Chief Executive's statement

As a result of our proactive approach to the challenges posed by the pandemic, Landsec is poised for recovery with a strategy that positions the business for long-term growth.

MARK ALLAN
CHIEF EXECUTIVE

OVERVIEW

I joined Landsec as Chief Executive in April 2020, in the early days of the Covid-19 pandemic, and our results for the year to March 2021 clearly reflect the challenges of both the pandemic and the government's policy response. However, from the very outset of the first lockdown we have been focused on ensuring that the business emerges from the pandemic in as strong a position as possible. The positive effects of this decisive action will become clearer in the years ahead.

Lockdowns meant that the vast majority of our portfolio was either closed or substantially unoccupied for over half of the year. Social distancing and other restrictions meant that, even when open, capacity and utilisation across all assets was still heavily impacted. Our key priorities throughout were (i) ensuring the safety of our employees and visitors to our properties; (ii) working collaboratively with our customers to support their businesses as effectively as possible; and (iii) maintaining our financial strength and flexibility. Our success and progress against each of these objectives, in the face of heightened uncertainty and persistent challenges, has gone some way to offset the significant negative financial impact of the pandemic. We did not benefit from any Government sponsored financial assistance.

We are now entering the recovery phase. Government action to support the economy was swift and the speed of the ongoing vaccination programme impressive. As a result, there is the real prospect of a strong consumption led recovery across the remainder of 2021 and 2022, although this is not without risk. Businesses will fail, jobs will be lost and management of the public finances will require a deft hand. However, as a result of our proactive approach to the challenges posed by the pandemic, Landsec is poised for the recovery with a strategy that positions the business for long-term growth.

RESULTS AND DIVIDEND

EPRA NTA was 985p at 31 March, a fall of 17.4% over the year attributable primarily to the effect of the global Covid-19 pandemic on our property values. Adjusted net debt fell £437m to £3,489m as a result of proactive asset disposals more than offsetting capex on our development programme. As a result, despite the valuation weakness, our Group LTV only increased marginally to 32.2%. Our balance sheet remains in a strong position.

Revenue profit for the year was £251m, down 39.4% relative to the prior year. The decline was almost entirely attributable to Covid-19, either as a result of lower operating income (such as rent on turnover leases) or as a result of rent concessions granted and bad debt provisioning.

We are proposing a final dividend for the year of 9.0p per share which, together with interim dividends already paid, makes for total dividends of 27.0p per share for the full year.

STRATEGY, CULTURE AND PEOPLE

We launched our new strategy in October 2020, confirming our intention to focus on creating long-term value for shareholders, as measured by total business return. We will achieve this by concentrating our activities and our capital on those sectors and opportunities where we believe we have sustainable or attainable competitive advantage. Importantly, it is a strategy grounded in a clear purpose – Sustainable Places. Connecting Communities. Realising Potential – which aims to create sustainable value for all our stakeholders.

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This strategy is captured in four strategic priorities, set out below, and each is covered in more detail later in the Operating and portfolio review, together with a clear update on progress made to date and more detail on near-term objectives.

1 OPTIMISE CENTRAL LONDON
2 REIMAGINE RETAIL
3 GROW THROUGH URBAN OPPORTUNITIES
4 REALISE CAPITAL FROM SUBSCALE SECTORS

In line with our strategy, we intend to increase portfolio recycling in the near term to effect our desired reallocation of capital and are prepared to take, in a considered way, more operational risk to create value and drive returns, with financial leverage managed accordingly. We have earmarked approximately £4bn of assets for disposal over the next few years, focused initially on high quality but defensive prime central London assets and, in due course, assets in Subscale sectors where we have little or no competitive advantage (hotels, leisure and retail parks).

When reinvesting capital from this portfolio recycling programme, we have identified two main areas of focus – value add opportunities in central London and urban mixed-use regeneration projects. We also believe that opportunities could begin to emerge in the retail sector in the short to medium term following the very substantial downward correction in asset values in that sector over the past few years.

Culture is as important as strategy. Successful execution of our strategy will be built on a reinvigorated culture at Landsec to ensure that we make the most of the considerable capability and expertise of our people and look to augment it in a targeted way. Clarity of strategic direction, coupled with a properly aligned organisational design, will allow us to foster a culture of greater empowerment and accountability. As a result, we will be better placed to assess and manage risk, make decisions more quickly and drive better returns. Where we judge that new or additional skills are required, for example in elements of our retail business or in regeneration and placemaking, we are moving quickly to address those needs.

Bridging both strategy and culture for Landsec are five key performance drivers that will underpin our competitive advantage for the long term: customer centricity; data-driven decisions; ESG leadership; capital discipline and development expertise. Our level of existing capability in each area is varied – development expertise and ESG leadership are already key strengths on which we can build further. Our capital discipline – both in the sourcing and allocation of capital – can be sharper and customer centricity and data-driven decisions are both areas where significant progress is needed. But these are areas where the wider real estate sector itself is not particularly strong and so both still represent opportunities to establish competitive advantage if we move quickly.

The past twelve months have been challenging for everyone. Across Landsec, as with many organisations, our teams have had to adapt quickly to ever changing conditions and have had to work harder than ever to balance the pressures of their roles with other priorities. It is testament, therefore, to their skill and dedication that so much has been achieved, and so much value protected, despite these persistent challenges. I have been deeply impressed by both the performance and potential of my new colleagues.

1

STRATEGIC PRIORITY:

OPTIMISE CENTRAL LONDON

Our Central London business represents 68% of our portfolio by value and is characterised by the quality, resilience and liquidity of our London office assets. These assets are a clear example of the value creation capabilities inherent in the Landsec business, given that the majority have been developed or refurbished and leased by us in the past 15 years. However, a number of the assets now have limited further value creation potential and so we intend to increase asset disposals over the next few years and recycle our investment out of these high quality, more defensive assets and increase our exposure to assets that offer greater upside, for example either through redevelopment or repositioning. This strategy better aligns our capital and capability, leading to greater value creation opportunities in the medium to longer term. Our sale of 1 & 2 New Ludgate for £552m in December and the subsequent acquisition of 55 Old Broad Street for £87m demonstrate the progress we are already making.

Chief Executive's statement
continued

Central London has been one of the areas hardest hit by the effects of the pandemic and social distancing restrictions, with physical office occupancy for the portfolio as a whole ranging from 1% to 21% at different times across the year and footfall across our Central London portfolio down by around 82%. We expect physical office occupancy to recover substantially across the second and third quarters of 2021. However, with tourism likely to be constrained, future office working patterns still unclear and residual concern about the safety of public transport likely to persist for a while yet, it will take longer for central London footfall to recover fully.

Given the pandemic related challenges, our Central London performance was remarkably resilient in valuation terms, falling only 6.5% to £7.3bn and reflecting a like-for-like equivalent yield of 4.6%. Investor demand for long let, prime London assets was strong and we expect it to remain so, reflecting both investors' willingness to look through near-term uncertainty and the relative value of London compared with other major cities around the world. Yields for prime assets appear well supported at current levels and we could even see some compression in the year ahead.

The nearer term prospects for office occupier markets are more difficult to judge. Vacancy rates are high but concentrated in second hand space. Hybrid working models are here to stay but the effect on occupiers' space requirements is far from clear and will not be uniform. And demand seems likely to be strongest for prime space, the recent and speculative supply of which has been muted. Overall we expect some weakness in rent levels but for this to be most significant for secondary space, of which we have very little.

Against this backdrop, there will be a clear opportunity for owners and occupiers to work together collaboratively to determine and deliver tailored requirements and this will offer potential for investors, developers and occupiers alike. Landsec's long track record and deep, strategic relationships with its customers should translate into clear competitive advantage. Besides our high quality development programme, it is also a particularly interesting time for us to be broadening the range of propositions we can offer to occupiers – our Myo, Customised and Blank Canvas offerings. Flexibility, adaptability and strong customer relationships are going to be critical attributes going forward.

From a development perspective, we worked hard during the year to preserve optionality on our speculative projects for as long as possible, allowing us time to assess and better understand the outlook for the occupier market. Taking all of our analysis into account, and having stress tested prospective returns, we have now committed to three of our five near-term office development opportunities and will be delivering them during 2022 and 2023. These three projects total 0.5 million sq ft and, including pre-let or pre-sold projects, take our total committed development programme to 1.1 million sq ft, of which 57% is either pre-let or pre-sold.

2

STRATEGIC PRIORITY:
REIMAGINE RETAIL

The pandemic has materially accelerated structural trends that were already underway in retail and, for most of the retail sector, it is clear that online is now the primary growth channel and will remain so. This does not, however, signal the end for retail property. Instead, it means that its role must change in an omnichannel world to offer something sufficiently compelling – either to be complementary to online or to offer something that cannot be easily replicated online. It is this reality that underpins our 'Reimagine retail' vision and we are confident that, with effective execution, we have a retail business that can thrive longer term.

Our outlets portfolio (£0.7bn value) serves a real purpose, offering visitors the opportunity to enjoy a day out shopping a variety of brands, with a great value offer and experience that isn't easily replicated online. The outlet model is fundamentally based on collaborative partnerships with our brand partners, most obviously through turnover based leases. During the year, our outlets have been relatively resilient, but values fell 18.5% and like-for-like equivalent yields moved out to 6.8%. However, based on their strong relative performance after each lockdown, we expect outlets to perform strongly in the recovery.

The picture for shopping centres remains more complex. Over the year, the value of our regional shopping centres fell on average 38.2% to £1.0bn, taking the decline from the peak to approximately 60%. The realities remain that going forward there will be fewer physical retail stores, rents will be lower and, in order to remain relevant, shopping centres will need to offer a combination of attributes that are either complementary to online or not easily replicated online.

Much more of this is now reflected in valuations than was the case a year ago, largely as a result of the accelerating effect of the pandemic. The vast majority of our forecast 40% decline in rents from peak to achieve a sustainable level has now been recognised. It is of course currently difficult to assess rental values given the effects of the pandemic and the increasing prevalence of turnover components to leases, and it is possible that the downward correction in rents overshoots in the short term. However, we remain confident in our sustainable rent forecasts overall.

All of this means that retail property will continue to become more operational in nature and our priorities reflect this. To be successful in the long term we need to be able to combine strong, strategic relationships with brand partners, effectively tailored guest experiences and deep asset management expertise. Landsec has always had strong asset management credentials but brand partner management and more tailored guest experiences are areas where we are targeting rapid enhancements. We have made good early progress and our appointment in December last year of Bruce Findlay as Managing Director – Retail, bringing considerable international retail experience from a range of global brands, is an important example of how we are enhancing the 'retailer perspective' in our approach.

The near-term outlook for retail remains challenging, particularly for shopping centres. We are likely to see a sharp increase in insolvency processes (such as CVAs, business restructurings or administrations) amongst occupiers as the Government's pandemic related support tapers off and businesses that were struggling before the pandemic continue to do so afterwards. As this happens, it will accelerate the fall in passing rents towards our forecast sustainable rent levels, increasingly reflected in valuations already. It will also open up opportunities for new brands and different propositions, including digitally native ones, to take space instead and help improve longer-term prospects.

Our longer-term view of retail is more positive. With the downward correction in rents and values now happening much more quickly than would have been the case before Covid-19, it represents an opportunity for the sector to recalibrate. Landsec's combination of a strong retail platform, deep asset management and development expertise and a strong balance sheet marks us out as increasingly unique in the sector and well positioned to take advantage of any appropriate opportunities should they emerge.

3

STRATEGIC PRIORITY:

GROW THROUGH URBAN OPPORTUNITIES

Our Urban opportunities portfolio currently consists of five suburban London shopping centres with significant repurposing potential in the medium to longer term. These assets offer the raw material for mixed-use, multi-phase developments that can offer a compelling blend of income, development and rental growth driven returns throughout their life. Well designed, mixed-use spaces can also cater for the increasing focus on the need for balanced communities and spaces that contribute positively to quality of life, both of which have been brought into sharper relief by the pandemic. With our existing development and asset management capabilities, we believe that Landsec is well placed to become a leading player in this sector, both through the realisation of existing opportunities within our own portfolio but also through targeted acquisitions.

The longer-term redevelopment potential of our Urban opportunities portfolio helped to support values during the year to some extent but they still saw a meaningful decline of 23.3% to £0.4bn as a result of their predominantly existing retail nature. Our focus in the year ahead is on progressing our redevelopment plans, with the submission of a planning application on our first project a key target. We are also actively evaluating potential new investment opportunities that can offer the right blend of income, development and rental growth driven returns, ideally in a way that can accelerate the return profile of this segment of the business.

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STRATEGIC PRIORITY:

REALISE CAPITAL FROM SUBSCALE SECTORS

Subscale sectors describes those parts of the portfolio where we have relatively little capital invested and judge ourselves to have little or no competitive advantage – hotels, leisure assets and retail parks. Our objective remains to realise capital from these assets over time and to reinvest that capital into new value creation opportunities.

Of course, these types of assets have been amongst the hardest hit by the pandemic, particularly hotels and leisure, and over the past 12 months the aggregate value of our investment in Subscale sectors fell 16.4% to £1.3bn. We do, however, expect these assets to be well placed beneficiaries of a strong consumption led recovery in the months and years ahead and for values to grow meaningfully as a result. Our anticipated timescale for disposals reflects this, with hotels and leisure assets unlikely to be sold for at least a couple of years so that we can capture a sensible proportion of the expected valuation upside ahead. Retail parks, which were more resilient in the pandemic and where investment markets have staged a recovery, may offer sale opportunities sooner. In all cases, we will be working hard to maximise value creation opportunities across the portfolio in the meantime.

THE YEAR AHEAD

Performance in the coming year will be determined by the shape of economic recovery from Covid-19 and the early signs are positive. The 12 April re-opening of non-essential retail saw some very strong trading for retailers across our portfolio and highlighted the potential for a strong consumer-led recovery over the remainder of 2021 and 2022. Our retail, leisure and hotel assets are well placed to benefit from such a recovery and, after a period of material downward movements in retail valuations in particular, the outlook for this part of our portfolio now appears under significantly less pressure.

We expect activity in central London to recover more slowly, with office occupational markets remaining more subdued for the time being, which could translate into some rental weakness. The London investment market, conversely, seems likely to display continued resilience with a significant amount of capital seeking prime investment opportunities and this could go some way to offsetting any rental weakness from a valuation perspective.

Against this backdrop, we expect to make good progress in executing our strategy. We took advantage of strong investor demand for prime London office assets to make two disposals in the year, with combined proceeds of £0.6bn, and more disposals are likely over the course of the next financial year. With improving economic prospects, we can now pursue opportunities to reinvest this capital with confidence.

Our reinvestment agenda includes our committed Central London development programme, but we also have capacity to pursue new acquisition opportunities in a targeted way. Our main target areas for investment are value add opportunities in central London and mixed-use, multi-phase urban regeneration projects, both of which offer the potential for above average total returns for shareholders. In addition, we are carefully monitoring the retail sector to determine whether this could provide interesting opportunities at potentially compelling returns.

Of course, our strategy is about more than capital allocation. We also intend to continue the reinvigoration of our culture in line with the principles of empowerment and accountability and to enhance some of the more operational and customer-oriented foundations that we believe will be critical to our long-term success. These include the continued roll out of a wider range of propositions for our Central London office customers, further investment in strategic brand partnerships and guest experience capability in retail and proving our placemaking credentials in Urban opportunities.

The Landsec business is poised for recovery with a strategy that positions the business for long-term growth.

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