Portfolio review

This review covers the entire financial year, including the impact of Covid-19 and our responses to it.

CGI of 21 Moorfields, EC2

Key 2020 figures

At a glance

8.8%[1]
Valuation deficit

-4.5%
Ungeared total property return

-0.4%
The portfolio underperformed the MSCI Quarterly Universe (All Property)

£39m
of investment lettings

2.4%
Like-for-like voids (31 March 2019: 2.4%)

Office

1.1%[1]
Valuation surplus

4.5%
Ungeared total property return

3.5%
The portfolio outperformed the MSCI Quarterly benchmark (Central and Inner London Office)

£11m
of investment lettings

1.3%
Like-for-like voids (31 March 2019: 1.0%)

Specialist

8.0%[1]
Valuation deficit

-3.9%
Ungeared total property return

£4m
of investment lettings

1.2%
Like-for-like voids (31 March 2019: 1.5%) and units in administration: 0.1% (31 March 2019: 0.2%)

Retail

20.5%[1]
Valuation deficit

-17.3%
Ungeared total property return

£24m
of investment lettings

3.9%
Like-for-like voids (31 March 2019: 4.0%) and units in administration: 1.9% (31 March 2019: 0.9%)

↓1.2%
Footfall in our regional retail and outlets was down 1.2% but was ahead of the ShopperTrak UK national benchmark (down 3.7%)[2]

-9.8%
The portfolio underperformed the MSCI Quarterly benchmark (All Retail)

↑0.9%
Same centre sales, taking into account new lettings and occupier changes, were up 0.9% (up 0.1% excluding automotive sales) (BRC national benchmark for physical stores down 3.2%; including online, down 1.1%)[2]

1. On a proportionate basis.
2. Year-on-year for the 48 week period to 1 March 2020, reflecting the period before the impact of Covid-19.

Actions and outcomes

Focus for 2019/20	Progress in 2019/20
— Maintaining like-for-like net rental income	— Like-for-like net rental income declined £4m (0.7%) before the effect of bad debt provisions relating to next year's rent
— Providing property as a service, harnessing data and technology, to improve customer experiences	— Capital allocation, asset management and leasing decisions are underpinned by improved data, research and technology including in our Retail segment where we analyse and blend multiple data sources to provide insight into the attractiveness of brands to our catchment — In our Office segment we are engaging directly with our occupiers' people to better understand their needs so that we can optimise our environment and ancillary retail and leisure offers
— Researching and trialling ways to build better, faster and for less	— Modern methods of construction (MMC) implemented at 105 Sumner Street, SE1 in kit-of-parts approach and automated processes — Design process embedded in development process at 25 Lavington Street, SE1 and Red Lion Court, SE1 — Hollow piling trial and Friendly Concrete used at Nova East, SW1
— Expanding customer offerings of Myo, Fitted and Landsec Lounges	— Myo and Fitted fully let at 123 Victoria Street, SW1 and being rolled out in earliest available space at Dashwood House, EC2 — Landsec Lounge in place or under construction at four of our London properties
— Progress on time and on budget at 21 Moorfields, EC2, Lucent, W1, Nova East, SW1 and 105 Sumner Street, SE1	— Prior to the impact of Covid-19 in March 2020, 21 Moorfields was on budget, with a three-month delay in expected completion to March 2022 due to tenant modifications. Subsequently we have seen a further delay of up to two months with the eventual impact dictated by productivity which is currently around 50% but improving — Pre-Covid-19, Lucent, Nova East and 105 Sumner Street were on-site progressing build-to-grade on time and on plan. We are now introducing greater flexibility by deferring contractual commitment to the more capital intensive elements of each of these schemes
— Progress plans for the future development pipeline of 2.6 million sq ft in the existing portfolio and seek to grow the pipeline through acquisitions and partnerships	— Planning and vacant possession achieved on Portland House, SW1 — Planning submitted for 25 Lavington Street, SE1 — Continuing to progress design at Red Lion Court, SE1 and master planning for residential development of four inner London retail destinations
— Delivery of key strategic MSUs at our major shopping centres	— Polo Ralph Lauren at Braintree Village opened November 2019 — Construction underway for Zara at Bluewater, Kent and contractor selected for their letting at St David's, Cardiff
— Generating £4m of social value across our community programmes, in support of £25m corporate target by 2025	— Over £4.8m of social value generated across our community programmes
— Improving energy management in support of 2030 energy management corporate commitments	— 21 energy management initiatives approved, which will result in a 3.2% reduction in energy consumption across the portfolio against a 2013/14 baseline

Focus for 2020/21

— Balance protecting like-for-like net rental income with the need to support customers facing cash flow difficulties in the wake of Covid-19

— Continue to reduce occupancy costs without compromising rental income by delivering further savings in service charge

— Get 24.0 million sq ft of real estate re-occupied and operating

— Work with our customers and partners to develop mutually beneficial solutions to the challenges of operating in the wake of Covid-19

— Work with our construction partner at 21 Moorfields, EC2 to ensure progress is as fast as possible while maintaining best practice health and safety on site

— Maintain our optionality over speculative developments by progressing build-to-grade works and design; tracking market indicators to take decisions about when and how to exercise our option to progress

— Obtain planning permission for our speculative office schemes in Southwark at 25 Lavington Street, SE1 and Red Lion Court, SE1

— Progress our master planning and design of residential-led re-purposing at our four suburban London shopping centres, widening the scope of the programme to include our regional retail portfolio

— Generate £4m of social value across our community programmes, in support of our £25m corporate target by 2025

— Improve energy management in support of 2030 energy management corporate commitments

— Deliver a review of the long-term strategic direction for our business, wide in our scope and bold in our thinking, taking into account the structural trends disrupting our sector, the short-term challenges of Covid-19 and its longer-term consequences

Portfolio review
continued

Overview

The London office market had continued to see strong demand for high-quality space despite political uncertainty in the lead up to the general election. A preference for new rather than second-hand space led to limited availability of new HQ stock. This lack of available supply of high-spec offices, with good transport connections and sustainability credentials, led to an increase in rental values.

The impact of Covid-19 will disrupt the market and, at this stage, the extent of any changes to short- or longer-term trends on the use of office space is uncertain. We anticipate that there is likely to be a greater emphasis on health, air quality and the flexibility of both layouts and working practices. We expect that this will only reinforce a 'flight to quality' and our portfolio is well positioned to meet these demands from occupiers. All of our office customers have been impacted by Covid-19 but the strength of our occupier base gives us confidence in the resilience of the portfolio.

In the very near term, Covid-19 will slow down progress at a number of our development sites. We are keen to progress our schemes as much as we can while minimising further commitments to capital expenditure in the short term but retain the option to pause all but 21 Moorfields, EC2, which is pre-let in its entirety. We remain optimistic about the long-term prospects of London and believe the fundamentals that make the capital the favoured home for business are unchanged.

Even before we saw the impact of Covid-19, it was clear that the retail market was having another tough year as it wrestled with structural challenges, and property values fell further as a result. Although occupancy levels and rental income at our retail assets were relatively resilient, we were affected by the pressures faced by retailers that, in some cases, saw them enter CVA or administration. All our retail assets fell in value but, in particular, regional centres and retail parks saw significant valuation declines as yields moved out.

The effect of Covid-19 on the already struggling retail sector will be significant. Following government action to address the Covid-19 outbreak, most of our shopping centres, outlets and leisure assets have closed save for essential shops. Apart from the major supermarkets and some pure online players, few retailers will emerge from Covid-19 in better financial condition than before the virus arrived. Our immediate focus has been to support our customers by reducing costs, agreeing rent relief for those in most need and working to enable them to reopen as soon as conditions allow and restrictions are lifted. We also continue to progress the re-purposing of excess space at our assets, notably the residential and office opportunities offered in key cities by our retail destinations.

The like-for-like portfolio

Office

We have a high quality office portfolio in one of the greatest cities in the world. Strong demand for quality means our best-in-class office space is virtually full. As a result, we achieved 17 new lettings in the year, totalling £11m, and completed ten rent reviews totalling £23m, 7% ahead of previous rent.

Our focus in the like-for-like portfolio remains on how we improve our assets to secure rental uplifts and lease extensions. Enhancing customer service and meeting future customer needs sit at the heart of our response and, as part of this, we are investing in amenities and introducing Landsec Lounges at a number of our assets.

The high occupancy across our three office products, HQ, Fitted and Myo, reflects the continued demand for space that offers quality, convenience and flexibility. HQ customers will continue to dominate our portfolio in the short term, giving us secure, stable income. Fitted launched in 2019 on two floors at 123 Victoria Street, SW1 and both are now let at a healthy premium to market rents. Our launch of Myo exceeded expectations; the space is now fully let and includes supporting existing HQ customers with their shorter-term needs, as well as customers who are new to us. We will roll out our flexible products within the development programme and our existing portfolio as expiries allow, including at Dashwood House in 2021.

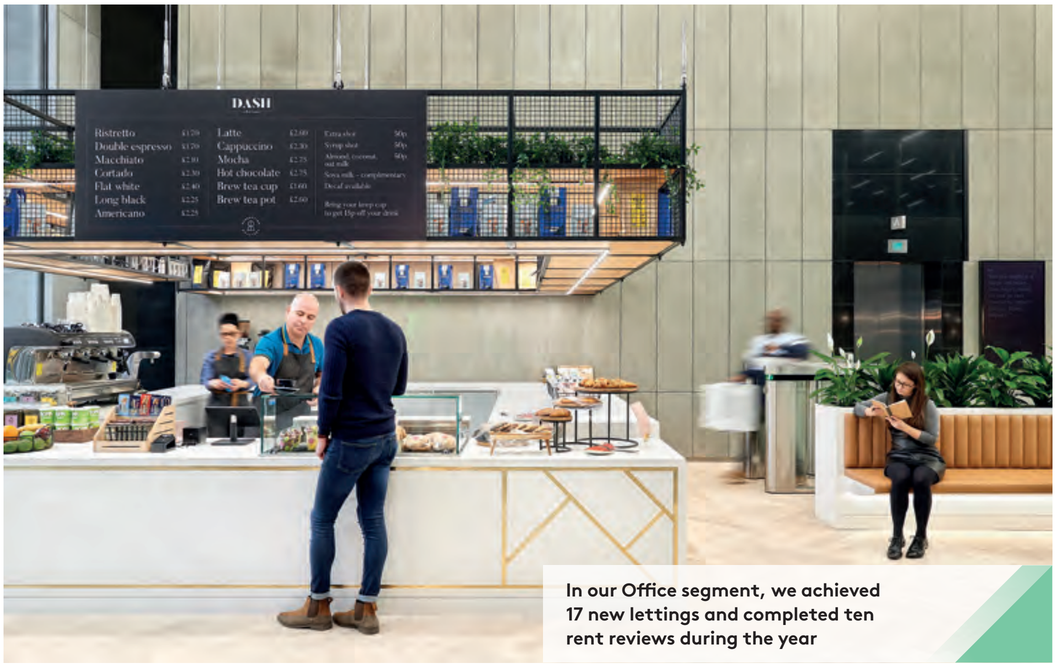
Covid-19 is impacting our office customers with over 90% of their employees now working from home. The vast majority of our customers continue to pay their rent and 89% of the rent due on 25 March 2020 and 1 April 2020 was collected within ten days compared with 98% for the same period last year. Open, collaborative conversations with our customers are key to how we manage our business, and these have been vital in recent weeks as we strive to balance protecting income with supporting customers facing cash flow issues. Under 10% of our occupier base is in sectors which we have identified as at particular risk from the impact of Covid-19 including commodities, serviced offices, construction, fashion and travel. This gives us confidence in the strength of our office occupier base and the resilience of the portfolio.

It's too early to predict the long-term impact of Covid-19 on the office market. However, the way businesses and people use workspaces will change. We anticipate a greater emphasis from customers on the need for healthy buildings with excellent air quality and higher lifting capacity. We expect our customers to operate with lower occupation densities and with more flexible working. They may require layout changes and that requires flexible buildings. We know that occupiers and their insurers demand standards of quality, safety and security of infrastructure that cannot be replicated in the home.

Our offices can respond to change. We developed the majority of our office portfolio and did so with adaptability in mind, describing them as stage sets: changeable to meet our occupiers' needs. With our strength of occupier base and high quality adaptable space, we believe the portfolio is well placed to meet the unprecedented challenges presented by Covid-19.

Retail

Prior to the impact of Covid-19, the retail market continued to face structural changes. Changing consumer shopping habits and rising costs for retailers put pressure on rents across the sector, and negotiations with customers have been challenging. This was reflected in asset pricing, with rental values and market yield movements leading to significant declines in valuations, particularly in regional retail and retail parks.



In our Office segment, we achieved 17 new lettings and completed ten rent reviews during the year

Our Myo space is now fully let and includes supporting existing HQ customers

We have been proactive in our response to the structural challenges the retail market is facing. We have been busy working to reduce service charge costs to ease pressure on retailers in the short term. And, where there is surplus space in our portfolio, we continue to progress our plans to re-purpose retail units, actively working to introduce office and residential, particularly in our key cities.

For the 48 weeks to 1 March 2020, same-centre sales at our regional destinations and outlets were up 0.9% (up 0.1% excluding automotive sales), ahead of the BRC benchmark, which was down 3.2%. Footfall was down 1.2%, but well ahead of the ShopperTrak UK national benchmark, down 3.7%.

The quality of our portfolio provided some protection against the overall impact of CVAs. Like-for-like net rental income was only down by 3.9% compared with last year, before provisions related to next year's rent. Where we were impacted by CVAs, our assets remained popular with occupiers and customers. We saw 94 units across 31 customers go into CVA or administration in the year – some of those entering administration having previously been in CVA – but of these only 29% of the stores closed as a result. Over the last three years, we have had reasonable success with stores that have closed, having now replaced over a third of the income lost from customers entering CVA or administration.

Outlets continued to be our best performer in the Retail segment, and we had a good year of letting activity, adding 33 new brands across the five outlets. Consumer research and sales data enabled us to target brands that will strengthen our line-up. At Gunwharf Quays, Portsmouth, we added retailers including Loake, Dune, Belstaff and Penhaligons, with Pho, Hubbox and The Alchemist enhancing the food and beverage offer. At Braintree Village, last year's opening of Polo Ralph Lauren continued to help the centre's performance. The brand also attracted other premium retailers to the centre including Lindt, Kate Spade and Lyle & Scott.

In regional retail, we continued to improve both tenant mix and experience. Customer data and insight informs our decisions, enabling us to find the right occupiers for customer demand, and the right unit for each occupier. At Bluewater, Kent, following Primark opening in March 2019, footfall was up 3.7% and sales at the centre were up 4.9% (excluding automotive sales) for the 48 weeks to 1 March 2020. Zara signed at St David's, Cardiff and are upsizing significantly at Bluewater. H&M also took a bigger store at Trinity Leeds. We've also introduced new types of retailer to our centres, adding cycling concept store Peloton at Bluewater and Westgate Oxford.

In London retail, the market showed similar trends to the rest of the UK, with restaurants and mid-market fashion struggling. However, we continued to see demand for space. Following the administration of Jamie's Italian, we re-let the majority of the vacated space to The Ivy. And at One New Change, a new flagship for Ivy Asia opened in the former Barbecoa unit. London retail continues to evolve and trends are accelerating. In the future, we anticipate a greater demand for service and experience-led occupiers in increasingly mixed use destinations.

Retail parks now make up 3.5% of our portfolio and we will continue to monitor our exposure to this sector. During the year we made one disposal, selling Poole Retail Park for £45m at a net initial yield to the purchaser of 8.0%.

Our Retail segment has seen a significant impact from Covid-19. The majority of our destinations are closed save for essential shops, and many of our customers are struggling. Only 38% of the rent due on 25 March 2020 and 1 April 2020 was collected within ten days compared with 90% for the same period last year. We have set up an £80m support fund to provide rent relief to those customers who are most in need of help, with a particular focus on supporting F&B customers and small and medium sized businesses. We are also working to reduce service charge costs further, while helping our customers to prepare to re-open as swiftly as possible when conditions allow.

Specialist

Prior to Covid-19, our leisure and hotel assets performed well and occupancy levels remained high. Cinemas continued to be popular, especially for blockbuster movies, and UK admissions were up 8.0% for the 11 months to the end of February compared with the same period last year. Mid-market restaurant chains continued to find the conditions challenging and we expect this trend to continue.

Our hotels provided good income, though performance across the year was variable, often affected by local or seasonal factors such as sporting or cultural events. The underlying site value of our hotels remained well ahead of book value, offering opportunities for future development.

Piccadilly Lights, W1 also performed well. We have two to three-year leases with our long-term partners Coca-Cola, Samsung and Hyundai and income from the shorter-let space continued to grow, exceeding our income expectations for the 11 months to February 2020.

Our Specialist segment has been hit hard by Covid-19. Our leisure operators along with food and beverage occupiers are currently unable to trade following government intervention and face financial difficulties as a result. Only 31% of the rent due on 25 March 2020 and 1 April 2020 was collected within ten days compared with 86% for the same period last year. Our £80m rent relief fund is designed to support these customers in particular. Many of our hotels, the majority of which are let on turnover only deals, are now closed and it remains unclear when they will reopen for business. Demand for Piccadilly Lights diminished in the early weeks of the pandemic, although we have been able to offer this space to Public Health England for essential public health messaging and remain in dialogue with customers regarding bookings on the Lights for later in the year.

Portfolio review
continued

Net rental income

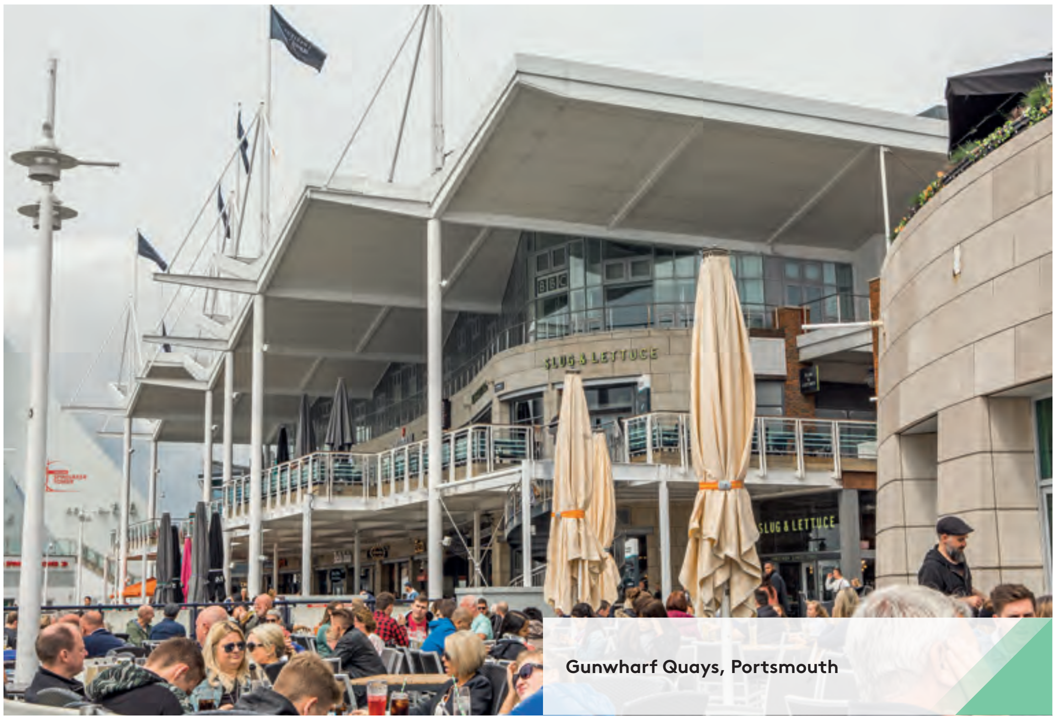
Net rental income from the Combined Portfolio declined by £35m in the year ended 31 March 2020 primarily due to a £23m provision against rental income invoiced prior to 31 March but which relates to the next financial year. This was in addition to a £4m decline in net rental income from our like-for-like portfolio which was the result of difficult trading conditions in our Retail segment as well as small reductions in income at our proposed developments and from properties acquired and sold since 1 April 2018.

Net rental income from our Office assets increased by £3m to £261m. Net rental income from our like-for-like properties increased by £7m due to rent reviews and new lettings. We lost £2m at our proposed development at Portland House, SW1 as we worked towards vacant possession and £1m from acquisitions where we incurred costs to maintain flexibility at 25 Lavington Street, SE1, acquired as a development site in the prior year.

In Retail, net rental income declined by £33m to £243m, predominantly due to a £19m provision against next year's rental income which was invoiced in March 2020 but where recovery is in doubt due to Covid-19. During the year, we saw a £10m reduction in income from our like-for-like properties, primarily due to the impact of CVAs and administrations across the portfolio. We also lost £2m as a result of the sale of Poole Retail Park this year.

In Specialist, we also took a provision of £4m against next year's rental income invoiced in March 2020 but in doubt due to Covid-19. This was the main driver for a £5m decrease in net rental income to £79m.


CGI of Lucent, W1



Gunwharf Quays, Portsmouth

Net rental income[1]

Table 7

	Office			Retail			Specialist			Combined Portfolio		
	31 March 2020 £m	31 March 2019 £m	**Change £m**	**31 March 2020 £m**	31 March 2019 £m	**Change £m**	**31 March 2020 £m**	31 March 2019 £m	**Change £m**	**31 March 2020 £m**	31 March 2019 £m	**Change £m**
Like-for-like investment properties	**250**	243	7	**246**	256	(10)	**83**	84	(1)	**579**	583	(4)
Like-for-like investment properties – provisions related to 2020/21 rent	**–**	–	–	**(19)**	–	(19)	**(4)**	–	(4)	**(23)**	–	(23)
Proposed developments	**10**	12	(2)	**–**	–	–	**–**	–	–	**10**	12	(2)
Development programme	**(1)**	–	(1)	**–**	1	(1)	**–**	–	–	**(1)**	1	(2)
Completed developments	**–**	–	–	**9**	9	–	**–**	–	–	**9**	9	–
Acquisitions since 1 April 2018	**(1)**	–	(1)	**–**	–	–	**–**	–	–	**(1)**	–	(1)
Sales since 1 April 2018	**–**	–	–	**2**	4	(2)	**–**	–	–	**2**	4	(2)
Non-property related income	**3**	3	–	**5**	6	(1)	**–**	–	–	**8**	9	(1)
Net rental income	**261**	258	3	**243**	276	(33)	**79**	84	(5)	**583**	618	(35)

1. On a proportionate basis.

The Development portfolio

We have over 4.0 million sq ft of development opportunities in London and are active at four schemes totalling 1.0 million sq ft, of which 56% is pre-let. We are making good progress across our London development programme but development activity has slowed due to Covid-19.

Importantly, however, the pipeline has been designed with flexibility: our speculative schemes in the development programme are all being built to grade, allowing us to call a stop to development activity at ground level if we choose to, and we have not yet committed to Portland House, SW1. This has enabled us to step down our committed total development cost by around £700m from where we had expected to be by March 2020, leaving around £340m of committed unspent development expenditure on sites currently in our development programme where we are still making good progress.

The majority of that commitment is at 21 Moorfields, EC2, our 564,000 sq ft scheme which is pre-let in its entirety. All construction contracts are agreed, and the steel framework has progressed well. A three-month delay in expected practical completion to March 2022 was due to tenant modifications and will not impact rent start date. Following the impact of Covid-19, we have experienced a further delay of up to two months. The eventual completion date will be dictated by productivity which is currently around 50% but improving. We continue to be in close dialogue with the occupier, Deutsche Bank.

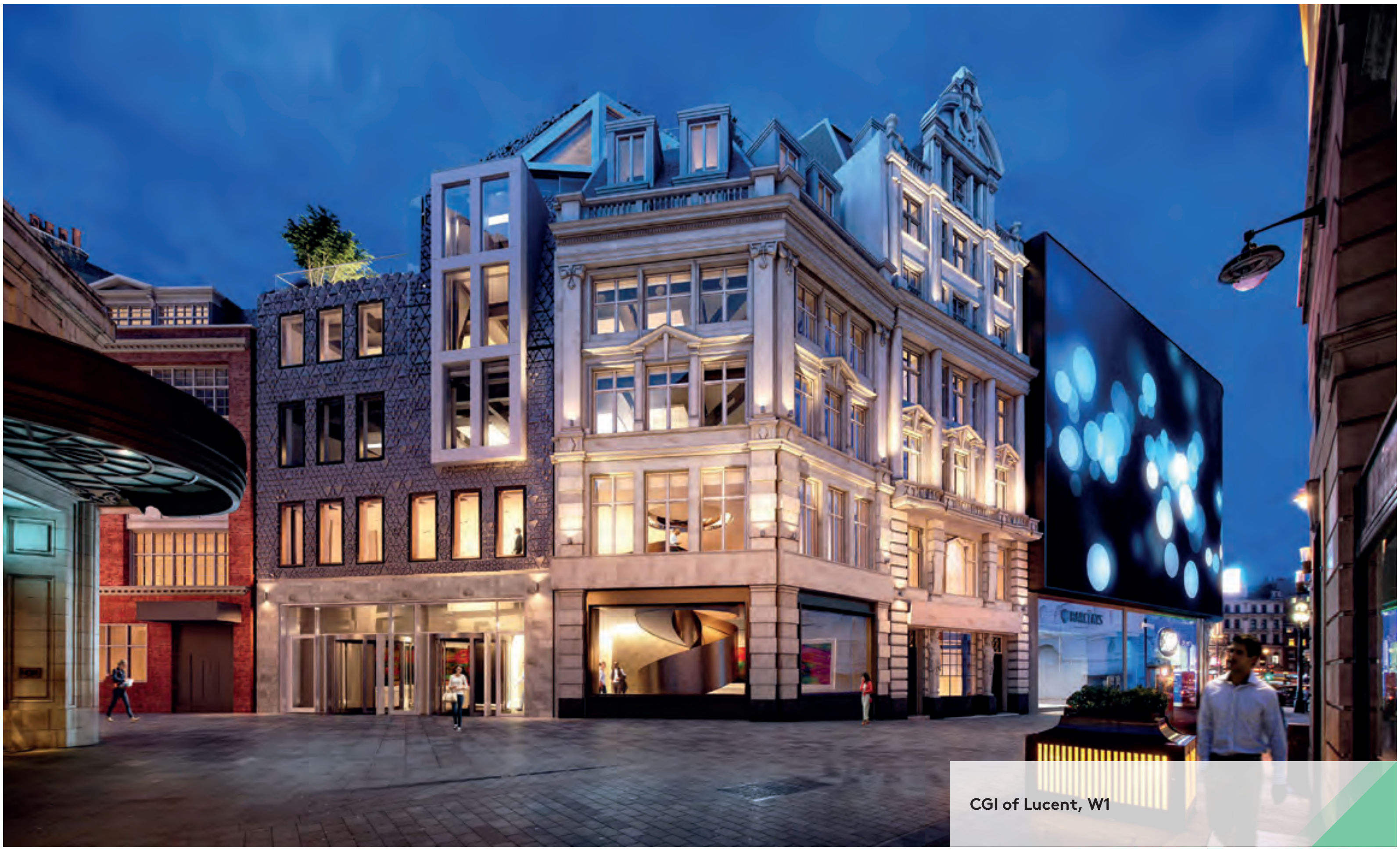
Where we are making additional commitments, we are doing so to preserve optionality. At Lucent, W1, Nova East, SW1 and 105 Sumner Street, SE1, we have committed £33m to progress as quickly as possible in the current environment and secure long lead-time packages. We have also negotiated break options before entering into main construction contracts. In doing so, we have deferred until September at the earliest the remaining £251m commitment needed for the most capital intensive stages of these three schemes. This flexibility allows us to keep reviewing the occupational market we might deliver into and to decide at multiple junctures whether to continue work, pause or to cease speculative development entirely.

On the ground, at Nova East, our 166,000 sq ft scheme, we are progressing the build-to-grade works, construction of the cores and detailed design as well as placing orders for certain packages of work.

At Lucent, our 144,000 sq ft scheme in the heart of the West End, demolition is complete and, here too, we are building to grade, constructing the cores and negotiating a flexible main contract with our contractor. At 105 Sumner Street, we have planning consent for two buildings totalling 140,000 sq ft plus a new public square. We'll use our new, partly automated efficient construction methods to reduce building time and cost, and to create our first net zero carbon development. We are building to grade, progressing construction of the basement and procuring long lead time packages as we progress the detailed designs.

At Portland House, we now have planning permission to add a 14-storey extension to the existing building. Our proposed scheme will create 400,000 sq ft of new or refurbished space. We intend to incorporate HQ, Fitted and Myo, together with wellness and leisure facilities and a roof-top restaurant. We achieved vacant possession at the end of March and we are now stripping out the building and advancing the design.

The remaining development opportunities are a mix of central London office-led schemes and mixed use residential-led retail re-purposing. At Lavington Street, SE1, we have submitted planning for two buildings totalling 378,000 sq ft. We aim to deliver a scheme with high sustainability credentials, and plan to use a hybrid cross-laminated timber and steel structure to reduce the carbon footprint of the development. At Red Lion Court, SE1, the existing occupier has extended their lease to 2022. In parallel, we're progressing our plans for a redevelopment of the building, aiming to submit a planning application in Summer 2021. We also continue to progress our plans for transforming our major city retail schemes into ambitious mixed use destinations. We are now working on plans for Finchley Road, NW3, Shepherd's Bush, W12, Southside, Wandsworth, Lewisham shopping centre and Buchanan Galleries, Glasgow.



CGI of Lucent, W1