Chief Executive's statement

Delivering increased dividends

26.3p

Our strong earnings growth during 2022 and confident outlook for 2023 means that we are recommending a 7.7 per cent increase in final dividend to 18.2 pence per share, resulting in a total distribution of 26.3 pence for 2022 as a whole.

David Sleath,
Chief Executive

David Sleath reports on SEGRO's performance over the past year and looks to the future.

Our business delivered strong operational results during 2022, a year where we saw significant geopolitical uncertainty and changes to the macroeconomic environment. This led to an unprecedented disconnect between the occupier and investment markets emerging over the summer months.

Actions taken by central banks to address high levels of inflation by sharply raising interest rates led to significantly reduced liquidity in the property investment markets in the second half of the year, as both buyers and sellers reacted to the increased volatility in capital markets and the higher cost of capital. Valuers increased yields to reflect this higher interest rate environment, leading to falls in property valuations across all markets. In contrast to former property cycles however, occupational demand and rental performance in the industrial and logistics sector has remained strong, supported by long-term structural tailwinds and tight supply.

The expertise and knowledge of our local teams on the ground across Europe meant we could respond quickly to the changing market environment and deliver progress in all our operating metrics throughout the year as well as continued growth in both earnings and dividends.

Looking back on 2022, our main highlights include:

- a record £98 million of new rent contracted, arising from a combination of active asset management of our existing portfolio, our expanded development programme, market rental growth and the benefits of indexation;
- 639,200 sq m of development completions, and a reduction of ten per cent in the average embodied carbon intensity of our development programme;
- the acquisition of key strategic land plots in some of Europe's most supply constrained urban markets such as London, Paris and Berlin;
- progress towards reducing our portfolio's carbon emissions with the introduction of green lease clauses, and a significant increase in our solar capacity;
- the launch of Community Investment Plans in ten key markets, providing tangible economic and social benefits for thousands of people in the communities closest to our assets;
- meaningful changes to promote diversity and inclusion within our workforce and the wider property sector, including, for example, changes to our recruitment process which resulted in a more diverse 2022 graduate intake.

This activity helped us to deliver a 6.5 per cent increase in Adjusted earnings per share (10.7 per cent excluding the SELP performance fee) and we are therefore recommending a 7.7 per cent increase in our final dividend to 18.2 pence per share, resulting in a total distribution of 26.3 pence for 2022 (2021: 24.3 pence).

Reflecting on 2022, three things stand out for me:

- the performance of our high-quality portfolio, and the benefits of the decade-long reshaping of both that and our balance sheet, particularly in the current market environment;
- the continued strength and diversity of occupier demand;
- the tangible progress that we have made with our Responsible SEGRO strategic priorities, and the long-term value that we are creating through our activities.

1 EPRA and Adjusted metrics: The Financial Statements are prepared under IFRS. SEGRO management monitors a number of adjusted performance indicators in assessing and managing the performance of the business which they believe reflect the underlying recurring performance of the property rental business which is the Group's core operating activity. These include those defined by EPRA as part of their mission to establish consistency of calculation across the European listed real estate sector. Page 171 contains more information about the adjustments and the reconciliation of these to IFRS equivalents. SEGRO discloses EPRA alternative metrics on pages 203-208. Adjusted NAV per share is in line with EPRA NTA.

Financial Highlights

Adjusted profit[1] before tax

£386m +8.4%

2021: £356m

IFRS loss[1] before tax

£-1,967m

2021: £4,355m profit before tax

Adjusted[1] earnings per share

31.0p +6.5%

2021: 29.1p

IFRS earnings per share

£-159.7p

2021: 339.0p

Adjusted NAV[1] per share

966p -15.0%

2021: 1,137p

IFRS NAV[1] per share

938p

2021: 1,115p

Portfolio value[2]

£17.9bn -11.0%

2021: £18.4bn

Chief Executive's statement
continued

Our spaces can be adapted to a variety of different uses, which means we are not overly exposed to a particular sector and also that we can capitalise on growth opportunities in non-traditional industrial and logistics occupiers, such as data centres and life sciences.

David Sleath
Chief Executive

Over a decade ago, we launched a strategy centred around an ambition to create a portfolio focused on the most attractive industrial and logistics markets across the UK and Continental Europe, one that would deliver attractive total returns throughout the cycle. An important element of this strategy was the strengthening of our balance sheet to provide resilience, and to ensure we could take advantage of opportunities for further growth even in more challenging market environments.

Since launching that strategy, the industrial and logistics sector has transformed. Long-term structural trends of digitalisation and urbanisation have led to increased occupier demand, driving down vacancy rates to record lows. This shortage of supply led to exceptional levels of rental growth, attracting huge amounts of investment into our sector and increased competition.

We adapted our strategy accordingly, selling non-core assets in secondary locations and buying new assets in our preferred locations. As competition for standing assets increased we moved away from acquiring them on-market, instead investing capital into development, where we believed we could produce better risk-adjusted returns. We also reduced leverage and worked hard to create a diverse, long-duration debt profile.

During 2022, our portfolio was not immune to the sharp rises in interest rates, which increased the cost of capital and consequently, yields on commercial properties. This led to a fall in valuation of 11.0 per cent during the year. At this time, benchmark information is not available for the Continent but in the UK our portfolio has outperformed the MSCI Quarterly All Industrial index which showed a decline in capital values of -17.4 per cent during 2022, versus SEGRO's UK portfolio which decreased by 15.5 per cent. This reflects the positive benefit of the changes made to our portfolio over the past ten years and our continued focus on Disciplined capital allocation.

Importantly, the strength of our balance sheet, has meant that, as long-term investors, we have been able to look through the current volatility, and focus on the areas that we can control: capitalising on the continued strength of occupier demand to drive rental growth; capturing a significant amount of the reversionary potential in our portfolio (which has grown once again due to further market rental growth in both the UK and Continental Europe); and signing pre-lets to build out our well-located land bank.

Consistent throughout 2022 was the strength of the occupier market. Demand from our customers has been, and continues to be, very resilient. Take-up remained very high and well above historical averages. Most notably, we saw increased demand from businesses which are attempting to make their supply-chains more resilient during 2022: holding more inventory locally and therefore requiring more space; moving parts of their operations back to Europe and the impacts of businesses choosing to source materials closer to their end destination.

We have also seen customers placing greater importance on the sustainability of the buildings they occupy. Many of our larger customers have their own net-zero targets and want the space that they occupy to contribute to this. Smaller businesses have been impacted by recent increases in energy prices and are recognising the benefits of choosing more energy efficient buildings and working with a landlord who will help them to understand their energy consumption and can provide solutions to help reduce it.

These structural drivers are resulting in demand from a diverse range of businesses and our teams have been working hard to capitalise on it. In 2022 we leased space to existing customers who value the excellent customer service that they receive from SEGRO, and to new customers who bring even greater diversity into our rent roll.

As part of the day-to-day management of our portfolio, our teams prioritise our three Responsible SEGRO strategic priorities and in 2022 we saw tangible benefits from these initiatives.

There were a number of innovations within our development programme that helped us to reduce our average embodied carbon intensity, such as using recycled roof materials to create asphalt for road surfaces. We have also significantly increased the number of solar panels installed on our warehouses, with one project in the Netherlands adding almost 20 per cent to our total Group capacity, which makes us excited about further similar opportunities across the portfolio.

We have launched ten Community Investment Plans (CIPs) in key markets, and projects are underway across the UK and Continental Europe that focus on employability, supporting local economies and improving local environments, making meaningful changes to the day-to-day lives of people in our local communities. Thousands of people have already benefited from projects linked to these and this is only the beginning.

We have also made great progress with our Nurturing talent ambitions, focusing on the wellbeing of our people (including providing extra support for those most impacted by the cost of living crisis) and actioning recommendations from the National Equality Standards audit to promote diversity and inclusion within our workplace and the wider property sector.

Not only are these initiatives creating additional value for our stakeholders, they are ensuring that our business is fit for the future and that it is truly delivering on its Purpose of creating the space that enables extraordinary things to happen.

2022 might not have been the year that we all expected, but our business has shown its quality and resilience and has continued to deliver value. I am proud of how everyone at SEGRO has come together and worked hard to make this happen.

Outlook

Our long-standing disciplined approach to portfolio management means that SEGRO has one of the best and most modern pan-European industrial warehouse portfolios, through which we can serve our customers' entire regional and local distribution needs. Two-thirds of this portfolio is located in Europe's most attractive urban markets, often in substantial clusters in key sub-markets, where the lack of available land means that supply-demand dynamics are tightest and where long-term growth and returns are therefore likely to be the highest. This is complemented by the remaining one-third of our portfolio, comprising clusters of high-quality logistics warehouses situated at key hubs along major transportation corridors.

Occupier demand for warehouse space across Europe continues to be positive and is derived from a wide variety of customer types. Our space is flexible and can be adapted to suit businesses from many different industries which, when coupled with our relentless focus on customer service through our market-leading operating platform, is reflected in high customer satisfaction and retention rates, as well as our asset management and leasing performance. Our business is therefore both resilient and positioned to support growth sectors and adapt to trends, including e-commerce, the digital sector (data centres), urbanisation and the consequential need for industrial and distribution space close to the end customer from a very broad range of businesses.

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Supply and availability of modern, sustainable warehouse space in the locations most desired by occupiers remains extremely limited across Europe. Vacancy levels are at historical lows and supply is likely to remain constrained given recent increases in financing and construction costs. We expect this contrast between positive demand and limited supply to drive further growth in rental levels. We already have £130 million of reversionary potential embedded in the portfolio (most of which will be captured through the five-yearly rent review process), as well as indexation provisions in almost half of our leases, both of which underpin future like-for-like rental income growth even before any further growth in market rental levels.

Our sizeable, mostly pre-let current development programme and well-located land bank, provide us with further potential to grow our rent roll profitably and allows us significant optionality due to the short construction periods of our assets. We will continue to be led by customer demand and our Disciplined approach to capital allocation as we make decisions regarding the execution of future projects.

With modest leverage, a long-average debt maturity of 8.6 years, no near-term refinancing requirements and virtually all of our debt at fixed or capped rates, we have significant financial flexibility to continue to invest capital in the development and acquisition opportunities that offer the most attractive risk-adjusted returns.

As we enter 2023, there are early signs of liquidity returning to the investment markets, as investors see value at current levels of pricing. As the path of future interest rates becomes more evident, we believe there is a significant volume of capital ready to be deployed into the industrial and logistics sector due to its attractive fundamentals. We will continue to respond tactically to changes in market conditions, but our long-term strategic focus is to ensure that our properties are of the highest quality and the most sought after, able to generate superior long-term growth, and therefore command a valuation premium.

We will also continue to invest in and de-risk the future of our business via the significant progress we have made with our Responsible SEGRO strategic priorities.

Our prime portfolio and market-leading operating platform combine to create a strong competitive advantage, and position us to create value through the cycle for all of our stakeholders. We therefore remain confident in our ability to deliver attractive returns and continued growth in earnings and dividends into the future.

David Sleath
Chief Executive