Our market

The Landsec property portfolio is invested in a number of sectors within the UK. We own high-quality offices in London, six regional shopping centres, five retail outlet centres and five suburban London retail assets, aiming to redevelop this final group into urban mixed-use schemes over time.

MARKET AT A GLANCE

232m sq ft
of office space in central London

732m sq ft[1]
of retail space in the UK

8.9%
vacancy rate in central London offices
(2020: 4.5%)

17.9%[2]
shopping centre vacancy rate
(2020: 14.1%)

£7.2bn
of investment transactions in central London in 2020

1. Source: JLL/GOAD
2. Source: LDC

In addition, we have assets in three sectors we will seek to exit over the medium term: retail parks, stand-alone leisure parks and hotels. The dynamics in each of these market sectors vary, as do the specific locations and assets.

MARKET DYNAMICS

LONDON OFFICES

The London office market comprises 232m sq ft of space. Some assets offer exclusively office facilities, but typically an office building will usually incorporate a collection of space for retail, food and beverage, and ancillary services and amenities such as health services. Office customers' needs are changing, with a greater demand for flexible space, healthier working environments, sustainable buildings and more services and amenities.

Office space requires regular refurbishment, and buildings are defined as grade A – new or recently refurbished space – and secondary – older space which needs investment. London is a global financial centre with a dynamic office market that is constantly renewed by development. It is a cyclical market, from both an investment and occupier perspective, and sees periods of rental and valuation growth with periods of decline. Successful property companies manage their assets, time their investment and development activity, and consider risk in relation to the supply and demand conditions in the market. The cycle is a consideration when making investment and disposal decisions, but it should not constrain a business from taking contrarian views when opportunities emerge.

Despite the recent impact of Covid-19 on its investment and occupational markets, London will remain a global financial centre, and its office market has long-term potential from both an asset-management and development perspective.

RETAIL

Retail space ranges from individual units on the high street through to large, regionally dominant shopping centres. In addition, retail space can be designed to satisfy different reasons to shop: retail parks focus on the convenience-led trip, whereas large shopping centres are destinations that provide a mix of retail, food and beverage, and leisure activities such as cinemas.

The vast majority of retailers have an omnichannel strategy which uses online as well as physical space to market and deliver their products and services to their customers. Physical stores are destinations, but are also used to support online retail through click & collect and returns services. Retailers have adapted their store networks in response to this, and in many cases now operate from a smaller number of larger units. The type of product and service offered by retailers ranges from the essential, such as food and healthcare, through to discretionary sectors such as luxury products and jewellery. Such a diverse range of products means particular parts of the retail sector can be affected by economic cycles and consumers' disposable income.

During the past 10 to 20 years, landlords have had to manage their retail assets during a period when retailers faced both cyclical and structural pressures. The nature and length of leases is changing, with landlords having to be more flexible in tailoring leases to the specific needs of their customers. Leisure services, such as cinemas, have become an increasingly important part of the mix of offers found in destination centres.

URBAN MIXED-USE

Urban mixed-use schemes represent a major growth opportunity for Landsec, underpinned by the global trends we have identified (see below). Rapid urbanisation, demographic and social change, and technologically advanced living are increasing the need for modern, well-configured places to live, shop, work and socialise.

Such schemes often have a large residential component, both of rented and owned apartments. The 'build to rent' market in the UK is still relatively nascent, and opportunities exist for larger operators to establish scale in this area. Opportunities exist to develop suburban sites in London as well as in larger UK cities such as Manchester and Birmingham.

Six 'Global Forces of Change' will impact our business over the next 10+ years.

MACRO TRENDS SHAPING OUR FUTURE MARKETS, CUSTOMERS AND COMPETITORS

1

RAPID URBANISATION

One in three people will live in cities of at least 500,000 habitants by the year 2030 (source: UN).

2

DEMOGRAPHIC AND SOCIAL CHANGE

A global population boom, paired with people living longer and having fewer children, will drive significant demographic shifts.

3

TECHNOLOGICALLY ADVANCED LIVING

The digital landscape will continue to disrupt how we live, work, communicate, shop and beyond.

4

CLIMATE CHANGE AND RESOURCE SCARCITY

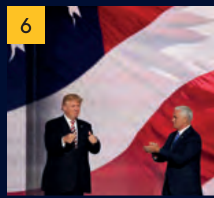
Growing energy, water and food demands, alongside rising weather and health events, show the global need to reverse environmental degradation.

5

BORDERLESS ACCESS

The liberalisation of global economic policy and the accessibility of air travel have opened borders, supply chains and trade patterns.

6



SHIFTS IN GLOBAL ECONOMIC POWER

Political unrest, populism, trade wars and mounting recessions are reshaping the map of economic power and driving new culture clashes.

COVID-19 IMPACT

ACCELERATING
Covid-19 has accelerated adoption of convenience culture, tech usage and urbanised consumption expectations.

DECELERATING
Covid-19 has created a fear of densely populated areas.

DECELERATING
Covid-19 has been more detrimental to ageing citizens and BAME populations. A Covid-19 economic downturn may also decelerate a focus on an evolved and more inclusive landscape.

ACCELERATING
We are likely to see accelerated demand for new products and greater connectivity. Fibre technology and 5G networks will increase accessibility leading to new applications for the way we work, communicate and live our lives.

ACCELERATING
Although we were expecting a decelerating trend at the beginning of the pandemic, we've seen the opposite. More companies are increasing their efforts to address climate change and committing to net zero. Climate change continues to top the Government agenda, with frequent announcements of related plans.

DECELERATING
Covid-19 has followed a decade of austerity, and political turmoil, and now health concerns may entirely reshape the globalisation of trade, commerce and attitudes. Nationalism will continue to flourish with added fuel.

ACCELERATING
A Covid-19 economic downturn will widen the wealth gap. Nationalistic attitudes fostered by 'alternative governments' will drive wider trade rifts, while Covid-19 fast-movers may gain the upper hand globally.

While Covid-19 is having immediate and unpredictable effects on citizens, businesses and markets globally, the pandemic is also accelerating and decelerating aspects of change that have long been growing.

Our market
continued

THE PAST 12 MONTHS

The last year has been dominated by the impact of the Covid-19 pandemic, with retailers, food and beverage, leisure operators and the hotel industry particularly hard hit.

The vast majority of offices in London remained open during the year, to provide a safe environment for those who could not work elsewhere. In addition, office occupiers continued to pay their rent during the year, with rent collection rates above 90% for the major office operators.

Occupational demand in the London office market was below the long-term average (see chart right). There is a growing distinction between demand for new, prime office space – which meets wellbeing as well as branding and operational requirements for its occupiers – and secondary space, which is difficult to adapt to more progressive requirements. The pandemic has increased this divergence.

The London office investment market remained active over the last year, with demand for larger assets coming mainly from overseas investors. There was less demand for secondary assets, and these may become buying opportunities for office developers who can redevelop the space to meet the needs of today's customers.

The retail and leisure sectors were hit very hard by Covid-19, with non-essential retailers forced to close their stores for parts of the year during the lockdowns. The sector saw a number of retailers go into administration, including the Arcadia brands and Debenhams. Rent collection levels were significantly lower than normal, and landlords have provided support through rental payment holidays and deferrals where appropriate.

The impact of Covid-19 was not uniform across the retail sector. Outlets, retail parks and some suburban shopping centres with a larger proportion of essential retail were relatively resilient but still saw valuation declines in the year.

In contrast, central London retail, heavily dependent on tourism and office workers, was one of the most significantly affected segments.

Encouragingly, footfall recovered strongly when shopping centres were allowed to open but, with social-distancing measures in place, it was still below pre-Covid levels.

The food and beverage, cinema and hotels sectors were affected by social-distancing restrictions and the lockdowns in similar ways to the retail sector. It is likely these sectors will rebound quickly when restrictions ease.

Online is now the primary growth channel for retailers. To remain relevant and successful, retail space will have to be compelling in its own right, complementary to online (e.g. through fulfilment services such as click & collect) or offer products, services and experiences which cannot be replicated online.

The pandemic has also accelerated a number of trends which will provide opportunities for Landsec:

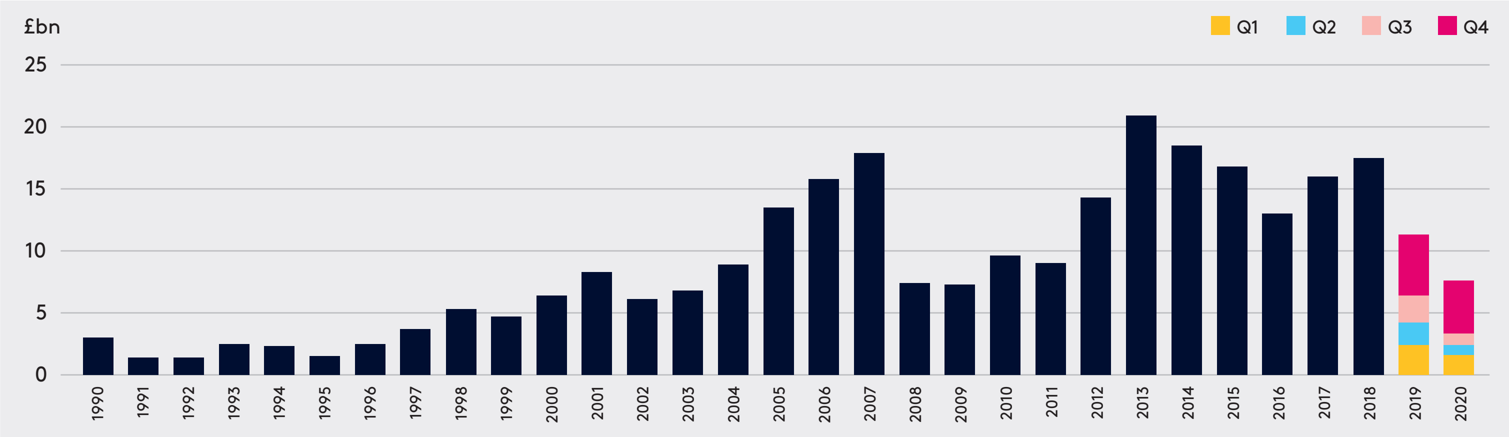
- CVAs and administrations are likely to increase following the end of the moratorium. This is an unwelcome event, but one which ultimately leads to the renewal of the sector.
- There is a flight to prime space as retailers demand the right space in the best locations.
- Retail winners are looking for fewer, larger stores.
- Digital native businesses are looking for prime physical space.
- Brand mix is changing to become more relevant and sustainable.
- Property companies need to be more operational to respond to changing customer needs.

As a result of these trends, struggling space will fall in value more quickly, enabling property companies to repurpose space earlier than would otherwise have been the case.

CENTRAL LONDON INVESTMENT MARKET

Investment volumes

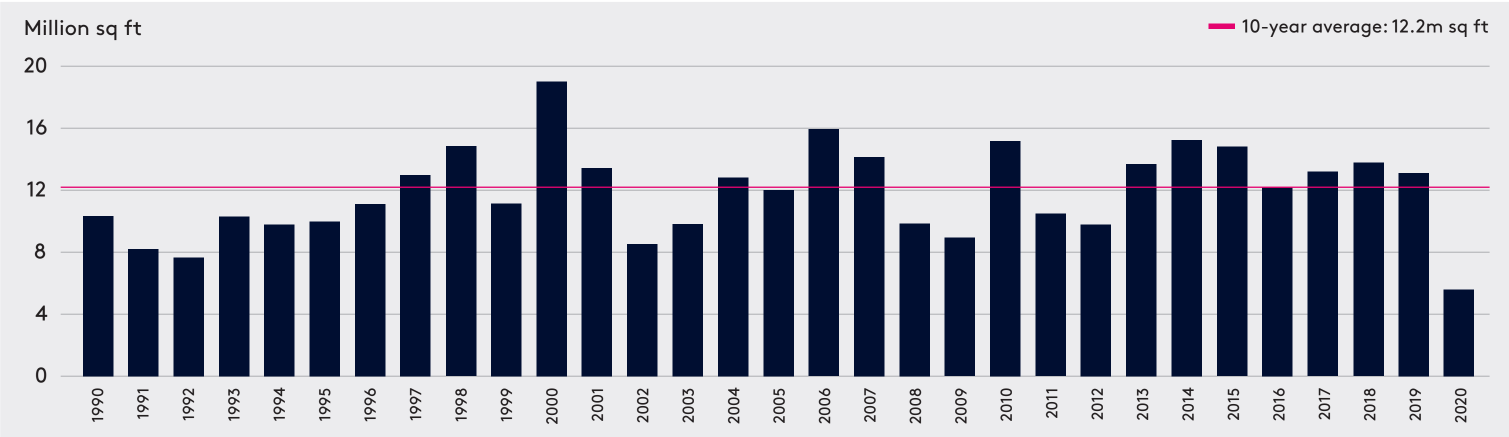
Investment volumes in London were lower in 2020, partly reflecting the impact of Covid-19 on viewings particularly by overseas investors. Demand held up for prime, long let assets.



CENTRAL LONDON OFFICE TAKE UP IN 2020 WAS A HISTORIC ANNUAL LOW OF 5.6M SQ FT

Source: CBRE Research

Covid-19 had a dramatic impact on central London office take-up with levels reaching a record low of 5.6m sq ft.



ONLINE SALES AS A SHARE OF TOTAL RETAIL SALES

Source: ONS

Online share of total UK retail sales has grown at a pace of 13% p.a. since 2008.
Short of any policy changes, online penetration is set to rise steadily.