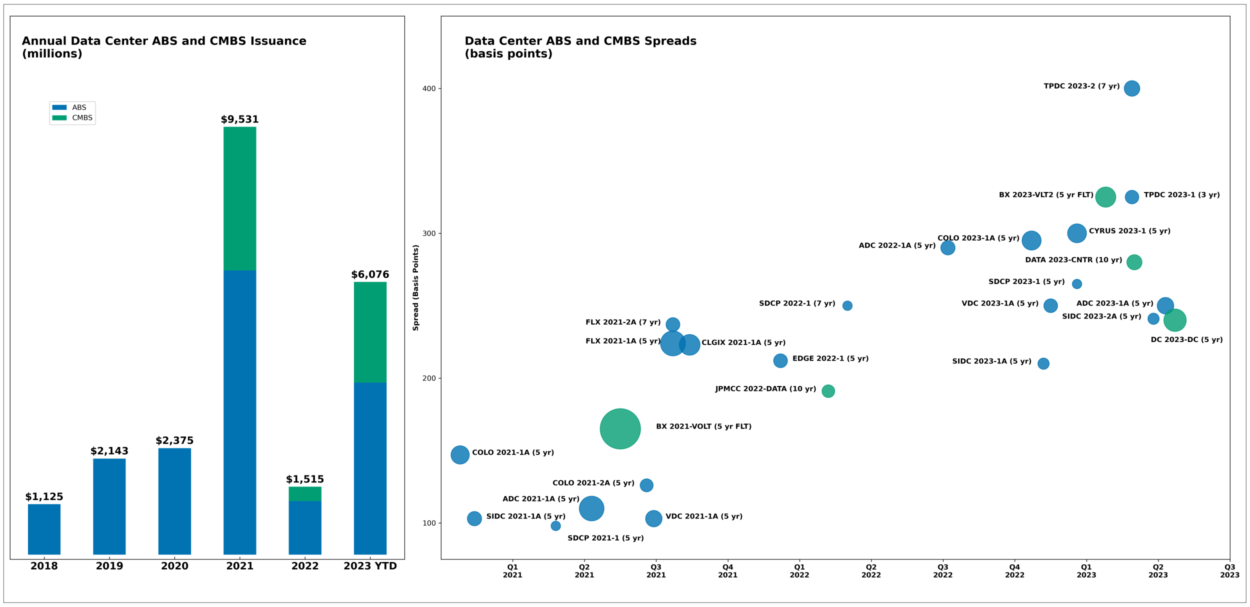
The flurry of data center issuance YTD, which included first-time issuers such as CyrusOne and TierPoint, underscores many similarities, and a handful of differences, between ABS and CMBS transactions in the segment. The steady stream of deals could also fully establish data centers as a near-core exposure for securitized portfolios, regardless of the issuance vehicle (REMIC or a master trust).

The market saw 12 data center deals so far this year, with a total outstanding volume of \$6.1 billion (Figure 1). This compares to a much more subdued issuance in 2022, that totaled \$1.5 billion.

Figure 1. Data Center ABS and CMBS Issuance and Spread Levels



Note: Spreads are relative to Treasuries for fixed-rate deals and discount margin for floating-rate deals (labeled with FLT)
Source: Bloomberg and Academy Securities

Some ABS and CMBS Deal Distinctions Fade

A review of the 2023-vintage data center deals suggests the following:

- **Data center types.** Several DC ABS deals in 2023 featured wholesale data centers, extending a seemingly counter-intuitive exposure we observed in earlier deals. Data center ABS securitizations aim to put emphasis on the strength and experience of the operators, rather than mostly on the building economics. As such, we would expect to see mostly retail colocation properties in ABS deals, as we discussed in a previous report.[1] But the ongoing inclusion of wholesale data centers in deals such as VDC 2023-1 continues to blur some of the distinctions between ABS and CMBS DC deals.

- **Primary and secondary markets.** The collateral diversity across the DC ABS deals offers investors a variety of geographic exposures. Data centers properties traditionally benefitted from clustering, or geographical concentration, similar to a few other CRE segments including life science. Northern Virginia is the dominant data center cluster, boasting >50% of the data center development in the U.S. Investors may have a preference on getting exposure to established, proven market. The Northern Virginia data center could also benefit from fresh tailwinds for operators. Notably, Dominion Energy stated in mid-2022 that it would not be able to provide expected power to some new data centers in the area, thereby limiting new supply and providing operators leverage in lease negotiations. In turn, some DC deals include exposures to secondary markets such as Central Washington (SDCP 2023-1) or San Antonio (Cyrus 2023-1). This provides investors with exposure to markets with growth opportunities and potentially muted supply.

- **Number of properties.** DC deals vary on the number of properties backing the deal. ABS deals can feature a relatively large number of properties, ranging from six (SDCP 2023-1) to 31 (TPDC 2023-1). This puts the emphasis on pool-level parameters and average levels. In contrast, CMBS deals can feature very few properties, heightening the focus on property-level underwriting and concentrated exposure. For example, the just-priced $990 million DC 2023-DC has exposure to only two data centers in Northern Virginia. Interestingly, this does show the DC ABS and CMBS deals can differ in their number of properties, but still have exposure to similar sub-markets.

1 Data Centers: A Strong Segment Juggles ABS and CMBS, Securitized Products Special Topics, Academy Securities, October 4, 2022

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