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The Rise of Johor as a Data Centre Hub

Introduction

Data centres are facilities that house infrastructure and equipment which store, process, and distribute large amounts of data for various purposes, such as cloud computing, e-commerce, online gaming, and digital media. Data centres have seen a boom due to the world's growing reliance on cloud-based technology and consumption of online content. More recently, data centre investments have become a strategic imperative for the Artificial Intelligence ("AI") era, given the massive amounts of compute and data involved in the training, testing and deployment of AI solutions and applications.

The escalating strategic competition between the United States and China has motivated companies from both China and the West to broaden their horizons and grow their presence in Southeast Asia, particularly in the semiconductor and digital infrastructure sectors. This trend has triggered a surge in the establishment of data centres across the Southeast Asian region, in particular Johor, Malaysia.

In this update, we will delve into the factors that drive the growing interest for data centre investments in Johor, and provide a brief overview on some of the issues that organisations should consider as they contemplate shifting to set up data centre operations in Johor.

Johor: An Attractive Alternative

Johor is currently witnessing a significant surge in the establishment of data centres. This growth is primarily attributed to its proximity to Singapore, one of the major financial and tech hubs in Southeast Asia, together with other advantages such as abundant land and cheaper power, making Johor an attractive alternative to Singapore for data centre operators. This is bolstered by the terrestrial connectivity between Singapore and Johor.

Johor started attracting attention as an alternative location for data centre operators after Singapore announced a moratorium on new data centre development in 2019 due to concerns about their significant energy consumption which was not in line with Singapore's sustainability goals. Although Singapore lifted its data centre moratorium in 2022, the Singapore Government has stressed that it would become more selective of which data centres it would accommodate, with new efficiency and sustainability linked requirements and limits put in place to manage the environmental impact of the sector. On 30 May 2024, the Singapore Infocomm Media Development Authority (IMDA) launched a Green Data Centre Roadmap to chart a sustainable pathway for the continued growth of data centres in Singapore.

The attractiveness of Johor as a potential spillover location for data centre demand is bolstered by regional economic cooperation and partnership initiatives.



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The first is the proposed Johor-Singapore Special Economic Zone ("**SEZ**"), which aims to strengthen economic ties between Malaysia and Singapore by boosting the cross-border flow of goods and people, including a passport-free clearance system, which is expected to facilitate trade, stimulate economic activities, and create job opportunities on both sides of the border. The SEZ will provide a platform for businesses to leverage the strengths of both regions, thereby fostering innovation, enhancing competitiveness, and driving growth. A Memorandum of Understanding ("**MOU**") on the SEZ was signed between Singapore and Malaysia on 11 January 2024, formalising this proposal and marking a significant step towards its realisation. If plans are approved, the Johor-Singapore SEZ would be nearly twice the size of China's Shenzhen SEZ at 3,505 square kilometres. This SEZ is expected to attract more multinationals to the region and further boost Johor's data centre investments.

Another initiative is the broader Singapore-Johor-Riau ("**SIJORI**") growth triangle, which also includes Riau, Indonesia. The SIJORI growth triangle is a regional economic cooperation initiative between Singapore, Malaysia and Indonesia that seeks to leverage the production complementarities and proximity of the three regions to boost their collective economic performance. The development of the Nongsa Digital Park in Batam, which is part of the Riau Islands, is expected to strengthen the region's position as a data centre hub.

These developments have not gone unnoticed by industry players. Leading data centre service provider GDS, for example, has announced that it has strategically deployed data centres in the SIJORI cities to cater to growing digital demands in the region which has intensified with the advent of the AI era. As another example, Singtel and Pt Telekomunikasi Indonesia International (Telin) have entered a Memorandum of Understanding to develop a new 100km INSICA cable to connect Singapore and Batam, Indonesia under the newly formed INSICA (Indonesia Singapore Cable System) consortium.

Conducive Environment and Incentives

In addition to the spillover effects, Johor has grown and developed as a data centre market in its own right due to its natural factors (strategic location, favourable climate, abundant natural resources), as well as Government instituted frameworks and incentives.

Several major players in the data centre industry have recognised these advantages and have set up operations in Johor. These include GDS; Nvidia, a prominent name in the tech industry known for its graphics processing units (GPUs); AirTrunk, a hyperscale data centre specialist; YTL Power, a utility company with a strong presence in the energy sector; and Princeton Digital Group, a leading investor, developer and operator of internet infrastructure. Microsoft has also announced that it has acquired land in Johor for data centre use. In fact, Johor is expected to attract RM 17 billion (US\$3.6 billion) in new data centre investments in 2024.

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The exponential growth and increasing demand for data centres in Johor are further facilitated by the investor-friendly approach adopted by the Malaysian Government and the conducive regulatory framework in Malaysia. In this regard, the Malaysian Government, through the Malaysian Digital Economy Corporation ("**MDEC**"), awards Malaysia Digital Status ("**MD Status**") to eligible companies that participate in and undertake certain prescribed activities, which include the operation of data centres as well as the provision of technology, software, design and support services in relation to the cloud. Subject to compliance with a set of criteria and conditions, the grant of MD Status by MDEC confers a set of incentives, rights, and privileges onto eligible companies.

Foreign data centre developers are ordinarily allowed to own up to 100% equity participation in the Malaysian entity(ies) incorporated to undertake development of data centres in Malaysia. However, foreign equity restrictions may apply depending on the type of services provided by the data centres. For instance, a data centre typically only requires a class licence that is not subject to foreign equity restrictions if it merely provides cloud services. However, if the data centre further provides connectivity services which are over and above the cloud services, then it is likely that an individual licence that is subject to foreign equity restrictions will be required from the Malaysian Communications and Multimedia Commission before that service may be provided. In addition, any purchase or lease of land by a foreign/foreign-controlled company is generally subject to approval from the state authority, and ownership of certain land or property may be subject to other conditions and approvals depending on the location of the land or property.

For the construction and development of data centres, there are a few key legal considerations which apply across the planning, construction, commissioning, pre-operational, and operational phases. These include obtaining planning permission, building plan approvals, procurement of electricity and water supply and application for telecommunications licences. Due to the time and effort required to obtain the necessary approvals, licences or supplies, a number of which need to be tackled concurrently, data centre developers are encouraged to consult with the relevant consultants, authorities and counterparties at the early stages, in order to have a clearer picture of the process, timeline and nuances that apply.

Opportunities and Challenges

Against this background, there is potential for Malaysian and Singaporean businesses to leverage new business opportunities and partnerships.

Within this growth area, Malaysian and Singaporean businesses can partner each other to contribute their competitive advantages and expertise. For one, Malaysian property developers can bring to the table their expertise in land acquisition, construction, and local market knowledge, while Singaporean data centre experts contribute their technical know-how, industry experience, and global best practices. This synergy allows for the development of state-of-the-art data centres that are not only physically

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robust but also technologically sophisticated, to meet the growing demand of modern day data centre operators.

As noted above, data centre operators that are considering setting up data centres in Malaysia must pay heed to the local regulatory requirements. The legal and regulatory landscape surrounding data centres is complex and multifaceted, encompassing a myriad of areas such as data protection and privacy, real estate, energy consumption and supply, environmental impact, and touching on issues such as telecom regulatory requirements, restrictions on purchase of land, regulatory restrictions pertaining to construction, electricity supply, deployment or leasing of terrestrial or subsea capacity for connectivity to the data centres, and more. Missteps could be extremely costly as they will expose the operator to heightened regulatory oversight or delays in operations.

Businesses (e.g. content providers or cloud service providers) that are considering shifting some of their data centre demand from Singapore to Johor will need to consider issues such as how they can connect the offshore data centres back to their primary data centres in Singapore, the types of deployments and deployments to shift (e.g. less latency sensitive applications), as well as cross-border data and data transfer regulations.

We invite you to reach out to us if you have any queries or wish to delve deeper into any of the issues above. With local teams in Singapore, Malaysia and across Southeast Asia, we are well placed to advise and support businesses on your data centre operations or investments in the region.

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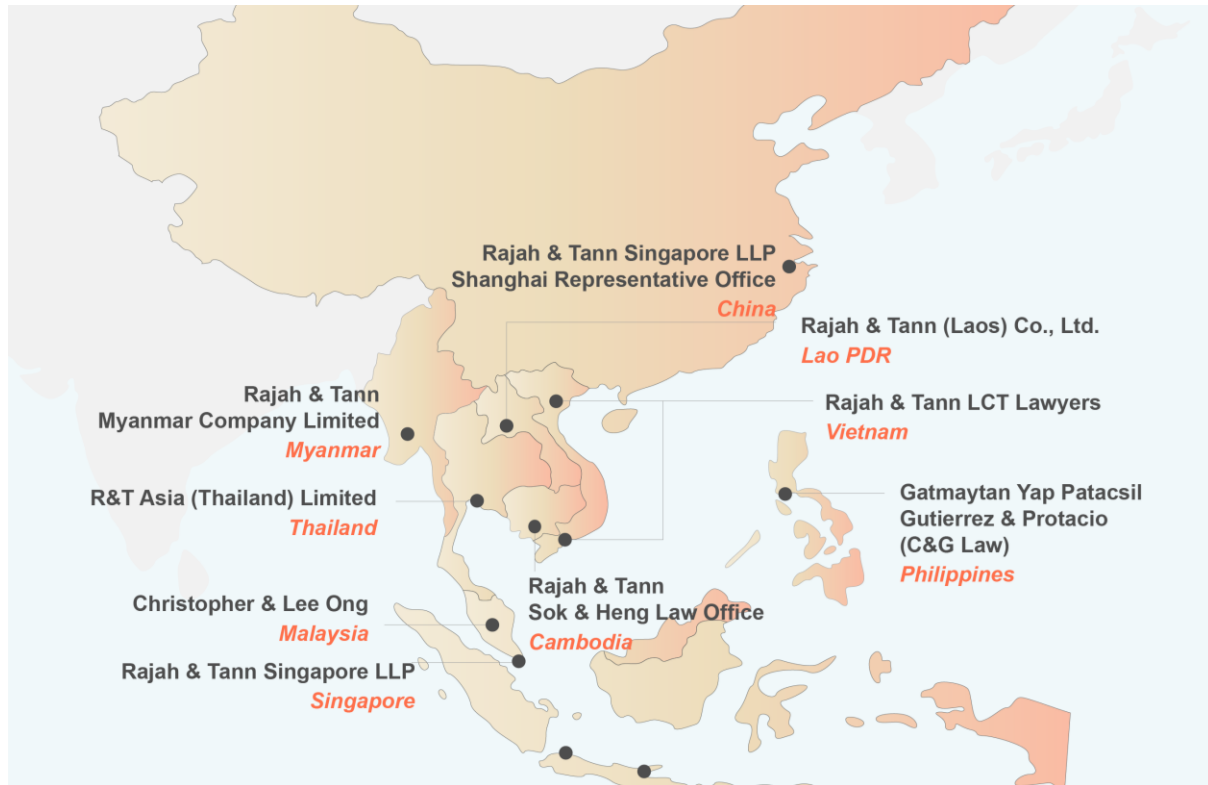
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