



FEDERAL REALTY INVESTMENT TRUST

retail

leadership

opportunity

quality

performance

2003 ANNUAL REPORT

ON THE COVER AND AT RIGHT:
Queens, N.Y., is home to Fresh Meadows,
a 408,000 square foot Federal Realty
shopping center. Acquired in 1997,
the center serves more than 555,000
people within a three-mile radius with an
average household income of \$73,000.

opportunity

Federal Realty Investment Trust is an equity real estate investment trust (REIT) specializing in the ownership, management, development, and redevelopment of shopping centers and street retail properties. Federal Realty's portfolio contains approximately 16.2 million square feet located primarily in strategic metropolitan markets in the Northeast, Mid-Atlantic, and California. The operating portfolio was approximately 93% leased by more than 2,200 national, regional, and local retailers as of December 31, 2003, with no single tenant accounting for more than 2.3% of rental revenue. **Federal Realty has paid quarterly dividends to its shareholders continuously since its founding in 1962, and has increased its dividend rate for 36 consecutive years, the longest consecutive record in the REIT industry.** Shares of Federal Realty are traded on the NYSE under the symbol FRT. Additional information about Federal Realty can be found on the Internet at www.federalrealty.com.

The Trust's properties are nearly all located in densely populated and affluent areas and, as a result, boast income and population demographics that significantly exceed any of our public company competitors. The aerial photographs in this report depict nearly 80% of our \$2.5 billion of gross real estate assets as of December 31, 2003. The statistics below demonstrate our focus in the strongest metropolitan markets on the East Coast and in California.

PRIMARY MARKET	FEDERAL REALTY SQUARE FOOTAGE	AVERAGES WITHIN A THREE-MILE RADIUS OF FEDERAL REALTY PROPERTIES	
		POPULATION	AVERAGE HOUSEHOLD INCOME
Washington, D.C. Metropolitan	5.0 million	123,000	\$103,000
New York/New Jersey/Connecticut	3.6 million	157,000	\$ 90,000
Philadelphia Metropolitan	2.4 million	128,000	\$ 80,000
California	1.5 million	193,000	\$ 95,000
Boston Metropolitan	0.6 million	67,000	\$ 86,000
Other	3.1 million	87,000	\$ 81,000
Total	16.2 million	129,000	\$ 91,000

All demographic data contained in this report was supplied by UBS Investment Research. Aggregated information is calculated on a weighted average basis.



Fresh Meadows Shopping Center

seized

For more than 40 years,
we've been innovative leaders
in the retail REIT industry.

We have an unsurpassed portfolio of high-
quality properties and strong leadership
focused on long-term performance.

Every day, we seek to create and increase the
value of our portfolio by seizing opportunities
to enhance value for our shareholders.

We are Federal Realty.

FINANCIAL HIGHLIGHTS

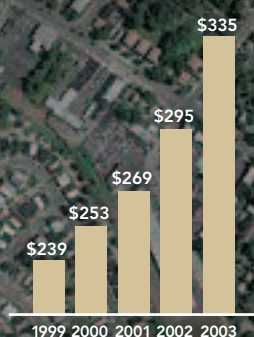
(in thousands, except per share amounts)	2003	2002	2001	2000	1999
Real Estate Owned, at Cost	\$2,470,149	\$2,306,826	\$2,104,304	\$1,854,913	\$1,721,459
Revenues	357,876	315,640	289,585	271,230	257,459
Funds From Operations ⁽¹⁾	131,257	90,503	110,432	102,173	96,795
Dividends Paid Per Share	1.95	1.93	1.90	1.84	1.78

(1)

REAL ESTATE ASSETS
(at cost, in millions)



RENTAL INCOME
(in millions)



PROPERTY OPERATING INCOME
(including interest income, in millions)



BACKGROUND:

Located in Philadelphia, Pa., Northeast Shopping Center has been in Federal Realty's portfolio since 1983. Redeveloped in 1990, the 292,000 square foot shopping center includes a mix of major national retailers and local shops. The community surrounding Northeast Shopping Center has 206,000 residents with an average household income of \$54,000 within three miles.

Northeast Shopping Center

DEAR SHAREHOLDERS,

It has been two years since we announced a significant shift in our business plan. This shift has moved us away from ground-up development of new, large-scale mixed-use projects and toward a renewed commitment and focus on our core business of operating our neighborhood and community shopping center and street retail properties. In 2003, our focus and clarity paid off in spades, with dozens of new redevelopment and acquisition opportunities seized and many more on the drawing board. We're batting for average, not swinging for the fences, and the continuous flow of base hits and doubles in 2003 has broadened our foundation and improved our position as one of the highest quality public real estate companies in the shopping center sector.

2003 was a year of careful execution—exploiting our strengths and managing our risk. Our strengths include:

- **innovative leasing and merchandising** in markets that we know well through years of on-the-ground experience;
- **property redevelopment** that takes advantage of retail voids brought on by changing community needs and other opportunities; and
- **identification and completion of acquisition opportunities** that play to our key strengths of leasing, merchandising, operations, and redevelopment.

Location remains the key to our ability to exploit our strengths. The Trust's properties are nearly all located in densely populated and affluent areas and, as a result, boast income and population demographics surrounding our centers that significantly exceed the properties of any of our public company competitors. Throughout this report, you'll notice that the background photography on each page represents actual aerial photographs of our shopping centers in our key markets. Notice the density of households and businesses surrounding our real estate and imagine the difficulty building competing supply. Our properties face less competing retail space per capita than any of the properties of our public company peers due to their in-fill nature. This strong demand and limited competing supply enable us to generate higher rents and improve our ability to increase those rents even in difficult economic conditions.



DONALD C. WOOD
PRESIDENT AND
CHIEF EXECUTIVE OFFICER

Innovative Leasing and Merchandising

In 2003, we had a record leasing year, completing 318 leases for over 1.6 million square feet of retail space. Most of those leases were written at our existing properties and could, therefore, be compared to a lease of a former tenant in the same space. The new leases were written at rents that were on average 15% greater than the rents for the expiring leases. Internal growth, through contractual rent increases and re-leasing, requires little capital investment and is the most significant and safest form of growth for the Trust. Federal Realty has consistently produced and expects to continue to produce the highest level of internal growth among our public company shopping center REIT peers, demonstrating the strength of our property locations and our significant leasing capabilities.

Included in the Trust's 2003 leasing results were four deals for new or expanded grocery stores. In fact, we have signed eight new or expanded grocery store deals since we announced our change in business strategy in early 2002 and, as of this writing, have four more in the works. While, on average, these deals will produce higher rents when the store construction is completed, the value of a new or expanded grocer at

one of our centers goes well beyond those dollars. The addition of a new supermarket to a property or the upgrading of an undersized grocer to prototypical size dramatically improves the quality of the center as a whole—as a prototypical grocery store will drive greater traffic to the surrounding tenants, improving their sales and the Trust’s ability to increase rents.

Some of the Trust’s most impressive leasing and merchandising progress in 2003 was made at Santana Row, Federal Realty’s mixed-use development in San Jose, California. At the end of 2002, Santana had recently opened with 36 retail tenants, 28 occupied residential units, and no full-service restaurants, all resulting from the devastating fire that occurred at the property in August 2002. As of this writing, with over 90 diverse retail tenants, 13 full-service restaurants, and 235 residential units occupied, Santana Row has established itself as the place to shop, live, eat, and entertain in Silicon Valley. Our fire insurance claim was fully satisfied with our insurance carrier last fall for \$129 million, very nearly covering all of the economic loss from the fire. Recently, we began construction of the next 256 residential units, which will be ready for occupancy in 2005. In just over one year, Santana Row has gone from the Trust’s single largest risk to our single greatest opportunity.

Property Redevelopment

We are fully immersed in the shopping center redevelopment business. Our team has identified opportunities to execute more than \$200 million of redevelopment over the next four years in real estate that we already own and control. I firmly believe that investments of this nature represent the best balance between risk and reward. Returns are generally higher as the land and infrastructure costs have already been largely

incurred, and the risk of consumer acceptance is far lower as the locations are already successful retail centers. In 2003, the Trust invested more than \$37 million in redevelopment, generating incremental unleveraged returns of over 11%.

We remain confident in our ability to identify and successfully execute \$30 million to \$50 million of annual redevelopment opportunities generating double-digit cash returns on investment for the foreseeable future. Redevelopment opportunities can stem from expiring leases, our ability to further utilize existing land, or from space we unexpectedly take possession of through tenant bankruptcy. At Federal Realty, all of our redevelopment opportunities share one unique characteristic—a quality property location—which limits redevelopment risk and greatly improves our ability to successfully create value for our shareholders.

The recapture of the 88,000 square foot Kmart space at Leesburg Plaza in 2003 is just one great example of our redevelopment philosophy. Leesburg Plaza is a 250,000 square foot, grocery-anchored shopping center in Leesburg, Virginia, a rapidly expanding Washington, D.C. suburb. While the re-leasing of the vacated Kmart space at higher rents was a low-risk alternative that could have produced positive incremental returns with limited disruption from an occupancy perspective, the value creation opportunity under this scenario was limited. Alternatively, because of the strong demand for small shop and mini-anchor space, we are now pursuing the approvals necessary to (1) demolish the Kmart space and replace it with 55,000 square feet of food and specialty retail space; (2) replace the previous Peebles department store with two better credit tenants; and (3) utilize a portion of the remaining entitlements to add up to three new, lucrative pad sites. Subject to obtaining the necessary

ANNUALIZED TOTAL RETURN COMPARISON

(through February 2004)

	1 YEAR	2 YEARS	3 YEARS	5 YEARS	10 YEARS	20 YEARS
Federal Realty Investment Trust	52.9%	38.3%	38.5%	23.3%	12.3%	14.2%
NAREIT Equity Total Return Index	47.5%	21.7%	20.1%	16.8%	11.9%	12.3%
S&P 500 Index	38.5%	3.5%	-1.0%	-0.1%	11.4%	13.4%
NASDAQ Composite Index	52.5%	8.8%	-1.5%	-2.0%	9.9%	11.0%

Source: Bloomberg
Assumes reinvestment of dividends

“Our team has identified opportunities to execute more than \$200 million of redevelopment over the next four years in real estate that we already own and control.”

approvals, we expect to invest approximately \$12 million in Leesburg Plaza over the next two years at an incremental unleveraged return of approximately 12%, while dramatically improving the retail merchandising mix, the credit strength of our tenant base, and, therefore, the value of the entire shopping center.

In November 2003, we successfully completed the \$26 million second phase of Santana Row consisting of 84,000 square feet of retail space that was 95% pre-leased to Best Buy and The Container Store. This phase was completed ahead of schedule and under budget, producing a 17% incremental unleveraged cash return. Also in 2003, we delivered a Santana Row pad site to Century Theaters, which is expected to open around Labor Day 2004. Finally, as I mentioned previously, Federal Realty's Investment Committee and Board of Trustees approved plans to build 256 additional townhomes and flats on Santana Row's building seven podium. This \$60 million incremental investment is anticipated to produce a 10.5% stabilized return, which is based on residential rents that we are now receiving at Santana Row. Delivery of the new units is scheduled to begin in early 2005. In short, our redevelopment pipeline is full, and our investment criteria have been stringently applied.

Identification and Completion of Acquisition Opportunities

Our final source of growth comes from the acquisition of neighborhood and community shopping centers in our core markets that have growth potential at or above our existing portfolio. In 2003, we acquired four such properties: Mount Vernon Plaza and South Valley Shopping Center, two contiguous properties in Alexandria, Virginia; Mercer Mall, a more than 400,000 square foot community shopping center in Mercer County, New Jersey; and Plaza del Mercado, a 96,000 square foot center in Silver Spring, Maryland. The acquisitions, representing a capital commitment of \$125 million, are

perfect examples of the Trust "batting for average."

Each is located in a strategic market for the Trust, allowing us to further leverage our existing leasing and property management expertise in those markets, and each possesses redevelopment and leasing opportunities that will play a significant role in fueling the Trust's future growth.

In addition, selling existing assets that are expected to produce below-average growth enhances Federal Realty's internal growth rate. In 2003, we sold assets generating net proceeds of \$44 million, all of which were fully leased with little opportunity for future rent growth. These dispositions included nine smaller single-tenant or multi-tenant street retail properties and a 17.7-acre parcel of land in Hillsboro, Oregon, that the Trust had planned to develop in accordance with our former business strategy. It is important to note that while all of our 2003 dispositions were street retail assets, we remain committed to and focused on the street retail asset category. The focus of our business strategy is on producing growth regardless of a property's classification as a shopping center or a street retail asset.

We're proud of our accomplishments in 2003, but more importantly, we're energized and committed to continuing our record of steady growth in dividends and opportunities to create value for you, our shareholders, in 2004 and beyond. On behalf of our Board of Trustees, our employees, and myself, thank you for your continued support. We look forward to a prosperous future together.

Sincerely,



Donald C. Wood
President and Chief Executive Officer

Gaithersburg Square Shopping Center
Quince Orchard Plaza

Plaza del Mercado

Magruder's Center
Courthouse Center

opportunity

Congressional Plaza
Federal Plaza
Mid-Pike Plaza

Laurel
Shopping
Center

Wildwood Shopping Center

MARYLAND

Leesburg
Plaza

Bethesda Row

Friendship Center

Sam's Park N Shop

Pike 7 Plaza

WASHINGTON, D.C.

Tyson's Station
Idylwood Plaza
Falls Plaza
Falls Plaza East

Pan Am Shopping Center
Loehmann's Plaza

VIRGINIA

Pentagon Row

The Village at Shirlington

Old Keene Mill Shopping Center
Tower Shopping Center

Mount Vernon Plaza
South Valley Shopping Center

seized

regional dominance



NORTHEAST



MID-ATLANTIC



CALIFORNIA

Federal Realty is the dominant retail landlord in the Washington, D.C. metropolitan area with 27 properties comprising five million square feet. One of the most stable markets in the country, the Washington, D.C. metropolitan area has a highly educated and affluent population. On average, 123,000 people with average household income levels of \$103,000 live within three miles of our properties in this market.

Owning high-quality assets in markets with the strongest demographics is the backbone of our success. Being a dominant retail landlord in these specific, key markets allows us to apply our local knowledge and industry expertise, providing greater operating leverage for leasing, marketing, and property management.

We merchandise our centers to give our tenants the best opportunity to succeed by assembling a combination of retail goods and services that are appropriate for the communities in which each center operates. As a dominant force in the retail landscape of these markets, we are able to provide a wide variety of retail choices to serve the needs of consumers.

In addition, retailers who are looking to enter into or expand in one of our key markets often seek a Federal Realty shopping center to help ensure their success based on our dominant presence and the quality of our locations.

The Trust is committed to increasing our presence in these key markets to better serve our tenants and their customers.

opportunity

Falls Plaza

Falls Plaza East



FALLS PLAZA
FALLS CHURCH, VA



ELLISBURG CIRCLE
CHERRY HILL, NJ



BARRACKS ROAD
CHARLOTTESVILLE, VA

BACKGROUND:

Falls Plaza is located in Falls Church, Va., situated inside the Capital Beltway seven miles west of Washington, D.C. Falls Plaza is surrounded by a large, affluent residential community with 131,000 people with average household income levels of \$118,000 within three miles of the center.

In 2000, Federal Realty completed the renovation of Falls Plaza and Falls Plaza East shopping centers. Through an innovative redevelopment plan, we were able to expand and upgrade an outdated and undersized Giant Food, upgrade the common area and architecturally combine the two properties. Since the opening of the expanded Giant Food, Federal Realty has been able to improve the tenant mix and continues to reap the benefits of redevelopment through consistently strong rent growth.

seized grocery expansions

Our merchandising expertise helps us identify outdated or undersized grocers who can expand their operations—repositioning the entire center.



HAUPPAUGE SHOPPING CENTER
HAUPPAUGE, NY



OLD KEENE MILL
SPRINGFIELD, VA



GARDEN MARKET
WESTERN SPRINGS, IL

Grocery stores play a vital role in Federal Realty's shopping centers by offering basic goods and services that provide ample, daily traffic instrumental to the success of the entire center in varying economic climates. More than 70% of our shopping center portfolio is anchored by grocery stores, generating sales well in excess of national and local averages.

Federal Realty continues to seize opportunities by ensuring that our centers appeal to grocery stores, accommodating those interested in expanding into prototypical stores or opening new grocers in our centers. Repositioning a shopping center with a new or expanded grocer dramatically improves the merchandising mix and generates tremendous synergies throughout the center, resulting in significant increases in traffic and sales, which allow us to increase rents and enhance the value of the real estate.

Since 1999, Federal Realty has expanded or added new grocery stores at 13 of its retail properties. Since the execution of these grocery store leases, we have signed leases for 730,000 square feet of other retail space at these properties, at average cash rent increases of 26% over the rent previously paid for those spaces. The expansion or addition of a grocery store, along with the positive impact on rents throughout the center, dramatically improves the underlying value of each of these assets.

Eight new or expanded grocery stores are currently under redevelopment, and an additional four leases are in active negotiation. Needless to say, adding and expanding grocers will play a key role in the Trust's internal growth strategy for years to come.



Clifton Plaza
Allwood Plaza

Troy Hills Shopping Center

NEW JERSEY

Blue Star Shopping Center

Rutgers Plaza

Brunswick Shopping Center

PENNSYLVANIA

Mercer Mall

Langhorne Square Shopping Center

Hamilton Square Plaza

Willow Grove Shopping Center

Feasterville Plaza

Flourtown
Shopping Center

Northeast Shopping Center

Andorra Shopping Center

PHILADELPHIA

Bala Cynwyd Shopping Center

Wynnewood Shopping Center

Ellisburg Circle
Shopping Center

Lawrence Park
Shopping Center

opportunity

Brick Plaza



MERCER MALL LAWRENCEVILLE, NJ

Mercer Mall, acquired in 2003, is located approximately four miles from Princeton, N.J., and 25 miles from Philadelphia, Pa. Currently underway is the redevelopment of a former Kmart into a World Class ShopRite, a premier New Jersey grocer—an important step in strengthening the position of the center. In addition, we have the opportunity to add another “big box” retailer, recapture and re-lease below-market retail space, and implement a comprehensive upgrade of the property’s common areas, facades, and signage.

Acquisitions in our core markets allow us to strengthen our presence in areas that possess solid demographics and high barriers to entry for competition. During 2003, we enhanced the quality of our portfolio and strengthened our operating platform through the sale of assets that detracted from our internal growth, redeploying the capital in our core markets into accretive, high-quality shopping centers with significant earnings growth potential through re-leasing and/or redevelopment.

seized new acquisitions

Philadelphia and northern New Jersey are key markets in Federal Realty’s strategic footprint. The Trust operates 19 properties comprising 4.6 million square feet in this historically vibrant region. Within a three-mile radius of our centers are, on average, 108,000 people with an average household income of \$85,000.

opportunity

FINLEY SQUARE SHOPPING CENTER DOWNERS GROVE, IL

Following the bankruptcy of several under-performing retailers, we implemented an extensive remerchandising plan to revitalize this center and reposition it to capitalize on the area's strong demographics. We were able to attract credit-worthy retailers, which already had a strong presence in the market, who relocated their stores to Finley Square. Today, the center contains leading retailers such as OfficeMax, Bed Bath and Beyond, PetsMart, and Wickes Furniture.

These remerchandising efforts, coupled with property improvements, have solidified the center's market position and its long-term growth prospects.



Finley Square Shopping Center



BACKGROUND:

Downers Grove, Ill., is a well-established, affluent community approximately 20 miles west of downtown Chicago. Finley Square is an attractive location for retailers with strong demographics, including a population of 84,000 and an average household income of \$111,000 within three miles.

seized improving the mix

We continually upgrade and redevelop our properties to improve their competitive position, creating value for our shareholders.



One of the most important ways to create value for our shareholders is through strategic redevelopments of existing properties. By improving or maintaining the physical condition and competitive position of our properties, we enhance the long-term value of our assets.

Seizing strategic redevelopment opportunities is key to maximizing income and enhancing property values. These opportunities come in many forms, including repositioning a shopping center through creative remerchandising or adding leasable square footage on land that we already own, further strengthening the overall retail environment.

Investing capital through opportunistic redevelopments is one of the safest and most accretive forms of long-term growth for the Trust. In 2003, over \$37 million of these opportunities, which included a variety of renovation, retenanting, and redevelopments, were stabilized at an unleveraged return on investment of over 11%. Looking ahead, our portfolio contains significant untapped value accessible through redevelopment opportunities, and the Trust anticipates investing \$30 million to \$50 million per year, at double-digit returns for the foreseeable future.

An aerial photograph of Northern California, showing a dense urban grid in the center and more rugged, hilly terrain to the west. The San Jose area is visible at the top.

Santana Row

SAN JOSE

opportunity

N. CALIFORNIA

LOS GATOS

Kings Court

Old Town Center

An aerial photograph of Southern California, showing a mix of urban areas and large green spaces. The Los Angeles area is visible on the right, and the Santa Monica coastline is on the left.

S. CALIFORNIA

Old Town Pasadena

PASADENA

Hollywood Boulevard

HOLLYWOOD

Third Street Promenade

SANTA MONICA

LOS ANGELES

HERMOSA BEACH

Hermosa Avenue

seized for the long term



SANTANA ROW, SAN JOSE, CA

After its first full year of operation, Santana Row has established itself as the premier residential, retail, restaurant, and entertainment destination in Silicon Valley, offering over a dozen restaurant choices, more than 90 retail stores, and a contemporary luxury hotel.

Santana Row achieved some important milestones in 2003. Best Buy, The Container Store, and Club One Fitness all opened with strong sales and heavy traffic. In addition, the parent company of Anthropologie, another Santana Row retailer, signed a lease for its Urban Outfitters concept, and construction is underway for a summer 2004 opening.

Looking forward, by late summer of this year, we anticipate completing Phase III, CineArts Theater, which will anchor the south end of Santana Row and add a new element to our entertainment and restaurant offerings. In addition, in 2005, we expect to begin delivering 256 additional residential units above the retail pedestal in building seven along with several amenities for all residents at Santana Row, including a lap pool, clubhouse, and business center.

Building on an established platform of properties in California, Federal Realty will embark on a strategically focused acquisition program to become a dominant owner of retail real estate in both northern and southern California.



BOSTON

Dedham Plaza

DEDHAM PLAZA
DEDHAM, MA

Located approximately 10 miles from downtown Boston, Dedham Plaza is situated on the Boston-Providence Turnpike, a major commuting thoroughfare into Boston. In 2003, the 245,000 square foot property was repositioned as a grocery-anchored shopping center following the departure of Ames through bankruptcy. The repositioning has enhanced this asset and will allow us to expand and improve the merchandising mix and take advantage of the synergy created by a grocery anchor.

In addition to Dedham Plaza, Federal Realty owns two other shopping centers in the Boston metropolitan market, Saugus Plaza and Queen Anne Plaza. Within a three-mile radius of these centers are, on average, 67,000 people with average household incomes of \$86,000.

Trustees



(LEFT TO RIGHT)

WALTER F. LOEB, PRESIDENT,
LOEB ASSOCIATES
DAVID W. FAEDER, MANAGING PARTNER,
FOUNTAIN SQUARE PROPERTIES
JOSEPH S. VASSALLUZZO, VICE CHAIRMAN,
STAPLES, INC.
KRISTIN GAMBLE, PRESIDENT,
FLOOD GAMBLE ASSOCIATES, INC.
DONALD C. WOOD, PRESIDENT AND
CHIEF EXECUTIVE OFFICER,
FEDERAL REALTY INVESTMENT TRUST
AMY B. LANE, DIRECTOR,
BORDERS GROUP
MARK S. ORDAN, CHAIRMAN,
FEDERAL REALTY INVESTMENT TRUST;
CHAIRMAN AND CHIEF EXECUTIVE OFFICER,
SUTTON GOURMET, LLC
DENNIS L. BERMAN, GENERAL PARTNER,
GDR PARTNERSHIPS (NOT PICTURED)

Executive Team



(LEFT TO RIGHT)

DAWN BECKER, SENIOR VICE PRESIDENT,
GENERAL COUNSEL AND SECRETARY
JEFF BERKES, SENIOR VICE PRESIDENT,
CHIEF INVESTMENT OFFICER
LARRY FINGER, SENIOR VICE PRESIDENT,
CHIEF FINANCIAL OFFICER AND TREASURER

Senior Management



(LEFT TO RIGHT)

ANDREW BLOCHER, VICE PRESIDENT,
CAPITAL MARKETS AND INVESTOR RELATIONS
JONATHAN KAYNE, VICE PRESIDENT,
CHIEF OPERATING OFFICER, EASTERN REGION
DEBBIE COLSON, VICE PRESIDENT,
LEGAL OPERATIONS
STUART BROWN, VICE PRESIDENT,
CHIEF ACCOUNTING OFFICER
CHRIS WEILMINSTER, VICE PRESIDENT,
ANCHOR TENANT LEASING
PHILIP ALTSCHULER, VICE PRESIDENT,
HUMAN RESOURCES
JAN SWEETNAM, VICE PRESIDENT,
CHIEF OPERATING OFFICER, WESTERN REGION
LISA DENSON, VICE PRESIDENT,
INFORMATION TECHNOLOGY AND
SPECIAL PROJECTS
JOHN TSCHIDERER, VICE PRESIDENT,
DEVELOPMENT

Property Portfolio

■ Shopping Centers ● Street Retail ▲ Apartments

Property Name	Location	Average Demographics Within a Three-Mile Radius ⁽¹⁾		Year Acquired	Total Investment (in thousands)	GLA ⁽²⁾	% Leased	Grocery Anchor ⁽³⁾	Other Principal Tenants
		Population	Average HH Income						
MID-ATLANTIC REGION									
WASHINGTON METROPOLITAN AREA									
● Bethesda Row	Bethesda, MD	132,000	\$145,000	1993–1998	\$ 79,501	434,000	99%	Giant Food	Barnes & Noble, Landmark Theater
■ Congressional Plaza	Rockville, MD	123,000	99,000	1965	66,482 ⁽⁴⁾	339,000	98%	Whole Foods	Buy Buy Baby, Container Store, Tower Records
■ Courthouse Center	Rockville, MD	83,000	106,000	1997	4,295	37,000	100%	Giant Food	CVS, Staples TJ Maxx, Comp USA, Ross
■ Falls Plaza	Falls Church, VA	131,000	118,000	1967	8,195	73,000	100%		
■ Falls Plaza—East	Falls Church, VA	131,000	118,000	1972	3,355	71,000	100%		
■ Federal Plaza	Rockville, MD	128,000	100,000	1989	61,925	247,000	98%		
● Friendship Center	Washington, DC	161,000	132,000	2001	33,309	119,000	100%	Magruder's	Borders, Linens 'n Things, Maggiano's
■ Gaithersburg Square	Gaithersburg, MD	135,000	82,000	1993	23,905	215,000	90%		Bed Bath & Beyond, Borders, Ross
■ Idylwood Plaza	Falls Church, VA	119,000	117,000	1994	14,914	73,000	97%	Whole Foods	Marshalls, Toys R Us Pier One Bally's, Linens 'n Things, Loehmann's
■ Laurel	Laurel, MD	78,000	75,000	1986	45,658	384,000	94%	Giant Food	
■ Leesburg Plaza	Leesburg, VA	33,000	76,000	1998	20,516	247,000	66%	Giant Food	
■ Loehmann's Plaza	Fairfax, VA	148,000	109,000	1983	25,394	242,000	98%		
■ Magruder's Center	Rockville, MD	84,000	104,000	1997	11,026	109,000	98%	Magruder's	Linens 'n Things, Toys R Us, Bally's, A.C. Moore
■ Mid-Pike Plaza	Rockville, MD	138,000	98,000	1982	17,280	304,000	100%		
■ Mount Vernon	Alexandria, VA	94,000	101,000	2003	19,790	254,000	68%	Shoppers Food Warehouse	Micro Center, Michaels Bally's, Bed Bath & Beyond, DSW, Cost Plus
■ Old Keene Mill	Springfield, VA	118,000	120,000	1976	5,152	92,000	100%	Whole Foods	
■ Pan Am	Fairfax, VA	106,000	116,000	1993	25,078	218,000	99%	Safeway	
● Pentagon Row	Arlington, VA	192,000	91,000	1999	87,538	296,000	99%	Harris Teeter	
■ Pike 7	Vienna, VA	89,000	130,000	1997	33,432	164,000	97%	Giant Food	Staples, TJ Maxx, Tower Records
■ Plaza del Mercado	Silver Spring, MD	104,000	85,000	2003	20,582	96,000	95%		Circuit City, Staples
■ Quince Orchard	Gaithersburg, MD	111,000	88,000	1993	19,112	252,000	95%		Petco Home Depot, TJ Maxx Virginia Fine Wine, Talbots
▲ Rollingwood Apartments	Silver Spring, MD			1971	6,688	N/A	95%		
● Sam's Park N Shop	Washington, DC	306,000	93,000	1995	11,786	50,000	100%		
■ South Valley	Alexandria, VA	94,000	101,000	2003	14,293	218,000	85%		
■ Tower	Springfield, VA	109,000	105,000	1998	18,455	106,000	99%		
■ Tyson's Station	Falls Church, VA	120,000	117,000	1978	3,351	50,000	85%	Trader Joe's	Cineplex Odeon
● Village at Shirlington	Arlington, VA	240,000	91,000	1995	33,262	204,000	96%		
■ Wildwood	Bethesda, MD	109,000	127,000	1969	16,584	86,000	99%	Sutton Place Gourmet	CVS
Total Washington Metropolitan Area ⁽⁵⁾		123,000	\$103,000		\$730,858	4,980,000	94%		
MID-ATLANTIC REGION—OTHER									
■ Barracks Road	Charlottesville, VA	67,000	\$ 62,000	1985	\$ 39,571	483,000	99%	Harris Teeter, Kroger	Bed Bath & Beyond, Barnes & Noble, Old Navy
■ Eastgate	Chapel Hill, NC	53,000	74,000	1986	16,536	159,000	90%	Southern Season	Stein Mart
■ Governor Plaza	Glen Burnie, MD	74,000	56,000	1985	18,640	269,000	100%		Bally's, Comp USA, Syms, Office Depot
■ Perring Plaza	Baltimore, MD	111,000	61,000	1985	23,989	402,000	90%	Shoppers Food Warehouse	Home Depot, Burlington Coat Factory
■ Shops at Willow Lawn	Richmond, VA	85,000	64,000	1983	60,890	488,000	74%	Kroger	Old Navy, Tower Records
● Winter Park	Winter Park, FL	86,000	73,000	1996	6,877	28,000	93%		
Total Mid-Atlantic Region—Other ⁽⁵⁾		82,000	\$ 63,000		\$166,503	1,829,000	89%		

Property Name	Location	Average Demographics Within a Three-Mile Radius ⁽¹⁾		Year Acquired	Total Investment (in thousands)	GLA ⁽²⁾	% Leased	Grocery Anchor ⁽³⁾	Other Principal Tenants
		Population	Average HH Income						
NORTHEAST REGION									
PHILADELPHIA METROPOLITAN AREA									
■ Andorra	Philadelphia, PA	88,000	\$ 94,000	1988	\$ 19,317	259,000	98%	Acme Markets	Kohl's, Staples
■ Bala Cynwyd	Bala Cynwyd, PA	238,000	60,000	1993	23,999	281,000	100%	Acme Markets	Lord & Taylor
■ Ellisburg Circle	Cherry Hill, NJ	95,000	83,000	1992	28,028	268,000	100%	Genuardi's	Bed Bath & Beyond, Ross
■ Feasterville	Feasterville, PA	72,000	83,000	1980	11,650	111,000	100%	Genuardi's	OfficeMax
■ Flourtown	Flourtown, PA	73,000	87,000	1980	8,756	187,000	54%	Genuardi's	
■ Langhorne Square	Levittown, PA	82,000	70,000	1985	17,637	216,000	87%	Redner's Warehouse Markets	
■ Lawrence Park	Broomall, PA	100,000	88,000	1980	25,822	345,000	94%	Acme Markets	Marshalls
■ Northeast	Philadelphia, PA	206,000	54,000	1983	21,830	292,000	96%		CHI, TJ Maxx, CVS
■ Willow Grove	Willow Grove, PA	86,000	88,000	1984	26,261	215,000	100%		Burlington Coat, Marshalls, Tower Records
■ Wynnewood	Wynnewood, PA	169,000	98,000	1996	35,251	255,000	99%	Genuardi's	Barnes & Noble, Marshalls, Toys R Us
Total Philadelphia Metropolitan Area ⁽⁵⁾		128,000	\$ 80,000		\$218,551	2,429,000	94%		Bed Bath & Beyond, Borders, Old Navy
NEW YORK/NEW JERSEY/CONNECTICUT									
■ Allwood	Clifton, NJ	198,000	\$ 86,000	1988	\$ 4,296	52,000	100%	Stop & Shop	Mandee Shop
■ Blue Star	Watchung, NJ	105,000	112,000	1988	39,520	407,000	97%	Shop Rite	Kohl's, Michaels, Toys R Us, Marshalls
■ Brick Plaza	Brick, NJ	69,000	57,000	1989	53,869	409,000	96%	A&P	Loews Theatre, Barnes & Noble, Sports Authority
■ Bristol Plaza	Bristol, CT	63,000	62,000	1995	22,332	280,000	94%	Super Stop & Shop	TJ Maxx
■ Brunswick	North Brunswick, NJ	124,000	84,000	1988	21,334	303,000	99%	A&P	
■ Clifton	Clifton, NJ	226,000	72,000	1988	4,951	80,000	93%	Acme Markets	Drug Fair, Dollar Express
● Forest Hills	Forest Hill, NY	914,000	66,000	1997	23,969	86,000	100%		Midway Theatre, Duane Reade, Gap
■ Fresh Meadows	Queens, NY	555,000	73,000	1997	64,647	408,000	92%		Value City, Kohl's, Cineplex Odeon
■ Greenlawn Plaza	Greenlawn, NY	78,000	104,000	2000	11,040	92,000	100%	Waldbaum's	
● Greenwich Avenue	Greenwich, CT	65,000	175,000	1994–1996	15,993	42,000	100%		Saks Fifth Avenue
■ Hamilton	Hamilton, NJ	83,000	76,000	1988	8,087	190,000	100%	Shop Rite	A.C. Moore, Stevens Furniture
■ Hauppauge	Hauppauge, NY	76,000	95,000	1998	26,320	131,000	100%	Shop Rite	
■ Huntington	Huntington, NY	71,000	116,000	1988	22,433	279,000	90%		Buy Buy Baby, Toys R Us, Bed Bath & Beyond
■ Mercer Mall	Lawrenceville, NJ	28,000	119,000	2003	76,583	360,000	86%	Shop Rite ⁽⁶⁾	Bed Bath & Beyond, DSW, TJ Maxx
■ Rutgers	Franklin, NJ	92,000	84,000	1988	15,925	217,000	99%	Stop & Shop	Kmart
■ Troy	Parsippany-Troy, NJ	55,000	105,000	1980	20,512	202,000	100%	Pathmark	A.C. Moore, Comp USA, Toys R Us
● West Hartford	West Hartford, CT	123,000	74,000	1994–1996	8,002	62,000	69%		
Total New York/New Jersey/Connecticut ⁽⁵⁾		157,000	\$ 90,000		\$439,813	3,600,000	95%		
BOSTON METROPOLITAN AREA									
■ Dedham Plaza	Dedham, MA	66,000	\$ 84,000	1993	\$ 29,650	245,000	97%	Shaw's Supermarket	Pier One
■ Queen Anne Plaza	Norwell, MA	27,000	96,000	1994	14,777	149,000	100%	Victory Supermarket	TJ Maxx
■ Saugus Plaza	Saugus, MA	103,000	79,000	1996	13,184	171,000	100%	Super Stop & Shop	Kmart
Total Boston Metropolitan Area ⁽⁵⁾		67,000	\$ 86,000		\$ 57,611	565,000	99%		

Property Name	Location	Average Demographics Within a Three-Mile Radius ⁽¹⁾		Year Acquired	Total Investment (in thousands)	GLA ⁽²⁾	% Leased	Grocery Anchor ⁽³⁾	Other Principal Tenants
		Population	Average HH Income						
CHICAGO METROPOLITAN AREA									
■ Crossroads	Highland Park, IL	59,000	\$208,000	1993	\$ 21,812	173,000	97%	Dominick's	Comp USA, Golfsmith, Guitar Center
● Evanston	Evanston, IL	112,000	129,000	1995	3,220	12,000	100%		Gap
■ Finley Square	Downers Grove, IL	84,000	111,000	1995	28,359	313,000	100%		Bed Bath & Beyond, Sports Authority
■ Garden Market	Western Springs, IL	101,000	116,000	1994	11,139	140,000	99%		Walgreens
■ North Lake Commons	Lake Zurich, IL	40,000	176,000	1998	12,993	129,000	93%		
Total Chicago Metropolitan Area ⁽⁵⁾		75,000	\$145,000		\$ 77,522	767,000	98%		
NORTHEAST REGION—OTHER									
■ Gratiot Plaza	Roseville, MI	123,000	\$ 58,000	1973	\$ 16,637	218,000	86%	Farmer Jack's	Bed Bath & Beyond, Best Buy
■ Lancaster	Lancaster, PA	99,000	58,000	1980	10,011	107,000	97%	Giant Food	
Total Northeast Region—Other ⁽⁵⁾		115,000	\$ 58,000		\$ 26,648	325,000	89%		
WEST REGION									
CALIFORNIA									
● Colorado Blvd.	Pasadena, CA	191,000	\$ 81,000	1996–1998	\$ 15,006	69,000	96%	Lunardi's Super Market	Pottery Barn, Banana Republic
■ Escondido Promenade	Escondido, CA	112,000	69,000	1996	24,854	222,000	95%		Cost Plus, TJ Maxx, Toys R Us
● Fifth Ave.	San Diego, CA	169,000	54,000	1996–1997	12,126	51,000	95%		Urban Outfitters
● Hermosa Ave.	Hermosa Beach, CA	148,000	104,000	1997	4,592	23,000	100%		
● Hollywood Blvd.	Hollywood, CA	303,000	70,000	1999	26,136	151,000	90%		Hollywood Entertainment Museum
■ Kings Court	Los Gatos, CA	83,000	151,000	1998	11,409	79,000	98%		Longs Drug Store
● Old Town	Los Gatos, CA	44,000	184,000	1997	33,508	95,000	96%		Borders, Gap Kids, Banana Republic
● Post Street	San Francisco, CA	364,000	84,000	1997	30,025	101,000	58%		Brooks Brothers
● Santana Row (Phase I & II)	San Jose, CA	226,000	97,000	1997	451,303	529,000	89%		Crate & Barrel, Container Store, Best Buy, Borders
● Third St. Promenade	Santa Monica, CA	154,000	93,000	1996–2000	72,266	209,000	98%		J. Crew, Banana Republic, Old Navy
Total California ⁽⁵⁾		193,000	\$ 95,000		\$ 681,225	1,529,000	91%		
WEST REGION—OTHER									
● Houston St.	San Antonio, TX	148,000	\$ 33,000	1998	\$ 60,350	170,000	67%		Hotel Valencia, Walgreens
● Mill Avenue	Tempe, AZ	101,000	45,000	1998	11,068	40,000	100%		Gordon Biersch
Total West Region—Other ⁽⁵⁾		45,000	\$ 35,000		\$ 71,418	210,000	73%		
Total Portfolio ⁽⁵⁾		129,000	\$ 91,000		\$2,470,149	16,234,000	93%		

⁽¹⁾ All demographic data supplied by UBS Investment Research.⁽²⁾ Excludes redevelopment square footage not yet in service, Santana Row residential, future phases of Santana Row, Rollingwood and the Crest at Congressional.⁽³⁾ Grocery anchor is defined as a grocery tenant leasing 15,000 square feet or more.⁽⁴⁾ Total investment includes dollars associated with the 146 units of the Crest at Congressional.⁽⁵⁾ Aggregate information is calculated on a weighted average basis.⁽⁶⁾ GLA for Shop Rite currently under construction.

Selected Financial Data

	Year Ended December 31,				
(in thousands, except per share data)	2003	2002	2001	2000	1999
OPERATING DATA					
Rental income	\$334,697	\$295,016	\$269,288	\$252,687	\$238,633
Property operating income	239,833	211,963	200,320	190,396	180,576
Income before gain (loss) on sale of real estate	74,444	45,833	59,571	56,842	55,493
Gain (loss) on sale of real estate	20,053	9,454	9,185	3,681	(7,050)
Net income	94,497	55,287	68,756	60,523	48,443
Net income available for common shareholders	75,990	35,862	59,722	52,573	40,493
Net cash provided by operating activities ⁽¹⁾	122,391	119,069	109,448	107,056	102,183
Net cash used in investing activities ⁽¹⁾	91,272	175,744	232,138	121,741	99,313
Net cash provided by (used in) financing activities ⁽¹⁾	(19,274)	62,235	128,896	14,304	(8,362)
Dividends declared on common shares	93,889	82,273	75,863	72,512	71,630
Weighted average number of common shares outstanding:					
Basic	47,379	41,624	39,164	38,796	39,574
Diluted	48,619	42,882	40,266	39,910	40,638
Earnings per share:					
Basic	\$ 1.60	\$ 0.86	\$ 1.52	\$ 1.36	\$ 1.02
Diluted	1.59	0.85	1.52	1.35	1.02
Dividends declared per common share	1.95	1.93	1.90	1.84	1.78
OTHER DATA					
Funds from operations ⁽²⁾⁽³⁾	131,257	90,503	110,432	102,173	96,795
Ratio of earnings to fixed charges ⁽⁴⁾	1.7x	1.3x	1.5x	1.5x	1.7x
Ratio of earnings to combined fixed charges and preferred share dividends ⁽⁴⁾	1.4x	1.0x	1.3x	1.4x	1.5x
Ratio of EBITDA to combined fixed charges and preferred share dividends ⁽⁴⁾⁽⁵⁾	2.1x	1.6x	1.9x	2.0x	2.1x

(1) Determined in accordance with Financial Accounting Standards Board, which we refer to as FASB, Statement No. 95, Statement of Cash Flows.

(2) We have historically reported our funds from operations ("FFO") in addition to our net income and net cash provided by operating activities. FFO is a supplemental non-GAAP financial measure of real estate companies' operating performance. The National Association of Real Estate Investment Trusts ("NAREIT") defines FFO as follows: income available for common shareholders before depreciation and amortization of real estate assets and before extraordinary items less gains on sale of real estate. NAREIT developed FFO as a relative measure of performance and liquidity of an equity REIT in order to recognize that the value of income-producing real estate historically has not depreciated on the basis determined under GAAP. However, FFO does not represent cash flows from operating activities in accordance with GAAP (which, unlike FFO, generally reflects all cash effects of transactions and other events in the determination of net income); should not be considered an alternative to net income as an indication of our performance; and is not necessarily indicative of cash flow as a measure of liquidity or ability to pay dividends. We consider FFO a meaningful, additional measure of operating performance because it primarily excludes the assumption that the value of the real estate assets diminishes predictably over time, and because industry analysts have accepted it as a performance measure. Comparison of our presentation of FFO to similarly titled measures for other REITs may not necessarily be meaningful due to possible differences in the application of the NAREIT definition used by such REITs. For a reconciliation of net income available for common shareholders to FFO, please see "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Funds From Operations."

(3) Includes approximately \$8.0 million of insurance proceeds in 2003 as well as a charge of \$3.4 million related to the redemption of preferred shares. Also includes an \$8.5 million restructuring charge incurred in the first quarter of 2002 and a \$13.8 million restructuring charge incurred in the fourth quarter of 2002. Excluding these charges, Funds from Operations in 2002 would have been \$112.8 million. Excluding these items, funds from operations in 2003 would have been \$119.7 million.

(4) Earnings consist of income before gain (loss) on sale of real estate and fixed charges. Fixed charges consist of interest on borrowed funds (including capitalized interest), amortization of debt discount and expense and the portion of rent expense representing an interest factor. Preferred share dividends consist of dividends paid on our outstanding Series A preferred shares and Series B preferred shares. Our Series A preferred shares were redeemed in full in June 2003.

(5) EBITDA is a non-GAAP measure that means net income or loss plus interest expense, income taxes, depreciation and amortization; adjusted for gain or loss on sale of assets, impairment provisions, provision for loss on equity securities and other nonrecurring expenses. EBITDA is presented because it provides useful information regarding our ability to service debt, although EBITDA should not be considered an alternative measure of operating results or cash flow from operations as determined in accordance with GAAP. EBITDA as presented may not be comparable to other similarly titled measures used by other REITs.

(in thousands, except per share data)	Year Ended December 31,				
	2003	2002	2001	2000	1999
BALANCE SHEET DATA					
Real estate owned, at cost	\$2,470,149	\$2,306,826	\$2,104,304	\$1,854,913	\$1,721,459
Total assets	2,143,435	1,999,378	1,834,881	1,618,885	1,532,764
Mortgage, construction loans and capital lease obligations	414,357	383,812	450,336	340,152	172,573
Notes payable	361,323	207,711	174,843	209,005	162,768
Senior notes	535,000	535,000	410,000	410,000	510,000
Convertible subordinated debentures	—	75,000	75,289	75,289	75,289
Redeemable preferred shares	135,000	235,000	235,000	100,000	100,000
Shareholders' equity	691,374	644,287	589,291	465,460	500,543
Number of common shares outstanding	49,201	43,535	40,071	39,469	40,201

REVENUES

Year Ended December 31,	Retail/Mixed-Use Properties	Residential Properties	Other	Total
2003	96%	3%	1%	100%
2002	97%	1%	2%	100%
2001	97%	1%	2%	100%

TAXABILITY OF DIVIDENDS

Following is the income tax status of dividends paid during the fiscal year ended December 31,

	2003	2002	2001	2000
Ordinary income	73%	81%	100%	92%
Return of capital	12%	—	—	6%
Long-term capital gain	15%	19%	—	2%

MARKET QUOTATIONS

Quarter Ended	High	Low	Dividends Paid
2003			
Fourth quarter	\$39.80	\$36.80	\$.490
Third quarter	36.86	32.82	.490
Second quarter	33.85	30.78	.485
First quarter	31.11	26.75	.485
2002			
Fourth quarter	\$28.75	\$24.55	\$.485
Third quarter	27.85	23.70	.485
Second quarter	28.50	25.56	.480
First quarter	26.34	22.93	.480

On March 9, 2004, there were 5,183 holders of record of our Common Shares.

Management's Discussion and Analysis of Financial Condition and Results of Operations

OVERVIEW

We are an equity real estate investment trust specializing in the ownership, management, development and redevelopment of high quality retail and mixed-use properties. As of December 31, 2003, we owned or had an interest in 62 community and neighborhood shopping centers comprising approximately 13.5 million square feet, primarily located in densely populated and affluent communities throughout the Northeast and Mid-Atlantic United States. In addition, we owned 49 urban and retail mixed-use properties comprising over 2.7 million square feet and one apartment complex, primarily located in strategic metropolitan markets in the Northeast and Mid-Atlantic regions and California. In total, our properties were 93.1% leased at December 31, 2003 and 94.7% leased at December 31, 2002.

RECENT DEVELOPMENTS

In January 2004, we issued \$75 million of fixed rate notes which mature in February 2011 and bear interest at 4.50%. The proceeds of this note offering were used to pay down our revolving credit facility.

Also in January 2004, we purchased an interest rate swap on our \$150 million term note which bears interest at LIBOR plus 95 basis-points and is due to mature in October 2008. The swap has locked in the LIBOR portion of the interest rate at 2.401% through October 2006.

We paid off our 6.74% Medium Term Notes on their due date of March 10, 2004 for their full principal balance of \$39.5 million.

2003 PROPERTY ACQUISITIONS AND DISPOSITIONS

Acquisitions

On March 21, 2003, a partnership in which one of our wholly owned subsidiaries is the general partner, purchased the 214,000 square foot South Valley Shopping Center in Alexandria, Virginia for a purchase price of approximately \$13.7 million in cash. All of the purchase price has been allocated to real estate assets except for approximately \$125,000 which has been allocated to prepaid and other assets associated with the net fair value assigned to above-market leases assumed and \$332,000 which has been allocated to other liabilities associated with the net fair value assigned to below-market leases assumed.

On March 31, 2003, the same partnership acquired the leasehold interest, which extends through December 31, 2077, in the 257,000 square foot Mount Vernon Plaza in Alexandria, Virginia, for aggregate consideration of approximately \$17.5 million in the form of approximately \$700,000 of cash, 120,000 partnership units valued at \$3.5 million and the assumption of a \$13.3 million mortgage. All of the purchase price has been allocated to real estate assets except for approximately \$756,000 which has been allocated to prepaid and other assets associated with the net fair value assigned to above-market leases assumed and \$1.75 million which has been allocated to other liabilities associated with the net fair value assigned to the assumed leases at the property assigned.

On October 14, 2003, the Trust acquired the leasehold interest, which extends through September 30, 2028, in the 321,000 square foot Mercer Mall in Lawrenceville, New Jersey for \$10.5 million paid out of proceeds from dispositions and from borrowings under our credit facility. The master lease includes a fixed purchase price option for \$55 million in 2023. If we fail to exercise our purchase option, the

owner of Mercer Mall has a put option which would require us to purchase Mercer Mall for \$60 million in 2025. All of the purchase price has been allocated to real estate assets except for approximately \$736,000 allocated to prepaid and other assets associated with the net fair value assigned to above-market leases assumed, and \$2.4 million allocated to other liabilities associated with the net fair value assigned to below-market leases assumed.

On October 31, 2003, FR Plaza del Mercado, LLC, a wholly owned subsidiary of the Trust, purchased the 96,000 square foot Plaza del Mercado shopping center located in Silver Spring, Maryland for a purchase price of approximately \$20 million in cash. All of the purchase price has been allocated to real estate assets except for approximately \$929,000 fair value assigned to above-market leases assumed and \$962,000 allocated to other liabilities associated with the net fair value assigned to below-market leases assumed.

On December 4, 2003, FR Mercer Mall, LLC, a wholly owned subsidiary of the Trust, purchased a 40,000 square foot out-parcel of Mercer Mall in Lawrenceville, New Jersey for a purchase price of approximately \$6.5 million including the assumption. All of the purchase price has been allocated to real estate assets except for approximately \$15,000 which has been allocated to prepaid and other assets associated with the net fair value assigned to above-market lease assumed.

Dispositions

For the year ended December 31, 2003, aggregate cash proceeds from dispositions were \$46.0 million. Costs of dispositions were approximately \$2.1 million which resulted in net proceeds from sale of real estate for 2003 being \$43.9 million compared to net proceeds from sale of real estate in 2002 of \$62.5 million.

On June 16, 2003 we sold the street retail property located at 4929 Bethesda Avenue in Bethesda, Maryland for approximately \$1.5 million resulting in a gain of \$551,000. Net proceeds were used to reduce borrowings under our credit facility.

In the third quarter of 2003, we sold three retail properties and one undeveloped parcel of land for gross cash proceeds of \$20.8 million. The properties sold were Coolidge Corner in Brookline, Massachusetts (13,000 retail square feet), Tanasbourne in Washington County, Oregon (undeveloped land), 4925 Bethesda Avenue in Bethesda, Maryland (3,400 square feet) and 2106 Central Avenue in Evanston, Illinois (19,000 square feet). The combined gain on the dispositions was \$7.2 million. The net proceeds were used to reduce borrowings under our credit facility or held in cash to be used to fund acquisitions which took place in October 2003 (see "Acquisitions" above).

On October 31, 2003, we sold a 15,000 square foot street retail asset located at 234 Greenwich Avenue in Greenwich, Connecticut for approximately \$8.0 million. As a result of this sale, the Trust recorded a gain of approximately \$4.5 million.

On December 18, 2003, we sold four street retail properties, totaling 62,000 square feet, located in West Hartford, Connecticut. The properties were sold for approximately \$15.7 million and resulted in a gain of approximately \$7.9 million.

During the first quarter of 2003 an action was filed by a local governmental authority to condemn a shopping center in Rockville, Maryland, owned by one of our partnerships to facilitate the author-

ity's redevelopment of its town center. The shopping center has a cost basis of \$10.5 million and contributes less than 1% to rental income. We have agreed on a condemnation value of \$14.3 million, subject to certain terms, with the governmental authority and anticipate closing of this transaction in mid-2004. Because the anticipated condemnation proceeds are in excess of our carrying value, we have not recorded any impairment in value of the property.

2003 FINANCING DEVELOPMENTS

On February 11, 2003, the \$24.4 million Woodmont East construction loan and the \$17.0 million Friendship Center mortgage were paid off through borrowings under our revolving credit facility.

On May 14, 2003, we issued 3.2 million common shares at \$30.457 per share (\$31.48 gross, before an aggregate 3.25% underwriters discount and selling concession), netting \$98.4 million in cash proceeds.

On June 13, 2003, we redeemed our \$100 million 7.95% Series A Cumulative Redeemable Preferred Shares using the proceeds from the May 14, 2003 common stock offering and additional borrowings under our line of credit.

On June 23, 2003, we redeemed and paid in full our \$75 million, 5¼% Convertible Subordinated Debentures originally due to mature on October 28, 2003, through borrowings under our revolving credit facility.

On October 8, 2003, we closed on a new \$550 million unsecured credit facility which replaced our \$300 million revolving credit facility and \$125 million term loan, both of which were due to mature on December 19, 2003. The new credit facility consists of a \$150 million five-year term loan, a \$100 million three-year term loan, and a \$300 million three-year revolving credit facility, with a one-year extension option. The term loans bear interest at LIBOR plus 95 basis points, while the revolving facility bears interest at LIBOR plus 75 basis points. The spread over LIBOR is subject to adjustment based on our credit rating. Covenants under the new credit facility are substantially the same type as were required under the previous facility. Concurrent with the replacement of our \$125 million term loan with the new credit facility, we unwound the related interest rate swaps which were due to expire on December 19, 2003 at a cost of approximately \$1.1 million. In January 2004, to hedge our exposure to interest rates on our \$150 million term loan issued in October 2003, we entered into an interest rate swap, which fixed the LIBOR portion of the interest rate on the term loan at 2.401% through October 2006. The interest rate on the term loan as of December 31, 2003 was LIBOR plus 95 basis points. Subsequent to entering into the swap, the interest rate was fixed at 3.351% (2.401% plus 0.95%) on notional amounts totaling \$150 million.

A \$5.9 million loan receivable, which currently bears interest at 7.88% and is secured by an office building in San Francisco, California, was due February 28, 2003 but was not repaid on the due date. We are currently negotiating with the borrower to extend the loan until March 31, 2005. When the loan modification is complete, the interest rate on the note will decrease to 6% retroactive to July 1, 2003. Interest on the loan is current through December 31, 2003 and based in part on the value of the underlying collateral, we believe that the loan is collectible, and as such, no reserve has been established at this time.

SANTANA ROW

In 2003, our single largest development capital need was the completion of Phase I and Phase II of Santana Row, a multi-phase, mixed-use project built on 42 acres in San Jose, California in the heart of Silicon Valley. The project consists of residential, retail and hotel components, creating a community with the feel of an urban district.

Phase I of the project includes eight buildings which contain approximately 444,000 square feet of retail space, 255 residential units, a 213 room hotel and the supporting infrastructure. The first building, containing 40,000 square feet and leased to Crate & Barrel opened on June 27, 2002. Six of the remaining seven buildings, consisting of approximately 317,000 square feet of retail space, opened on November 7, 2002. The remaining building, "Building Seven," contained approximately 87,000 square feet of retail space, approximately 1,000 parking spaces and 246 residential units until a fire on August 19, 2002, prior to its scheduled opening. The fire in August 2002 destroyed all but 11 of the 246 residential units and damaged the retail units and a parking structure resulting in a delay of the opening of the retail units from September 2002 until February 2003. We estimate the total cost of Phase I to be approximately \$443 million, net of related insurance proceeds.

In December 2003, we reached final settlement with our insurance company regarding the Santana Row fire claim and received a final payment of \$26.9 million bringing the total settlement to \$129.0 million. In total, all of the proceeds except approximately \$11 million has been accounted for as a reduction in the cost basis of the property or reimbursement of costs to clean-up and restore damaged property or reimbursements to third parties. The remaining \$11 million has been accounted for as a reimbursement of lost rents of which \$8 million was recognized in 2003 as part of rental income and the remainder will be recognized as rental income in 2004. A gain of \$200,000 was recognized in the second quarter of 2003 to account for that portion of the insurance proceeds received in excess of costs of the constructed assets.

On February 7, 2003, we announced plans for Phase II of Santana Row, which includes approximately 84,000 square feet of retail space on two pad sites and 275 additional parking spaces. The Phase II retail space was opened and operating prior to year-end 2003 with total development costs of approximately \$26 million. The two primary tenants of Phase II, The Container Store and Best Buy, opened in the fourth quarter of 2003.

In November 2003, we announced the planned development of 96 townhomes and 160 flats on the Building 7 podium to replace the units that were destroyed in the August 2002 fire. Construction began in late 2003 and the first units are expected to be available in early 2005 with the balance delivered later in that year. The Trust will invest nearly \$60 million of incremental capital to complete the residential development.

The success of Santana Row will depend on many factors which cannot be assured and are not entirely within our control. These factors include among others, the demand for retail and residential space, the cost of operations, including utilities and insurance, the availability and cost of capital and the general economy, particularly in and around Silicon Valley.

RESULTS OF OPERATIONS

Same Center

Throughout this section, we have provided certain information on a "same center" basis. Information provided on a same center basis is provided for only those properties that we owned and operated for the entirety of both periods being compared and includes properties which were redeveloped or expanded during the periods being compared. Properties purchased or sold and properties under development at any time during the periods being compared are excluded.

For purposes of the following discussion of our results of operations on a same center basis for the year ended December 31, 2003 compared to the year ended December 31, 2002, we exclude the four shopping centers acquired during 2003 and 2002 (Mount Vernon Plaza, South Valley Shopping Center, Plaza del Mercado and Mercer Mall) as well as the dispositions (two buildings in Bethesda, Maryland, an undeveloped parcel in Washington County, Oregon, one building in Evanston, Illinois, one building in Greenwich, Connecticut, one

property in Brookline, Massachusetts, and four buildings in West Hartford, Connecticut). We also exclude the six properties sold in 2002 (one property in Greenwich, Connecticut; two properties in Westport, Connecticut; one property in Westfield, New Jersey; one property in Hollywood, California; and one property in Portland, Oregon) and properties under development in 2003 or 2002, including two of our street retail properties, Santana Row in San Jose, California and Pentagon Row in Arlington, Virginia.

Same center information for the year ended December 31, 2002 excludes the six properties sold in 2002, the Williamsburg Shopping Center in Williamsburg, Virginia, 101 E. Oak Street in Chicago, Illinois and 70/10 Austin Street in Forest Hills, New York which were sold in 2001, Friendship Center in Washington, D.C. which was purchased on September 21, 2001, the office building located at 580 Market Street in San Francisco, California which was exchanged for the minority partner's interest in Santana Row and properties under development in 2001 and 2002, including Pentagon Row in Arlington, Virginia and Santana Row in San Jose, California.

Year Ended December 31, 2003 to Year Ended December 31, 2002

<i>(in thousands)</i>	2003	2002	Increase Decrease/	% Change
Rental Income	\$334,697	\$295,016	\$ 39,681	13.5%
Other property income	17,800	15,468	2,332	15.1%
Interest and other income	5,379	5,156	223	4.3%
Total revenues	357,876	315,640	42,236	13.4%
Rental expenses	83,447	72,990	10,457	14.3%
Real estate taxes	34,596	30,687	3,909	12.7%
Total expenses	118,043	103,677	14,366	13.9%
Property operating income	239,833	211,963	27,870	13.1%
Interest	75,232	65,058	10,174	15.6%
Administrative	11,820	13,790	(1,970)	(14.3)%
Restructuring	—	22,269	(22,269)	
Depreciation and amortization	75,089	63,777	11,312	17.7%
Total other expenses	162,141	164,894	(2,753)	(1.7)%
Income before minority interests and discontinued operations	77,692	47,069	(30,623)	65.1%
Minority interests	(4,670)	(4,112)	(558)	13.6%
Operating income from discontinued operations	1,422	2,876	(1,454)	(50.6)%
Gain on sale of real estate net of loss on abandoned developments held for sale	20,053	9,454	10,599	112.1%
Net income	\$ 94,497	\$ 55,287	\$ 39,210	70.9%

REVENUES

Total revenues in 2003 were \$357.9 million which represents an increase of \$42.2 million or 13.4% over total revenues of \$315.6 million in 2002. The primary drivers of this growth are acquisitions, an increase in same center revenues from higher rent on tenant rollovers as detailed below and income of approximately \$8.0 million resulting from the portion of the settlement of our insurance claims for the August 2002 fire at Santana Row that related to lost rent. In addition, we experienced increased cost recoveries related to higher operating costs.

The percentage leased at our shopping centers declined to 93.1% at December 31, 2003 compared to 94.7% at year end 2002 due to acquisitions of centers with lower occupancy rates and the bankruptcies of several principal tenants (including K-mart and Today's Man) as well as an increase in redevelopment activity which results in leaseable space being taken out of service for more extended periods.

Rental Income. Rental income consists primarily of minimum rent, percentage rent and cost recoveries from tenants of common area maintenance and real estate taxes. Rental income increased \$39.7 million, or 13.5% , in 2003 versus 2002 due largely to the following:

- an increase of approximately \$22.0 million due to properties acquired in 2003 and from Santana Row, which was considered to be under development,
- approximately \$8.0 million from the Santana Row fire insurance settlement, and
- on a same center basis, an increase of over \$8.0 million, or approximately 3.0%, due mainly to increased minimum rents associated with tenant rollovers and developments, but also due to increased real estate tax recoveries.

Other Property Income. Other property income increased \$2.3 million, or 15.1%, to \$17.8 million for the year ended December 31, 2003, compared to \$15.5 million for the year ended December 31, 2002.

Included in other property income are items, which although recurring, tend to fluctuate more than rental income from period to period, such as utility reimbursements, lease termination fees and temporary tenant income. The increase in other property income in 2003 is primarily the result of higher utility reimbursements at Santana Row as the property has come on line and higher temporary tenant income partly offset by lower lease termination fees.

Interest and Other Income. Interest and other income consisted primarily of interest earned on mortgage notes receivable and overnight cash investments. In 2002, there was also income on tax-deferred exchange escrow deposits, as well as a provision for estimated losses related to various unconsolidated restaurant joint ventures at Santana Row. Interest and other income remained relatively flat from 2002 to 2003 as the reduced losses related to the restaurant joint ventures were offset by reduced interest income on the tax-deferred exchange escrow accounts and other interest income.

EXPENSES

Total property operating expenses were \$118.0 million, or an increase of \$14.4 million when compared to \$103.7 million in 2002. The total increase in expenses is due almost entirely to higher real estate taxes, increased maintenance costs related to snow removal in 2003 and the impact of acquisitions and developments.

Rental Expense. Rental expense increased \$10.5 million, or 14.3%, to \$83.4 million in 2003 from \$73.0 million in 2002. Of this increase:

- rental expenses at centers acquired and developed during 2003 (including Santana Row) were \$8.3 million;
- snow removal costs increased approximately \$3.8 million in the first quarter of 2003; and
- other maintenance and rental expenses, on a same center basis, were reduced approximately \$1.7 million.

Property expense reductions related to disposed properties were not significant.

As a result of these changes in rental expenses, rental income and other property income, rental expense as a percentage of rental income plus other property income increased slightly from 23.5% in 2002 to 23.7% in 2003. We refer to rental income plus other property income as "property income."

Real Estate Taxes. Real estate tax expense rose 12.7% in 2003 to \$34.6 million compared to \$30.7 million in 2002. The increase in 2003 is due largely to higher tax assessments for our properties in the East Coast segment as well as increased assessments of \$1.8 million related to acquired and developed properties, including Santana Row which was brought into service starting in late 2002.

Property Operating Income. Property operating income was \$239.8 million for the year ended December 31, 2003, an increase of \$27.9 million compared to \$212.0 million in 2002. Of this amount approximately \$8.0 million relates to the Santana Row fire insurance proceeds attributable to rental income lost as a result of the fire. Excluding these proceeds, property operating income rose \$19.9 million during 2003 due primarily to:

- earnings growth at Santana Row which has been phased into service,
- same center earnings increases, and
- earnings resulting from our acquisitions.

Same center property operating income rose 2.7% or almost \$5.7 million in 2003 due to increased rental income associated with

tenant rollovers and higher real estate tax recoveries and reduced property administrative expenses partly offset by property expenses which rose higher than the related recoveries, particularly the snow removal costs.

Interest Expense. Interest expense rose \$10.2 million, or 15.6%, to \$75.2 million in 2003. This substantial rise is almost entirely due to lower capitalization of interest and therefore higher interest expense as most of our property under development, particularly at Santana Row, was placed into service. Gross interest expense in 2003 was \$88.7 million versus \$88.6 million in 2002. Capitalized interest amounted to \$13.5 million and \$23.5 million in 2003 and 2002, respectively.

Administrative Expense. Administrative expenses decreased by \$2.0 million during 2003, or 14.3% to \$11.8 million compared to \$13.8 million in 2002. This \$2.0 million decrease resulted primarily from payroll and related benefits savings resulting from the management restructuring which began in February 2002. In addition, we experienced savings in legal costs and costs to support and maintain our information systems. These savings were largely offset by increased expensing of costs which had previously had been capitalized related to personnel involved in the development of Santana Row. In 2004, we expect administrative expenses to rise to those levels seen in 2002 due to higher costs of personnel and related expenditures.

Restructuring Expense. The restructuring expenses incurred in 2002 related to our adoption of a new business and management succession plan resulting in a charge of \$8.5 million, all of which was expended in 2002. In December 2002, we recorded a charge of \$13.8 million as a result of an accelerated executive transition plan of which \$12.7 million was expended in 2003, \$0.3 million was reversed and \$0.8 million remains to be expended as of December 31, 2003.

Depreciation and Amortization Expense. Expenses attributable to depreciation and amortization rose \$11.3 million to \$75.1 million in 2003 from \$63.8 million in 2002, an increase of 17.7%. The increase is due to depreciation on properties which were acquired in 2003 as well as depreciation of Santana Row which started opening in late 2002, and Pentagon Row, which came fully into service during 2002.

OTHER

Minority Interests. The increase in income to minority interests of \$0.6 million from \$4.1 million in 2002 to \$4.7 million in 2003 is the result of increased earnings as well as an increase in the number of operating partnership units held by minority investors. Units which were issued in connection with our acquisition of Mount Vernon Shopping Center were partially offset by a decrease in units outstanding as a result of redemptions during the year.

Operating Income from Discontinued Operations. Operating income from discontinued operations represents the operating income of properties that have been disposed of which, under SFAS No. 144, are required to be reported separately from results of ongoing operations. The reported operating income of \$1.4 million and \$2.9 million in 2003 and 2002, respectively, represent the operating income for the period during which we owned the ten properties sold in 2003 and the six properties sold in 2002.

Gain on Sale of Real Estate Net of Loss on Abandoned Developments Held for Sale. The gain on sale of real estate in 2003 was \$20.1 million for the disposal of properties as outlined above. None of the properties sold in 2003 resulted in a loss. The gain in 2002 of \$9.5 million is the result of the sale of six properties partly offset by the recognition of a \$9.7 million impairment loss associated with our change in business plan in that year.

Comparison of Year Ended December 31, 2002 to Year Ended December 31, 2001

(in thousands)	2002	2001	Increase Decrease/	% Change
Rental Income	\$295,016	\$269,288	\$ 25,728	9.6%
Other property income	15,468	13,707	1,761	12.8%
Interest and other income	5,156	6,590	(1,434)	(21.8)%
Total revenues	315,640	289,585	26,055	9.0%
Rental expenses	72,990	61,619	11,371	18.5%
Real estate taxes	30,687	27,646	3,041	11.0%
Total expenses	103,677	89,265	14,412	16.1%
Property operating income	211,963	200,320	11,643	5.8%
Interest	65,058	69,313	(4,255)	(6.1)%
Administrative	13,790	14,281	(491)	(3.4)%
Restructuring	22,269	—	22,269	
Depreciation and amortization	63,777	58,231	5,546	9.5%
Total other expenses	164,894	141,825	23,069	16.3%
Income before minority interests and discontinued operations	47,069	58,495	(11,426)	(19.5)%
Minority interests	(4,112)	(5,170)	1,058	(20.5)%
Operating income from discontinued operations	2,876	6,246	(3,370)	(54.0)%
Gain on sale of real estate net of loss on abandoned developments for sale	9,454	9,185	269	2.9%
Net income	\$ 55,287	\$ 68,756	\$(13,469)	(19.6)%

REVENUES

Total revenues increased \$26.1 million, or 9.0%, to \$315.6 million for the year ended December 31, 2002, as compared to \$289.6 million for the year ended December 31, 2001. The primary components of the increase in total revenues are discussed below.

Rental Income. Rental income consists of minimum rent, percentage rent and cost recoveries for common area maintenance and real estate taxes. The increase in rental income of \$25.7 million, or 9.6%, for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is attributable to:

- an increase of \$15.4 million, or 5.7%, on a same center basis due primarily to the increased rental rates at redeveloped and retented centers, as well as increased rental rates associated with lease rollovers, an increase in recovery income from a refinement of our recovery accrual processes, and higher cost recoveries as a result of increased rental expenses and real estate tax expenses; and
- an increase of \$8.1 million in rental income attributable to the properties acquired subsequent to January 1, 2001 and properties under development in 2001 and 2002 which phased into service during 2001 and 2002, specifically Santana Row and Pentagon Row. These increases were offset by properties sold in 2001.

Other Property Income. Other property income includes items, which although recurring, tend to fluctuate more than rental income from period to period, such as utility reimbursements, lease termination fees and temporary tenant income. The increase in other property income of \$1.8 million, or 12.8%, for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is attributable to:

- increases of \$1.3 million in parking income, utility reimbursements and lease termination fees at Pentagon Row, which began phasing into service in the second quarter of 2001, Santana Row, which began phasing into service in the fourth quarter of 2002 and Friendship Center which was purchased in the third quarter of 2001; partially offset by

- a one-time \$800,000 perpetual easement payment from a residential developer that has commenced development on an adjacent site at the Pentagon Row project; and
- a same center decrease of approximately \$500,000 due to lower lease termination fees and parking income from properties owned and operated in both periods.

Interest and Other Income. Interest and other income includes interest earned on mortgage notes receivable, overnight cash investments, including tax-deferred exchange escrow deposits, as well as a provision for estimated losses related to various unconsolidated restaurant joint ventures at Santana Row. The decrease in interest and other income of \$1.4 million, or 21.8% for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is attributable to a write down associated with the estimated impairment of \$1.3 million in these joint ventures which represented our best estimate of the diminution of value based upon the then current economic climate surrounding these joint ventures.

EXPENSES

Total property operating expenses increased \$14.4 million to \$103.7 million for the year ended December 31, 2002, as compared to \$89.3 million for the year ended December 31, 2001. The primary components of the increase in total expenses are discussed below.

Rental Expense. The increase in rental expense of \$11.4 million, or 18.5%, for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is attributable to:

- an increase of \$9.1 million in non-capitalized operating, leasing and marketing costs associated with our development projects, primarily operating, pre-opening and marketing expenses at our Santana Row project, as well as increased costs reflecting a full year of operating activity at the Pentagon Row project; and
- an increase of \$1.8 million, or 3.1%, on a same center basis due primarily to increased maintenance, insurance and utility costs, offset by lower bad debt and property management costs.

Rental expense as a percentage of rental income and other property income, which we refer to as property income, increased slightly from 21.8% in 2001 to 23.5% in 2002 due primarily to increased marketing and pre-opening expenses at Santana Row. Same center rental expense, excluding the effect of property redevelopments and expansions, as a percentage of property income decreased slightly from 20.0% in 2001 to 19.6% in 2002 and overall for the year ended December 31, 2002 increased 2.2% from 2001.

Real Estate Taxes. The increase in real estate taxes of \$3.0 million, or 11.0%, for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is attributable to the impact of taxes at Santana Row which started coming into service in 2002, the impact of other acquired and developed properties and a general increase in tax assessments. On a same center basis, real estate taxes increased 7.0% due primarily to increased taxes on recently redeveloped properties and overall increases in tax assessments at various projects, principally Woodmont East, Fresh Meadows, Garden Market and Mid-Pike. Same center real estate taxes, excluding the effect of property redevelopments and expansions, for the year ended December 31, 2002 increased 6.1% from 2001.

Property Operating Income. As a result of the changes and variances explained above, property operating income, total income less rental expenses and real estate taxes, increased \$11.6 million, or 5.8%, to \$212.0 million for the year ended December 31, 2002 as compared to \$200.3 million for the year ended December 31, 2001.

Interest Expense. In 2002, we incurred interest of \$88.6 million, of which \$23.5 million was capitalized yielding interest expense of \$65.1 million, as compared to interest incurred of \$87.1 million in 2001, of which \$17.8 million was capitalized yielding interest expense of \$69.3 million. The decrease in interest expense of \$4.2 million, or 6.1%, for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is attributable to:

- increased capitalized interest at the Santana Row project which was under construction for the majority of 2002 and began to be phased into service beginning with the first tenant opening in June 2002; and
- a decrease in the weighted-average interest rate on our debt from 7.6% in 2001 to 7.4% in 2002, primarily as a result of decreasing interest rates on our variable rate debt.

Administrative Expense. The decrease in administrative expense of \$0.5 million, or 3.4%, for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is mostly attributable to lower payroll costs in 2002 as a result of our corporate restructuring. As a result, administrative expenses as a percentage of revenue decreased from 4.8% in the year ended December 31, 2001 to 4.3% in the year ended December 31, 2002.

Restructuring Charge. On February 28, 2002, we adopted a new business plan which returned our primary focus to our traditional business of acquiring and redeveloping community and neighborhood shopping centers that are anchored by supermarkets, drug stores, or high volume, value oriented retailers that provide consumer necessities. Concurrent with the adoption of the business plan, we adopted a management succession plan and restructured our management team. In connection with these plans, we recorded a charge of \$18.2 million. This charge included a reserve for a restructuring charge of \$8.5 million made up of \$6.9 million of severance and other compensation costs for several of our senior officers related to the management restructuring, as well as the write-off of \$1.6 million of our development costs. All charges against this February 2002 reserve, totaling \$8.5 million, were expended during 2002.

In addition, in the fourth quarter of 2002 we recorded a charge of \$13.8 million as a result of the accelerated executive transition whereby Donald C. Wood, the Trust's President and Chief Operating Officer, replaced Steven Guttman as Chief Executive Officer of the Trust. The fourth quarter charge includes an accrual of \$7.9 million at December 31, 2002 for payments and benefits due to Mr. Guttman pursuant to his contractual arrangements with us and for other transition related costs. No cash payments were made against this charge in 2002 and the majority of the accrual was expended in 2003.

Depreciation and Amortization Expense. The increase in depreciation and amortization expense of \$5.5 million, or 9.5%, for the year ended December 31, 2002, as compared to the year ended December 31, 2001 reflects the impact of recent new developments, tenant improvements and property redevelopments which were placed into service throughout 2001 and 2002.

OTHER

Minority Interests. The decrease in investors' share of operations of \$1.1 million, or 20.5%, for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is attributable to our 2001 purchase of the minority interest in nine street retail buildings in southern California and three street retail buildings in Forest Hills, New York and the operating unit holders' share of the decrease in operating income in 2002.

Gain on Sale of Real Estate Net of Loss on Abandoned Developments Held for Sale. The approximately \$300,000 increase in gain on sale of real estate, net of loss on abandoned developments held for sale for the year ended December 31, 2002, as compared to the year ended December 31, 2001, is attributable to:

- an increase in net gains recognized in 2002 from the sale of six properties for a combined gain of \$19.1 million in the second quarter of 2002, as compared to the sale of one shopping center in the second quarter of 2001 for a gain of \$7.9 million, the sale of one street retail property in the fourth quarter of 2001 for a gain of \$1.8 million and the exchange of a 90% interest in a street retail building for a 10% interest in three street retail buildings with a minority partner which resulted in a loss of \$500,000 in the fourth quarter of 2001; primarily offset by
- the impairment loss of \$9.7 million on the abandonment of developments held for sale (see Note 13 of the Notes to Consolidated Financial Statements for more information).

Operating Income from Discontinued Operations. Beginning in 2002, SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," requires that gains and losses from dispositions of properties and all operating earnings from these properties be reported as income from operations of discontinued assets. This also requires that all past earnings applicable to a property disposed of subsequent to January 1, 2002 be reported as income from operations of discontinued assets. As a result, the presentation of reported income will be updated each time a property is sold. This requirement is for presentation only and has no impact on net income. As described above, in 2002, we sold six properties for a combined gain of \$19.1 million. The earnings generated from these properties have been reported as income from operations of discontinued assets in accordance with SFAS No. 144. Income from operations of discontinued assets for the years ended December 31, 2002 and 2001 was \$2.9 million and \$6.2 million, respectively with the decrease being primarily due to the fact that these properties were owned for less than a full year in 2002.

Segment Results

We operate our business on an asset management model, where teams are responsible for a portfolio of assets. We have divided our portfolio of properties into three operating regions: the Mid-Atlantic, Northeast and West. Each region is operated under the direction of an asset manager, with dedicated leasing, property management and financial staff and operates largely autonomously with respect to day to day operating decisions. Incentive compensation throughout the regional teams is tied to the property operating income of the respective portfolios.

The following selected key segment data presented is for the full year, except real estate assets and gross leasable area which is presented as of year-end. The results of properties which have been disposed are excluded from property operating income presented below in accordance with SFAS No. 144.

Property operating income consists of rental income, other property income and interest income, less rental expense and real estate taxes. This measure is used internally to evaluate the performance of our regional operations and we consider it to be a significant measurement.

(in thousands)	Key Segment Financial Data		
	2003	2002	2001
MID-ATLANTIC			
Rental income	\$151,206	\$139,487	\$123,932
Total revenue	\$159,040	\$147,933	\$131,063
Property operating income	\$112,753	\$104,304	\$ 92,883
Property operating income as a percent of total revenue	70.9%	70.5%	70.9%
Real estate assets, at cost	\$903,878	\$827,090	\$793,566
Gross leasable area (square feet)	6,809	6,266	6,139
NORTHEAST			
Rental income	\$121,325	\$120,302	\$111,083
Total revenue	\$129,797	\$129,518	\$120,892
Property operating income	\$ 88,397	\$ 91,021	\$ 83,257
Property operating income as a percent of total revenue	68.1%	70.3%	68.9%
Real estate assets, at cost	\$813,617	\$747,778	\$760,849
Gross leasable area (square feet)	7,686	7,441	7,501
WEST			
Rental income	\$ 62,166	\$ 35,227	\$ 34,273
Total revenue	\$ 69,039	\$ 38,189	\$ 37,630
Property operating income	\$ 38,683	\$ 16,638	\$ 24,180
Property operating income as a percent of total revenue	56.0%	43.6%	64.3%
Real estate assets, at cost	\$752,654	\$731,958	\$549,889
Gross leasable area (square feet)	1,739	1,538	1,121

MID-ATLANTIC

The Mid-Atlantic region extends roughly from Baltimore south through metropolitan Washington, D.C. and further south through Virginia and North Carolina. Two properties in Florida are also included in this region. As of December 31, 2003, the Mid-Atlantic included 35 properties after three acquisitions in 2003 (Mount Vernon Plaza, South Valley Shopping Center and Plaza del Mercado) and two disposals in 2003 (4929 and 4925 Bethesda Avenue). There was no acquisition or disposal activity in 2002 in this region but 2002 saw increased results from Pentagon Row which was phased into service between 2001 and 2002 and from the impact of Friendship Center

which was acquired in 2001. The Williamsburg Shopping Center was sold in 2001.

Total revenue in the Mid-Atlantic grew 8.0% in 2003 after showing 13% growth in 2002. The revenue growth in 2003 largely reflects the increase in leasable area related to acquisitions as well as increased expense recovery. The significant growth in 2002 is due primarily to the acquisition of Friendship Center but also to the additional income from Pentagon Row which opened in late 2001 and the successful retreating at several shopping centers. Development fees earned in 2003 and 2002 amounted to \$1.0 million and \$0.8 million, respectively, and tend to be non-recurring.

The percentage leased was 93%, 96% and 96% as of year end 2003, 2002 and 2001, respectively. The decrease in 2003 occupancy reflects the impact of several anchor closings, including K-mart, the impact of acquiring Mt. Vernon Plaza and South Valley Shopping Center, both of which had lower than average occupancy when acquired, and an increase in redevelopment activity which will keep leasable space out of service until the redevelopments are complete. We expect that the increased redevelopment activity will continue in 2004 and 2005.

The improved rate of operating income to total revenue in the Mid-Atlantic in 2003 was caused largely by a decrease in expenses which are not recoverable from tenants, particularly legal costs, and lower overhead expenses. The property operating margin to revenue decreased in 2002 when compared to 2001 as a rise in property taxes was not completely offset by a similar rise in cost recoveries for the year.

NORTHEAST

The Northeast region extends from suburban Philadelphia north through New York and its suburbs into New England. This region also includes several properties located in Illinois and one located in Michigan. As of December 31, 2003, the Northeast region had 42 properties which reflects one acquisition and seven buildings disposed in 2003 and four small buildings disposed in 2002. One property was sold in 2001.

In the Northeast, total revenue was flat in 2003 when compared to 2002 after rising 7% in 2002 when compared to 2001. Northeast total revenue was flat in 2003 versus 2002 as a decrease in occupancy rates was offset by an increase in common area expense recoveries, particularly related to snow removal in the first quarter of 2003, and to real estate tax recoveries. The growth in 2002 over 2001 was driven primarily by an increase in rental rates at redeveloped, expanded and retreating centers as well as increased rental rates on rollovers and increased recoveries related to refinements in the recovery accrual process.

The percentage leased was 95%, 96% and 96% as of December 31, 2003, 2002 and 2001, respectively. The slight decrease in 2003 reflects the closing of several principal tenants, including K-mart, an increase in redevelopment activity which has taken leasable space out of service and the acquisition of Mercer Mall whose leased rate is currently below that of the rest of the region. Mercer Mall had a leased rate of approximately 80% when acquired in October 2003. We expect that the increased redevelopment activity will continue in 2004 and 2005.

The decrease in the rate of operating income to total revenue in 2003 when compared to 2002 was caused largely by a lower recovery rate on higher common area expenses, particularly due to the snow removal costs incurred in the first quarter of 2003. In addition, the region experienced lower lease termination fees in 2003 and higher costs to provide utilities at our Fresh Meadows property. The increased operating income margin in 2002 over 2001 was due to improved cost recoveries on relatively flat rental expenses.

WEST

As of December 31, 2003, 34 of our properties, including Santana Row, were located in the West region. The West region extends from Texas to the West Coast. In 2003, we disposed of one parcel of undeveloped land while in 2002 we disposed of one shopping center and exchanged the property at 580 Market Street in San Francisco, California for the minority partner's interest in Santana Row. In 2001, we sold one shopping center in the West region.

Total revenue in the West rose \$30.8 million, or 81%, in 2003 over 2002 of which \$21.3 million relates to increased total revenues at Santana Row as well as the impact of the 2002 \$1.3 million write-down associated with the impairment of our restaurant joint ventures, which was charged to other income in 2002. In addition, approximately \$8.0 million of the rental income growth comes from the insurance proceeds received related to the fire at Santana Row. The insurance proceeds are reported as part of rental income as they relate largely to lost rents on the delayed opening of the residential and retail units and rental concessions to tenants. Excluding the Santana Row revenue growth and the insurance proceeds, total revenue growth in 2003 was 4% as higher income in San Antonio, Texas and southern California more than offset lower revenue at our property at 150 Post Street in San Francisco, California. Total revenue growth in 2002 over 2001 was due largely to increased rental rates at redeveloped and retented properties and Santana Row coming on line in 2002 which was offset by a decrease in revenue related to 580 Market Street which was sold in 2002. Income from the insurance proceeds of approximately \$3.0 million will be recognized in 2004.

For the West region, the percentage leased was 88%, 84% and 93% at years ending 2003, 2002 and 2001, respectively. The Santana Row development added approximately 529,000 square feet of retail space to the West Coast since the end of 2001. The improved occupancy as of year end 2003 compared to the end of 2002 is due largely to increases at Santana Row and Houston Street in San Antonio, Texas.

The West region's property operating income margin to revenue improved in 2003 over 2002 due almost entirely to the significant growth in revenue at Santana Row. The operating expenses associated with Santana Row started increasing in 2002 as a result of leasing, marketing and other start-up costs in preparation for and during the opening of this project. In 2003, we incurred a full year of operating expenses but rental revenues continued growing during the year as occupancy increased. The West's property operating income margin dropped in 2002 compared to 2001 due to the opening of Santana described above partly offset by an increase in interest income from mortgage notes receivable. We expect the margin to again increase in 2004 due to higher occupancy at Santana Row and our property in San Antonio, Texas but at a slower pace than the improvement in 2003.

The success of Santana Row and Houston Street in San Antonio, Texas will depend on many factors which are not entirely within our control. We monitor current and long-term economic forecasts for these markets in order to evaluate the long-term financial returns of these projects. The overall return on investment in the West segment significantly lags the Northeast and Mid-Atlantic due to the phasing into service of Santana Row and Houston Street. We expect that the returns on investment in the West will continue to rise as these projects come into service but not necessarily to the same level of overall returns as generated in the other segments.

LIQUIDITY AND CAPITAL RESOURCES

Due to the nature of our business and our strategy, we are generally in a position to generate significant amounts of cash from operations. The cash generated from operations is primarily paid to shareholders in the form of dividends. One of the requirements of our maintaining our status as a REIT is the requirement that we distribute at least 90% of our REIT taxable income each year. Therefore, cash needs for executing our strategy and investing in new properties as well as payment of debt maturities must come from cash not distributed to shareholders, from proceeds of property dispositions, or from the proceeds of raising new capital by issuing equity or debt securities.

It is management's intention that we continually have access to the capital resources necessary to expand and develop our business. As such, we intend to operate with and maintain a conservative capital structure that will allow us to maintain strong debt service coverage and fixed charge coverage ratios as part of our commitment to investment-grade debt ratings. At December 31, 2003, our level of debt to total market capitalization was 39%. We may, from time to time, seek to obtain funds through additional equity offerings, unsecured debt financings and/or mortgage financings and other debt and equity alternatives, including formation of joint-ventures, in a manner consistent with our intention to operate with a conservative debt structure.

In 2003, we undertook several transactions to improve our liquidity, including the redemption of \$100 million of 7.95% preferred stock with the proceeds of a common equity offering, the redemption and payment in June 2003 of the \$75 million of our 5% Convertible Subordinated Debentures outstanding and due to mature in October 2003 with borrowings under our lower interest rate credit facility, and the refinancing and replacement of our \$300 million revolving credit facility and \$125 million term loan, both scheduled to mature in December 2003, with a new \$550 million unsecured credit facility. The new credit facility consists of a \$150 million five-year term loan, a \$100 million three-year term loan, and a \$300 million three-year revolving credit facility with a one-year extension option. The term loans bear interest at LIBOR plus 95 basis points while the revolving facility bears interest at LIBOR plus 75 basis points. See "Recent Developments" above for a discussion of our financing transactions subsequent to year end 2003.

Our cash and cash equivalents at December 31, 2003 were \$35.0 million, an increase from \$23.1 million at December 31, 2002.

Summary of Cashflows

<i>(in thousands)</i>	For the Year Ended December 31, 2003
Cash Provided by Operating Activities	\$122,391
Cash Used in Investing Activities	(91,272)
Cash Used by Financing Activities	(19,274)
Increase in Cash and Cash Equivalents	11,845
Cash and Cash Equivalents, Beginning of Period	23,123
Cash and Cash Equivalents, End of Period	<u>\$ 34,968</u>

The cash provided by operating activities is primarily attributable to the operation of our properties and includes \$8 million of insurance proceeds related to reimbursement of lost rent at Santana Row. We used cash of \$26.7 million to increase our working capital primarily as a result of an increase in notes receivable and an increase in current assets related to properties acquired.

We used net cash of \$91.3 million in investing activities during 2003, consisting of \$139.8 million of cash provided by investing activities and \$231.1 million of cash used in investing activities.

The net cash provided by our investing activities represents:

- \$95.9 million of proceeds from our final insurance settlement related to the fire at Santana Row used to reduce our cost basis; and
- \$43.9 million of net proceeds from the sale of real estate.

The net cash used in our investing activities reflects:

- an investment of \$123.9 million in property development activities;
- the use of \$50.6 million for capital expenditures in connection with redevelopment of properties and tenant improvements;
- an investment of \$50.6 million to acquire properties; and
- the repayment of \$5.9 million of mortgage notes outstanding.

We expect that capital expenditures for development activities, particularly at Santana Row, will decrease in 2004. We are not able to project our level of acquisitions or dispositions in future years but

expect that we will be able to fund acquisitions and our redevelopment pipeline through available means of financing.

We used net cash of \$19.3 million for financing activities during 2003, consisting of \$324.7 million used in financing activities and \$305.4 million of cash provided by financing activities.

The cash used in financing activities primarily reflects:

- payments on mortgages, capital leases and notes payable of \$117.9 million;
- payment of dividends of \$104.8 million; and
- redemption of preferred shares of \$100.0 million.

The cash provided by our financing activities primarily represents:

- proceeds from the issuance of common shares in a public offering of \$98.4 million;
- proceeds from the issuance of common shares for exercise of options and operating units of approximately \$53.0 million;
- net proceeds from issuing term notes of \$125.0 million; and
- increased borrowings under short-term debt of \$28.8 million.

Contractual Commitments

The following table provides a summary of our fixed, noncancelable obligations as of December 31, 2003.

Contractual Obligations ^{(a)(b)(c)(d)(e)}	Total	Less than 1 year	From 1–3 years	From 4–5 years	After 5 years
(in thousands)					
Current and long-term debt	\$1,151,364	\$142,373	\$187,663	\$317,922	\$503,406
Capital lease obligations, principal only	159,486	487	2,413	2,884	153,702
Operating leases	291,331	4,320	8,705	8,832	269,474
Development and redevelopment obligations	79,171	14,189	3,682	1,300	60,000
Restaurant joint ventures	421	421	—	—	—
Contractual operating obligations	6,774	3,349	3,318	107	—
Total contractual cash obligations	\$1,688,547	\$165,139	\$205,781	\$331,045	\$986,582

(a) Under the terms of the Congressional Plaza partnership agreement, from and after January 1, 1986, an unaffiliated third party, has the right to require us and the two other minority partners to purchase from half to all of its 37.5% interest in Congressional Plaza at the interest's then-current fair market value. Based on management's current estimate of fair market value, our estimated liability upon exercise of the put option is approximately \$28.0 million. In conjunction with the construction of apartments at the property completed in 2003, we have agreed to acquire 7.5% of the third party's interest in Congressional Plaza, thereby lowering its ownership percentage to 30%, in exchange for funding approximately \$7 million of the third party's share of the redevelopment cost. The development funding has taken place in 2003 and the acquisition of its 7.5% interest is anticipated to be completed in 2004. After the completion of this transaction, our estimated liability upon the exercise of the put option will be approximately \$21 million.

(b) Under the terms of four other partnerships which own street retail properties in southern California with a cost of approximately \$61 million, if certain leasing and revenue levels are obtained for the properties owned by the partnerships, the other partners may require us to purchase their partnership interests at a formula price based upon property operating income. The purchase price may be paid in cash or for two of the partnerships, a limited number of our common shares at the election of the other partners. In those partnerships, if the other partners do not redeem their interest, we may choose to purchase the limited partnership interests upon the same terms.

(c) Street Retail San Antonio LP, a wholly-owned subsidiary of the Trust, entered into a Development Agreement (the "Agreement") on March 13, 2000 with the City of San Antonio, Texas (the "City") related to the redevelopment of land and buildings that we own along Houston Street. Houston Street and the surrounding area have been designated by the City as a Reinvestment Zone (the "Zone"). The City agreed to facilitate redevelopment of the Zone by undertaking and financing certain public improvements based on our agreement to redevelop our properties in the Zone. Under the terms of the Agreement, the City issued debt to fund specific public improvements within the Zone. The initial and primary source of funding to the City for repayment of the debt and debt service is the incremental tax revenue that accretes to the City as the taxable value of the redeveloped properties within the Zone increases. We are required to issue an annual letter of credit, commencing on October 1, 2002 through September 30, 2014, that covers our designated portion of the debt service should the incremental tax revenue generated in the Zone not cover the debt service. We posted a letter of credit with the City on September 25, 2002 for \$795,000. Our obligation under this Agreement is estimated to range from \$1.6 million to \$3.0 million of which approximately \$360,000 has been funded in 2003. We have accrued for additional payments of \$1.2 million as of September 30, 2003 as part of the project costs in anticipation of a shortfall of incremental tax revenues to the City. We could be required to provide funding beyond the \$1.2 million currently accrued under the Agreement prior to its expiration on September 30, 2014. We do not anticipate that such obligation would exceed \$600,000 in any year nor exceed \$3 million in total. If the Zone creates sufficient tax increment funding to repay the City's debt prior to the expiration of the Agreement, we will be eligible to receive reimbursement of amounts paid for debt service shortfalls together with interest thereon.

(d) Under the terms of various other partnerships which own shopping center properties with a cost of approximately \$88.5 million, including one of the two shopping centers purchased in the first quarter of 2003, the partners may exchange their 852,222 operating units for cash or the same number of our common shares, at our option. On February 14, 2003 we paid \$333,000 to redeem 12,000 operating units. On April 3, 2003 we issued 64,952 of our common shares valued at \$1.9 million in exchange for 64,952 operating units. On January 5, 2004, we paid \$199,000 to redeem an additional 5,100 operating units.

(e) In addition to our contractual obligations we have other short-term liquidity requirements consisting primarily of normal recurring operating expenses, regular debt service requirements (including debt service relating to additional and replacement debt), recurring corporate expenditures including compensation agreements, non-recurring corporate expenditures (such as tenant improvements and redevelopments) and dividends to common and preferred shareholders. Overall capital requirements will depend upon acquisition opportunities, the level of improvements and redevelopments on existing properties and the timing and cost of future phases of Santana Row.

Debt Financing Arrangements

As of December 31, 2003, we had total debt outstanding of \$1.3 billion.

The following is a summary of our total debt outstanding as of December 31, 2003. Certain additional detailed information about our debt is included in Notes 4, 5 and 6 of our Notes to Consolidated Financial Statements.

Description of Debt (in thousands)	Original Debt Issued or Available	Principal Balance as of December 31, 2003	Interest Rate as of December 31, 2003	Maturity Date
Mortgage Loans				
Secured Fixed Rate				
Leesburg Plaza	\$ 9,900	\$ 9,900	6.510%	October 1, 2008
164 E. Houston Street	345	230	7.500%	October 6, 2008
Mercer Mall	Acquired	4,693	8.375%	April 1, 2009
Federal Plaza	36,500	35,543	6.750%	June 1, 2011
Tysons Station	7,000	6,753	7.400%	September 1, 2011
Barracks Road	44,300	44,222	7.950%	November 1, 2015
Hauppauge	16,700	16,670	7.950%	November 1, 2015
Lawrence Park	31,400	31,344	7.950%	November 1, 2015
Wildwood	27,600	27,551	7.950%	November 1, 2015
Wynnewood	32,000	31,943	7.950%	November 1, 2015
Brick Plaza	33,000	32,936	7.415%	November 1, 2015
Mount Vernon ⁽¹⁾	13,250	13,086	5.660%	April 15, 2028
Total Mortgage Loans		<u>\$ 254,871</u>		
Notes Payable				
Unsecured Fixed Rate				
Perring Plaza Renovation	\$ 3,087	\$ 2,128	10.00%	January 31, 2013
Other	295	45	Various	Various
Unsecured Variable Rate				
Term note with banks	100,000	100,000	LIBOR + 0.95%	October 8, 2006
Term note with banks ⁽²⁾	150,000	150,000	LIBOR + 0.95%	October 8, 2008
Escondido (Municipal Bonds) ⁽³⁾	9,400	9,400	3.060%	October 1, 2016
Revolving credit facilities ⁽⁴⁾	300,000	99,750	LIBOR + 0.75%	October 8, 2006
Total Notes Payable		<u>\$ 361,323</u>		
Senior Notes and Debentures				
Unsecured Fixed Rate				
6.74% Medium Term Notes ⁽⁵⁾	\$ 39,500	\$ 39,500	6.370%	March 10, 2004
6.625% Notes	40,000	40,000	6.625%	December 1, 2005
6.99% Medium Term Notes ⁽⁶⁾	40,500	40,500	6.894%	March 10, 2006
6.125% Notes ⁽⁷⁾	150,000	150,000	6.325%	November 15, 2007
8.75% Notes	175,000	175,000	8.750%	December 1, 2009
7.48% Debentures ⁽⁸⁾	50,000	50,000	7.480%	August 15, 2026
6.82% Medium Term Notes ⁽⁹⁾	40,000	40,000	6.820%	August 1, 2027
Total Senior Notes and Debentures		<u>\$ 535,000</u>		
Capital Lease Obligations				
Various		159,486	Various	Various through 2077
Total Debt and Capital Leases Obligations		<u>\$1,310,680</u>		

- The interest rate is fixed at 5.66% for the first ten years and then is reset to a market rate. The lender has the option to call the loan after year ten.
- This loan currently bears interest at LIBOR plus 95 basis points. In January 2004, we purchased interest rate swaps or hedges on this note, thereby locking in the LIBOR portion of the interest rate at 2.401% through October 2006.
- The loan requires monthly interest only payments through maturity. This loan bears interest at a variable rate determined weekly to be the interest rate which would enable the bonds to be remarketed at 100% of their principal amount. The weighted average interest rate for the year ended December 31, 2003 was 3.060%. The property is not encumbered by a lien.
- On October 8, 2003, we closed on a new credit agreement replacing our then existing credit agreement. The new agreement includes \$300 million three-year revolving credit facility which currently bears interest at LIBOR plus 75 basis points. The spread over LIBOR is subject to adjustment based on our credit rating. The maximum amount drawn under our old and new facilities during 2003 was \$225 million. The weighted average interest rate on borrowings under these facilities for the year ended December 31, 2003 was 3.39%.
- We purchased interest rate swaps at issuance, thereby reducing the effective interest rate from 6.74% to 6.37%.
- We purchased interest rate swaps at issuance, thereby reducing the effective interest rate from 6.99% to 6.894%.
- The Trust purchased an interest rate lock to hedge a planned note offering. A hedge loss of \$1.5 million associated with this hedge is being amortized into the November 2002 note offering thereby increasing the effective interest rate on these notes to 6.325%.
- Beginning on August 15, 2008, the debentures are redeemable by the holders thereof at the original purchase price.
- Beginning on August 1, 2007, the notes are redeemable by the holders thereof at the original purchase price.

Our credit facility and other debt agreements include financial covenants that may limit our operating activities in the future. These covenants require us to comply with a number of financial provisions using calculations of ratios and other amounts that are not normally useful to a financial statement reader and are calculated in a manner that is not in accordance with GAAP. Accordingly, the numeric information set forth below is calculated as required by our various loan agreements rather than in accordance with GAAP. We have not included a reconciliation of this information to GAAP information because, in this case, there is no directly comparable GAAP measure, similarly titled GAAP measures are not relevant in determining whether or not we are in compliance with our financial covenants and we believe that the ratios on our material covenants are relevant to the reader. These covenants require us to:

- limit the amount of debt so that our interest and other fixed charge coverage will exceed 1.75 to 1 (we maintained a ratio of 2.38 to 1 as of December 31, 2003);
- limit the amount of debt as a percentage of total asset value to less than .55 to 1 (we maintained a ratio of 0.51 to 1 as of December 31, 2003);
- limit the amount of secured debt as a percentage of total asset value to less than .30 to 1 (we maintained a ratio of 0.16 to 1 as of December 31, 2003);
- limit the amount of unsecured debt so that unencumbered asset value to unsecured debt will equal or exceed 1.75 to 1 (we maintained a ratio of 2.26 to 1 as of December 31, 2003); and
- limit the total cost of development projects under construction to 15% or less of total asset value (the total budgeted cost of our projects under construction at December 31, 2003 represented 2.7% of gross asset value).

We are also obligated to comply with other covenants, including, among others, provisions:

- relating to the maintenance of any property securing a mortgage;
- restricting our ability to pledge assets or create liens;
- restricting our ability to incur additional debt;
- restricting our ability to amend or modify existing leases;
- restricting our ability to enter into transactions with affiliates; and
- restricting our ability to consolidate, merge or sell all or substantially all of our assets.

As of December 31, 2003, we were in compliance with all of our financial covenants. If we were to breach any of our debt covenants, including the listed covenants, and did not cure the breach within any applicable cure period, our lenders could require us to repay the debt immediately, and, if the debt is secured, could immediately begin proceedings to take possession of the property securing the loan. Many of our debt arrangements, including our public notes and our credit facility, are cross-defaulted which means that the lenders under those debt arrangements can put us in default and require immediate repayment of their debt if we breach and fail to cure a covenant under certain of our other debt obligations. As a result, any default under our debt covenants could have a material adverse effect on our financial condition, our results of operations, our ability to meet our obligations and the market value of our shares.

Below are the aggregate principal payments required as of December 31, 2003 under our debt financing arrangements by year. Scheduled principal installments and amounts due at maturity are included.

<i>(in thousands)</i>	Secured	Capital Lease	Unsecured	Total
2004	\$ 2,803	\$ 486	\$ 39,652	\$ 42,941
2005	3,229	1,143	40,168	44,540
2006	3,581	1,271	240,435	245,287
2007	3,858	1,374	150,204	155,436
2008	13,633	1,510	150,227	165,370
2009 and thereafter	227,767	153,702	275,637	657,106
	<u>\$254,871</u>	<u>\$159,486</u>	<u>\$896,323</u>	<u>\$1,310,680</u>

Our organizational documents do not limit the level or amount of debt that we may incur.

INTEREST RATE HEDGING

We enter into derivative contracts, which qualify as cash flow hedges under SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities," in order to manage interest rate risk. Derivatives are not purchased for speculation.

In January 2004, to hedge our exposure to interest rates on our \$150 million, five-year term loan issued in October 2003, we entered into interest rate swaps, which fixed the LIBOR portion of the interest rate on the term loan at 2.401% through October 2006. The interest rate on the term loan as of December 31, 2003 was LIBOR plus 95 basis points, thus, subsequent to year end we swapped the floating rate debt to a fixed interest rate of 3.351% on notional amounts totaling \$150 million. On the January 2004 hedge, we are exposed to credit loss in the event of non-performance by the counterparty to the interest rate protection agreement should interest rates exceed the cap. However, management does not anticipate non-performance by the counterparty. The counterparty has a long-term debt rating of "A" by Standard and Poor's Ratings Service ("S&P") and "A1" by Moody's Investors Service ("Moody's") as of March 8, 2004. Although our swap is not exchange traded, there are a number of financial institutions which enter into these types of transactions as part of their day-to-day activities. The swap has been documented as a cash flow hedge and designated as effective at inception of the swap contract.

Consequently, the unrealized gain or loss upon measuring the swap at its fair value will be recorded as a component of other comprehensive income within shareholders' equity and either a derivative instrument asset or liability is recorded on the balance sheet.

The hedges open at the end of the third quarter 2003 relating to our \$125 million term loan which was to mature on December 19, 2003, were unwound on October 8, 2003, in connection with the repayment of that loan, at a cost of approximately \$1.1 million which was charged to interest expense in the fourth quarter of 2003.

Liquidity Requirements

Short-term liquidity requirements consist primarily of obligations under capital and operating leases, normal recurring operating expenses, regular debt service requirements (including debt service relating to additional or replacement debt, as well as scheduled debt maturities), recurring corporate expenditures, non-recurring corporate expenditures (such as tenant improvements and redevelopments) and dividends to common and preferred shareholders. Overall capital requirements in 2004 and beyond will depend upon acquisition opportunities, the level of improvements and redevelopments on existing properties and the timing and cost of future phases of Santana Row. We expect to fund our capital requirements, as well as our development and redevelopment costs, acquisitions and normal recurring operating costs through a combination of cash provided by operating activities, borrowings under our credit facility and other funding sources which may consist of additional and replacement debt, both secured and unsecured, additional equity, joint venture relationships and property dispositions.

We expect to fund our long-term capital requirements, which consist primarily of maturities under our long-term debt, development and redevelopment costs and potential acquisition opportunities through a combination of funding sources which we believe will be available to us including debt, both secured and unsecured, additional equity, joint venture relationships and property dispositions.

The following factors could affect our ability to meet our liquidity requirements:

- we may be unable to obtain debt or equity financing on favorable terms, or at all, as a result of our financial condition or market conditions at the time we seek additional financing;
- restrictions in our debt instruments or outstanding equity may prohibit us from incurring debt or issuing equity at all, or on terms available under then-prevailing market conditions; and
- we may be unable to service additional or replacement debt due to increases in interest rates or a decline in our operating performance.

REIT Qualification

We intend to maintain our qualification as a REIT under Section 856(c) of the Code. As a REIT, we generally will not be subject to corporate federal income taxes as long as we satisfy certain technical requirements of the Code, including the requirement to distribute 90% of our REIT taxable income to our shareholders.

FUNDS FROM OPERATIONS

We have historically reported our FFO in addition to our net income and net cash provided by operating activities. FFO is a supplemental non-GAAP financial measure of real estate companies' operating performance. NAREIT defines FFO as follows: income available for common shareholders before depreciation and amortization of real estate assets and before extraordinary items less gains on sale of real estate.

NAREIT developed FFO as a relative measure of performance and liquidity of an equity REIT in order to recognize that the value of income-producing real estate historically has not depreciated on the basis determined under GAAP. However, FFO:

- does not represent cash flows from operating activities in accordance with GAAP (which, unlike FFO, generally reflects all cash effects of transactions and other events in the determination of net income);
- should not be considered an alternative to net income as an indication of our performance; and
- is not necessarily indicative of cash flow as a measure of liquidity or ability to pay dividends.

We consider FFO a meaningful, additional measure of operating performance because it primarily excludes the assumption that the value of the real estate assets diminishes predictably over time, and because industry analysts have accepted it as a performance measure. Comparison of our presentation of FFO to similarly titled measures for other REITs may not necessarily be meaningful due to possible differences in the application of the NAREIT definition used by such REITs.

An increase or decrease in FFO does not necessarily result in an increase or decrease in aggregate distributions because our Board of Trustees is not required to increase distributions on a quarterly basis unless necessary for us to maintain REIT status. However, we must distribute 90% of our REIT taxable income (as defined in the Code) to remain qualified as a REIT. Therefore, a significant increase in FFO will generally require an increase in distributions to shareholders although not necessarily on a proportionate basis.

The reconciliation of net income available for common shareholders to funds from operations for the years ended December 31, 2003 and 2002 is as follows:

(in thousands)	For the Years Ended December 31,	
	2003	2002
Net income available for common shareholders—basic	\$ 75,990	\$35,862
(Gain) on sale of real estate net of loss on abandoned developments held for sale	(20,053)	(9,454)
Depreciation and amortization of real estate assets	68,202	58,605
Amortization of initial direct costs of leases	5,801	4,750
Income attributable to operating partnership units	1,317	740
Funds from operations for common shareholders	<u>\$131,257</u>	<u>\$90,503</u>
Weighted average number of common shares used to compute basic FFO per share	<u>47,379</u>	<u>41,624</u>
Weighted average number of common shares used to compute diluted FFO per share	<u>48,619</u>	<u>42,882</u>

RISK FACTORS

This Annual Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act of 1995. Also, documents that we “incorporate by reference” into this Annual Report, including documents that we subsequently file with the Securities and Exchange Commission, which we refer to as the SEC, will contain forward-looking statements. When we refer to forward-looking statements or information, sometimes we use words such as “may,” “will,” “could,” “should,” “plans,” “intends,” “expects,” “believes,” “estimates,” “anticipates” and “continues.” In particular, the risk factors included or incorporated by reference in this Annual Report describe forward-looking information. The risk factors describe risks that may affect these statements but are not all-inclusive, particularly with respect to possible future events. Many things can happen that can cause actual results to be different from those we describe. These factors include, but are not limited to:

- risks that our tenants will not pay rent;
- risks of financing, such as our ability to consummate additional financings or obtain replacement financing on terms which are acceptable to us, our ability to comply with our existing financial covenants and the possibility of increases in interest rates that would result in increased interest expense;
- risks normally associated with the real estate industry, including risks that we may be unable to renew leases or relet space at favorable rents as leases expire, that new acquisitions and our development, construction and renovation projects may fail to perform as expected, that competition for acquisitions could result in increased prices, that we may encounter environmental issues, and, because real estate is illiquid, that we may not be able to sell properties when appropriate;
- risks that our growth will be limited if we cannot obtain additional capital; and
- risks related to our status as a real estate investment trust, commonly referred to as a REIT, for federal income tax purposes, such as our obligation to comply with complex tax regulations relating to our status as a REIT, the effect of future changes in REIT requirements as a result of new legislation and the adverse consequences if we fail to qualify as a REIT.

Given these uncertainties, readers are cautioned not to place undue reliance on these forward-looking statements or those incorporated into this Annual Report. We also make no promise to update any of the forward-looking statements. You should carefully review the risks and the risk factors incorporated herein by reference from our Form 8-K filed on March 11, 2004 before making any investment in us.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America, which we refer to as GAAP, requires management to make estimates and assumptions that in certain circumstances affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and revenues and expenses. These estimates are prepared using management's best judgment, after considering past and current events and economic conditions. In addition, information relied upon by management in preparing such estimates includes internally generated financial and operating information, external market information when available, and when necessary, information obtained from consultations with third party experts. Actual results could differ from these estimates. Management considers an accounting estimate to be critical if it requires assumptions to be made that were uncertain at the time the estimate was made, and changes in the estimate or different estimates could have a material impact on our consolidated results of operations or financial condition.

The most significant accounting policies which involve the use of estimates and assumptions as to future uncertainties and, therefore, may result in actual amounts that differ from estimates, are as follows.

Revenue Recognition and Accounts Receivable

Leases with tenants are classified as operating leases. Base rents are recognized on a straight-line basis over the terms of the related leases, net of valuation adjustments, based on management's assessment of credit, collection and other business risk. We make estimates of the collectibility of our accounts receivable related to base rents, including receivables from recording rent on a straight-line basis, expense reimbursements and other revenue or income taking into account payment history, industry trends and the period of recovery. In doing so, we generally reserve for straight-line rents due to be collected beyond ten years because of uncertainty of collection. In some cases the ultimate collectibility of these claims extends beyond one year. These estimates have a direct impact on our net income. Historically we have recognized bad debt expense between 1.0% and 1.5% of rental income. If we were to have experienced an increase in bad debt of 0.5% of rental income in 2003, our net income would have been reduced by approximately \$1.6 million.

Real Estate

The nature of our business as an owner, re-developer and operator of retail shopping centers means that we are very capital intensive. Depreciation and maintenance of our shopping centers and mixed-use properties constitutes a substantial cost for the Trust as well as the industry as a whole. The Trust capitalizes real estate investments and depreciates it in accordance with GAAP and consistent with industry standards based on our best estimates of the assets' physical and economic useful lives. The cost of our real estate investments less salvage value, if any, is charged to depreciation expense over the estimated life of the asset using straight-line rates for financial statement purposes. We periodically review the lives of our assets and implement changes, as necessary, to the depreciation rates. These reviews take into account the historical retirement and replacement of our assets, the repairs required to maintain the condition of our assets, the cost of redevelopments which may extend the useful lives of our assets and general economic and real estate factors. A newly developed neighborhood shopping center building would typically have an

economic useful life of 50 to 60 years, but since many of our assets are not newly developed buildings, estimating the useful lives of assets that are long-lived as well as their salvage value requires significant management judgment. Accordingly, we believe that the estimates we make to determine our depreciation expense for accounting purposes are critical.

Land, buildings and real estate under development are recorded at cost. Depreciation is computed using the straight-line method with useful lives ranging generally from 35 years to a maximum of 50 years on buildings and improvements. Maintenance and repair costs are charged to operations as incurred. Tenant work and other major improvements, which improve or extend the life of the asset, are capitalized and depreciated over the life of the lease or the estimated useful life of the improvements, whichever is shorter. Minor improvements, furniture and equipment are capitalized and depreciated over useful lives ranging from three to 15 years. Certain external and internal costs directly related to the development, redevelopment and leasing of real estate, including applicable salaries and the related direct costs, are capitalized. The capitalized costs associated with developments, redevelopments and leasing are depreciated or amortized over the life of the improvement and lease, respectively. Unamortized leasing costs are charged to operations if the applicable tenant vacates before the expiration of its lease. Undepreciated tenant work is charged to operations if the applicable tenant vacates and the tenant work is replaced.

When applicable as lessee, we classify our leases of land and building as operating or capital leases in accordance with the provisions of Statement of Financial Accounting Standard (SFAS) No. 13, "Accounting for Leases." We are required to use judgment and make estimates in determining the lease term, the estimated economic life of the property and the interest rate to be used in applying the provisions of SFAS No. 13. These estimates determine whether or not the lease meets the qualification of a capital lease and is recorded as an asset.

We are required to make subjective assessments as to the useful lives of our real estate for purposes of determining the amount of depreciation to reflect on an annual basis. These assessments have a direct impact on net income. Certain events could occur that would materially affect our estimates and assumptions related to depreciation. Unforeseen competition or changes in customer shopping habits could substantially alter our assumptions regarding our ability to realize the return on investment in the property and therefore reduce the economic life of the asset and affect the amount of depreciation expense to charge against both the current and future revenues. We will continue to periodically review the lives of assets and any decrease in asset lives could have the effect of increasing depreciation expense while any analysis indicating that lives are longer than we have assumed could have the effect of decreasing depreciation expense. In order to determine the impact on depreciation expense of a different average life of our real estate assets taken as a whole, we used 25 years, which is the approximate average life of all assets being depreciated at the end of 2003. If the estimated useful lives of all assets being depreciated were increased by one year, the consolidated depreciation expense would have decreased by approximately

\$3.0 million. If the estimated useful lives of all assets being depreciated were decreased by one year, the consolidated depreciation expense would have increased by approximately \$3.0 million.

Interest costs on developments and major redevelopments are capitalized as part of developments and redevelopments not yet placed in service. Capitalization of interest commences when development activities and expenditures begin and end upon completion, which is when the asset is ready for its intended use. Generally, rental property is considered substantially complete and ready for its intended use upon completion of tenant improvements, but no later than one year from completion of major construction activity. We make judgments as to the time period over which to capitalize such costs and these assumptions have a direct impact on net income because capitalized costs are not subtracted in calculating net income. If the time period for capitalizing interest is extended, more interest is capitalized, thereby decreasing interest expense and increasing net income during that period.

Long-Lived Assets

There are estimates and assumptions made by management in preparing the consolidated financial statements for which the actual results will emerge over long periods of time. This includes the recoverability of long-lived assets, including our properties which have been acquired or developed. Management must evaluate properties for possible impairment of value and, for those properties where impairment may be indicated, make estimates of future cash flows including revenues, operating expenses, required maintenance and development expenditures, market conditions, demand for space by tenants and rental rates over very long periods. Because our properties typically have a very long life, the assumptions used to estimate the future recoverability of book value requires significant management judgment.

In August 2001 the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (effective for us on January 1, 2002). SFAS No. 144 requires that one accounting model be used for long-lived assets to be disposed of by sale, whether previously held and used or newly-acquired, and broadens the presentation of discontinued operations to include components of an entity comprising operations and cash flows that can be distinguished operationally and for financial reporting purposes from the rest of the entity. As a result, the sale of a property, or the classification of a property as held for sale, requires us to report the results of that property as "discontinued operations."

We are required to make estimates of undiscounted cash flows in determining whether there is an impairment of an asset. Actual results could be significantly different from the estimates. These estimates have a direct impact on net income, because recording an impairment charge results in a negative adjustment to net income.

Contingencies

We are sometimes involved in lawsuits and environmental matters arising in the ordinary course of business. Management makes assumptions and estimates concerning the amount and likelihood of loss relating to these matters. These estimates and assumptions have a direct impact on net income.

Consolidated Balance Sheets

(in thousands, except share data)	December 31,	
	2003	2002
ASSETS		
Real estate, at cost		
Operating	\$2,342,315	\$1,940,312
Development	127,834	340,488
Discontinued operations	—	26,026
	2,470,149	2,306,826
Less accumulated depreciation and amortization	(514,177)	(450,697)
Net real estate investments	1,955,972	1,856,129
Cash and cash equivalents	34,968	23,123
Mortgage notes receivable	41,500	35,577
Accounts and notes receivable	31,207	18,722
Prepaid expenses and other assets, principally lease commissions and property taxes	69,335	57,257
Debt issuance costs, net of accumulated amortization of \$3,111 and \$6,344, respectively	10,453	8,570
	<u>\$2,143,435</u>	<u>\$1,999,378</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Obligations under capital leases	\$ 159,486	\$ 104,395
Mortgages and construction loans payable	254,871	279,417
Notes payable	361,323	207,711
Accounts payable and accrued expenses	61,018	79,517
Dividends payable	26,021	24,356
Security deposits	7,208	6,685
Prepaid rents	17,552	13,644
Senior notes and debentures	535,000	535,000
5¼% Convertible subordinated debentures	—	75,000
Total liabilities	1,422,479	1,325,725
Minority interests	29,582	29,366
Commitments and contingencies		
Shareholders' equity		
Preferred stock, authorized 15,000,000 shares, \$.01 par:		
7.95% Series A Cumulative Redeemable Preferred Shares, (stated at liquidation preference \$25 per share), 4,000,000 shares issued in 1997	—	100,000
8.5% Series B Cumulative Redeemable Preferred Shares, (stated at liquidation preference \$25 per share), 5,400,000 shares issued in 2001	135,000	135,000
Common shares of beneficial interest, \$.01 par, 100,000,000 shares authorized, 50,670,851 and 44,996,382 issued, respectively	506	450
Additional paid in capital	980,227	818,290
Accumulated dividends in excess of Trust net income	(386,738)	(368,839)
	728,995	684,901
Less:		
1,470,275 and 1,461,147 common shares in treasury—at cost, respectively	(28,445)	(28,193)
Deferred compensation on restricted shares	(5,474)	(2,657)
Notes receivable from employee stock plans	(3,615)	(5,151)
Accumulated other comprehensive income (loss)	(87)	(4,613)
Total shareholders' equity	691,374	644,287
	<u>\$2,143,435</u>	<u>\$1,999,378</u>

The accompanying notes are an integral part of these consolidated statements.

Consolidated Statements of Operations

(unaudited)

(in thousands, except per share data)	Year ended December 31,		
	2003	2002	2001
REVENUE			
Rental income	\$334,697	\$295,016	\$269,288
Other property income	17,800	15,468	13,707
Interest and other income	5,379	5,156	6,590
	<u>357,876</u>	<u>315,640</u>	<u>289,585</u>
EXPENSES			
Rental	83,447	72,990	61,619
Real estate taxes	34,596	30,687	27,646
Interest	75,232	65,058	69,313
Administrative	11,820	13,790	14,281
Restructuring	—	22,269	—
Depreciation and amortization	75,089	63,777	58,231
	<u>280,184</u>	<u>268,571</u>	<u>231,090</u>
Income before minority interests and discontinued operations	77,692	47,069	58,495
Minority Interests	(4,670)	(4,112)	(5,170)
Income from continuing operations	<u>73,022</u>	<u>42,957</u>	<u>53,325</u>
Operating income from discontinued operations	1,422	2,876	6,246
Gain on sale of real estate	20,053	9,454	9,185
Income from discontinued operations	<u>21,475</u>	<u>12,330</u>	<u>15,431</u>
Net income	94,497	55,287	68,756
Dividends on preferred stock	(15,084)	(19,425)	(9,034)
Preferred stock redemption—excess of redemption cost over carrying value	(3,423)	—	—
Net income available for common shareholders	<u>\$ 75,990</u>	<u>\$ 35,862</u>	<u>\$ 59,722</u>
BASIC EARNINGS PER COMMON SHARE			
Income from continuing operations	\$ 1.15	\$ 0.57	\$ 1.13
Discontinued operations	0.45	0.29	0.39
	<u>\$ 1.60</u>	<u>\$ 0.86</u>	<u>\$ 1.52</u>
Weighted average number of common shares, basic	<u>47,379</u>	<u>41,624</u>	<u>39,164</u>
DILUTED EARNINGS PER COMMON SHARE			
Income from continuing operations	\$ 1.15	\$ 0.57	\$ 1.13
Discontinued operations	0.44	0.28	0.39
	<u>\$ 1.59</u>	<u>\$ 0.85</u>	<u>\$ 1.52</u>
Weighted average number of common shares, diluted	<u>48,619</u>	<u>42,882</u>	<u>40,266</u>

The accompanying notes are an integral part of these consolidated statements.

Consolidated Statements of Common Shareholders' Equity

	Year ended December 31,								
	2003			2002			2001		
	Shares	Amount	Additional Paid-in Capital	Shares	Amount	Additional Paid-in Capital	Shares	Amount	Additional Paid-in Capital
<i>(in thousands, except share data)</i>									
Common Shares of Beneficial Interest									
Balance, beginning of year	44,996,382	\$ 450	\$818,290	41,524,165	\$ 417	\$730,835	40,910,972	\$ 410	\$723,078
Exercise of stock options	2,124,869	21	50,749	951,971	9	20,857	22,066	—	459
Shares issued under dividend reinvestment plan	109,835	1	3,541	134,247	1	3,488	159,234	2	3,277
Performance and Restricted Shares granted, net of									
Restricted Shares retired	138,568	1	3,960	98,092	—	2,468	96,657	2	1,877
Issuance of shares in public offering	3,236,245	32	98,368	2,185,000	22	56,631	—	—	—
Reclassification for preferred stock redemption		—	3,423		—	—	—	—	—
Shares issued to purchase operating partnership units	64,952	1	1,896	100,000	1	2,769	—	—	—
Cost of 8.5% Series B Cumulative Preferred Shares							—	—	(4,775)
Accelerated vesting of options and restricted shares						1,165	—	—	—
Shares issued to purchase partnership interest		—	—	2,907	—	77	335,236	3	6,919
Balance, end of period	50,670,851	\$ 506	\$980,227	44,996,382	\$ 450	\$818,290	41,524,165	\$ 417	\$730,835
Accumulated Dividends in Excess of Trust Net Income									
Balance, beginning of year		\$(368,839)			\$(322,428)			\$(306,287)	
Net income		94,497			55,287			68,756	
Dividends declared to common shareholders		(93,889)			(82,273)			(75,863)	
Dividends declared to preferred shareholders and redemption costs		(18,507)			(19,425)			(9,034)	
Balance, end of period		\$(386,738)			\$(368,839)			\$(322,428)	
Common Shares of Beneficial Interest in Treasury									
Balance, beginning of year	(1,461,147)	\$ (28,193)		(1,452,926)	\$ (27,990)		(1,441,594)	\$ (27,753)	
Performance and Restricted Shares forfeited	(9,128)	(252)		(8,221)	(203)		(11,322)	(237)	
Balance, end of period	(1,470,275)	\$ (28,445)		(1,461,147)	\$ (28,193)		(1,452,916)	\$ (27,990)	
Deferred Compensation on Restricted Shares									
Balance, beginning of year	(153,993)	\$ (2,657)		(666,656)	\$ (15,005)		(735,875)	\$ (17,254)	
Performance and Restricted Shares issued, net of forfeitures	(118,400)	(3,371)		(73,821)	(1,763)		(61,369)	(830)	
Vesting of Performance and Restricted Shares	51,727	554		586,484	14,111		130,588	3,079	
Balance, end of period	(220,666)	\$ (5,474)		(153,993)	\$ (2,657)		(666,656)	\$ (15,005)	
Subscriptions receivable from employee stock plans									
Balance, beginning of year	(184,063)	\$ (5,151)		(218,555)	\$ (7,245)		(242,638)	\$ (6,734)	
Subscription loans issued	(87,641)	(1,999)		(93,469)	(2,986)		(3,333)	(973)	
Subscription loans paid	115,430	3,535		127,961	5,080		27,416	462	
Balance, end of period	(156,274)	\$ (3,615)		(184,063)	\$ (5,151)		(218,555)	\$ (7,245)	
Accumulated other comprehensive income (loss)									
Balance, beginning of year		\$ (4,613)			\$ (4,293)			\$ —	
Change due to recognizing (loss) gain on securities		(92)			(44)			49	
Change in valuation on interest rate swap		3,563			(276)			(4,342)	
Loss on interest rate hedge transaction		1,055			—			—	
Balance, end of period		\$ (87)			\$ (4,613)			\$ (4,293)	
Comprehensive income									
Net income		\$ 94,497			\$ 55,287			\$ 68,756	
Change due to recognizing loss on securities		(92)			(44)			49	
Change in valuation on interest rate swap		3,563			(276)			(4,342)	
Loss on interest rate hedge transaction		1,055			—			—	
Total comprehensive income		\$ 99,023			\$ 54,967			\$ 64,463	

The accompanying notes are an integral part of these consolidated statements.

Consolidated Statements of Cash Flows

(in thousands)	Year ended December 31,		
	2003	2002	2001
OPERATING ACTIVITIES			
Net income	\$ 94,497	\$ 55,287	\$ 68,756
Items not requiring cash outlays			
Depreciation and amortization, including discontinued operations	74,616	64,529	59,914
Gain on sale of real estate	(20,053)	(19,101)	(9,185)
Loss on abandoned developments held for sale	—	9,647	—
Non-cash portion of restructuring expense	—	19,586	—
Other, net	3,649	4,792	1,041
Changes in assets and liabilities			
Increase in accounts and notes receivable	(12,485)	(3,239)	(4,641)
Increase in prepaid expenses and other assets before depreciation and amortization	(22,614)	(19,762)	(18,305)
Increase in operating accounts payable, security deposits and prepaid rent	4,147	2,996	4,132
Increase in accrued expenses	634	4,334	7,736
Net cash provided by operating activities	122,391	119,069	109,448
INVESTING ACTIVITIES			
Acquisition of real estate	(50,629)	—	(61,415)
Capital expenditures—development	(123,883)	(221,357)	(158,048)
Capital expenditures—other	(50,641)	(43,579)	(41,013)
Santana Row fire insurance proceeds reducing cost basis	95,895	21,000	—
Proceeds from sale of real estate	43,909	62,544	25,063
(Issuance) repayment of mortgage notes receivable, net	(5,923)	5,648	3,275
Net cash used in investing activities	(91,272)	(175,744)	(232,138)
FINANCING ACTIVITIES			
Borrowing (repayment) of short-term debt, net	28,750	27,000	(34,000)
(Repayment) proceeds from mortgage and construction financing, net of costs	—	(60,718)	145,427
Increase in term notes to banks, net	125,000	—	—
Note issuance (repayment), net of costs	—	148,746	—
Issuance of Series B Preferred shares, net of costs	—	—	130,225
Repayment of Series A Preferred shares	(100,000)	—	—
Issuance of common shares, net of subscriptions receivable	151,614	76,701	398
Payments on mortgages, capital leases and notes payable	(117,913)	(29,627)	(31,550)
Dividends paid	(104,802)	(96,461)	(80,593)
(Decrease) increase in minority interest, net	(1,923)	(3,406)	(1,011)
Net cash (used in) provided by financing activities	(19,274)	62,235	128,896
Increase in cash	11,845	5,560	6,206
Cash at beginning of year	23,123	17,563	11,357
Cash at end of year	\$ 34,968	\$ 23,123	\$ 17,563

The accompanying notes are an integral part of these consolidated statements.

Notes to Consolidated Financial Statements

December 31, 2003, 2002 and 2001

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Federal Realty Investment Trust (the "Trust") is an equity real estate investment trust specializing in the ownership, management, development and redevelopment of high quality community and neighborhood shopping centers and main street mixed-use properties located in densely developed urban and suburban areas in strategic metropolitan markets in the Mid-Atlantic and Northeast regions and California.

We operate in a manner intended to enable us to qualify as a real estate investment trust for federal income tax purposes. A trust which distributes at least 90% of its real estate investment trust taxable income to its shareholders each year and which meets certain other conditions will not be taxed on that portion of its taxable income which is distributed to its shareholders. Therefore, Federal income taxes have been and are generally expected to be immaterial. We are obligated for state taxes, generally consisting of franchise or gross receipts taxes in certain states. Such state taxes have not been material.

Our consolidated financial statements include the accounts of the Trust, its corporate subsidiaries, and numerous partnerships and limited liability companies, all of which we control. The equity interests of other investors are reflected as investors' interest in consolidated assets. All significant intercompany transactions and balances are eliminated in consolidation. We account for our interests in joint ventures which we do not control or manage using the equity method of accounting.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America, which we refer to as GAAP, requires management to make estimates and assumptions that in certain circumstances affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and revenues and expenses. These estimates are prepared using management's best judgment, after considering past and current events and economic conditions. Actual results could differ from these estimates.

Revenue Recognition and Accounts Receivable. Leases with tenants are classified as operating leases. Minimum rents are recognized on a straight-line basis over the terms of the related leases net of valuation adjustments based on management's assessment of credit, collection and other business risk. Percentage rents, which represent additional rents based on gross tenant sales, are recognized at the end of the lease year or other period in which tenant sales' thresholds have been reached and the percentage rents are due. Real estate tax and other cost reimbursements are recognized on an accrual basis over the periods in which the expenditures occurred. We make estimates of the collectibility of our accounts receivable related to base rents, including straight line rentals, expense reimbursements and other revenue or income. In some cases the ultimate collectibility of these claims extends beyond one year. We generally reserve for straight-line rents due beyond ten years due to uncertainty of collection.

Real Estate. Land, buildings and real estate under development are recorded at cost. Depreciation is computed using the straight-line method. Estimated useful lives range generally from 35 years to a

maximum of 50 years on buildings and improvements. Maintenance and repair costs are charged to operations as incurred. Tenant work and other major improvements are capitalized and depreciated over the life of the lease or their estimated useful life, respectively. Upon termination of a lease, undepreciated tenant improvement costs are charged to operations if the assets are replaced and the asset and the corresponding accumulated depreciation are retired. Minor improvements, furniture and equipment are capitalized and depreciated over useful lives ranging from three to 15 years. In accordance with Statement of Financial Accounting Standard ("SFAS") No. 66, "Accounting for Sales of Real Estate," sales are recognized at closing only when sufficient down payments have been obtained, possession and other attributes of ownership have been transferred to the buyer and we have no significant continuing involvement. The gain or loss resulting from the sale of properties is included in net income at the time of sale.

We evaluate the carrying value of our long-lived assets in accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." In cases where particular assets are being held for sale, impairment is based on whether the fair value (estimated sales price less costs of disposal) of each individual property to be sold is less than the net book value. Otherwise, impairment is based on whether it is probable that undiscounted future cash flows from each property will be less than its net book value. If a property is impaired, its basis is adjusted to its estimated fair market value.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (effective for us on January 1, 2002). SFAS No. 144 requires that one accounting model be used for long-lived assets to be disposed of by sale, whether previously held and used or newly-acquired, and broadens the presentation of discontinued operations to include components of an entity comprising operations and cash flows that can be distinguished, operationally and for financial reporting purposes from the rest of the entity.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," which addresses accounting and processing for costs associated with exit or disposal activities. SFAS No. 146 requires the recognition of a liability for a cost associated with an exit or disposal activity when the liability is incurred versus the date the Trust commits to an exit plan. In addition, SFAS No. 146 states that the liability should be initially measured at fair value. The requirements of SFAS No. 146 are effective for exit or disposal activities that are initiated after December 31, 2002. This pronouncement has not had a material impact on our financial position or results of operations.

When applicable as lessee, we classify our leases of land and buildings as operating or capital leases in accordance with the provisions of SFAS No. 13, "Accounting for Leases."

Certain external and internal costs directly related to the development, redevelopment and leasing of real estate including applicable salaries and their related direct costs are capitalized. The capitalized costs associated with developments, redevelopments and leasing are depreciated or amortized over the life of the improvement or lease,

whichever is shorter. Unamortized leasing costs are charged to operations if the applicable tenant vacates before the expiration of its lease.

Interest costs on developments and major redevelopments are capitalized as part of the development and redevelopment until it is placed in service. Capitalization of interest commences when development activities and expenditures begin and end upon completion, i.e. when the asset is ready for its intended use. Generally rental property is considered substantially complete and ready for its intended use upon completion of tenant improvements, but no later than one year from the completion of major construction activity.

Debt Issue Costs. Costs related to the issuance of debt instruments are capitalized and are amortized as interest expense over the life of the related issue using the effective interest method. Upon conversion or in the event of early redemption, any unamortized costs are charged to operations.

Cash and Cash Equivalents. We define cash as cash on hand, demand deposits with financial institutions and short term liquid investments with an initial maturity under three months. Cash balances in individual banks may exceed insurable amounts.

Risk Management. We enter into derivative contracts, which qualify as cash flow hedges under SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities," in order to manage interest rate risk. Derivatives are not purchased for speculation. During 2001, to hedge our exposure to interest rates on our \$125 million term loan, we entered into interest rate swaps, which fixed the LIBOR interest rate on that term loan at 5.27%. The interest rate on this term loan was LIBOR plus 95 basis points, thus fixing the interest rate at 6.22% on notional amounts totaling \$125 million. The swaps were documented as cash flow hedges and designated as effective at inception of the swap contract. Consequently, the unrealized gain or loss upon measuring the swaps at their fair market value is recorded as a component of other comprehensive income within shareholders' equity and either a derivative instrument asset or liability is recorded on the balance sheet. At December 31, 2002, a cumulative unrealized loss of \$4.6 million, representing the difference between the then current market value and the 6.22% fixed interest rate on the swap, was recorded in other comprehensive income with a corresponding derivative liability on the balance sheet. In October 2003, we unwound the interest rate swaps which were due to expire December 19, 2003 at a cost of approximately \$1.1 million. There were no open derivative contracts at December 31, 2003. In January 2004, to hedge our exposure to interest rates on our \$150 million term loan issued in October 2003, we entered into interest rate swaps, which fixed the LIBOR portion of the interest rate on the term loan at 2.40% through October 2006.

In anticipation of a \$150 million Senior Unsecured Note offering, on August 1, 2002, we entered into a treasury rate lock that fixed the benchmark five year treasury rate at 3.472% through August 19, 2002. The rate lock was documented as a cash flow hedge of a forecasted transaction and designated as effective at the inception of the contract. On August 16, 2002, we priced the Senior Unsecured Notes with a scheduled closing date of August 21, 2002 and closed out the associated rate lock. Five year treasury rates declined between the pricing period and the settlement of the hedge purchase; therefore, to settle the rate lock, we paid \$1.5 million. As a result of the August 19, 2002 fire at Santana Row, we were not able to proceed with the note offering at that time. However, we consummated a \$150 million Senior Unsecured Note offering on November 15, 2002, and thus, the hedge loss is being amortized into interest expense over the life of the related Notes.

Acquisition, Development and Construction Loan Arrangements. We have made certain mortgage loans that, because of their nature, qualify as loan receivables. At the time the loans were made, we did not intend for the arrangement to be anything other than a financing and did not contemplate a real estate investment. Using guidance set forth in the Third Notice to Practitioners issued by the AICPA in February 1986 entitled "ADC Arrangements" ("the Third Notice"), we evaluate each investment to determine whether the loan arrangement qualifies under the Third Notice as a loan, joint venture or real estate investment and the appropriate accounting thereon. Such determination affects our balance sheet classification of these investments and the recognition of interest income derived therefrom. Generally, we receive additional interest on these loans, however we never receive in excess of 50% of the residual profit in the project (as defined in the Third Notice) and because the borrower has either a substantial investment in the project or has guaranteed all or a portion of our loan (or a combination thereof) the loans qualify for loan accounting. The amounts under ADC arrangements at December 31, 2003 and 2002 were \$48.9 million and \$35.6 million respectively and interest income recognized thereon was \$3.7 million and \$4.3 million, respectively.

Comprehensive Income. Our interest rate swaps were documented as cash flow hedges and designated as effective at inception of the swap contract, therefore, the unrealized gain or loss upon measuring the swaps at their fair market value is recorded as a component of other comprehensive income within shareholders' equity. In accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," investments purchased in connection with our nonqualified deferred compensation plan are classified as available for sale securities and reported at fair value. Unrealized gains or losses on these investments purchased to match our obligation to the participants is also recorded as a component of other comprehensive income. At December 31, 2003 these investments consisted of mutual funds and are stated at market value.

Earnings Per Share. We calculate basic and diluted earnings per share in accordance with SFAS No. 128, "Earnings Per Share." Basic EPS excludes dilution and is computed by dividing net income available for common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted into common shares and then shared in our earnings.

The following table sets forth the reconciliation between basic and diluted EPS (in thousands, except per share data):

	2003	2002	2001
Numerator			
Net income available for common shareholders—basic	\$75,990	\$35,862	\$59,722
Income attributable to operating partnership units	1,317	740	1,384
Net income available for common shareholders—diluted	<u>\$77,307</u>	<u>\$36,602</u>	<u>\$61,106</u>
Denominator			
Denominator for basic EPS—weighted average shares	47,379	41,624	39,164
Effect of dilutive securities, stock options and awards	412	417	197
Operating partnership units	828	841	905
Weighted average shares—diluted	<u>48,619</u>	<u>42,882</u>	<u>40,266</u>
Earnings per common share—basic	<u>\$1.60</u>	<u>\$0.86</u>	<u>\$1.52</u>
Earnings per common share—diluted	<u>\$1.59</u>	<u>\$0.85</u>	<u>\$1.52</u>

Stock-Based Compensation. In December 2002 the FASB issued SFAS No. 148, "Accounting for Stock Based Compensation-Transition and Disclosure" as an amendment of FASB Statement No. 123, "Accounting for Stock-Based Compensation." SFAS No. 148 amends the disclosure provisions to require prominent disclosure about the effects on reported net income of an entity's accounting policy decisions with respect to stock-based compensation. Stock options are accounted for using the intrinsic method in accordance with APB No. 25, "Accounting for Stock Issued to Employees," as interpreted, whereby if options are priced at fair market value or above at the date of grant and the number of shares is fixed or certain, no compensation expense is recognized. In addition, certain of our stock-based compensation arrangements provide for performance-based vesting which calls for the use of "variable plan accounting" whereby compensation expense is periodically recorded for the intrinsic value of vested shares. Historically, compensation arising from such arrangements has not been material to operations. The pro forma information is as follows (in thousands except for earnings per share):

	2003	2002	2001
Net income available to common shareholders	\$75,990	\$35,862	\$59,722
Stock-based employee compensation cost included in net income as reported	—	—	—
Stock-based employee compensation cost under the fair value method of SFAS No. 123	\$ 606	\$ 432	\$ 680
Pro forma net income available to common shareholders	\$75,384	\$35,430	\$59,042
Earnings per common share, basic	\$ 1.60	\$ 0.86	\$ 1.52
Earnings per common share, diluted	\$ 1.59	\$ 0.85	\$ 1.52
Pro forma earnings per common share, basic	\$ 1.59	\$ 0.85	\$ 1.51
Pro forma earnings per common share, diluted	\$ 1.58	\$ 0.84	\$ 1.50

Reclassifications. Certain components of rental income, other property income, rental expense, real estate tax expense and depreciation and amortization on the December 31, 2002 and 2001 Consolidated Statements of Operations have been reclassified to Income from operations of discontinued assets to assure comparability of all periods presented. In addition, certain balance sheet accounts have been reclassified to assure comparability of all periods presented.

Redemption of Preferred Stock. On June 13, 2003, we redeemed our \$100 million 7.95% Series A Cumulative Redeemable Preferred Shares at their face value. The original issuance costs of \$3.4 million were charged to shareholders' equity in 1997, when the shares were issued. On July 31, 2003, the Emerging Issues Task Force provided clarification on the treatment of the difference between the redemption value and the carrying value, adjusting for issuance costs, for GAAP financial reporting. In accordance with this clarification, we are required to make a change in accounting to retroactively reflect this difference as a reduction of net earnings to arrive at net earnings available to common shareholders. As a result of this change in accounting presentation, our Consolidated Statement of Operations for the year ended December 31, 2003 reflects a charge of \$3.4 million in the line "Preferred stock redemption—excess of redemption cost over carrying value" as a reduction of net income in computing net income available for common shareholders.

Guarantor's Accounting. In November 2002, the FASB issued FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Guarantees of Indebtedness of Others" ("FIN 45"). FIN 45 addresses the disclosure requirements of a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. FIN 45 also requires a guarantor to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The disclosure requirements of FIN 45 were effective for us on December 31, 2002. The liability recognition requirements are applicable prospectively to all guarantees issued or modified after December 31, 2002. The adoption of this pronouncement has not had a material impact on our financial position or results of operations.

Variable Interest Entities. On January 31, 2003, the FASB issued FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46"). FIN 46 clarifies existing accounting for whether interest entities should be consolidated in financial statements based upon the investees ability to finance its activities without additional financial support and whether investors possess characteristics of a controlling financial interest. We have evaluated the applicability of FIN 46 to our investments in certain restaurant joint ventures established in 2001 and 2002 at Santana Row and have determined that these joint ventures do not meet the definition of a Variable Interest Entity and therefore consolidation of these ventures is not required. Accordingly, these investments will continue to be accounted for using the equity method.

As of December 31, 2003, we have invested approximately \$7.8 million in these ventures, principally to fund buildout costs of each restaurant. Of this amount, \$6.5 million has been capitalized as an investment in these ventures and \$1.3 million was expensed in 2002 to reflect our estimate of the permanent impairment of our investment in two of these ventures due principally to declining economic conditions. We are currently committed to invest a total of \$8.0 million in these ventures and as such, our maximum exposure to further losses as a result of involvement in these ventures is \$6.7 million at December 31, 2003.

Statement of Financial Accounting Standards No. 149. In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities" which clarifies the accounting and reporting for derivative instruments. The statement is effective for contracts entered into or modified after June 30, 2003. The adoption of SFAS 149 has not had a material effect on the Trust's financial statements.

Statement of Financial Accounting Standards No. 150. In May 2003, the FASB issued SFAS No. 150 "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." SFAS No. 150 addresses the classification and measurement of freestanding financial instruments, including mandatorily redeemable preferred and common stock, and requires an issuer to classify certain instruments as liabilities. The adoption of SFAS No. 150 has not had a material effect on the Trust's financial Statements.

NOTE 2. REAL ESTATE AND ENCUMBRANCES

A summary of our properties at December 31, 2003 and 2002 is as follows (in thousands):

	Cost	Accumulated depreciation and amortization	Encumbrances
2003			
Retail and mixed-use properties	\$2,197,276	\$434,063	\$254,871
Retail properties under capital leases	246,143	73,767	159,486
Residential	26,730	6,347	—
	<u>\$2,470,149</u>	<u>\$514,177</u>	<u>\$414,357</u>
2002			
Retail and mixed-use properties	\$2,123,890	\$378,148	\$288,817
Retail properties under capital leases	176,253	66,538	104,395
Residential	6,683	6,011	—
	<u>\$2,306,826</u>	<u>\$450,697</u>	<u>\$393,212</u>

Retail and mixed-use properties includes the residential portion of our Santana Row development partner. The residential property investments comprised our investments in Rollingwood Apartments and Crest Apartments at Congressional Plaza.

During 2003 we expended cash of \$174.5 million to improve, redevelop and develop our existing real estate. Of the \$174.5 million spent in 2003 on our existing real estate portfolio, approximately \$123.9 million was invested in our Santana Row development project, located in San Jose, California. The remaining \$50.6 million of capital expenditures relates to improvements to common areas, tenant work and various redevelopments, including the cost of Congressional Apartments in Rockville, Maryland, the redevelopment of retail buildings in San Antonio, Texas and the completion of tenant work at the Woodmont East development in Bethesda, Maryland.

During 2003, we expended cash of \$50.6 million acquiring four shopping centers and \$55.4 million of assets were acquired through capital leases.

On March 21, 2003, a partnership in which one of our wholly owned subsidiaries is the general partner, purchased the 214,000 square foot South Valley Shopping Center in Alexandria, Virginia for a purchase price of approximately \$13.7 million in cash. All of the purchase price has been allocated to real estate assets except for approximately \$125,000 which has been allocated to prepaid and other assets associated with the net fair value assigned to above-market leases assumed and \$332,000 which has been allocated to other liabilities associated with the net fair value assigned to below-market leases assumed.

On March 31, 2003, the same partnership acquired the leasehold interest, which extends through December 31, 2077, in the 257,000 square foot Mount Vernon Plaza in Alexandria, Virginia, for aggregate consideration of approximately \$17.5 million in the form of approximately \$700,000 of cash, 120,000 partnership units valued at \$3.5 million and the assumption of a \$13.3 million mortgage. All of the purchase price has been allocated to real estate assets except for approximately \$756,000 which has been allocated to prepaid and other assets associated with the net fair value assigned to above-market leases assumed and \$1.75 million which has been allocated to other liabilities associated with the net fair value assigned to the assumed leases at the property assigned.

On October 14, 2003, the Trust acquired the leasehold interest, which extends through September 30, 2028, in the 321,000 square foot Mercer Mall in Lawrenceville, New Jersey for \$10.5 million paid out of proceeds from dispositions and from borrowings under our credit facility. The master lease includes a fixed purchase price option for \$55 million in 2023. If we fail to exercise our purchase option, the owner of Mercer Mall has a put option which would require us to purchase Mercer Mall for \$60 million in 2025. All of the purchase price has been allocated to real estate assets except for approximately \$736,000 allocated to prepaid and other assets associated with the net fair value assigned to above-market leases assumed, and \$2.4 million allocated to other liabilities associated with the net fair value assigned to below-market leases assumed.

On October 31, 2003, FR Plaza del Mercado, LLC, a wholly owned subsidiary of the Trust, purchased the 96,000 square foot Plaza del Mercado shopping center located in Silver Spring, Maryland for a purchase price of approximately \$20 million in cash. All of the purchase price has been allocated to real estate assets except for approximately \$929,000 fair value assigned to above-market leases assumed and \$962,000 allocated to other liabilities associated with the net fair value assigned to below-market leases assumed.

On December 4, 2003, FR Mercer Mall, LLC, a wholly owned subsidiary of the Trust, purchased a 40,000 square foot out-parcel of Mercer Mall in Lawrenceville, New Jersey for a purchase price of approximately \$6.5 million including the assumption. All of the purchase price has been allocated to real estate assets except for approximately \$15,000 which has been allocated to prepaid and other assets associated with the net fair value assigned to above-market lease assumed.

On June 16, 2003, we sold the street retail property located at 4929 Bethesda Avenue in Bethesda, Maryland for approximately \$1.5 million resulting in a gain of \$551,000.

During the first quarter of 2003 an action was filed by a local governmental authority to condemn a shopping center in Rockville, Maryland, owned by one of our partnerships to facilitate the authority's redevelopment of its town center. The shopping center has a cost basis of \$10.5 million and contributes less than 1% to our rental income. We have agreed with the governmental authority on a condemnation value of \$14.3 million, subject to certain terms, and anticipate closing of this transaction in mid-2004. Because the anticipated condemnation proceeds are in excess of our carrying value, we have not recorded any impairment in value of the property.

On July 31, 2003 we sold the street retail property located at 4925 Bethesda Avenue in Bethesda, Maryland for approximately \$1.1 million resulting in a gain of \$157,000.

On September 12, 2003 we sold the undeveloped land located in Washington County, Oregon for approximately \$9.7 million resulting in a gain of \$1.9 million.

On September 15, 2003 we sold the street retail property located in Brookline, Massachusetts for approximately \$8.2 million resulting in a gain of \$4.3 million.

On September 22, 2003 we sold a street retail property located at 2106 Central Avenue in North Evanston, Illinois for approximately \$1.8 million resulting in a gain of \$780,000.

On October 31, 2003 we sold a street retail property located at 234 Greenwich Avenue in Greenwich, Connecticut for approximately \$8.0 million, resulting in a gain of \$4.5 million.

On December 18, 2003 we sold four street retail properties located in West Hartford, Connecticut for approximately \$15.7 million, resulting in a gain of approximately \$7.9 million.

These property sales constitute discontinued operations and as such, the accompanying financial statements have been restated to reclassify the operations of these properties as discontinued operations. A summary of the financial information for the discontinued operations is as follows:

	2003	2002	2001
Revenue from discontinued operations	\$2,792	\$5,328	\$10,917
Income from operations of discontinued operations	\$1,422	\$2,876	\$ 6,246

On February 1, 2002, we redeemed the minority partner's interest in Santana Row in exchange for a \$2.6 million investment in a partnership. We made a \$5.9 million loan to the partnership in January 2001 that was due February 28, 2003 but was not repaid on the due date. The loan currently bears interest at 7.88% and is secured by an office building in San Francisco, California. We are currently negotiating with the borrower to extend the loan through March 31, 2005. When the loan modification is complete, the interest rate on the note will decrease to 6%, retroactive to July 1, 2003. Interest on the loan is current through December 31, 2003 and, based in part on the value of the underlying collateral, we believe the loan is collectible and as such, no reserve has been established at this time.

Our 111 retail properties at December 31, 2003 are located in 14 states and the District of Columbia. There are approximately 2,200 tenants providing a wide range of retail products and services. These tenants range from sole proprietorships to national retailers; no one tenant or corporate group of tenants accounts for more than 2.3% of annualized base rent.

Mortgage notes receivable of \$48.9 million are due over various terms from February 2003 to May 2021 and have a weighted average interest rate of 9.07%. Under the terms of certain of these mortgages, we will receive additional interest based upon the gross income of the secured properties and, upon sale of the properties, we will share in the appreciation of the properties.

Mortgages payable and capital lease obligations are due in installments over various terms extending to 2028 and 2060, respectively, with interest rates ranging from 3.14% to 11.25%. Certain of the capital lease obligations require additional interest payments based upon property performance.

On November 19, 2002 we used the proceeds from our \$150 million public note offering, as well as \$20 million of available insurance proceeds relating to the Santana Row fire and approximately \$7.1 million in borrowings under our credit facility, to pay in full and retire the Santana Row construction loan.

At December 31, 2002 there was \$24.4 million borrowed under the construction loan for our Woodmont East development in Bethesda, Maryland. The loan had a floating interest rate of LIBOR plus 120 basis points. On February 11, 2003 the \$24.4 million Woodmont East construction loan and the \$17.0 million Friendship Center mortgage were paid off through borrowings under our revolving credit facility.

Scheduled principal payments on mortgage and construction loan indebtedness as of December 31, 2003 are as follows (in thousands):

Year ending December 31,	
2004	\$ 2,803
2005	3,229
2006	3,581
2007	3,858
2008	13,633
Thereafter	<u>227,767</u>
	<u>\$254,871</u>

Future minimum lease payments and their present value for property under capital leases as of December 31, 2003, are as follows (in thousands):

Year ending December 31,	
2004	\$ 14,389
2005	15,637
2006	15,799
2007	15,911
2008	16,075
Thereafter	<u>629,066</u>
	<u>706,877</u>
Less amount representing interest	<u>(547,391)</u>
Present value	<u>\$ 159,486</u>

Leasing Arrangements

Our leases with commercial property and residential tenants are classified as operating leases. Leases on apartments are generally for a period of one year or less. Commercial property leases generally range from three to ten years (certain leases with anchor tenants may be longer), and in addition to minimum rents, usually provide for contingent rentals based on the tenant's gross sales and sharing of certain operating costs.

Minimum future commercial property rentals on noncancelable operating leases, before any reserve for uncollectible amounts, on operating properties as of December 31, 2003 are as follows (in thousands):

Year ending December 31,	
2004	\$ 263,004
2005	246,652
2006	223,276
2007	197,582
2008	168,818
Thereafter	<u>1,225,755</u>
	<u>\$2,325,087</u>

Income Statement Components

The components of rental income are as follows:

(in thousands)	Year ended December 31,		
	2003	2002	2001
Retail and mixed-use properties			
Minimum rents	\$262,525	\$233,801	\$214,492
Cost reimbursements	56,837	52,252	45,978
Percentage rent	6,184	5,635	5,833
Residential—rents	9,151	3,328	2,985
	<u>\$334,697</u>	<u>\$295,016</u>	<u>\$269,288</u>

The income statement adjustment recorded to recognize rent on a straight-line basis was an increase to minimum rents of \$1.9 million, \$1.7 million and \$0.7 million for the year ended December 31, 2003, 2002 and 2001, respectively.

The components of rental expense are as follows:

(in thousands)	Year ended December 31,		
	2003	2002	2001
Repairs and maintenance	\$24,121	\$18,632	\$17,017
Management fees and costs	10,746	12,039	11,484
Utilities	12,930	8,939	7,995
Payroll—properties	7,915	5,878	4,499
Ground rent	5,052	4,904	3,317
Insurance	6,728	4,198	3,082
Other operating	15,955	18,400	14,225
	<u>\$83,447</u>	<u>\$72,990</u>	<u>\$61,619</u>

NOTE 3. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following disclosure of estimated fair value was determined by us, using available market information and appropriate valuation methods. Considerable judgment is necessary to develop estimates of fair value. The estimates presented herein are not necessarily indicative of the amounts that could be realized upon disposition of the financial instruments.

We estimate the fair value of our financial instruments using the following methods and assumptions: (1) quoted market prices, when available, are used to estimate the fair value of investments in marketable debt and equity securities; (2) quoted market prices were used to estimate the fair value of our marketable convertible subordinated debentures; (3) discounted cash flow analyses are used to estimate the fair value of mortgage notes receivable and payable, using our estimate of current interest rates for similar notes in 2003, the carrying amount on the balance sheet was used to approximate fair value for mortgage notes receivable since these notes are for specific deals, some contain participation provisions based on the property performance and also are convertible into ownership of the properties;

(4) carrying amounts on the balance sheet approximate fair value for cash, accounts payable, accrued expenses and short term borrowings. Notes receivable from officers are excluded from fair value estimation since they have been issued in connection with employee stock ownership programs.

(in thousands)	December 31, 2003		December 31, 2002	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash & equivalents	\$ 34,968	\$ 34,968	\$ 23,123	\$ 23,123
Investments	\$ 8,919	\$ 8,919	\$ 5,929	\$ 5,929
Mortgage notes receivable	\$ 41,500	\$ 41,500	\$ 35,577	\$ 35,577
Mortgages and construction loans and notes payable	\$616,194	\$640,957	\$487,128	\$543,535
Convertible debentures	\$ —	\$ —	\$ 75,000	\$ 75,103
Senior notes	\$535,000	\$592,300	\$535,000	\$581,293

NOTE 4. NOTES PAYABLE

Our notes payable consist of the following:

(in thousands)	2003	2002
Revolving credit facilities	\$ 99,750	\$ 71,000
Term notes with banks	250,000	125,000
Other	11,573	11,711
	<u>\$361,323</u>	<u>\$207,711</u>

On October 8, 2003, we closed on a new \$550 million unsecured credit facility which replaced our \$300 million revolving credit facility and \$125 million term loan, both of which were due to mature on December 19, 2003. The new credit facility consists of a \$150 million five-year term loan, a \$100 million three-year term loan, and a \$300 million three-year revolving credit facility, with a one-year extension option. The term loans currently bear interest at LIBOR plus 95 basis points, while the revolving facility currently bears interest at LIBOR plus 75 basis points. The spread over LIBOR is subject to adjustment based on our credit rating. Covenants under the new credit facility are substantially the same type as were required under the previous facility. Concurrent with the replacement of our \$125 million term loan with the new credit facility, we unwound the related interest rate swaps which were due to expire on December 19, 2003 at a cost of approximately \$1.1 million.

The maximum amount drawn under these revolving credit facilities during 2003, 2002 and 2001 was \$215.0 million, \$225.0 million and \$308.5 million, respectively. In 2003, 2002 and 2001, the weighted average interest rate on borrowings was 3.4%, 5.0% and 5.6%, respectively, and the average amount outstanding was \$96.9 million, \$189.1 million and \$269.7 million, respectively.

In January 2004, we issued \$75 million of fixed rate notes which mature in February 2011 and bear interest at 4.50%. The proceeds of this note offering were used to pay down our revolving credit facility.

NOTE 5. 5¼% CONVERTIBLE SUBORDINATED DEBENTURES

In October 1993, we issued \$75.0 million of 5¼% convertible subordinated debentures, realizing cash proceeds of approximately \$73.0 million. The debentures which were convertible into shares of beneficial interest at \$36 per share were not registered under the Securities Act of 1933 and were not publicly distributed within the United States. We redeemed and paid in full our \$75.0 million debentures originally due to mature on October 28, 2003, on June 23, 2003.

NOTE 6. SENIOR NOTES AND DEBENTURES

Unsecured senior notes and debentures at December 31, 2003 and 2002 consist of the following:

<i>(in thousands)</i>	2003	2002
6.74% Medium-Term Notes due March 10, 2004	\$ 39,500	\$ 39,500
6.625% Notes due December 1, 2005	40,000	40,000
6.99% Medium-Term Notes due March 10, 2006	40,500	40,500
6.82% Medium-Term Notes due August 1, 2027, redeemable at par by holder August 1, 2007	40,000	40,000
6.125% Notes due November 15, 2007	150,000	150,000
7.48% Debentures due August 15, 2026, redeemable at par by holder August 15, 2008	50,000	50,000
8.75% Notes due December 1, 2009	175,000	175,000
	<u>\$535,000</u>	<u>\$535,000</u>

On November 19, 2002, we completed the sale of \$150 million of senior notes in an underwritten public offering under our shelf registration statement declared effective by the SEC on September 30, 1998. Net proceeds, after deducting the discounts and commissions to the underwriters and other expenses of this offering, totaled approximately \$148.7 million. The net proceeds, together with \$20 million in available insurance proceeds relating to the Santana Row fire, and approximately \$7.1 million in borrowings under our credit facility, were used to pay in full and retire the Santana Row construction loan, including all interest owed on the loan.

The loan agreements contain various covenants, including limitations on the amount of debt and minimum debt service coverage ratios. We are in compliance with all covenants. No principal is due on these notes prior to maturity.

In October 2002, we filed a \$500 million shelf registration statement, declared effective on November 6, 2002, with the Securities and Exchange Commission which allows the issuance of debt securities, preferred shares and common shares. As of December 31, 2003, \$400 million was available under the shelf registration. Subsequent to December 31, 2003, the capacity was reduced by \$75 million as a result of a note offering in January 2004.

NOTE 7. DIVIDENDS

On December 2, 2003 the Trustees declared a quarterly cash dividend of \$0.49 per common share, payable January 15, 2004 to common shareholders of record January 2, 2004. The total dividend declared per common share for 2003 was \$1.95.

Also on December 2, 2003 the Trustees declared a quarterly cash dividend of \$0.53125 per share on its Series B Cumulative Redeemable Preferred Shares, payable on January 30, 2004 to shareholders of record on January 15, 2004, respectively.

For the year ended December 31, 2003, \$0.29 of dividends paid per common share represent a capital gain. \$0.36 of dividends paid per Series B preferred share represent a capital gain. \$0.21 dividends paid per Series A preferred share represent a capital gain. For the year ended December 31, 2002, \$0.37 of dividends paid per common share and per Series B preferred share represent a capital gain. \$0.38 of dividends paid per Series A preferred share represent a capital gain.

NOTE 8. COMMITMENTS AND CONTINGENCIES

We are involved in various lawsuits and environmental matters arising in the normal course of business. Management believes that such matters will not have a material effect on our financial condition or results of operations.

As detailed at Note 1, "Summary of Significant Accounting Policies—Investment in Restaurant Joint Ventures at Santana Row," we are currently committed to invest approximately \$8.0 million in these joint ventures. As of December 31, 2003 we have invested approximately \$7.8 million.

Under the terms of the Congressional Plaza partnership agreement, from and after January 1, 1986, an unaffiliated third party, has the right to require us and the two other minority partners to purchase from half to all of its 37.5% interest in Congressional Plaza at the interest's then-current fair market value. Based on management's current estimate of fair market value, our estimated liability upon exercise of the put option is approximately \$28.0 million. In conjunction with the construction of apartments at the property completed in 2003, we have agreed to acquire 7.5% of the third party's interest in Congressional Plaza, thereby lowering its ownership percentage to 30%, in exchange for our funding approximately \$7 million of its share of the redevelopment cost. The development funding has taken place in 2003 and the acquisition of the third party's 7.5% interest is anticipated to be completed in 2004. After the completion of this transaction, our estimated liability upon the exercise of the put option will be approximately \$21 million.

Under the terms of various other partnerships which own shopping center properties with a cost of approximately \$88.5 million, the partners may exchange their 852,222 operating units for cash or the same number of our common shares, at our option. On February 14, 2003 we paid \$333,000 to redeem 12,000 operating units. On March 31, 2003 in connection with the acquisition of Mount Vernon Plaza we issued approximately 120,000 operating units. On April 3, 2003 we issued 64,952 of our common shares valued at \$1.9 million in exchange for 64,952 operating units. On January 5, 2004 we paid \$199,000 to redeem an additional 5,100 operating units.

Under the terms of four other partnerships which own street retail properties in southern California with a cost of approximately \$61 million, if certain leasing and revenue levels are obtained for the properties owned by the partnerships, the other partners may require us to purchase their partnership interests at a formula price based upon net operating income. The purchase price may be paid in cash or for two of the partnerships, a limited number of our common shares at the election of the other partners. In these partnerships, if the other partners do not redeem their interest, we may choose to purchase the limited partnership interests upon the same terms.

Street Retail San Antonio LP, a wholly-owned subsidiary of the Trust, entered into a Development Agreement (the "Agreement") on March 13, 2000 with the City of San Antonio, Texas (the "City") related to the redevelopment of land and buildings that we own along Houston Street in the City. Houston Street and the surrounding area have been designated by the City as a Reinvestment Zone (the "Zone"). The City has agreed to facilitate redevelopment of the Zone by undertaking and financing certain public improvements based on our agreement to redevelop our properties in the Zone. Under the terms of the Agreement, the City issued debt to fund specific public improvements within the Zone. The initial and primary source of funding to the City for repayment of the debt and debt service is the incremental tax revenue that accretes to the City as the taxable value of the redeveloped properties within the Zone increase. We are required to issue an annual letter of credit, commencing on October 1, 2002 through September 30, 2014, that covers our designated portion of the debt service should the incremental tax revenue generated in the Zone not cover the debt service. We posted a letter of credit with the City on September 25, 2002 for \$795,000. Our obligation under this Agreement is estimated to range from \$1.6 million to \$3.0 million of which approximately \$360,000 has been funded in 2003. We were not required to provide any funding in 2002 or for the semi-annual payment due March 15, 2003. We have accrued for additional payments of \$1.2 million as of September 30, 2003 as part of the project costs due to the estimated shortfall of incremental tax revenues to the City. We could be required to provide funding beyond the \$1.2 million currently accrued under the Agreement prior to its expiration on September 30, 2014. We do not anticipate that such obligation would exceed \$600,000 in any year nor exceed \$3 million in total. If the Zone creates sufficient tax increment funding to repay the City's debt prior to the expiration of the Agreement, we will be eligible to receive reimbursement of amounts paid for debt service shortfalls together with interest thereon.

As of December 31, 2003 in connection with renovation and development projects, the Trust has contractual obligations of approximately \$79 million.

We are obligated under ground lease agreements on several shopping centers requiring minimum annual payments as follows:

(in thousands)

2004	\$ 4,320
2005	4,329
2006	4,376
2007	4,423
2008	4,409
Thereafter	<u>269,474</u>
	<u>\$291,331</u>

NOTE 9. SHAREHOLDERS' EQUITY

In May 1999, we reorganized as a Maryland real estate investment trust by amending and restating our declaration of trust and bylaws. The Amended Declaration of Trust changed the number of authorized shares of common and preferred shares from unlimited to 100,000,000 and 15,000,000, respectively. In addition, all common shares of beneficial interest, no par value, which were issued and outstanding were changed to common shares of beneficial interest, \$0.01 par value per share and all Series A Cumulative Redeemable Preferred Shares of beneficial interest, no par value, which were issued and outstanding were changed to Series A Cumulative Redeemable Preferred Shares of beneficial interest, \$0.01 par value per share.

On October 6, 1997 we issued four million 7.95% Series A Cumulative Redeemable Preferred Shares at \$25 per share in a public offering, realizing cash proceeds of approximately \$96.6 million after costs of \$3.4 million. The Series A Preferred Shares were not redeemable prior to October 6, 2002. On June 13, 2003, we redeemed these Preferred Shares using the proceeds from the May 14, 2003 common stock offering and available funds. Dividends on the Preferred Shares were payable quarterly in arrears on the last day of January, April, July and October.

On November 19, 2001 we issued 5.4 million 8.5% Series B Cumulative Redeemable Preferred Shares at \$25 per share in a public offering, realizing cash proceeds of approximately \$130.2 million after costs of \$4.8 million. The Series B Preferred Shares are not redeemable prior to November 27, 2006. On or after that date, the Preferred Shares may be redeemed, in whole or in part, at our option, at a redemption price of \$25 per share plus all accrued and unpaid dividends. Dividends on the Preferred Shares are payable quarterly in arrears on the last day of January, April, July and October.

On June 12, 2002, we issued 2.2 million common shares at \$25.9825 per share (\$27.35 gross, before a 5.00% underwriters discount and selling concession) netting \$56.6 million in cash proceeds after all expenses of the offering.

On May 14, 2003, we issued 3.2 million common shares at \$30.457 per share (\$31.48 gross, before an aggregate 3.25% underwriters discount and selling concession) netting \$98.4 million in cash proceeds, after all expenses of the offering.

We have a Dividend Reinvestment Plan, whereby shareholders may use their dividends and optional cash payments to purchase shares. In 2003, 2002 and 2001, 109,835 shares, 134,247 shares and 159,234 shares, respectively, were issued under the Plan.

In December 1999, the Trustees authorized a share repurchase program for calendar year 2000 of up to an aggregate of 4 million of our common shares. During 2000, a total of 1,325,900 shares were repurchased, at a cost of \$25.2 million. We did not repurchase shares in 2003, 2002 or 2001.

In 2003, 2002 and 2001, 138,568 common shares, 98,092 common shares and 96,657 common shares, respectively, were awarded to key employees, including our former Chief Executive Officer, under various incentive compensation programs designed to directly link a significant portion of their current and long term compensation to the prosperity of the Trust and its shareholders. The shares vest over terms from 3 to 5 years. Vesting of common shares awarded to the former Chief Executive Officer was accelerated pursuant to his contractual arrangement.

On January 26, 1998, we granted 75,000 Performance Shares to an employee for which vesting was tied to leasing performance as it relates to Santana Row and other projects. Performance was to be measured at three separate dates extending to 2003. By December 31, 2002, the first two performance measures had been met. In connection with the restructuring (See Note 13) the 2003 performance measure was accelerated and granted as of December 31, 2002. We applied variable accounting to these awards by valuing the shares at each date the performance measures were either met or accelerated and recorded a charge of \$712,000 as part of the restructuring charge.

In February 2002 and February 2003, we granted Performance Awards of 30,000 and 120,000, respectively, to certain officers and employees of the Trust. Pursuant to the terms of these awards, 20% of the Performance Shares will vest for any calendar year in which we exceed certain performance targets for the same period. Any performance awards which remain unvested after 2011 and 2012, respectively, will be forfeited. We employ variable accounting for these Performance Awards. Compensation expense resulting from this accounting was not material in 2002 or 2003.

Tax loans with a balance of \$300,000 in 2003, \$1.8 million in 2002 and \$3.1 million in 2001 have been made in connection with restricted share grants to certain of our officers and in connection with the Share Purchase Plans. The loans, which bear interest ranging from 1.95% to 6.54%, are due over periods ranging from 8 to 13 years from the date of the loan. During 2003 tax loans in the amount of \$1.5 million were repaid.

On April 13, 1999, the Shareholder Rights Plan adopted in 1989 expired. On March 11, 1999 we entered into an Amended and Restated Rights Agreement with American Stock Transfer and Trust Company, pursuant to which (i) the expiration date of our shareholder rights plan was extended for an additional ten years to April 24, 2009, (ii) the beneficial ownership percentage at which a person becomes an "Acquiring Person" under the plan was reduced from 20% to 15%, and (iii) certain other amendments were made. On October 29, 2003, we further amended the Amended and Restated Rights Agreement to increase the beneficial ownership percentage at which a person becomes an "Acquiring Person" under the plan from 15% to 20% and to require that the Trust's Board of Trustees review the plan on a periodic basis.

NOTE 10. STOCK OPTION PLAN

The 1993 Long Term Incentive Plan ("Plan") authorizes the grant of options and other stock based awards for up to 5.5 million shares. Options granted under the Plan have ten year terms and vest in one to five years. The Plan expired in May 2003.

In May 2001 our shareholders approved the 2001 Long Term Incentive Plan ("2001 Plan") which authorized an additional 1,750,000 shares for future option and other stock based awards.

The option price to acquire shares under the 2001 Plan and previous plans is required to be at least the fair market value at the date of grant. As a result of the exercise of options, we had outstanding from our officers and employees notes for \$3.3 million, \$2.5 million and \$2.5 million at December 31, 2003, 2002 and 2001, respectively. Notes issued after 2001 bear interest at LIBOR plus a market-rate spread with the rate adjusted annually. Notes issued prior to 2002 bear interest at the lesser of (i) our borrowing rate on the date of exercise or (ii) the dividend rate on the date of exercise divided by the purchase price of such shares. The notes issued under the previous plans bear interest at the lesser of (i) our borrowing rate or (ii) the current indicated annual dividend rate on the shares acquired pursuant to the option, divided by the purchase price of such shares. The notes are collateralized by the shares with recourse to the borrower and have five-year terms. Option awards made in 2001 and later do not provide for employees to be able to exercise their options with a loan from the Trust.

SFAS No. 123, "Accounting for Stock-Based Compensation" requires pro forma information regarding net income and earnings per share as if we accounted for our stock options under the fair value method of that Statement. Where at the date of grant, either the number of shares or exercise price are not known, we record compensation expense in accordance with variable accounting. The fair value for options issued in 2003, 2002 and 2001 has been estimated as \$582,000, \$536,000 and \$350,000, respectively, as of the date of grant, using a Black Scholes model with the following weighted-average assumptions for 2003, 2002 and 2001, respectively: risk-free interest rates of 3.2%, 4.5% and 4.9%; volatility factors of the expected market price of our shares of 20%, 16% and 20%; and a weighted average expected life of the option of 6.0 years, 6.9 years and 6.9 years. Our assumed weighted average dividend yield used to estimate the fair value of the options issued was 8.85% in 2003.

Because option valuation models require the input of highly subjective assumptions, such as the expected stock price volatility, and because changes in these subjective input assumptions can materially affect the fair value estimate, the existing model may not necessarily provide a reliable single measure of the fair value of its stock options.

A summary of our stock option activity for the years ended December 31, is as follows:

	Shares Under Option	Weighted Average Exercise Price
Outstanding at January 1, 2001	3,718,281	\$23.46
Options granted 2001	417,500	19.80
Options exercised 2001	(27,566)	20.81
Options forfeited 2001	(351,834)	22.88
Outstanding at December 31, 2001	3,756,381	23.12
Options granted 2002	435,500	25.26
Options exercised 2002	(951,971)	21.92
Options forfeited 2002	(19,168)	23.95
Outstanding at December 31, 2002	3,220,742	23.76
Options granted 2003	419,500	28.30
Options exercised 2003	(2,124,869)	23.89
Options forfeited 2003	(53,333)	25.00
Outstanding at December 31, 2003	<u>1,462,040</u>	24.86

At December 31, 2003, 2002 and 2001, options for 900,000, 2.5 million shares and 2.7 million shares, respectively, were exercisable. The average remaining contractual life of options outstanding at December 31, 2003, 2002 and 2001 was 6.3 years, 5.4 years and 5.8 years, respectively. The weighted average grant date fair value per option for options granted in 2003, 2002 and 2001 was \$1.32, \$1.23 and \$1.04, respectively. The exercise price of options outstanding at December 31, 2003 ranged from \$18.00 per share to \$35.91 per share.

NOTE 11. SAVINGS AND RETIREMENT PLANS

We have a savings and retirement plan in accordance with the provisions of Section 401(k) of the Internal Revenue Code. For employees who choose to contribute, their contributions range, at their discretion, from 1% to 20% of compensation up to a maximum of \$11,000. Under the plan, we contribute out of our current net income, 50% of each employee's first 5% of contributions. In addition, we may make discretionary contributions within the limits of deductibility set forth by the Code. Our employees are immediately eligible to become plan participants. Employees are not eligible to receive matching contributions until their first anniversary of employment. Our expense for the years ended December 31, 2003, 2002 and 2001 was \$255,000, \$271,000 and \$243,000, respectively.

A nonqualified deferred compensation plan for our officers and certain other employees was established in 1994. The plan allows the participants to defer future income until the earlier of age 65 or termination of employment. As of December 31, 2003, we are liable to participants for approximately \$3.2 million under this plan. Although this is an unfunded plan, we have purchased certain investments with which to match this obligation. Our obligation under this plan and the related investments are both included in the accompanying financial statements.

NOTE 12. INTEREST EXPENSE

We incurred interest totaling \$88.7 million, \$88.6 million and \$87.1 million in 2003, 2002 and 2001, respectively, of which \$13.5 million, \$23.5 million, and \$17.8 million respectively, was capitalized. Interest paid was \$85.7 million in 2003, \$86.2 million in 2002 and \$84.1 million in 2001.

NOTE 13. CHANGE IN BUSINESS PLAN

On February 28, 2002, we adopted a new business plan which returned our primary focus to our traditional business of acquiring and redeveloping community and neighborhood shopping centers that are anchored by supermarkets, drug stores, or high volume, value oriented retailers that provide consumer necessities. We will complete Bethesda Row and Santana Row (Pentagon Row was completed in 2002) but do not plan to develop any new large-scale, mixed-use, ground-up development projects. Rather, we will seek to acquire income producing centers in and around our existing markets and will identify and execute redevelopment opportunities in our existing portfolio. Concurrent with the adoption of the business plan, we adopted a management succession plan and restructured our management team.

In connection with this change in our business plan, we recorded a charge of \$18.2 million. This charge included a reserve for a restructuring charge of \$8.5 million made up of \$6.9 million of severance and other compensation costs for several of our senior officers related to the management restructuring, as well as the write-off of \$1.6 million of our development costs. All charges against the reserve, totaling \$8.5 million, were expended during 2002. An additional component of the restructuring charge is an impairment loss of \$9.7 million representing the estimated loss on the abandonment of development projects held for sale, primarily the Tanasbourne development project located in Washington County, Oregon, thereby adjusting the value of these assets to their estimated fair value. The Tanasbourne land was sold in 2003 for approximately \$9.7 million resulting in a gain of \$1.9 million.

On December 20, 2002, we announced the resignation of Steven J. Guttman as Trustee, Chief Executive Officer and Chairman of the Board of Trustees effective January 1, 2003. Donald C. Wood, our then President and Chief Operating Officer, was named Chief Executive Officer and a member of the Board of Trustees. Mark Ordan, a member of the Board of Trustees since 1996, was named non-executive chairman of the board. As a result of this transition, we recorded a charge of \$13.8 million in the fourth quarter of 2002 for payments and benefits to Mr. Guttman pursuant to his contractual arrangements with the Trust and for other transition related costs. Of this amount, \$7.9 million had not been paid as of December 31, 2002 and \$0.8 million remains to be expended as of December 31, 2003.

NOTE 14. SUBSEQUENT EVENTS (UNAUDITED)

Pursuant to the 2003 Incentive Bonus Plan, vice presidents and certain key employees receive part of their 2003 bonus in our common shares which vest over three years. Consequently, on February 12, 2004, 9,025 shares were awarded under this plan. In addition, on February 12, 2004, 75,522 restricted shares which will vest over three years were awarded to the Trust's officers. All of the restricted share awards were made under the 2001 Plan.

NOTE 15. SEGMENT INFORMATION

We operate our portfolio of properties in three geographic operating regions: Northeast, Mid-Atlantic and West, which constitutes our segments under Statement of Financial Accounting Standard No. 131, "Disclosures about Segments of an Enterprise and Related Information."

A summary of our operations by geographic region is presented below (in thousands):

	Northeast	Mid-Atlantic	West	Other	Total
2003					
Rental income	\$121,325	\$151,206	\$ 62,166	\$ 0	\$ 334,697
Other property income	5,063	7,525	5,212	—	17,800
Interest and other income	3,409	309	1,661	—	5,379
Rental expense	(24,519)	(33,168)	(25,760)	—	(83,447)
Real estate tax	(16,881)	(13,119)	(4,596)	—	(34,596)
Property operating income	88,397	112,753	38,683	-	239,833
Interest expense	—	—	—	(75,232)	(75,232)
Administrative expense	—	—	—	(11,820)	(11,820)
Depreciation and amortization	(27,732)	(29,533)	(16,814)	(1,010)	(75,089)
Income before minority interests and discontinued operations	\$ 60,665	\$ 83,220	\$ 21,869	\$(88,062)	\$ 77,692
Capital expenditures	\$ 82,944	\$ 81,165	\$124,122		\$ 288,231
Real estate assets	\$813,617	\$903,878	\$752,654		\$2,470,149
	Northeast	Mid-Atlantic	West	Other	Total
2002					
Rental income	\$120,302	\$139,487	\$ 35,227	\$ 0	\$ 295,016
Other property income	5,480	7,509	2,479	—	15,468
Interest and other income	3,736	937	483	—	5,156
Rental expense	(22,751)	(31,872)	(18,367)	—	(72,990)
Real estate tax	(15,746)	(11,757)	(3,184)	—	(30,687)
Property operating income	91,021	104,304	16,638	—	211,963
Interest expense	—	—	—	(65,058)	(65,058)
Administrative expense	—	—	—	(13,790)	(13,790)
Restructuring expense	—	—	—	(22,269)	(22,269)
Depreciation and amortization	(27,338)	(27,045)	(8,583)	(811)	(63,777)
Income before minority interests and discontinued operations	\$ 63,683	\$ 77,259	\$ 8,055	\$(101,928)	\$ 47,069
Capital expenditures	\$ 10,539	\$ 34,265	\$220,539		\$ 265,343
Real estate assets	\$747,778	\$827,090	\$731,958		\$2,306,826
	Northeast	Mid-Atlantic	West	Other	Total
2001					
Rental income	\$111,083	\$123,932	\$ 34,273	\$ 0	\$ 269,288
Other property income	5,430	5,697	2,580	—	13,707
Interest and other income	4,379	1,434	777	—	6,590
Rental expense	(22,676)	(28,239)	(10,704)	—	(61,619)
Real estate tax	(14,959)	(9,941)	(2,746)	—	(27,646)
Property operating income	83,257	92,883	24,180	-	200,320
Interest expense	—	—	—	(69,313)	(69,313)
Administrative expense	—	—	—	(14,281)	(14,281)
Depreciation and amortization	(26,475)	(23,736)	(6,986)	(1,034)	(58,231)
Income before minority interests and discontinued operations	\$ 56,782	\$ 69,147	\$ 17,194	\$(84,628)	\$ 58,495
Capital expenditures	\$ 15,386	\$ 87,706	\$169,278		\$ 272,370
Real estate assets	\$760,849	\$793,566	\$549,889		\$2,104,304

There are no transactions between geographic areas.

NOTE 16. QUARTERLY DATA (UNAUDITED)

The following summary represents the results of operations for each quarter in 2003 and 2002 (in thousands, except per share data):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2003				
Revenue ⁽¹⁾	\$84,091	\$84,745	\$85,836	\$97,825
Net income (loss) available for common shares	11,520	10,213	21,726	31,998
Earnings (loss) per common share—basic	0.26	0.22	0.44	0.66
Earnings (loss) per common share—diluted	0.26	0.21	0.43	0.64

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2002				
Revenue ⁽¹⁾	\$73,975	\$74,939	\$76,010	\$90,716
Net income available for common shares	(6,187)	30,479	13,648	(2,078)
Earnings per common share—basic	(0.15)	0.75	0.32	(0.05)
Earnings per common share—diluted	(0.15)	0.74	0.31	(0.05)

(1) As required by SFAS No. 144 revenue has been reduced to reflect the discontinued assets sold. Total revenue from these discontinued assets, by quarter, is summarized as follows (in thousands):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2003 Revenue from discontinued assets	0	(9)	(180)	2,565
2002 Revenue from discontinued assets	1,219	624	590	3,137

Report of Independent Certified Public Accountants

TRUSTEES AND SHAREHOLDERS OF FEDERAL REALTY INVESTMENT TRUST:

We have audited the consolidated balance sheet of Federal Realty Investment Trust (a Maryland real estate investment trust) (the Trust) and subsidiaries as of December 31, 2003 and 2002, and the related consolidated statements of operations, common shareholders' equity, and cash flows for each of the two years in the period ended December 31, 2003. These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits. The consolidated financial statements of Federal Realty Investment Trust and subsidiaries as of December 31, 2001, and for the year then ended, were audited by other auditors who have ceased operations. Those auditors expressed an unqualified opinion on those consolidated financial statements in their report dated February 11, 2002.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Federal Realty Investment Trust and subsidiaries as of December 31, 2003 and 2002, and the consolidated results of its operations and its consolidated cash flows for each of the two years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States of America.

We have also audited Schedules III and IV for the years ended December 31, 2003 and 2002. In our opinion, these schedules present fairly, in all material respects, the information therein when considered in relation to the basic financial statements taken as a whole.

As discussed above, the consolidated financial statements of Federal Realty Investment Trust and subsidiaries as of December 31, 2001, and for the year then ended, were audited by other auditors who have ceased operations. As described in Note 1, these financial statements have been restated to reflect discontinued operations. We have audited the adjustments described in Note 1 that were applied to restate the 2001 financial statements. In our opinion, such adjustments are appropriate and have been properly applied. However, we were not engaged to audit, review or apply any procedures to the 2001 financial statements of the Trust other than with respect to such adjustments, and, accordingly, we do not express an opinion or any other form of assurance on the 2001 financial statements taken as a whole.

/s/ GRANT THORNTON LLP
Vienna, Virginia
February 5, 2004

Report of Independent Public Accountants

TO THE TRUSTEES AND SHAREHOLDERS OF FEDERAL REALTY INVESTMENT TRUST:

We have audited the accompanying consolidated balance sheets of Federal Realty Investment Trust (a Maryland real estate investment trust) and subsidiaries as of December 31, 2001 and 2000 and the related consolidated statements of operations, common shareholders' equity and cash flows for each of the years in the three year period ended December 31, 2001. These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Federal Realty Investment Trust and subsidiaries as of December 31, 2001 and 2000 and the results of their operations and their cash flows for each of the years in the three year period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States.

Our audit was made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The financial statement schedules included on pages F-29 through F-34 of the Form 10-K are presented for purposes of complying with the Securities and Exchange Commission's rules and are not a required part of the basic consolidated financial statements. These schedules have been subjected to the auditing procedures applied in our audit of the basic consolidated financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

/s/ ARTHUR ANDERSEN LLP

Vienna, Virginia

February 11, 2002

Note: As permitted by Rule 2-02(e) of Regulation S-X promulgated under the Securities Act, this is a copy of the audit report previously issued by Arthur Andersen LLP in connection with the filing of our Form 10-K for the fiscal year ended December 31, 2001. After reasonable efforts, we have been unable to have Arthur Andersen LLP reissue this audit report in connection with the filing of this Form 10-K. See "Item 8. Financial Statements and Supplemental Data - Notice Regarding Arthur Andersen LLP" for a further discussion. The consolidated balance sheet as of December 31, 2000, and the related consolidated statements of operations, changes in shareholders' equity and other comprehensive income, and cash flows for the two fiscal years ended December 31, 2000 referred to in this report have not been included in the accompanying financial statements or schedules. In addition, Arthur Andersen's audit report relates to the financial statements of the Trust for 2000 and 2001 before restatement adjustments to reflect discontinued operations. The restatement adjustments for these years have been audited by Grant Thornton LLP.

Corporate Information

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COMMON STOCK LISTING

New York Stock Exchange
Symbol: FRT

SEC FORM 10-K

Copies of Federal Realty's Annual Report filed with the Securities and Exchange Commission on Form 10-K are available, without charge, upon written request to the Investor Relations department at the Trust.

MEMBERSHIPS

National Association of Real Estate Investment Trusts
International Council of Shopping Centers

ANNUAL MEETING

Federal Realty Investment Trust will hold its Annual Shareholder Meeting at 10:00 a.m. on May 5, 2004 at Woodmont Country Club, 1201 Rockville Pike, Rockville, Maryland.

CORPORATE GOVERNANCE

The Trust's Corporate Governance Guidelines and the charters for each of the Audit Committee, the Compensation Committee and the Nominating and Corporate Governance Committee are available in the Investor Information section of our website at www.federalrealty.com.

DIVIDEND REINVESTMENT AND SHARE PURCHASE PLAN

The Trust offers a Dividend Reinvestment and Share Purchase Plan (DRP) which enables its shareholders to automatically reinvest dividends as well as make voluntary cash payments towards the purchase of additional shares. Information and enrollment forms regarding the Plan and automatic cash investment can be obtained by calling (800) 937-5449. Shareholders may enroll on-line at www.amstock.com.

DIRECT DEPOSIT

Federal Realty now offers shareholders direct deposit of dividends. Interested shareholders should call (800) 937-5449 to request the appropriate enrollment forms. Shareholders may sign up on-line at www.amstock.com.

INTERNET

www.federalrealty.com

Visitors to the site can search for and download Securities and Exchange Commission filings, review Federal Realty's Dividend Reinvestment Plan, obtain current stock quotes and read recent press releases. Visitors can also request printed materials or sign up to receive news by e-mail.

INVESTOR RELATIONS CONTACT

You may communicate directly with Federal Realty's Investor Relations department via telephone at (800) 658-8980 or by electronic mail at IR@federalrealty.com.



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