VAN LANSCHOT KEMPEN

INVESTMENT MANAGEMENT

Market Musings 11/26

For Professional Investors only

Data centres: life after mid-terms

Return of nuance

Data centres and affordability were in the spotlight at the US mid-term elections, with many governors, senators, and House candidates making the two issues focal points of their campaigns. This focus has a direct impact on new data centre build-out, and an impact on the listed US utility companies that are positioned for the step up in electricity demand growth. After the Democratic sweep, we don't think the data centre build-out is over. Instead it gets more nuanced – which helps active investors.

Affordability & data centres

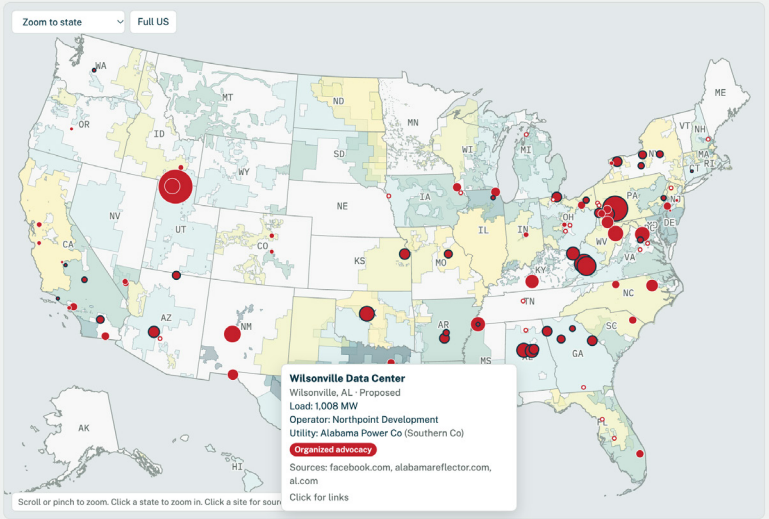
The central question raised during the election is who will pay for this data centre build-out, as households are already facing higher bills. According to EIA data[1], average US residential electricity prices are expected to rise 10.5% between 2024 and 2026, almost double the 5.8% increase in consumer prices. As bills climb, some residents have become increasingly unhappy about data centres being built near their neighbourhoods. Welcome to NIMBY – *not in my backyard.*

Mapping opposition to data centres

Using the Fractracker Alliance database, which links each data centre's status to organised opposition tracked on social media sites (Facebook, Youtube etc.), we can see where opposition against data centres is trending in the US: see the red dots[2].

It's an easy layer to add to our asset maps, allowing us to see exactly which data centre operators and which electric utility companies need to address NIMBY concerns more urgently.

Organised opposition to data centres



Source: Fractracker.org The popup of Wilsonville Data Center provides an example of how we can view key data for each project.

[1]Electricity Bills / Prices: U.S. Energy Information Administration (EIA), Analysis & Projections [https://ww.../index.php]
[2]EIA: Annual Electric Power Industry Report, Form EIA-861 detailed data files Annual Electric Power Industry Report, Form EIA-861 detailed data files - U.S. Energy Information Administration (EIA)

How to sweeten the deal? Money talks.

Utility companies need to keep their residential customers happy – these are the voters that can change governors, that appoint regulatory commissioners. One tool utilities can use is to have a pricing framework for charging one price to residential customers, and another to large load customers (data centres, industrial and commercial clients). Some utilities under our coverage go so far as to use the data centre customers to subsidise the electricity cost for residential customers. This additional charge for larger customers is designed to pay for additional infrastructure and electricity needed to serve them rather than shifting those costs to residential consumers.

In our stock selection we focus on listed utility companies that already have this framework in place, either through self-designed tariffs for data centre customers or tariffs mandated by their state. In the map above, those areas with the most pushback (the red dots), are the areas where it is more material to look for this pricing framework. As an extra step, we then overlay our proprietary **affordability analysis** – which considers how material electricity bills are as a percentage of income in each service area, as well as the rate of increase[3]. This helps assess whether the pricing framework goes far enough. Together these inputs inform our valuation work.

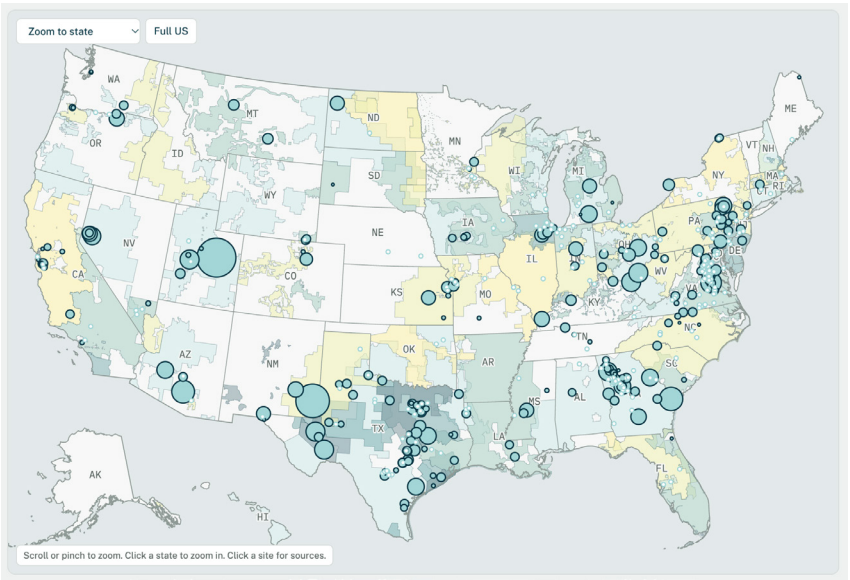
Texas: a case for sensible regulation

Texas illustrates how sensible regulation could look. Congratulations to Governor-elect Gina Hinojosa. One of her campaign promises was a moratorium on data centres. We see three categories of data centres:

- **Already operational**
- **Under construction**
- **Planned**

The moratorium applies mostly to the third category. This map shows their locations:

Locations of planned data centres



Source: Fracktracker.org

The moratorium doesn't necessarily mean a full stop. In order for these data centres to move beyond the planning phase, they need to disclose how much electricity and water they will use, and from which supplier. This seems like a sensible regulatory requirement to us, and we believe this helps electric utility companies, whose name needs to be added to the planning request, get more control over tariffs and prices paid by different customers. Without the named utility, the planned data centre doesn't make it off the PowerPoint slide.

Investment implications

We don't believe this is the moment where politics ended the AI theme. We do believe it marks the start of more sensible regulation and a further shift in power from data centres towards utilities. At the same time, a more nuanced build-out creates opportunities for bottom-up stock pickers to find alpha.

[3]Electricity Bills / Prices: U.S. Energy Information Administration (EIA), Analysis & Projections [https://ww.../index.php]

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