TRITAX BIG BOX REIT

2021 Full Year Results

3rd March 2022

Transcript

TRITAX RESULTS WEBCAST TRANSCRIPT – 03/03/22

IAN:

Good morning and welcome to Tritax Big Box's results presentation for the financial year ended 31 December 2021.

I am Ian Brown, the Head of Investor Relations for Tritax.

Before I hand over to Aubrey, our Chairman I will quickly run through some housekeeping points.
Firstly, today's presentation is being recorded and a replay and transcript will be available on our website.
And secondly, there will be an opportunity for investors and analysts to put questions to the team at the end of the presentation. To submit a question, please use the text box in the webcast viewer to type your question.

Thank you.

AUBREY:

Good morning everyone and welcome to Tritax Big Box REIT's results presentation for the year ended 31 December 2021. And what a year it was!

We are today reporting an outstanding set of results, which demonstrate that our strategy is working. Long-term shifts in behavioural patterns resulting from the Covid pandemic and exacerbated by Brexit have increased the importance of logistics and quality supply chains. Being in the right location with the right infrastructure in place is now mission critical for businesses.

With demand set to continue to outstrip supply, we have a clear vision for the future, which will enable us to further capitalise on this huge opportunity available to us. We are accelerating the development of our existing substantial land platform – the biggest in the UK for logistics – to address this demand as we target starting 3-4 million sq ft of development in the year ahead. And we have the potential to accelerate this development programme further. This will also create further asset management opportunities as we continue to focus on delivering strong attractive and sustainable total returns for our shareholders from our complementary development and investment portfolio.

There have been some changes to the Board over the year. I am delighted to be here today for the first time as Chair of the Board, having previously acted as Senior Independent Director. Alastair Hughes has replaced me in this role. We are also pleased to welcome two hugely experienced Non-Executive Directors – Wu Gang and Elizabeth Brown – who we will look to introduce you to during the year ahead. Sir Richard Jewson and Susanne Given have stepped down from the Board. I want to personally thank them for their huge contributions and wish them every success for the future.

It just leaves me to thank you – our shareholders and the wider Tritax team – for your support during the year. We are excited about the opportunity ahead in logistics and have the team, the strategy, the appetite and supportive market fundamentals for future delivery.

Thank you again for joining us today. I will now hand over to Colin and Frankie for the formal part of the results presentation.

COLIN:
Thank you Aubrey, and good morning everyone.

I'm really pleased to be presenting the 2021 full year results for Tritax Big Box, and to provide you with an update on the further excellent progress that we are making.

My name is Colin Godfrey, and I am CEO to Tritax Big Box. I am pleased to be joined in the presentation today by Frankie Whitehead, Chief Financial Officer.

I'll kick off the presentation with a brief introduction, Frankie will then run through our financial results, and I will return with a strategic update. Ian will then coordinate Q&A.

In 2021 we delivered the strongest performance in our history. Looking forwards though, we remain very excited about the outlook for our market and the ability of our business to deliver attractive returns, because we are implementing a clear strategy that anticipated the market conditions we are experiencing today.

This combines the resilient income from our high-quality investment portfolio, together with the ability to produce attractive returns from development, which is delivering sustainable investments in-house. And there is a terrific runway of opportunity embedded within our land portfolio, the UK's largest, with potential to deliver over 40m sq ft of logistics facilities.

And this is all captured in the Key Messages from today's presentation:

A set of record results: in terms of earnings growth, nav growth and total returns.

A clear and compelling strategy that is delivering now but is also positioned to take advantage of the market dynamics to deliver into the longer term.

Powerful fundamentals: noting a highly favourable occupational supply and demand imbalance, barriers to entry and a strong investment market.

And finally, the combination of our investment and development portfolios are producing excellent returns now but also offer the opportunity to capture strengthening income growth and accelerate development activity to enhance capital growth.

Put simply, we have never been more excited than we are today about the long-term prospects for our business.

Critically, the strong performance we've announced this morning has been underpinned by delivery. We are consistently doing what we said we would do.

Looking at the left-hand column, we said that we would produce 2-3m sq ft of developments, grow rents, improve our leading ESG credentials and deliver attractive performance.

Turning to the middle column: In 2021 we exceeded expectations, having delivered 3.7m sq ft of development starts, grown our income at a faster rate, achieved improved ratings across all major ESG indices, and delivered record total returns.

And on the right-hand column, looking forwards, we see even more to come, with significant opportunity to enhance sustainability, accelerate our development activity and capex, and capture strengthening market rental growth, all supported by a market which we believe will underpin attractive returns into the longer term. And as I said, this is possible because of our strategy, and how we have positioned the business to take advantage.

We will return to the theme of delivering our strategy in a few minutes, but first I'll hand over to Frankie to run through the financial results.

Frankie.

Thank you Colin, and good morning everyone.

2021 really has been an outstanding year for the Company in terms of its financial performance. I am pleased to be presenting our strongest set of results ever and we are confident that our strategy of combining high-quality investment assets, with our significant development pipeline is one that will continue to deliver attractive returns to shareholders both over the short and longer term.

And you can see this outstanding performance from our headline figures here:

The Adjusted EPS is up nearly 15% to 8.23 pence, driven by development completions, rental growth across the investment portfolio and higher levels of DMA profit recorded in the year.

You will hear from Colin in a moment that our market fundamentals are exceptionally strong, which has helped us deliver a record 27% increase in NAV to 222.6 pence.

And that has resulted in a Total Accounting Return of 30.5% for the year, again another record for the company.

And finally, our balance sheet remains extremely well positioned to support and finance our Near-term development and value-add opportunities.

In January of this year, due to increased levels of visibility on our near-term development pipeline, we increased our development Capex target for 2022. And we expect that to translate into further attractive growth for shareholders this coming year.

On this slide we can see that our delivery of net rental income growth along with our efficient cost base…. is leading to strong underlying Earnings growth.

The Group net rental income increased by 14.3%. As expected, this was predominantly driven by in-year development completions, which added £24.0 million to annual passing rent. The total contracted annual rent grew to over £195 million as at the end of December.

Our operating costs have again shown further improvement on a relative basis, the operational benefits of further scale have been seen through our EPRA Cost ratio reducing to 13.9%, which remains one of the lowest within the REIT sector.

The Adjusted Earnings per Share has increased by nearly 15% to 8.23 pence, which is inclusive of the full amount of development management income recognised during the year.

As in previous periods, we also look through to our Adjusted earnings which we consider to be recurring, this is by stripping out the exceptional element of the DMA income. On this basis, Adjusted EPS has risen to 7.38 pence, which is an increase of just under 7%.

And In terms of the dividend per share, we have declared a 1.9p dividend this morning for Q4, taking the total dividend to 6.7 pence, an increase of just under 5%. This translates into a dividend pay-out ratio of 91% as we look to deliver attractive and sustainable dividend progression over the long-term.

When we look at the 2021 earnings bridge, it clearly sets out the drivers to our strong underlying EPS growth. It also sets out the scale of the development management income received in the year.

A key driver of income growth is through our development activity. As expected, it's the 3.7 million sq ft of development completions this year, which has had the biggest effect on underlying earnings. With 0.9p added from our development activity.

The like-for-like rental growth across the portfolio was 3.3% and this has added a further 0.3 pence to current year earnings.

Elsewhere, the impact of our disposal activity in 2020 outweighs our investment activity during the course of this year. We also note the reduction in licence fee income, as this has now converted into rental income as those buildings have reached practical completion.

And these items get us the majority of the way to the Adjusted earnings excluding exceptional DMA of 7.38p, which is growth of just under 7%.

It's worth pointing out that both the 6.91p starting position and the 7.38p include £4m of DMA income, which is the mid-point of our medium-term guidance range.

In terms of the development management income for 2021. We have recognised an additional £15 million of profit this year. This has principally come from one contract, which has now been fully delivered and for this reason it's considered as non-recurring.

We therefore base our dividend assessment against the 7.38p and the surplus DMA income is effectively reinvested into opportunities to create recurring earnings growth in the future.

The strong income performance is mirrored in our delivery of capital growth, where we have delivered improvement across all key balance sheet performance metrics.

The total Portfolio value grew to approximately £5.5 billion at December. The valuation surplus recorded across the portfolio totalled 19.1%, which contributed £840 million to NAV growth.

We have deployed £372 million of capital during the period, and as targeted, the majority of this has been channelled towards our attractive development pipeline.

Our EPRA NTA increases to over £4bn, which equates to 222.60 pence. This is an increase of 27% over the 12 months.

With an LTV positioned at 23.5%, this allows us to approach our near-term opportunities with conviction. Having secured new financing in the year, to support us with delivery, the balance sheet position now allows us to focus heavily on execution whilst also being reactive to other opportunities as they present themselves. Put simply, we have had a fantastic year, with the financial performance culminating in a record Total Accounting Return for the Company of over 30%.

Turning to the detail behind our strong NAV growth.

The continuing strength and weight of capital in the investment market has caused yields to tighten by approximately 45 bps across our portfolio, now with an Equivalent Yield positioned at 4.1% we still feel there is opportunity for further value growth to come. The Portfolio ERV growth has also accelerated in the second half, increasing by 7.5% across the year. This Investment portfolio performance has allowed us to add 39.0p to our NAV.

Our development assets have added a further 6.0 pence to performance and we are expecting to be able to improve on this component, as our development activity increases.

When noting the impact of the operating profit and dividends paid in the period, this takes us to the closing EPRA NTA of 223 pence per share.

So, we've had a year of compelling financial performance, but the really exciting thing for us is the huge opportunity ahead; and the ability to significantly accelerate our income growth.

This rental income bridge illustrates the potential we have to grow todays passing rent from £195 million as shown on the left-hand side, by approximately 2.5 times, up to an estimated £480 million.

So, moving from left to right – the current year ERV growth has increased our portfolio rental reversion to an attractive 11%, or £21 million.

As set out at the recent Investor Seminar, the increase in occupational demand has led to an acceleration in activity within Our Near-Term pipeline, and you can see this coming through within the green bars on the chart.

Starting with those items in green - We can add £10 million of potential rent from our Current Development Pipeline, £2.5 million of which has been secured.

Q1 2022 has already started well with 1.8 million sq ft of construction having already commenced, these assets have the potential to add a further £13 million to passing rent, of which approximately half has been pre-let.

And looking at the final green bar, a further potential £14 million could be added from the remainder of our targeted 2022 development starts.

Taking all of this into account, this gets us to the bar totalling £253m. So, including our current development pipeline, the targeted 2022 development starts and the rental reversion, we have the opportunity to grow passing rent by £58 million or 30% over the near-term, which, from a timing perspective, we would expect to translate into an acceleration our earnings growth from 2023 onwards.

The scale of our medium- and longer-term future pipeline is unique to us and to the UK, and without factoring in any future rental income growth into these figures, the land portfolio has significant embedded potential, which means we have confidence in the short and longer term over our delivery of future income growth. Moving on and our Balance Sheet also really is in great shape.

Noting the increase in visibility we now have over the near-term pipeline, as I have just walked you through, we took the decision to remove the associated near-term financing risk. Last September, we issued £300 million of new equity, in what was a significantly oversubscribed issuance, reflecting the confidence we have in the deployment of this into attractive opportunities.

We are now extremely well positioned, with a Loan to Value at 24% and over £600m of available liquidity.

This means we can we run hard and focus on the execution across that Near-term pipeline, whilst still providing flexibility within our capital structure to run even harder should further opportunities present themselves beyond what we anticipate today.

I just want to finish by providing some guidance and set out how our I see our positive long-term Outlook. The investment portfolio provides our core income return, and we are confident that it will deliver sustainable earnings growth.

This includes over 50% of the rent roll which is subject to rent review over the next 2 years, alongside an ability to capture the significant rental reversion.

We have plans to recycle capital this year, but it's about optimising the performance of the portfolio and managing investment disposal timings with the delivery of income from our developments. Our longer-term guidance on disposals is £100-200 million per annum.

We will continue to manage our balance sheet efficiently, ensuring we maintain financial discipline, as we have done during 2021. Investment purchases will be looked at in an opportunistic manner, but these will have to meet our strict returns criteria.

We intend to continue investing for growth; we have increased our development Capex guidance for 2022, targeting £350 - 400 million of Capex into development this year. From a yield on cost perspective, we continue to manage cost price pressures well internally, both rental growth and yield compression are mitigating a lot of this from feeding through into performance. But there has been some downward pressure on our Yield on Cost compared to 12 months ago.

We remain within the 6-8% range across the portfolio and expect to deliver between 6 and 7% on the Near-Term pipeline, whilst noting that there is still a very attractive arbitrage here between this and prime investment yields.

And we expect to deliver attractive future accounting returns. From an earnings perspective, I've set out how we expect to grow our income through our near-term development pipeline, remembering that the timing of income delivery will be linked to construction timelines and therefore earnings growth is likely to steeping as we move into 2023 and 2024.

And finally, we expect that to translate into sustainable, attractive dividend growth for Shareholders, with a policy of paying out at least 90% of our recurring Adjusted earnings.

So that concludes the financial review, where we are looking to build upon a very strong set of results, capitalising on an extremely strong market backdrop, with a development portfolio that provides us with a real competitive advantage to drive returns.

And I shall now hand you back to Colin.

COLIN:
Thanks Frankie.

So, Frankie's described our record performance in 2021, the momentum we have taking us forwards, and why we are financially well positioned for the future.

I'll now explain the market dynamics, demonstrate our strategy in action, look at the growth opportunity and consider why we are well positioned to deliver a consistent, strong performance into the long term. Essentially, as you've heard us say before, it's about the enduring strength of our market and how our strategy and our expertise are aligned to take advantage.

Three of the key drivers to occupational demand are:

- Continued growth in e-commerce.

- Increasingly complex supply chains which need to be resilient in the face of continued disruption.

- And occupiers seeking operational efficiencies through consolidation into larger, modern and more efficient facilities.

With that backdrop, let's look at the themes we're seeing in the market that are contributing to the success of our business.

In the top left chart, we see 2021 was another very strong year for lettings at 42.4m sq ft, broadly on par with the previous year, but this was undoubtedly suppressed by constrained supply. You will see also depicted by the terracotta bar that unsatisfied demand is equivalent to around 4 years of average take-up, which bodes well given that supply of new buildings remains constrained.

It also explains our confidence, because the structural changes we are seeing are still in their infancy, underpinning the significant scale and duration of the opportunity, which is positive for our future.

Turning to the top right chart: As just mentioned, supply has significantly lagged demand, producing the lowest vacancy rate ever reported of only 1.6%. And there are now only 2 buildings available to let that are over 500,000 sq ft, one of which is in the course of speculative development and the other is older, second-hand space.

Bottom left, we see that the increasingly acute supply/demand imbalance continues to drive rental growth, and agency forecasts have strengthened for the next few years. And this is reflected in our own development portfolio, where we have witnessed strong double-digit rental growth in some locations, well ahead of our original expectations.

And bottom right; strengthening and resilient rental growth has encouraged increased investment demand, with 2021 producing the highest level of investment activity recorded for industrial and logistics property.

There remains a wall of unsatisfied capital, and we do expect to see further yield-induced value gains in 2022. That would be good news for our investment assets, our land, and the assets that we are developing.

For us, this slide demonstrates the growing and long-term need for high-quality logistics space capable of helping our customers respond to these dynamics.

And these drivers are part of the ongoing market back-drop which support our strong performance.

It's worth reminding you that we designed our strategy in anticipation of these long-term trends in our market. Again, you will be familiar with our strategy by now, but I'll just highlight the key points.

In essence, there are three key components.

You can see at the top of the triangle, that we have deliberately built a portfolio of high-quality assets attracting great customers. We have also built the capabilities to add value to these assets through direct and active management. And we apply our skills, insights and innovation, gained from being the UK's largest investor in logistics, to develop our land portfolio at a very attractive yield on cost.

And I really want to emphasise the point at the bottom here; this strategy is underpinned by a very disciplined approach to capital allocation, with sustainability being embedded across the portfolio.

Now this case study is a great example of our strategy in action: high-quality customers, proactive management and development, working together to create opportunities for growth.

B&Q is an existing customer at Worksop, in Nottinghamshire.

Over several years we have built a strong relationship with B&Q and grown our understanding of their operations. As part of this, we undertook an in-depth analysis of their entire supply chain network and shared our findings with the senior team at B&Q. This highlighted a requirement for additional space in the Yorkshire area to support their growing Leisure business.

Our geographically diverse land portfolio included a site at Doncaster that fulfilled the brief for a large cross-docked facility. We had already secured detailed planning consent, and this enabled us to offer a swift delivery of the building.

B&Q felt this met their requirements in terms of location, scale and timing, and subsequently committed to a new 15-year pre-let of 430,000 sq ft, the development of which has already started, and practical completion is targeted for this December.

The building will be constructed to BREEAM Very Good and an EPC rating of A. It will have 20% solar PV panels and will be net zero carbon in construction.

So, you can see that this encapsulates the full journey of our strategy, from investment, through active and direct management, to development, and producing a new, high-quality, and sustainable investment.
This brings me on to how we are leading in ESG across our business.

ESG is a key strategic priority for our business. Here I want to provide an updated snapshot on our strong sustainability position and the progress that we continue to make.

We have hand-picked and built a modern and sustainable portfolio and it is modern buildings that occupiers are demanding. 95% of our floorspace has an EPC rating of A to C. Also, approximately half of total floorspace is certified to BREEAM Very Good or Excellent, well above the industry average and this is reflected in our leading ESG position.

This is a critical factor, because our portfolio modernity means that we don’t face significant future capex requirements to enhance environmental performance and meet government targets. This reduces the risk of ’brown discounts’ to capital value and ensures that our buildings are fit for future occupiers and purchasers. Our development activities allow us to integrate ESG performance throughout the lifecycle of a building from design to construction, to asset management. Our net zero carbon pathway targets are set to reduce embedded carbon and deliver new buildings which are net zero in construction; the new B&Q building at Doncaster being a good example.

Our focus on social impact is to support local communities through job creation and local charity partnerships.

In tandem we are working hard to implement initiatives which produce biodiversity net gains on our sites, and in the local area.

We are implementing increased levels of renewable power, and in 2021 generated 903 Megawatts of solar PV power for our customers, avoiding over 208 Tonnes of Carbon emissions.

Every year we poll our occupiers on what’s important to them. We’ve seen a notable increase in ESG as key factor in their decision making, with nearly 70% saying it was very important to them – that’s up from around 50% four years ago.

This activity is being recognised in our ESG scores, with improvements in our ratings from every major agency.

As mentioned, our portfolio already screens well, but we will continue to improve these ESG credentials, both for our investment properties, and our developments.

As I said earlier, the first key element of our strategy is our modern, long-let investment portfolio. But we don’t just sit back – we actively manage our portfolio to optimise its performance – the second key element of our strategy.

All our investment assets are regularly reviewed for opportunities and threats. Our objective is to maximise total return whilst optimising our income growth and ensuring that we maintain a balanced portfolio with low underlying risk.

We will seek to dispose of assets which we believe have maximised value in our hands and acquire investments that we believe will be accretive to portfolio performance.

Investment sales will also help fund the opportunity in our development portfolio, which is accelerating. Turning to income composition and timing, the first thing to say is that all our lease rent reviews are upwards only.

You can see here on the pie graphs that we've created an attractive blend of rent review types:

- about half of our investments are subject to inflation linked reviews (which have cap and floor arrangements)
- with around a third being open market
- and the remainder fixed or hybrid.

As to timing, 20% of our rents are subject to annual rent reviews, providing attractive and regular compounded growth, with the remainder reviewed 5-yearly.

And the recent growth in market rents is embedding within our portfolio. This is demonstrated by the growing rental reversion up from 6% in 2020 to 11% in 2021, which I will come back to in a moment.

So, let's look at how we are putting this into practise.

This slide captures the way we are complementing rental growth with active management.

During the period we negotiated the lengthening of two leases, one by 2 years and the other by 10 years. Of the 37% of our rents up for review in 2021 we concluded 32%. This delivered a £5m pa increase in passing rent and reflected like for like rental growth of 3.3% annualised.

We expect further progress as we conclude the remaining reviews this year, with 5% carried over from last year, added to the 35% due for review in 2022 as shown in the chart.

So, this positive active management momentum, is going to be yet another driver of both income and capital growth in our investment portfolio, but also for our development activities and our land assets.

Now to update you on the great progress we've been making in the third key element of our strategy – development.

In January we held an investor seminar focused on the detail of our development activities. This can be viewed on our website.

At the year-end our Investment Portfolio represented around 92% of GAV, and the Development Portfolio approximately 8%; this balance has been a conscious decision so that our development activities are supported by high quality and robust income from our investment assets.

Let's now look at what we are seeing on the ground.

We are seeing significant and accelerating demand for a range of building sizes and locations, which plays to our strengths, because we have a geographically diverse portfolio and flexibility within our sites.

But of particular value is the ability to offer larger format buildings which competitor sites often cannot. And this is paying off because you will see on the left pie chart that most enquiries received have been for buildings over 300,000 sq ft in size.

Equally positive for us is a broad range of occupier types, as shown by the middle pie chart, with online enquiries remaining strong at nearly half of the total but also store retail and third-party logistics operators being particularly active. Savills recently reported that over the last two years, 257 companies had leased new space, indicating significant breadth to occupational market demand.

Strong relationships with existing customers are creating repeat business for our development activities, but we are also expanding our customer diversity, with a healthy list of high calibre enquiries – in 2021 we added DPD, Harper Collins, Ikea and Apple as new customers.

This all translates into unprecedented enquiry levels.

At the year-end we had over 26m sq ft of live enquiries. This breaks down into over 16m sq ft of high-level discussions, and over 10m sq ft of negotiations in final stages (which includes deals where terms are agreed, or which are in solicitors' hands).

So how can we fulfil this demand?

Here we've presented our development pipeline, which is matching up market demand with our available land.

You've heard me say before that there are barriers to entry, and it can take many years to achieve planning consent – our own portfolio has taken over 10 years to assemble and finesse to get to a position where it can fulfil the levels of demand we see.

Our team is highly experienced, has excellent relationships with local authorities and landowners, built up over many years, and a tremendous success record on planning.

Our land portfolio is constantly evolving - as sites and projects move through the planning and development process from allocation to planning consents.

The goal of this dynamic model is to create a rolling programme of consented land running off the planning conveyor belt – ultimately, producing a continuous flow of buildings under construction and development.
To help provide a bit more granularity, this chart breaks down the development pipeline into the 3 'buckets' that you will be familiar with from previous reporting:

- the current development pipeline – including the projects under construction.
- the near-term pipeline – which we have now split into:
    - anticipated development starts over the next 12 months
    - and starts over the following 24 months.
- and the future development pipeline - comprising the strategic land portfolio that is further back in the planning process.

As you can see, in addition to the 1.3m sq ft already under construction, and in response to the greater visibility of occupier demand, we expect to accelerate development starts in 2022 to around 3.7m sq ft.
In the following two years of the near-term pipeline - we expect activity to revert to be more in line with the long-run average of 2-3m sq ft per annum.

We will, however, be looking to bring forward planning consents where possible, and also consider enlarging the quantum of land draw-downs where this flexibility exists and if occupier demand remains strong.
In other words, we will seek to maximise the opportunity that is in front of us now - whilst also carefully managing the risk.

And you will see at the bottom of this chart the potential additional income generation at each stage.
Key here, is that we have sites at all stages of this evolutionary process. That is an optimal position in our view. So that's the timeline, let's now look at how we're going to capture the opportunity.

What are we capable of achieving from our development land portfolio?

Well, as you can see on the left, we have all of the attributes for long-term success, and I am pleased to report that we are making very good progress, consistent with our guidance.

This is now showing through in both what we have achieved and increased confidence in our near-term delivery:
2021 was the year that our development activities came of age:

- We delivered 3.7m sq ft of lease completions
- Added £24m to our rent roll
- Commenced construction of 1.3m sq ft
- And secured a further 3m sq ft of further planning consents.

Turning to 2022, we have made a terrific start:

- We have already commenced 1.8m sq ft of development;
- And because of the heightened level of demand and our ability to respond, we are messaging an acceleration from 2-3m sq ft of development starts to 3 to 4m sq ft this year.

The 1.3m sq ft of developments under construction will complete in 2022, which, when added to the 3.7m sq ft of lease completions in 2021 provide visibility on £36m of potential additional rent.

To close on development, I simply want to say that we are in a unique position, and we will look to exploit the development opportunity within our business, to take advantage of our expertise and market dynamics, whilst employing a risk-controlled approach to our activities.

So, to sum up and before we get to Q&A, I just want to emphasise the hugely positive key points from today:

- We have a strong balance sheet, a number of funding options, and the financial discipline to deliver attractive and sustainable performance

- Our clear strategy is now delivering, both for investment and development assets, and we expect enhanced activity in both areas of our business in 2022, taking advantage of the very favourable market conditions

- Structural change is, and will continue to benefit our market, with inelastic supply, and unprecedented occupier demand, driving strong rental growth, and attracting increased inflows from worldwide capital

- And we control the UK's largest logistics focused land portfolio, capable of delivering over 40m sq ft at very attractive yields, with the objective of enhanced earnings growth and the creation of new, high-quality investments.

So our excitement and enthusiasm stem from being at the right place, at the right time, with the right strategy, the right product, and the right team to unlock value; and we are doing so, right now.
Thank you for listening.
That concludes today's results presentation. I will now hand over to Ian who will coordinate the audio Q&A session.

IAN:
Thank you Colin.
That concludes are presentation and we will now turn to Q&A. As a reminder, to submit your question please use the text box within the webcast viewer to type your question.

Q&A

Ian Brown: Great. We've had a couple of questions come in through the webcast through the course of the presentation, a number relating to rental growth, the first being, could you expand upon the prospects for future rental growth from the portfolio?

Colin Godfrey: Sure. As I mentioned in the presentation, 32% of our portfolio was reviewed in 2021, delivering a like-for-like rental growth, 3.3%. Now, this is obviously backward-looking over a five-year time horizon, typically, which incorporated a period with lower inflation and lower market rental growth. Obviously, rental growth has been increasing in the intervening period of time, and I think that's evidenced, as I've mentioned, in our strong ERV growth in the portfolio, up 7.5%.

Colin Godfrey: Just noting how we can access that and the 11% reversion that we now have in our portfolio, firstly, we've got a good balance of rent reviews, index-linked reviews - broadly half of our portfolio - providing a natural hedge, and of course, open market rent reviews, which together with the hybrids, which are the higher of, around about 40%, enable us to capture that true market rental tone.

Colin Godfrey: In addition to that, of course, we do have our development pipeline which enables us to capture market-leading rents at the coal face on brand new buildings, and there's a cross-read from that, of course, against our investment portfolio, which further allows us to drive income growth. That's part of the power of the development portfolio.

Colin Godfrey: Of course, the very low occupancy levels that we're seeing across the market are allowing us to beat the levels which we've embedded into our development appraisals, so that's very positive. Finally, just to mention that around 19% of our income expires within the next five years, and again, this will enable us to capture that rental reversion in the near term on new lettings for some of our existing stock. Hopefully that covers the point.

Ian Brown: Great. Thanks, Colin. The next question relates to inflation and the experience we have within cost inflation within the development pipeline.

Frankie Whitehead...: Thank you, Ian. Yes, we have been experiencing certain cost price pressures with regards to materials and to labour. I would say we're seeing some stabilisation in that of late in the last few months, but we continue to monitor that closely. We're mitigating where we can, and that includes the entry of fixed-priced build contracts on all of our developments.

Frankie Whitehead..: Also, rental growth and yield shift continues to prevent a large part of that from impacting on performance metrics. As reiterated today, we're still confident in delivering within that 6% to 8% yield on cost range for future developments and note that we're expected to be in the lower half of that range for our near-term portfolio.

Ian Brown: Great. Thank you. Next question is from Alison Sun at Bank of America, who asks if we have any exposure to Eastern European tenants?

Colin Godfrey: The short answer is, no, we don't. Obviously, we are concerned about events in Ukraine. Our thoughts are very much with the people that are being impacted, and it's clearly a very uncertain situation that's moving day by day and we're monitoring it closely, but we don't have any Eastern European exposure, and we're not seeing any significant impact on our business operations because we're fortunate enough to have a highly resilient portfolio. I think that was demonstrated during COVID, where we've had 100% rent collection. I think that's because our buildings are, obviously, UK only, but they're intrinsically important to our customers.

Ian Brown: Thank you. Next question from Shayan Ratnasingam at Winterflood, who asks, "Is the conversion of license fee to rent recognised in the adjusted earnings, and does the impact net off the loss of license income?"

Frankie Whitehead...: Thank you, Shayan. Yes. The answer that is, yes, the license fee reduction here is essentially netted off the adjusted earnings figure, so yes, it's all reflected.

Ian Brown: Great. Next question from Paul May at Barclays. "How up to date do you feel your valuations are? While the ERV growth of 7.5%, 45 basis points yield compression, and valuation growth are all strong, they appear conservative relative to the underlying market moves, especially the 4.1% equivalent yield."

Colin Godfrey: Thanks, Paul. It's a good question. Look, the CBRE prime yield at the year end was 3.5% for 15-year income. Valuation is a backward-looking exercise, picking up comparable evidence. We were aware, for instance, at the year end, well, very close to the year end, there was a deal done for an Amazon 15-year lease for a new building at Peterborough. From memory, it was done around about 3.2% mark.

Colin Godfrey: We are aware of assets and indeed portfolios which are currently being marketed and/or are under offer off-market, and, assuming that they progress to completion, they're at levels which would demonstrate further yield compression, even in the first two months of this year. We do feel that the positive momentum that was seen in Q4 of 2021 has been carried forward into 2022, and this talks to the relative confidence we have in further yield compression being evidenced in 2022. Off our current 4.1% equivalent yield, yes, we feel pretty positive about the prospects for further capital appreciation during the course of this year.

Ian Brown: Great. I've had a couple of questions around disposals, so thematically, I think the question is around why there have been no disposals during 2021 and prospects for disposals moving into 2022.

Frankie Whitehead...: Thank you, Ian. Yes, that's correct. No disposals in 2021. I think that's reflective of our view of market conditions, given the level of yield compression we experienced. We believe that holding onto those assets was the right thing to do and enhanced our performance in respect of 2021. Going forward, clearly, asset recycling is a good investment discipline, and we'll look to do that in order to optimise the performance of our portfolio.

Frankie Whitehead...: We have provided some guidance this morning in terms of both the near and longer-term disposal targets of £100 to £200 million per annum, so we see that we are looking to optimise performance of the portfolio, as we look to recycle that capital into more creative opportunities.

Ian Brown: Question from Tom Musson at Liberum, who asks, "If the demand in the market is currently four years of average take-up, why not commit to three to four million square feet if developments starts for more than just the next 12 months? How much is the business operationally able to commit to in any given year?"

Colin Godfrey: Thanks for that, Tom. Well, look, I think it's fair to say that during the last six months or so, we've gained increased visibility on occupation interest, particularly in relation to our near-term pipeline and, as you quite rightly say, we've increased our guidance up from two to three million square feet in 2021 to three to four million square feet in 2022.

Colin Godfrey: Now, whilst we're giving longer-term guidance of two to three million square feet, there's nothing to prevent us from maintaining a three to four million square feet level into the medium term, subject to the demand being there. We're just being relatively prudent. We don't have that crystal ball, and you're absolutely right. The backdrop to the market is very positive, and it could well be that we continue to travel at that level.

Colin Godfrey: I think it's important to recognise, however, that we continue to bring land through the planning process, and three million square feet consented last year. Also, implementing infrastructure works at a given rate, and mindful of the rate at which we can bring through continued new planning, and we want to continue to be able to replenish that planning consented bucket, so we don't run out of planning consented space.

Colin Godfrey: I mean, that's important to continue to attract occupier interest right the way across our sites across the UK, and indeed, I think there are some developers that are probably a little bit concerned about the run rate at which they're burning up their planning consented sites, bearing in mind that there are natural barriers to entry within the planning system which are going to control the supply side. I think that will keep the supply and demand in balance, very, very healthy, but it does mean that one's got to manage that process. I don't think we're worried at about the potential for upscaling even to five-million-plus square feet in the context of our manpower capabilities within the business.

Colin Godfrey: The last thing, just to mention, is that one's got to think about the context of that total in terms of number of buildings and the size of those buildings and the type of those buildings. For instance, if you get a multi-decked building let to a major online retailer, by way of example, and it could be two million square feet in one building, that's a very different proposition than creating 10 buildings of 200,000 square feet each. There needs to be a bit of understanding about that component part, as well. Hopefully that sort of gives you a bit of a feel for how we see the future guidance.

Ian Brown: A couple of questions along a similar theme here, around inflation more generally. How is your appetite for inflation-linked leases evolving, especially for new developments? What is your preferred rent review clause for new leases now? Similarly, are we likely to see more or less open market review clauses, given open market rent review gains are higher than inflation currently? The second part of this question, on the inflation-linked reviews, most of these are capped and collared with your average range of 1.5% to 3.4%. Do you see the spread being stretched, given current rates of inflation, and are tenants willing to agree high inflation-linked caps?

Colin Godfrey: Okay. There are quite a few components in there. Shall I start, Frankie, and then we can play a bit of tag team here? I think the first thing to say is that I think we are very well-positioned to mitigate most of the downside risks and capture the upside but, as I said earlier, 50% of our leases are inflation-linked that act as a cap. Open market reviews are uncapped, typically.

Colin Godfrey: It's very, very rare to see an uncapped inflation-linked rent review. The uncapped component is typically through open market. Certainly, in the current market, we are seeing stronger growth in terms of open market rents, than we've seen ever before.

Obviously, inflation's particularly high at the moment, but I think in the medium term, we should see probably stronger growth from market rents.

Colin Godfrey: There is potential to capture a higher proportion of market rents through our development platform. Occupiers, certainly the larger-scale corporates, they do like the relative certainty of knowing that their rents are moving in tandem with underlying inflation. However, of course, this is a landlord's market in many, many respects. We do have strength and depth of interest on most of our sites, and that enables us to negotiate from a position of strength in relation to the type of rent review that we would like to see.

Colin Godfrey: Clearly, if an occupier is going to be resistant to the potential for open market rent reviews, then they may well lose that opportunity and find themselves struggling to meet that requirement, having to move to a location which is less favourable for them, and not securing that building when they need it. Typically, we're seeing sensible conversations being had.

Colin Godfrey: We are now seeing more conversations along the lines of the best of both worlds, the higher of open market or inflation, as well, so I think we're seeing sort of a trend in that direction, which is positive news for us. Frankie, do you want to pick up generally on the interest rate point? Is there anything more to say on that, or have we covered it off?

Ian Brown: Just looking at the next question, coming from Luqman Hamid at NinetyOne, who asks, "What are the likely effects of substantial cost pressures on your tenants' ability to absorb substantial rental increases? He also asks, are labour issues limiting tenants' ability to roll out new warehouse locations?"

Colin Godfrey: That's a great question. The first thing to say is that from the analysis that we've undertaken, property costs, say for an average retailer, typically sit at around or less than 1% of total operational costs. If your rent goes up by 10%, it's sort of 10 bps on your total operational costs. It's relatively small amounts of money. I mean, what occupiers are telling us is, it's much, much more important for them.

Colin Godfrey: Clearly, they don't want to pay more than they need to, but they have to be in the right place at the right time to fulfil the requirements of their customers, and that's much more important when we're facing structural change and ever-more-complex supply chains, customers demanding product more quickly, more reliably. I think that's the primary focus for them.

Colin Godfrey: We're not seeing much in the way of cross-price resistance to escalation in rent. Clearly, there is a consideration in terms of affordability, ultimately, and ever was it the case, but it's more about the space race for getting the right buildings and the right locations right now. In terms of... I think the last point you mentioned, was it labour? Labour cost?

Ian Brown: Labour benefit.

Colin Godfrey: That's a very, very good point. I think the old adage of location, location, location has sort of changed a little bit to, I would say, location, power, and labour, and with power becoming an increasing important component part of occupier thinking, particularly with increased levels of automation, but the labour is very important, as well.

Colin Godfrey: What you don't want to do as an occupier is to sort of cut your own throat in competition with a competitor next door because there just isn't the right labour pool. Most occupiers do a lot of work on this. Now, this is something we saw, really, when we set up our business back in 2013, and we recognised that what I would describe is the sort of devolution of the distribution network in the UK emanating away from the central focus of the golden triangle, and ever that has continued.

Colin Godfrey: You see lots of major occupiers now moving out into locations where the motorway network's less congested, where they can more readily capture labour, appropriately skilled labour, and by the way, lots of these buildings now are providing labour for highly skilled workforces, at appropriate pricing points where they can retain that labour and invest into that labour with training, and obviously, retain that labour in the longer term. It's a really, really important point, and that's one of the reasons why we're seeing the emergence of new parks and new locations, but we need it, because there's so much demand in the market. We need the emergence of new locations in the UK.

Ian Brown: Great. Thanks, Colin. Next question is from Mike Prew at Jefferies, who's asking, "Are you holding back marketing developments to capture the rising rents through the construction phase, or is there still a pre-letting requirement before breaking ground?"

Frankie Whitehead...: Thank you, Mike. With regards to the development strategy, this really is about a balance between pre-let and speculative activity. I think that good demonstration of that is in the year-to-date activity, we've commenced 1.8 million square feet, of which around 56% has been pre-let, demonstrating that balance.

Frankie Whitehead...: Typically, on the larger-format buildings, we will look to secure a pre-let, derisking that aspect of the strategy. On the smaller speculative assets, we are willing to, obviously, break ground there, commence construction, hold back the rents, potentially quoting a range, looking to capture the live level of rental growth and the live market perspective in terms of securing those rents. Answer is, it's a combination of both.

Ian Brown: Great. Thanks, Frankie. Next, I think this is going to be our last question, given time, a question from Alison Sun at Bank of America. "You mentioned the CBRE prime yield is 3.5% as at year end, and your reported net initial yield was 3.56%. Should we interpret this as not lagging the CBRE data, or am I looking at the data incorrectly?"

Colin Godfrey: The short answer is, it's an incorrect interpretation. The way to think about this is that the CBRE yield is for a rack-rented building. In that circumstance, your initial equivalent and reversionary yields are all same, i.e., 3.5%. The 3.56 you referred to as an initial yield is not taking into account the intrinsic benefit of the reversion which is inherent within our business, and that's why we point to the 4.1% equivalent yield, which is the number that one should view as comparable with the 3.5% figure that I mentioned from CBRE. That's the point of the comparison. It's 4.1 versus 3.5.

Colin Godfrey: When one looks at the quality of our assets, the length of our leases, et cetera, we do believe that there's further room for value growth in our portfolio during the course of this year, but one has to be cognisant of the backdrop of macroeconomic instability and the effect that could have on market. Whilst the investment market's currently very strong, we still, obviously, have the remaining part of 2022 to play out.

Ian Brown: Great. I think that's it for questions, Colin.

Colin Godfrey: Splendid. Well, look, thank you very much, everybody, for supporting the business during the course of last year, and for taking the time to join us today and provide us with your questions. We really appreciate the continued interest, and we wish you a splendid rest of the day. Thanks very much. Goodbye.

Ian Brown: Thank you.