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Results analysis: Schroder Real Estate

SREI delivers a positive total return as property values begin to stabilise...

Update
12 June 2025

- **Schroder Real Estate's (SREI) final results to 31/03/2025 show a NAV total return of 11.0% for the year, comprising a 4.8% increase in NAV per share and a 3.5p dividend (2024: 3.34p +4%). The dividend was 100% covered by earnings and at the current share price SREI's dividend yield is 6.6%.**

- **SREI's underlying property portfolio gave a total return of 9.1%, a continuation of the long-term outperformance of the benchmark MSCI UK Balanced Portfolios Quarterly Property Index, which saw a total return of 6.2%.**

- **Performance was driven by a mixture of sector weightings compared to the benchmark, with SREI's overweight positions in retail warehouse and industrial sectors, detailed below, and active management, with capital expenditure on targeted assets and leasing up on SREI's flagship net zero industrial asset at Stanley Green all contributing to the outperformance. A further £6.7m of capex was invested in asset management and redevelopment projects expected to drive further income and capital growth.**

- **SREI's main sector weightings are industrial 51% (benchmark: 33%), retail warehouse 13% (benchmark: 10%), offices 23% (benchmark 22%) and standard retail 8% (benchmark 10%).**

- **SREI's industrial assets recorded a total return of 11% compared to the benchmark's 9%, retail assets' total return was 14% compared to the benchmark's 9%. The broader office sector generally performed less well, with the benchmark total return 1.5% but SREI's office assets outperformed with a 2.7% total return.**

- **SREI's net initial yield is 5.6% (benchmark: 5.1%) and the reversionary yield is 8.4% (benchmark 6.2%), which gives it significant upside on the existing portfolio. With several asset improvement programmes underway, the void rate c. 12%, is higher than the benchmark's 9%, although c. four percentage points of this is now either let or under offer.**

- **SREI's weighted average lease length is 5.3 years, significantly lower than the benchmark's c. 11 years, giving greater opportunities for active management of leases.**

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- **SREI's net gearing was 36.9% on an LTV basis (2024: 37.1%), or 59% of net asset value . The average interest rate was 3.5%, with 88% of debt at fixed rates with an average maturity of 8.5 years. This is slightly higher than the long-term target range of 25-35%.**

- **During the year, SREI made one small disposal for £1.475m, a 51% increase on the 31/03/2024 valuation, and post year end an asset was sold for £1.25m, a 28% premium. The manager expects to make further disposals of smaller assets with the aim of recycling into larger assets.**

- **SREI'S Global Real Estate Sustainability Benchmark ('GRESB') score remained at 79 out of 100. 15 of SREI's 38 assets now have an ESG scorecard completed by an external consultant along with a sustainability audit or net zero carbon audit, giving a baseline against which to measure future performance. Three**

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assets achieved an improved score compared to their baseline at 01/04/2024.

- **During the year Nick Montgomery, SREI's long-term manager, was appointed Schroder's head of real estate. Bradley Biggins, who has worked alongside Nick on SREI since 2022 will remain as co-manager and a further co-manager is expected to be announced in due course.**

- **From 01/10/2025 SREI's management fee, 0.90%, will be updated so that 50% will be charged on the lower of market cap or NAV, with the balance charged on NAV. Charging fees on market cap creates greater alignment between the manager and shareholders.**

- **Alastair Hughes, chair, said "Looking forward, and despite near term market uncertainty, our clear investment strategy and focus on owning assets in more structurally supported sectors positions us to be a beneficiary in an improving environment for commercial real estate. The Board and Manager are highly focused on delivering sustainable earnings growth through crystallising the portfolio reversionary potential, completing selective disposals to repay debt and recycle into higher yielding investments, and careful management of expenses. Successful implementation of this strategy should support the progressive dividend policy over time."**

Kepler View

A year ago, we thought **Schroder Real Estate's (SREI)** share price, then a 26% discount to the NAV, significantly undervalued SREI's assets, with the yield on the property assets at a significant spread to UK 10-year gilts. SREI's NAV total return over the year, an impressive 11%, confirms the mounting evidence that property values have stablished and, in the right sectors, started to rise. SREI's share price has steadily risen by c. 20% since then so it's fair to ask where things stand now.

SREI has always had a focus on high-yielding assets and this means that SREI's net initial yield, 5.6%, is still at approximately a 100bp premium to UK 10-year gilts, and the dividend yield, 6.6%, over 200bps. On the basis of a snapshot today this is about right for property, but of course SREI isn't a static portfolio and one of the most striking numbers summarised above is SREI's reversionary yield, 8.4%, compared to the benchmark's 6.2%. The potential for the manager to grow income is therefore very strong and post-year end activity should bring the void rate down, it was just over 12% at the balance sheet date, with 4% now let or under offer. Further, SREIs shorter average lease length gives it greater scope to release some of that reversionary potential in the next couple of years.

Another striking number that highlights how central sustainability is to commercial property assets is that SREI's flagship industrial asset, Stanley Green, achieves almost a 40% premium on rents for the units the manager has upgraded to achieve the highest EPC (energy efficiency) rating, compared to the remaining half of the estate that is pending upgrades. Energy prices are a significant factor for tenants and more efficient buildings have real world benefits for tenants and landlords. Further, the SREI team note that in many cases inflation and skills shortages mean that replacement costs for buildings are higher than current valuations, which has placed a brake on new supply. All of which adds up to the potential for SREI to grow its earnings significantly over the next few years.

In our view this is also the right time to be geared, and SREI's balance sheet is in really good shape, with most of its debt at low, fixed costs and with maturities into the next decade. A lingering issue for some property companies is the near-term refinancing of cheap debt taken out late in the low interest rate cycle. SREI doesn't face that issue and has a significant positive carry on its borrowing costs compared to the yield on its assets. Thus, while SREI's current 14% discount is obviously much narrower than it has been, the forward looking potential for the NAV and income to grow is high, and thus SREI remains, in our view, undervalued.

Click here to read the FY report on RNS

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