



# Saul Centers

## 2004 Annual Report to Shareholders

# SAUL CENTERS, INC.

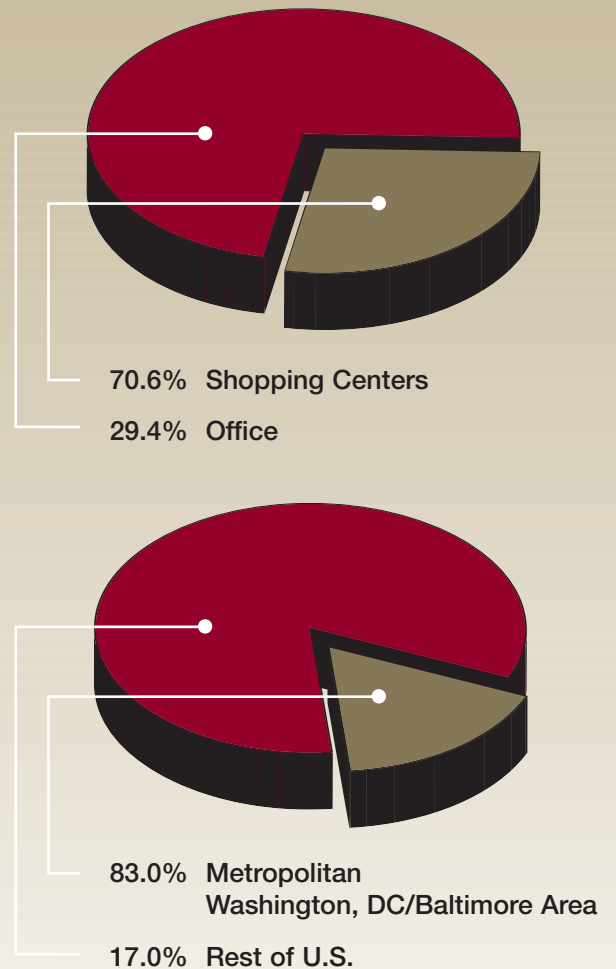
## PORTFOLIO COMPOSITION

### Saul Centers, Inc.

is a self-managed, self-administered equity real estate investment trust headquartered in Bethesda, Maryland. After the March 2005 acquisition of Palm Springs Center, Saul Centers operates and manages a real estate portfolio of 41 community and neighborhood shopping centers and office properties totaling approximately 7.3 million square feet of leasable area. Over 83% of our cash flow is generated from properties in the metropolitan Washington, DC/Baltimore area.

Saul Centers' primary operating strategy is to focus on continuing its program of internal growth, renovations, and expansions of community and neighborhood shopping centers, which primarily service the day-to-day necessities and services sub-sector of the overall retail market. The Company plans to supplement its growth through effective development of new office and retail properties and acquisitions of operating properties as appropriate opportunities arise.

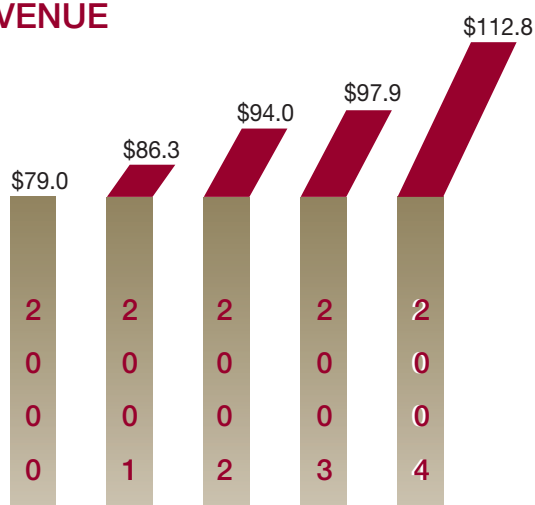
### PORTFOLIO COMPOSITION Based on 2004 Operating Income



*Broadlands Village II*

## TOTAL REVENUE

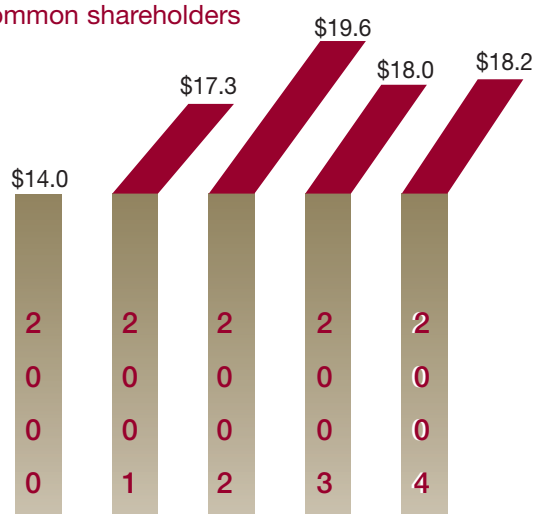
(In millions)



Leesburg Pike

## NET INCOME

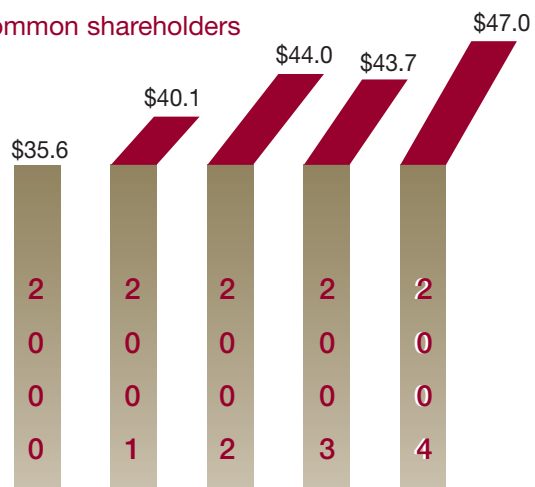
available to common shareholders  
(In millions)



Cruse MarketPlace

## FUNDS FROM OPERATIONS\*

available to common shareholders  
(In millions)



Shops at Fairfax

\* Funds From Operations (FFO) is a non-GAAP financial measure. See page 49 for a definition of FFO and reconciliation to net income.



## ANALYSIS

## COMPARATIVE ANALYSIS

	Year ended December 31,				
	2004	2003	2002	2001	2000
<b>Summary Financial Data</b>					
Total Revenue	\$ 112,842,000	\$ 97,884,000	\$ 93,963,000	\$ 86,308,000	\$ 79,029,000
Net Income Available to Common Stockholders	\$ 18,174,000	\$ 17,998,000	\$ 19,566,000	\$ 17,314,000	\$ 14,045,000
FFO Available to Common Shareholders	\$ 47,031,000	\$ 43,740,000	\$ 44,031,000	\$ 40,141,000	\$ 35,648,000
Average Common Stock Outstanding	16,210,736	15,607,890	14,886,505	14,210,470	13,623,330
Average Shares and Units Outstanding	21,404,976	20,790,216	20,059,264	19,382,720	18,795,571
FFO Available to Common Shareholders Per Share (Diluted)	\$ 2.20	\$ 2.10	\$ 2.20	\$ 2.07	\$ 1.90
Net Income Available to Common Stockholders Per Share (Diluted)	\$ 1.12	\$ 1.15	\$ 1.31	\$ 1.22	\$ 1.03
Common Dividend as a Percentage of FFO (Per Share)	71%	74%	71%	75%	82%
Interest Expense Coverage <sup>a</sup>	3.14	2.78	2.78	2.63	2.51
<b>Property Data</b>					
Number of Properties <sup>b</sup>	40	36	34	33	33
Total Portfolio Square Feet	7,217,000	6,532,000	6,272,000	6,159,000	6,143,000
Shopping Center Square Feet	6,012,000	5,328,000	5,069,000	4,956,000	4,941,000
Office Square Feet	1,205,000	1,204,000	1,203,000	1,203,000	1,202,000
Average Percentage Leased	94%	93%	94%	93%	93% <sup>c</sup>

(a) Interest expense coverage is defined as operating income before the sum of interest expense and amortization of deferred debt, and depreciation and amortization, divided by interest expense.

(b) Excludes development land parcels (Lansdowne, Kentlands Place, Broadlands Village III, Clarendon Center and Ashland Square).

(c) Excludes Washington Square, which was under development.



White Oak

*Broadlands Village**White Oak**Boca Valley Plaza*

**2004** was a year in which Saul Centers successfully completed its largest retail acquisition and development volume since going public in 1993, fully investing the proceeds from our November 2003 \$100 million preferred stock offering. We invested over \$120 million in operating property acquisitions and land developments, to increase our combined office and retail portfolio by more than 10%, or approximately 700,000 square feet of space.

During the first quarter of 2005, we invested an additional \$17.5 million to acquire the 126,000 square foot, Albertson's anchored Palm Springs Center in Altamonte Springs, a suburb of Orlando, Florida. Our core property retail and office markets continued to be healthy, demonstrated by strong leasing activity. During 2004, we signed 147 retail leases, totaling 520,000 square feet of space. Of the leases that expired, 70% were renewed, a strong indicator that tenants wish to remain in our well located centers. At 2004 year end, our retail centers were 93.5% leased and our office properties were 95.9% leased.

Long term interest rates remained at historic low levels throughout 2004. We continued our strategy of financing our assets with long-term debt and, during 2004, obtained \$95 million of 15-year debt at a weighted average interest rate of 5.63%.

Going into 2005, we had available cash of \$34 million, a diversified capital structure and 100% of our debt had fixed interest rates, with a weighted average remaining term of over 9.9 years. Only \$9.2 million of debt matures before 2011. We have a new \$150 million credit line with no outstanding borrowings, providing available funds for working capital requirements and for property acquisition and development opportunities.

### Financial Results

For the 2004 year, total revenues increased 15.3% to \$112,842,000 compared to \$97,884,000 for 2003. Operating income increased 24.2% to \$33,707,000 compared to \$27,146,000 in 2003. Net income available to common stockholders was \$18,174,000, or \$1.12 per diluted share, a 2.6% per share decrease from prior year results. Increased operating income was offset by a full year of preferred stock dividends (totaling \$8 million versus a partial year of \$1.2 million in 2003), by increased general and administrative expenses as a result of a larger acquisition staff and by increased accounting and administrative expenses related to new Sarbanes-Oxley documentation and compliance requirements.

Funds From Operations (FFO) available to common shareholders increased 7.5% to \$47,031,000 in 2004. FFO per diluted share available to common shareholders increased 4.8% to \$2.20 per share in 2004 compared to \$2.10 for 2003. The \$3,291,000 increase in FFO available to common shareholders in 2004 resulted from the combination of (1) increased operating income from retail acquisition and development properties and (2) successful leasing efforts in the core portfolio, primarily at 601 Pennsylvania Avenue, offset in part by the full year of preferred dividends relating to the November 2003 offering and increased general and administrative expenses.



*Village Center*



*Olde Forte Village*



*Ashburn Village*

## Retail Highlights

At year end 2004, we had 35 operating shopping center properties totaling over 6 million square feet of leasable area. These shopping centers contributed 71% of Saul Centers' property operating income. During 2004, we acquired four operating shopping centers and completed developments at three centers, increasing our shopping center portfolio leasable area by over 13%, or approximately 700,000 square feet of space. We invested \$87.1 million for the four shopping centers, totaling 539,000 square feet of space. Two of the centers are located in the Washington, DC metropolitan area and are anchored by Safeway. The other two centers, one located in suburban Atlanta, Georgia and the other located in Boca Raton, Florida, are both anchored by Publix, the market share leader in each location. The demographic characteristics of the neighborhoods surrounding each center are attractive, each densely populated with average 1-mile and 3-mile household incomes of \$103,000 and \$99,000, respectively.

Our three recently completed developments were operating at year end 2004 and are over 88% leased. The Shops at Monocacy is a 107,000 square foot Giant anchored retail center in Frederick, Maryland. Development costs, including the 2003 land acquisition, totaled \$22.3 million. The center is well located in the fast growing Frederick, Maryland area. We invested \$6.5 million in a 30,000 square foot expansion to our Broadlands Village shopping center located near Dulles Airport in Ashburn, Virginia and invested \$2.1 million in 15,000 square feet of new shop space at Thruway, located in Winston-Salem, North Carolina.

During 2004, our same center core retail portfolio operating income increased 2.2%. Retail spaces were relet at average initial cash rental rates of approximately 6% over rents paid on expiring leases for the 340,000 square feet of same store lease rollovers. Core portfolio real estate taxes and property operating expenses remained flat in 2004 as compared to 2003, primarily due to a substantial decrease in snow removal expenses in 2004, offsetting the modest expense increases in other categories.



*601 Pennsylvania Avenue**Avenel Business Park**Washington Square*

Based upon data provided by tenants who report sales, overall retail sales, including anchor and shop space, totaled \$290 per square foot in 2004. On a same store basis, sales increased 3.3% compared to 2003, with average annual increases of 0.7% over the past three years. Based upon current reports for just the 25 grocery stores in our portfolio, sales are averaging \$460 per square foot. On a same store basis, grocery sales decreased a modest 0.9% over the prior year but have increased at a compounded average annual rate of 1.8% over the past 5 years.

Leasing activity within the retail portfolio continues to be strong. Of the approximately 500,000 square feet of retail space scheduled to expire during 2005, over 50% of the leases have already been renewed or extended as of March 23, 2005.

We maintain that tenant diversity is critical to the stability of our retail portfolio cash flow. Only four retail tenants in 2004 paid annual rent in excess of 1.5% of total revenues. Giant Food and Safeway contributed 4.8% and 2.9% of total revenues, respectively. Lowe's Home Improvement and Home Depot, each with two locations, contributed 2.0% and 1.6% of revenues, respectively.

## Office Highlights

The office portfolio is comprised of five properties, totaling approximately 1,200,000 square feet, and contributed 29% of our 2004 property operating income. The 225,000 square foot 601 Pennsylvania Avenue office building, located between the White House and the U.S. Capitol, is the Company's largest asset, as measured by property operating income. This building is 100% leased with long term leases, and none of these leases are due to expire prior to 2008. During 2003 and 2004, we successfully re-leased over 140,000 square feet of office space in the building by replacing an expiring government lease with tenants such as the American Association of Health Plans, the Pharmaceutical Care Association and the National Gallery of Art. The re-leasing of 601 Pennsylvania Avenue contributed substantially to the office portfolio's 11.2% same property operating income increase in 2004. Excluding the impact of 601 Pennsylvania Avenue, the office portfolio's 2004 same property operating income growth was 3.2%.

Only two office tenants, the United States Government at 3.5%, and the American Association of Health Plans at 2.2%, contributed more than 1.5% of 2004 total revenues. Our office buildings were 95.9% leased at year end 2004. Over 90% of the office lease base rents have fixed annual escalations averaging over 2.5% per year. Only 52,000 square feet of leases are scheduled to expire during the balance of 2005.

# MESSAGE

## MESSAGE TO OUR SHAREHOLDERS

### 2004 Acquisitions

Early in 2004, we acquired four shopping centers. We added Publix as one of our grocery tenants with the acquisition of Boca Valley Plaza and Cruse MarketPlace. Boca Valley Plaza is a 121,000 square foot neighborhood shopping center on U.S. Highway 1 in South Florida. The center was 91% leased at year end and is anchored by a 42,000 square foot Publix supermarket. The demographics in the center's market area are very attractive with 1-mile and 3-mile household incomes averaging \$113,000 and \$97,000, respectively and a population of 58,000 within 3 miles. Publix is the dominant grocer in South Florida, with an estimated grocery market share exceeding 40%.



*Briggs Chaney Plaza*



*Broadlands Village*



*Thruway*

The Cruse MarketPlace acquisition in suburban Atlanta has 79,000 square feet of space, including a Publix supermarket. The shopping center was 97% leased at year end. Forsyth County is one of the fastest growing counties in the country and the center's surrounding 1-mile and 3-mile household incomes average \$105,000 and \$100,000, respectively.

We acquired two Safeway anchored shopping centers in our core Washington, DC metropolitan market area. Countryside, our fourth Loudoun County property, is a 95% leased, 142,000 square foot neighborhood shopping center. The center is conveniently located along Route 7 within a planned community of 3,000 homes. No other undeveloped retail zoned land exists within this community.

Briggs Chaney Plaza, a 197,000 square foot Safeway anchored neighborhood center in Silver Spring, Maryland, is well located on the Route 29 corridor of Montgomery County, Maryland. The center is 94% leased. Since the April acquisition of Briggs Chaney Plaza, we completed an interior renovation of 11,000 square feet of previously vacant space. We reconfigured the space into six small shops, five of which are currently leased. We are finalizing plans for a facade renovation of this shopping center, projected to be substantially completed in mid-2005.

### 2004 Developments and Redevelopment

During 2004, we developed and constructed Shops at Monocacy, a Giant anchored 107,000 square foot neighborhood shopping center in Frederick, Maryland. The center was substantially completed and Giant opened for business during October 2004. The property was 84% leased at year end.

Construction of a 30,000 square foot second phase of our Broadlands Village shopping center was completed in November 2004. This phase was 96% leased at year end, and includes Original Steakhouse and Bonefish Grill, both quality restaurants that recently opened.



*Boca Valley Plaza**The Glen**Countryside*

In April 2004, we completed construction of 15,000 square feet of new small shop space at the Thruway shopping center located in Winston-Salem, North Carolina. The new development replaced a former 6,100 square foot single-tenant pad building with a new multi-tenant building. The space is 100% leased to tenants which include Ann Taylor Loft, Jos. A Banks Clothiers, Chico's and Liz Claiborne.

In January 2004, we purchased 3.4 acres of undeveloped land adjacent to our 109,000 square foot Kentlands Square shopping center located in Gaithersburg, Maryland. By April 2004, we commenced construction of a 41,000 square foot retail/office building, comprised of 24,000 square feet of in-line retail space and 17,000 square feet of professional office suites. Construction of the development, named Kentlands Place, was completed in early 2005. As of March 2005, Kentlands Place is 77% leased.

In August 2003, we acquired Olde Forte Village, a Safeway anchored neighborhood shopping center located in Fort Washington, Maryland. Redevelopment of the center commenced when Safeway constructed and opened a 58,000 square foot grocery store in March 2003 after relocating from a smaller store within the center. We are continuing the redevelopment by creating approximately 33,000

square feet of small shop space, which was formerly the Safeway space and some adjoining area. Construction of site improvements and the new space were substantially completed during the first quarter of 2005. A total of 8,000 square feet of the redeveloped space has been leased, and leases are under negotiation for another 10,000 square feet.

We expect the value added by ongoing development and redevelopment projects to fuel a significant part of Saul Centers' growth platform in future years.

## Development Pipeline

We continued to add land to our future development pipeline with the December 2004 acquisition of a 19.3 acre parcel of land in Prince William County, Virginia. The site is zoned for development of a grocery anchored neighborhood shopping center to be known as Ashland Square. We are in the process of finalizing a site plan to submit for County approvals during the second quarter of 2005 and are actively marketing the project to grocers and other retail tenants. In March 2005, we closed on the acquisition of a 7.1 acre land parcel in New Market, Maryland, in a growing area of Frederick County. Also, we have approximately 40 acres adjacent to this parcel under contract, with closing expected later this year.

In February 2005, we commenced construction of a 22,000 square foot expansion to The Glen, a 112,000 square foot Safeway anchored shopping center located in Lake Ridge, Virginia. The Glen is currently 100% leased. The new shop space is 40% pre-leased and construction is scheduled to be completed in September 2005.

We continue to work on three additional development opportunities in the metropolitan Washington, DC area. We have 5.5 acres of undeveloped land remaining at the Broadlands Village shopping center in Loudoun County, and are working to develop a final phase of approximately 30,000 square feet of retail shops and pad space. Approximately three miles away, we have recently received zoning approvals from Loudoun County for a 150,000 square foot neighborhood retail project in the Lansdowne community. We are negotiating a lease with a grocer to anchor the new community shopping center. Our third project is located in the popular Clarendon neighborhood of Arlington, Virginia. We continue to pursue zoning approvals for a significant mixed-use project on land we have assembled adjacent to the Clarendon Metro Station.

## Capital Structure

During the latter half of 1997, we set in place a program to refinance our short-term, variable rate debt with long-term, fixed-rate, non-recourse mortgage debt. As a result of consistently applying the program, we have reduced our exposure to short-term swings in interest rates and market liquidity.

At year end 2004, debt balances totaled \$454 million, 100% of which was long-term, fixed-rate, non-recourse debt. The weighted average interest rate was 7.03% and the weighted average remaining term was 9.9 years. Our debt to total assets ratio (leverage) is currently between 35% and 40%, well within our target maximum of 50%. Earnings before interest, depreciation and amortization (EBITDA) exceeded interest expense for 2004 by 3.1 times (interest expense coverage).

We are prepared to fund future acquisition and development requirements as the opportunities arise by utilizing our credit line. In January 2005, we executed a new \$150 million unsecured revolving credit facility to replace our former line. With no outstanding borrowings on the line, we have capacity to meet our capital requirements for future developments and acquisitions.

Saul Centers has remained focused on executing its long-term strategic plans to grow operating property income within the constraints of a prudent capital structure. We will continue to pursue selected development and acquisition opportunities. While today's real estate investments currently command very low initial yields, we will and must maintain our discipline and allocate our capital to acquisitions only if we firmly believe in the long term viability of a sub-market and our ability to add value to the real estate over the coming years.

For the Board



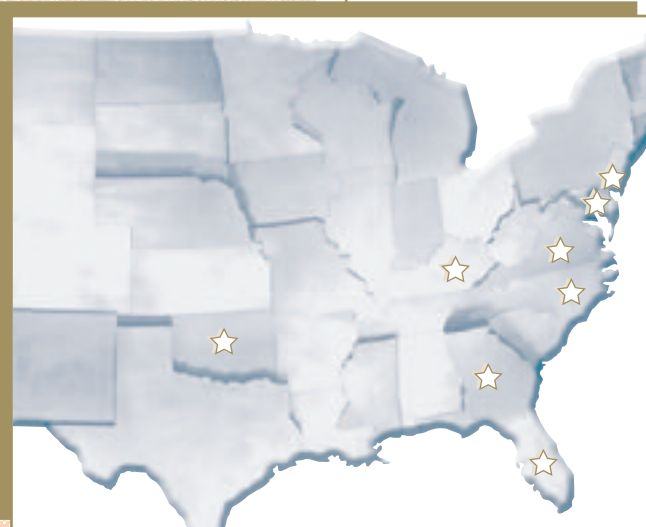
B. Francis Saul II

March 23, 2005



Seven Corners

As of December 31, 2004, Saul Centers' portfolio properties were located in Virginia, Maryland, Washington, DC, North Carolina, Oklahoma, New Jersey, Georgia, Florida and Kentucky. In March 2005, a property in Altamonte Springs, Florida was added to the portfolio. Properties in the metropolitan Washington, DC/Baltimore area represent 70% of the portfolio's gross leasable area.



Property/Location		Gross Leasable Square Feet
<b>Shopping Centers</b>		
Ashburn Village	Ashburn, VA	211,327
Beacon Center	Alexandria, VA	352,915
Belvedere	Baltimore, MD	54,941
Boca Valley Plaza	Boca Raton, FL	121,269
Boulevard	Fairfax, VA	56,350
Briggs Chaney Plaza	Silver Spring, MD	197,486
Broadlands Village	Loudoun County, VA	107,286
Broadlands Village II	Loudoun County, VA	30,193
Clarendon	Arlington, VA	11,808
Countryside	Loudoun County, VA	141,696
Cruse MarketPlace	Forsyth County, GA	78,686
Flagship Center	Rockville, MD	21,500
French Market	Oklahoma City, OK	244,724
Germantown	Germantown, MD	27,241
Giant	Baltimore, MD	70,040
The Glen	Lake Ridge, VA	112,229
Great Eastern	District Heights, MD	254,448
Hampshire Langley	Takoma Park, MD	131,700
Kentlands Square	Gaithersburg, MD	114,381
Leesburg Pike	Baileys Crossroads, VA	97,752
Lexington Mall	Lexington, KY	314,535
Lumberton Plaza	Lumberton, NJ	193,044
Shops at Monocacy	Frederick, MD	107,000

Property/Location		Gross Leasable Square Feet
Olde Forte Village	Ft. Washington, MD	143,062
Olney	Olney, MD	53,765
Ravenwood	Baltimore, MD	85,958
Seven Corners	Falls Church, VA	560,998
Shops at Fairfax	Fairfax, VA	68,743
Southdale	Glen Burnie, MD	484,115
Southside Plaza	Richmond, VA	347,651
South Dekalb Plaza	Atlanta, GA	163,418
Thruway	Winston-Salem, NC	352,355
Village Center	Centreville, VA	143,109
West Park	Oklahoma City, OK	76,610
White Oak	Silver Spring, MD	480,156
<b>Total Shopping Centers</b>		<b>6,012,491</b>

<b>Office Properties</b>		
Avenel Business Park	Gaithersburg, MD	390,479
Crosstown Business Center	Tulsa, OK	197,135
601 Pennsylvania Ave	Washington, DC	226,604
Van Ness Square	Washington, DC	156,493
Washington Square	Alexandria, VA	234,775
<b>Total Office Properties</b>		<b>1,205,486</b>

**Total Portfolio** **7,217,977**  
(as of December 31, 2004)

Additional development parcels include Broadlands Village III, Kentlands Place (41,300 square foot retail/office building under construction), Clarendon Center, Lansdowne, and Ashland Square.





Thruway



Shops at Monocacy



Seven Corners

# MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

## Assessment of Effectiveness of Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Management used the criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control - Integrated Framework to assess the effectiveness of the Company's internal control over financial reporting. Based upon the assessments, the Company's management has concluded that, as of December 31, 2004, the Company's internal control over financial reporting was effective. The Company's independent registered public accounting firm has issued an attestation report on management's assessment of the Company's internal control over financial reporting, which appears on page 14 of this Annual Report.





## REPORT

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING  
FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

Board of Directors and Stockholders  
Saul Centers, Inc.

We have audited management's Assessment of Effectiveness of Internal Control Over Financial Reporting included on page 13 of this Annual Report, that Saul Centers, Inc. maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Saul Centers, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with

generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Saul Centers, Inc. maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, Saul Centers, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Saul Centers, Inc. as of December 31, 2004 and 2003, the related consolidated statements of operations, stockholders' equity (deficit), and cash flows for each of the three years in the period ended December 31, 2004 of Saul Centers, Inc. and our report dated March 10, 2005 expressed an unqualified opinion thereon.

Ernst & Young LLP  
McLean, Virginia  
March 10, 2005



Board of Directors and Stockholders  
Saul Centers, Inc.

We have audited the accompanying consolidated balance sheets of Saul Centers, Inc. as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity (deficit), and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of Saul Centers, Inc. at December 31, 2004 and 2003, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Saul Centers, Inc.'s internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 10, 2005 expressed an unqualified opinion thereon.

Ernst & Young LLP  
McLean, Virginia  
March 10, 2005

# SAUL CENTERS, INC.

## CONSOLIDATED BALANCE SHEETS

December 31,

(In thousands, except per share amounts)

2004

2003

<b>Assets</b>		
Real estate investments		
Land	\$ 119,029	\$ 82,256
Buildings and equipment	521,161	436,371
Construction in progress	42,618	33,488
	682,808	552,115
Accumulated depreciation	(181,420)	(164,823)
	501,388	387,292
Cash and cash equivalents	33,561	45,244
Accounts receivable and accrued income, net	20,654	14,642
Leasing costs, net	17,745	15,344
Prepaid expenses	2,421	2,609
Deferred debt costs, net	5,011	4,224
Other assets	2,616	2,261
Total assets	\$ 583,396	\$ 471,616
<b>Liabilities</b>		
Mortgage notes payable	\$ 453,646	\$ 357,248
Dividends and distributions payable	10,424	9,454
Accounts payable, accrued expenses and other liabilities	12,318	7,793
Deferred income	6,044	4,478
Total liabilities	482,432	378,973
<b>Stockholders' equity</b>		
Series A Cumulative Redeemable Preferred stock, 1,000,000 shares authorized and 40,000 shares issued and outstanding	100,000	100,000
Common stock, par value \$0.01 per share, 30,000,000 shares authorized, 16,399,442 and 15,861,234 shares issued and outstanding, respectively	164	159
Additional paid-in capital	106,886	91,469
Accumulated deficit	(106,086)	(98,985)
Total stockholders' equity	100,964	92,643
Total liabilities and stockholders' equity	\$ 583,396	\$ 471,616

The accompanying notes are an integral part of these statements.

# SAUL CENTERS, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

17

For the Year Ended December 31,

(In thousands, except per share amounts)

2004

2003

2002

### Revenue

Base rent	\$ 91,125	\$ 78,167	\$ 75,699
Expense recoveries	16,712	14,438	12,680
Percentage rent	1,635	1,695	1,850
Other	3,370	3,584	3,734
Total revenue	112,842	97,884	93,963

### Operating expenses

Property operating expenses	12,070	11,363	10,115
Provision for credit losses	488	171	421
Real estate taxes	9,789	8,580	8,021
Interest expense and amortization of deferred debt	27,022	26,573	25,838
Depreciation and amortization	21,324	17,838	17,821
General and administrative	8,442	6,213	5,537
Total operating expenses	79,135	70,738	67,753

### Operating income before minority interests and gain on sale of property

33,707	27,146	26,210
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### Non-operating item

Gain on sale of property	572	182	1,426
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### Income before minority interests

34,279	27,328	27,636
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### Minority interests

Minority share of income	(6,386)	(6,495)	(7,130)
Distributions in excess of earnings	(1,719)	(1,591)	(940)
Total minority interests	(8,105)	(8,086)	(8,070)

### Net income

Preferred dividends	(8,000)	(1,244)	--
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### Net income available to common stockholders

\$ 18,174	\$ 17,998	\$ 19,566
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### Per share net income available to common stockholders

Basic	\$ 1.13	\$ 1.15	\$ 1.32
Diluted	\$ 1.12	\$ 1.15	\$ 1.31

### Distributions declared per common share outstanding

\$ 1.56	\$ 1.56	\$ 1.56
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The accompanying notes are an integral part of these statements.



# SAUL CENTERS, INC.

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)

<i>(In thousands, except per share amounts)</i>	Preferred Stock	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Total
<b>Stockholders' equity (deficit)</b>					
Balance, December 31, 2001	\$ --	\$ 145	\$ 64,564	\$ (88,832)	\$ (24,123)
Issuance of 660,779 shares of common stock:					
556,872 shares - dividend reinvestment plan	--	6	12,469	--	12,475
103,907 shares - employee stock options and directors deferred stock plan	--	1	2,098	--	2,099
Net income	--	--	--	19,566	19,566
Distributions – common stock	--	--	--	(17,360)	(17,360)
Distributions payable common stock (\$0.39 per share)	--	--	--	(5,924)	(5,924)
Balance, December 31, 2002	--	152	79,131	(92,550)	(13,267)
Issuance of 664,651 shares of common stock:					
552,170 shares - dividend reinvestment plan	--	6	13,697	--	13,703
112,481 shares - employee stock options and directors deferred stock plan	--	1	2,314	--	2,315
Issuance of 40,000 shares of preferred stock	100,000	--	(3,673)	--	96,327
Net income	--	--	--	19,242	19,242
Distributions payable preferred stock (\$31.00 per share)	--	--	--	(1,244)	(1,244)
Distributions – common stock	--	--	--	(18,247)	(18,247)
Distributions payable common stock (\$0.39 per share)	--	--	--	(6,186)	(6,186)
Balance, December 31, 2003	100,000	159	91,469	(98,985)	92,643
Issuance of 538,208 shares of common stock:					
497,282 shares - dividend reinvestment plan	--	5	14,077	--	14,082
40,928 shares - employee stock options and directors deferred stock plan	--	--	1,340	--	1,340
Net income	--	--	--	26,174	26,174
Preferred stock distributions	--	--	--	(6,000)	(6,000)
Distributions payable preferred stock (\$50.00 per share)	--	--	--	(2,000)	(2,000)
Distributions – common stock	--	--	--	(18,879)	(18,879)
Distributions payable common stock (\$0.39 per share)	--	--	--	(6,396)	(6,396)
Balance, December 31, 2004	\$ 100,000	\$ 164	\$ 106,886	\$ (106,086)	\$ 100,964

The accompanying notes are an integral part of these statements.

# SAUL CENTERS, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

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(In thousands)	For the Year Ended December 31,		
	2004	2003	2002
<b>Cash flows from operating activities</b>			
Net income	\$ 26,174	\$ 19,242	\$ 19,566
Adjustments to reconcile net income to net cash provided by operating activities:			
Gain on sale of property	(572)	(182)	(1,426)
Minority interests	8,105	8,086	8,070
Depreciation and amortization	21,324	17,838	17,821
Amortization of deferred debt	929	801	725
Provision for credit losses	488	171	421
Increase in accounts receivable and accrued income	(6,500)	(2,308)	(3,709)
Increase in leasing costs	(2,266)	(2,303)	(848)
Decrease (increase) in prepaid expenses	188	(3,250)	(6,458)
(Increase) decrease in other assets	(355)	171	15
Increase (decrease) in accounts payable, accrued expenses and other liabilities	1,630	(897)	1,717
Increase (decrease) in deferred income	1,566	(6)	475
Net cash provided by operating activities	50,711	37,363	36,369
<b>Cash flows from investing activities</b>			
Acquisitions of real estate investments, net*	(79,105)	(26,375)	(29,226)
Additions to real estate investments	(6,425)	(7,709)	(3,382)
Additions to development and redevelopment activities	(29,366)	(15,317)	(8,987)
Proceeds from sale of assets	833	280	1,426
Net cash used in investing activities	(114,063)	(49,121)	(40,169)
<b>Cash flows from financing activities</b>			
Proceeds from mortgage notes payable	94,800	93,134	991
Repayments on mortgage notes payable	(16,427)	(69,879)	(6,624)
Proceeds from revolving credit facility	33,000	35,000	44,750
Repayments on revolving credit facility	(33,000)	(81,750)	(18,000)
Additions to deferred debt expense	(1,716)	(900)	(1,287)
Proceeds from the issuance of preferred stock, net of issuance costs	--	96,327	--
Proceeds from the issuance of common stock and convertible limited partnership units in the Operating Partnership	15,422	16,018	14,574
Distributions to preferred stockholders	(7,244)	--	--
Distributions to common stockholders and holders of convertible limited partnership units in the Operating Partnership	(33,166)	(32,257)	(31,100)
Net cash provided by financing activities	51,669	55,693	3,304
Net (decrease) increase in cash and cash equivalents	(11,683)	43,935	(496)
Cash and cash equivalents, beginning of year	45,244	1,309	1,805
Cash and cash equivalents, end of year	\$ 33,561	\$ 45,244	\$ 1,309
<b>Supplemental disclosures of cash flow information:</b>			
Cash paid for interest	\$ 28,682	\$ 26,878	\$ 25,637

\* Supplemental discussion of non-cash investing and financing activities: The \$79,105,000 shown as 2004 real estate acquisitions does not include \$18,025,000 in total assumed mortgages for 2 of the properties acquired as the assumption of these mortgages was a non-cash acquisition cost. On February 13, 2004, the Company purchased Boca Valley Plaza for an acquisition cost of \$17,678,000 and assumed a mortgage in the amount of \$9,200,000 with the balance being paid in cash. On March 25, 2004, the Company purchased Cruse MarketPlace for an acquisition cost of \$12,897,000 and assumed a mortgage of \$8,825,000 with the balance being paid in cash. For 2002, the \$29,226,000 figure does not include \$7,806,000 in an assumed mortgage of an acquisition cost of \$14,300,000 on September 8, 2002 of the Company's Kentlands Square property with the balance being paid in cash.

The accompanying notes are an integral part of these statements.

## 1. ORGANIZATION, FORMATION, AND BASIS OF PRESENTATION

### Organization

Saul Centers, Inc. ("Saul Centers") was incorporated under the Maryland General Corporation Law on June 10, 1993. Saul Centers operates as a real estate investment trust (a "REIT") under the Internal Revenue Code of 1986, as amended (the "Code"). Saul Centers generally will not be subject to federal income tax, provided it annually distributes at least 90% of its REIT taxable income to its stockholders and meets certain organizational and other requirements. Saul Centers has made and intends to continue to make regular quarterly distributions to its stockholders. Saul Centers, together with its wholly owned subsidiaries and the limited partnerships of which Saul Centers or one of its subsidiaries is the sole general partner, are referred to collectively as the "Company". B. Francis Saul II serves as Chairman of the Board of Directors and Chief Executive Officer of Saul Centers.

### Formation and Structure of Company

Saul Centers was formed to continue and expand the shopping center business previously owned and conducted by the B.F. Saul Real Estate Investment Trust, the B.F. Saul Company, Chevy Chase Bank, F.S.B. and certain other affiliated entities, each of which is controlled by B. Francis Saul II and his family members (collectively, "The Saul Organization"). On August 26, 1993, members of The Saul Organization transferred to Saul Holdings Limited Partnership, a newly formed Maryland limited partnership (the "Operating Partnership"), and two newly formed subsidiary limited partnerships (the "Subsidiary Partnerships", and collectively with the Operating Partnership, the "Partnerships"), shopping center and office properties, and the management functions related to the transferred properties. Since its formation, the Company has developed and purchased additional properties. During 2004 and 2003, the Company developed and purchased several properties. In July 2003, the Company purchased Olde Forte Village, a grocery anchored neighborhood shopping center located in Fort Washington, Maryland. In November 2003, the Company purchased a land parcel located in Frederick, Maryland, upon which it developed a grocery anchored shopping center named Shops at Monocacy, completed during the fourth

quarter of 2004. Also during the fourth quarter of 2003, the Company completed development of Broadlands Village Phase I, an in-line retail and retail pad, grocery anchored shopping center. The Company completed Phase II, a 30,000 square foot addition to the center during the fourth quarter of 2004. During 2004, the Company purchased a land parcel which it is currently developing into a 41,000 square foot retail/office property to be known as Kentlands Place, adjacent to its Kentlands Square shopping center. The Company also purchased a land parcel in Dumfries, Virginia, which it plans to develop into a grocery anchored shopping center to be known as Ashland Square. Also during 2004, the Company acquired four grocery anchored shopping centers; (1) Boca Valley Plaza, 121,000 square feet, located in Boca Raton, Florida, (2) Countryside, 142,000 square feet located in Loudoun County, Virginia (3) Cruse MarketPlace, 79,000 square feet, located in Forsyth County, Georgia, and (4) Briggs Chaney Plaza, 197,000 square feet, located in Silver Spring, Maryland. As of December 31, 2004, the Company's properties (the "Current Portfolio Properties") consisted of 35 shopping center operating properties (the "Shopping Centers"), five predominantly office operating properties (the "Office Properties") and five development and/or redevelopment (non-operating) properties.

The Company established Saul QRS, Inc., a wholly owned subsidiary of Saul Centers, to facilitate the placement of collateralized mortgage debt. Saul QRS, Inc. was created to succeed to the interest of Saul Centers as the sole general partner of Saul Subsidiary I Limited Partnership. The remaining limited partnership interests in Saul Subsidiary I Limited Partnership and Saul Subsidiary II Limited Partnership are held by the Operating Partnership as the sole limited partner. Through this structure, the Company owns 100% of the Current Portfolio Properties.

### Basis of Presentation

The accompanying financial statements of the Company have been presented on the historical cost basis of The Saul Organization because of affiliated ownership and common management and because the assets and liabilities were the subject of a business combination with the Operating Partnership, the Subsidiary Partnerships and Saul Centers, all newly formed entities with no prior operations.



## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Nature of Operations

The Company, which conducts all of its activities through its subsidiaries, the Operating Partnership and Subsidiary Partnerships, engages in the ownership, operation, management, leasing, acquisition, renovation, expansion, development and financing of community and neighborhood shopping centers and office properties, primarily in the Washington, DC/Baltimore metropolitan area. Because the properties are located primarily in the Washington, DC/Baltimore metropolitan area, the Company is subject to a concentration of credit risk related to these properties. A majority of the Shopping Centers are anchored by several major tenants. Twenty-four of the Shopping Centers are anchored by a grocery store and offer primarily day-to-day necessities and services. As of December 31, 2004, no single property accounted for more than 7.8% of the total gross leasable area. Only two retail tenants, Giant Food (4.8%), a tenant at nine Shopping Centers and Safeway (2.9%), a tenant at six Shopping Centers and one office tenant, the United States Government (3.5%), a tenant at five properties, individually accounted for more than 2.5% of the Company's total revenues for the year ended December 31, 2004.

### Principles of Consolidation

The accompanying consolidated financial statements of the Company include the accounts of Saul Centers, its subsidiaries, and the Operating Partnership and Subsidiary Partnerships which are majority owned by Saul Centers. All significant intercompany balances and transactions have been eliminated in consolidation.

### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### Real Estate Investment Properties

The Company purchases real estate investment properties from time to time and allocates the purchase price to various components, such as land, buildings, and intangibles related to in-place leases and customer relationships in accordance with Financial Accounting Standards Board ("FASB") Statement of Financial

Accounting Standards ("SFAS") 141, "Business Combinations." The purchase price is allocated based on the relative fair value of each component. The fair value of buildings is determined as if the buildings were vacant upon acquisition and subsequently leased at market rental rates. As such, the determination of fair value considers the present value of all cash flows expected to be generated from the property including an initial lease up period. The Company determines the fair value of above and below market intangibles associated with in-place leases by assessing the net effective rent and remaining term of the lease relative to market terms for similar leases at acquisition. In the case of below market leases, the Company considers the remaining contractual lease period and renewal periods, taking into consideration the likelihood of the tenant exercising its renewal options. The fair value of a below market lease component is recorded as deferred income and amortized as additional lease revenue over the remaining contractual lease period and any renewal option periods included in the valuation analysis. The fair value of above market lease intangibles is recorded as a deferred asset and is amortized as a reduction of lease revenue over the remaining contractual lease term. The Company determines the fair value of at-market in-place leases considering the cost of acquiring similar leases, the foregone rents associated with the lease-up period and carrying costs associated with the lease-up period. Intangible assets associated with at-market in-place leases are amortized as additional lease expense over the remaining contractual lease term. To the extent customer relationship intangibles are present in an acquisition, the fair value of the intangibles are amortized over the life of the customer relationship.

Real estate investment properties are reviewed for potential impairment losses quarterly or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If there is an event or change in circumstance indicating the potential for an impairment in the value of a real estate investment property, the Company's policy is to assess potential impairment in value by making a comparison of the current and projected operating cash flows of the property over its remaining useful life, on an undiscounted basis, to the carrying amount of that property. If such carrying amount is in excess of the estimated projected operating cash flows of the property, the Company would recognize an impairment loss equivalent to an amount required to adjust the carrying amount to its estimated fair market value. The Company has not recognized an impairment loss in 2004, 2003 or 2002 on any of its real estate.

Interest, real estate taxes and other carrying costs are capitalized on projects under development and construction. Once construction is substantially completed and the assets are placed in service, their rental income, real estate tax expense, property operating expenses (consisting of payroll, repairs and maintenance, utilities, insurance and other property related expenses) and depreciation are included in current operations. Property operating expenses are charged to operations as incurred. Repairs and maintenance expense totaled \$4,927,000, \$4,943,000 and \$3,852,000, for 2004, 2003 and 2002, respectively, and is included in operating expenses in the accompanying consolidated financial statements. Interest expense capitalized totaled \$3,227,000, \$1,382,000 and \$548,000, for 2004, 2003 and 2002, respectively.

In the initial rental operations of development projects, a project is considered substantially complete and available for occupancy upon completion of tenant improvements, but no later than one year from the cessation of major construction activity. Substantially completed portions of a project are accounted for as separate projects. Depreciation is calculated using the straight-line method and estimated useful lives of 35 to 50 years for base buildings and up to 20 years for certain other improvements. Depreciation expense for the years ended December 31, 2004, 2003 and 2002 was \$17,061,000, \$14,649,000 and \$15,526,000, respectively. Leasehold improvements are amortized, over the shorter of the lives of the related leases or the useful life of the improvement, using the straight-line method.

#### Lease Acquisition Costs

Certain initial direct costs incurred by the Company in negotiating and consummating a successful lease are capitalized and amortized over the initial base term of the lease. These costs total \$17,745,000 and \$15,344,000, net of accumulated amortization of \$9,461,000 and \$6,671,000, as of December 31, 2004 and 2003, respectively. Amortization expense, included in depreciation and amortization in the consolidated statements of operations, totaled \$4,263,000, \$3,189,000 and \$2,295,000, for the years ended December 31, 2004, 2003 and 2002, respectively. Capitalized leasing costs consist of commissions paid to third party leasing agents as well as internal direct costs such as employee compensation and payroll related fringe benefits directly related to time spent performing leasing related activities. Such activities include evaluating the prospective tenant's financial

condition, evaluating and recording guarantees, collateral and other security arrangements, negotiating lease terms, preparing lease documents and closing the transaction. The carrying amount of costs are written-off to expense if the applicable lease is terminated prior to expiration of the initial lease term.

#### Construction in Progress

Construction in progress includes preconstruction costs and development costs of active projects. Preconstruction costs associated with these active projects include legal, zoning and permitting costs and other project carrying costs incurred prior to the commencement of construction. Development costs include direct construction costs and indirect costs incurred subsequent to the start of construction such as architectural, engineering, construction management and carrying costs consisting of interest, real estate taxes and insurance. Construction in progress balances as of December 31, 2004 and 2003 are as follows:

<b>Construction in Progress</b>		
<i>(In thousands)</i>	December 31,	
	2004	2003
Clarendon Center	\$ 14,976	\$ 13,209
Shops at Monocacy	--	9,818
Broadlands Village II	--	1,151
Broadlands Village III	1,660	1,527
Lansdowne Town Square	6,872	6,138
Ashland Square	6,411	--
Kentlands Place	5,905	--
Olde Forte Village	4,755	116
Briggs Chaney Plaza	660	--
Other	1,379	1,529
<b>Total</b>	<b>\$ 42,618</b>	<b>\$ 33,488</b>

#### Accounts Receivable and Accrued Income

Accounts receivable primarily represent amounts currently due from tenants in accordance with the terms of the respective leases. Receivables are reviewed monthly and reserves are established with a charge to current period operations when, in the opinion of management, collection of the receivable is doubtful. Accounts receivable in the accompanying consolidated financial statements are shown net of an allowance for doubtful accounts of \$1,125,000 and \$881,000, at December 31, 2004 and 2003, respectively.

**Allowance for Doubtful Accounts**

(In thousands)	For the Year Ended December 31,	
	2004	2003
Beginning Balance	\$ 881	\$ 1,001
Provision for Credit Losses	488	171
Charge-offs	(244)	(291)
Ending Balance	\$ 1,125	\$ 881

In addition to rents due currently, accounts receivable include \$12,101,000 and \$9,370,000, at December 31, 2004 and 2003, respectively, representing minimum rental income accrued on a straight-line basis to be paid by tenants over the remaining term of their respective leases. These amounts are presented after netting allowances of \$237,000 and \$548,000, respectively, for tenants whose rent payment history or financial condition cast doubt upon the tenant's ability to perform under its lease obligations.

**Cash and Cash Equivalents**

Cash and cash equivalents include short-term investments. Short-term investments are highly liquid investments that are both readily convertible to cash and so near their maturity that they present insignificant risk of changes in value arising from interest rate fluctuations. Short-term investments include money market accounts and other investments which generally mature within three months, measured from the acquisition date.

**Deferred Debt Costs**

Deferred debt costs consist of fees and costs incurred to obtain long-term financing, construction financing and the revolving line of credit. These fees and costs are being amortized over the terms of the respective loans or agreements, which approximates the effective interest method. Deferred debt costs totaled \$5,011,000 and \$4,224,000, net of accumulated amortization of \$4,229,000 and \$3,300,000, at December 31, 2004 and 2003, respectively.

**Deferred Income**

Deferred income consists of payments received from tenants prior to the time they are earned and recognized by the Company as revenue. These payments include prepayment of the following month's rent, prepayment of real estate taxes when the taxing jurisdiction has a fiscal year differing from the calendar year reimbursements specified in the lease agreement and advance payments by tenants for tenant construction work provided by the Company.

**Revenue Recognition**

Rental and interest income is accrued as earned except when doubt exists as to collectibility, in which case the accrual is discontinued. When rental payments due under leases vary from a straight-line basis because of free rent periods or stepped increases, income is recognized on a straight-line basis in accordance with accounting principles generally accepted in the United States. Expense recoveries represent a portion of property operating expenses billed to the tenants, including common area maintenance, real estate taxes and other recoverable costs. Expense recoveries are recognized in the period when the expenses are incurred. Rental income based on a tenant's revenues ("percentage rent") is accrued when a tenant reports sales that exceed a specified breakpoint.

**Income Taxes**

The Company made an election to be treated, and intends to continue operating so as to qualify as a REIT under sections 856 through 860 of the Internal Revenue Code of 1986, as amended, commencing with its taxable year ending December 31, 1993. A REIT generally will not be subject to federal income taxation on that portion of its income that qualifies as REIT taxable income to the extent that it distributes at least 90% of its REIT taxable income to stockholders and complies with certain other requirements. Therefore, no provision has been made for federal income taxes in the accompanying consolidated financial statements.

**Stock Based Employee Compensation, Deferred Compensation and Stock Plan for Directors**

Effective January 2003, the Company adopted the fair value method to value and account for employee stock options using the prospective transition method specified under SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure." The Company had no options eligible for valuation prior to the grant of options in 2003 and 2004. The fair value of the 2003 and 2004 options was determined at the time of each award using the Black-Scholes model, a widely used method for valuing stock based employee compensation, and the following assumptions: (1) Expected Volatility. Because Saul Centers common stock is thinly traded, with average daily trading volume averaging less than 50,000 shares (since the Company's inception), expected volatility is determined using the entire trading history of the Company's common stock (month-end closing prices since its inception), (2) Average Expected Term.



The options are assumed to be outstanding for a term calculated as the period of time from grant until the midpoint between the full vesting date and expiration date, (3) Expected Dividend Yield. This rate is a value management determines after considering the Company's current and historic dividend yield rates, the Company's yield in relation to other retail REITs and the Company's market yield at the grant date, and (4) Risk-free Interest Rate. This rate is based upon the market yields of US Treasury obligations with maturities corresponding to the average expected term of the options at the grant date. The Company recognizes the value of options granted, ratably over the vesting period, as compensation expense included in general and administrative expenses.

The Company established a stock option plan in 1993 (the "1993 Plan") for the purpose of attracting and retaining executive officers and other key personnel. The 1993 Plan provides for grants of options to purchase a specified number of shares of common stock. A total of 400,000 shares were made available under the 1993 Plan. The 1993 Plan authorizes the Compensation Committee of the Board of Directors to grant options at an exercise price which may not be less than the market value of the common stock on the date the option is granted. On May 23, 2003, the Compensation Committee granted options to purchase a total of 220,000 shares (80,000 shares from incentive stock options and 140,000 shares from nonqualified stock options) to six Company officers (the "2003 Options"). Following the grant of the 2003 Options, no shares were available for issuance under the 1993 Plan. The 2003 Options vest 25% per year over four years and have a term of ten years, subject to earlier expiration upon termination of employment.

At the annual meeting of the Company's stockholders in 2004, the stockholders approved the adoption of the 2004 stock plan (the "2004 Plan") for the purpose of attracting and retaining executive officers, directors and other key personnel. The 2004 Plan provides for grants of options to purchase up to 500,000 shares of common stock as well as grants of up to 100,000 shares of common stock to directors. The 2004 Plan authorizes the Compensation Committee of the Board of Directors to grant options at an exercise price which may not be less than the market value of the common stock on the date the option is granted.

Effective April 26, 2004, the Compensation Committee granted options to purchase a total of 152,500 shares (27,500 shares of incentive stock options and 125,000 shares of nonqualified stock options) to eleven

Company officers (122,500 options) and to the twelve Company directors (30,000 options), (combined, the "2004 Options"). The officers' 2004 Options vest 25% per year over four years and have a term of ten years, subject to earlier expiration upon termination of employment. The directors' options are exercisable immediately. (See Note 10. Stock Option Plan)

Pursuant to the 2004 Plan, the Compensation Committee established a Deferred Compensation Plan for Directors (the "Plan") for the benefit of its directors and their beneficiaries. The Plan replaces the Company's previous Deferred Compensation and Stock Plan for Directors. A director may elect to defer all or part of his or her director's fees and has the option to have the fees paid in cash, in shares of common stock or in a combination of cash and shares of common stock upon termination from the Board. If the director elects to have fees paid in stock, fees earned during a calendar quarter are aggregated and divided by the market price of the common stock on the quarter's last trading day to determine the number of shares to be allocated to the director. As of December 31, 2004, 168,000 shares had been credited to the directors' deferred fee accounts.

The Compensation Committee has also approved an annual award of shares of the Company's common stock as additional compensation to each director serving on the Board of Directors as of the record date for the Annual Meeting of Stockholders. The shares are awarded as of each Annual Meeting of Shareholders, and their issuance may not be deferred. Each director was issued 200, 100 and 100 shares, for the years ended December 31, 2004, 2003 and 2002, respectively. The shares were valued at the closing stock price on the dates the shares were awarded and included in general and administrative expenses in the total amounts of \$71,000, \$29,000 and \$25,000, for the years ended December 31, 2004, 2003 and 2002, respectively.

### Minority Interests

Saul Centers, Inc. is the sole general partner of the Operating Partnership, owning a 75.9% interest as of December 31, 2004. Minority interests in the Operating Partnership are comprised of limited partnership units owned by The Saul Organization. Minority interests are increased for earnings allocated to limited partnership units and decreased for distributions. Amounts distributed in excess of the limited partners' share of earnings also increase minority interests, are expensed in the respective period and are classified in the income statement as distributions in excess of earnings.

**Per Share Data**

Per share data is calculated in accordance with SFAS No. 128, "Earnings Per Share." Per share data for net income (basic and diluted) is computed using weighted average shares of common stock. Convertible limited partnership units and employee stock options are the Company's potentially dilutive securities. For all periods presented, the convertible limited partnership units are anti-dilutive. For the years ended December 31, 2004, 2003 and 2002 the options are dilutive because the average share price of the Company's common stock exceeded the exercise prices. The treasury share method was used to measure the effect of the dilution.

<b>Basic and Diluted Shares Outstanding</b>			
<i>(In thousands, except per share amounts)</i>	<b>December 31,</b>		
	<b>2004</b>	<b>2003</b>	<b>2002</b>
Weighted average common shares outstanding – Basic	16,154	15,591	14,865
Effect of dilutive options	57	17	22
Weighted average common shares outstanding – Diluted	16,211	15,608	14,887
Average Share Price	\$ 30.66	\$ 25.77	\$ 22.90

**Reclassifications**

Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation. The reclassifications have no impact on operating results previously reported.

**Recent Accounting Pronouncements**

In December 2004, the FASB issued FAS No. 123 (revised 2004), "Share-Based Payment" ("FAS No. 123R"), which is a revision of FAS No. 123, "Accounting for Stock-Based Compensation." FAS No. 123R supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees," and amends FAS No. 95, "Statement of Cash Flows." FAS No. 123R requires all share-based payments to employees, including grants of employee stock options, to be recorded as an expense based on their fair values. The grant-date fair value of employee share options and similar instruments will be estimated using an option-pricing model adjusted for any unique characteristics of a particular instrument. If an equity award is modified after

the grant date, incremental compensation cost will be recognized in an amount equal to the excess of the fair value of the modified award over the fair value of the original award immediately before the modification. The Company already values stock option awards using the fair value method and expenses the option value over the vesting period of the options. We believe the adoption of FAS No. 123R will not have a material impact upon the Company's financial statements.

**3. REAL ESTATE ACQUIRED****Boca Valley Plaza**

On February 13, 2004, the Company acquired Boca Valley Plaza in Boca Raton, Florida. Boca Valley Plaza is a 121,000 square foot neighborhood shopping center on U.S. Highway 1 in South Florida. The center, constructed in 1988, is 91% leased and anchored by a 42,000 square foot Publix supermarket. The property was acquired for a purchase price of \$17.5 million, subject to the assumption of a \$9.2 million mortgage (See Note 5. Mortgage Notes Payable). The mortgage assumption was treated as a non-cash acquisition in the Statement of Cash Flows.

**Countryside**

On February 17, 2004, the Company completed the acquisition of the 142,000 square foot Safeway anchored Countryside shopping center, its fourth neighborhood shopping center investment in Loudoun County, Virginia. The center is 95% leased and was acquired for a purchase price of \$29.7 million.

**Cruse MarketPlace**

On March 25, 2004, the Company completed the acquisition of the 79,000 square foot Publix anchored, Cruse MarketPlace located in Forsyth County, Georgia. Cruse MarketPlace was constructed in 2002 and is 97% leased. The center was purchased for \$12.6 million subject to the assumption of an \$8.8 million mortgage (See Note 5. Mortgage Notes Payable). The mortgage assumption was treated as a non-cash acquisition in the Statement of Cash Flows.

**Briggs Chaney Plaza**

On April 23, 2004, the Company completed the acquisition of the 197,000 square foot Safeway anchored Briggs Chaney Plaza shopping center located in Silver Spring, Maryland. The center is 94% leased and was acquired for a purchase price of \$27.3 million.

**Ashland Square**

On December 15, 2004, the Company acquired a 19.3 acre parcel of land in Dumfries, Prince William County, Virginia for a purchase price of \$6.3 million. The Company has preliminary plans to develop the parcel into a grocery anchored neighborhood shopping center.

The Company accounted for the acquisition of the operating properties, Boca Valley Plaza, Countryside, Cruse MarketPlace and Briggs Chaney, using the purchase method of accounting in accordance with SFAS No. 141, "Business Combinations." The Company allocates the purchase price to various components, such as land, buildings and intangibles related to in-place leases and customer relationships, if applicable, as described in Note 2. Significant Accounting Policies-Real Estate Investment Properties. Of the combined \$89,299,000 total cost of the acquisitions in 2004 and \$26,375,000 in 2003, of which both amounts include the properties' purchase price and closing costs, a total of \$4,403,000 and \$901,000, was allocated as lease intangible assets and included in lease acquisition costs at December 31, 2004 and December 31, 2003, respectively. Each year's lease intangible assets are being amortized over the remaining periods of the leases acquired, a weighted average term of 9 and 17 years, respectively. For the 2004 and 2003 acquisitions, the value of below market leases totaled \$1,094,000 and \$65,000, respectively, are being amortized over a weighted average term of 14 and 3 years, respectively, and are included in deferred income. The value of above market leases totaled \$497,000 and \$41,000, are being amortized over a weighted average term of 5 and 6 years, for 2004 and 2003, respectively, and are included as a deferred asset in accounts receivable.

As of December 31, 2004 and 2003, the gross carrying amount of lease intangible assets included in lease acquisition costs was \$5,598,000 and \$1,196,000, respectively, and accumulated amortization was \$1,584,000 and \$128,000 respectively. Total amortization of these assets was \$1,456,000 and \$128,000, for the years ended December 31, 2004 and 2003, respectively. As of December 31, 2004 and 2003, the gross carrying amount of below market lease intangible assets included in deferred income was \$1,159,000 and \$65,000, respectively, and accumulated amortization was \$148,000 and \$12,000 respectively. Total amortization of these assets was \$136,000 and \$12,000, for the years ended December 31, 2004 and 2003, respectively. As of December 31, 2004 and 2003, the gross carrying amount of above

market lease intangible assets included in accounts receivable was \$538,000 and \$41,000, respectively, and accumulated amortization was \$142,000 and 5,000 respectively. Total amortization of these assets was \$137,000 and \$5,000, for the years ended December 31, 2004 and 2003, respectively.

<b>Amortization of Intangible Assets Related to In-place Leases</b>				
<i>(In thousands)</i>	<b>Lease acquisition costs</b>	<b>Above market leases</b>	<b>Below market leases</b>	<b>Total</b>
2005	\$ (1,134)	\$ (139)	\$ 155	\$(1,118)
2006	(870)	(92)	123	(839)
2007	(609)	(66)	92	(583)
2008	(397)	(54)	74	(377)
2009	(227)	(27)	68	(186)
Thereafter	(777)	(18)	499	(296)
<b>Total</b>	<b>\$ (4,014)</b>	<b>\$ (396)</b>	<b>\$1,011</b>	<b>\$(3,399)</b>

The results of operations of the acquired properties are included in the consolidated statements of operations as of the acquisition date. The following unaudited pro-forma combined condensed statements of operations set forth the consolidated results of operations for the years ended December 31, 2004 and 2003, respectively, as if the above described operating property acquisitions had occurred on January 1, 2004 and 2003, respectively. The unaudited pro-forma information does not purport to be indicative of the results that actually would have occurred if the combinations had been in effect for the years ended December 31, 2004 and 2003, respectively.

<b>Pro-Forma Consolidated Condensed Statements of Operations</b>		
<i>(In thousands, except per share amounts, unaudited)</i>		
	<b>Year ended December 31,</b>	
	<b>2004</b>	<b>2003</b>
Total revenue	\$ 114,540	\$ 106,304
Net income available to common shareholders	\$ 18,325	\$ 18,947
Net income per common share – basic	\$ 1.13	\$ 1.22
Net income per common share – diluted	\$ 1.13	\$ 1.21



#### 4. MINORITY INTERESTS - HOLDERS OF CONVERTIBLE LIMITED PARTNERSHIP UNITS IN THE OPERATING PARTNERSHIP

The Saul Organization has a 24.1% limited partnership interest, represented by 5,199,000 convertible limited partnership units, in the Operating Partnership, as of December 31, 2004. These convertible limited partnership units are convertible into shares of Saul Centers' common stock, at the option of the unitholders, on a one-for-one basis, provided the rights may not be exercised at any time that The Saul Organization beneficially owns, directly or indirectly, in the aggregate more than 24.9% of the outstanding equity securities of Saul Centers. The limited partnership units were not convertible as of December 31, 2004 because The Saul Organization owned in excess of 24.9% of the Company's equity securities. The impact of The Saul Organization's 24.1% limited partnership interest in the Operating Partnership is reflected as minority interests in the accompanying consolidated financial statements. Fully converted partnership units and diluted weighted average shares outstanding for the years ended December 31, 2004, 2003 and 2002, were 21,405,000, 20,790,000 and 20,059,000, respectively.

#### 5. MORTGAGE NOTES PAYABLE, REVOLVING CREDIT FACILITY, INTEREST EXPENSE AND AMORTIZATION OF DEFERRED DEBT COSTS

Notes payable totaled \$453,646,000 at December 31, 2004, all of which was fixed rate debt. At the prior year's end, notes payable totaled \$357,248,000, all of which was fixed rate debt. At December 31, 2004, the Company had a \$125 million unsecured revolving credit facility with no outstanding borrowings. The facility was due to mature August 2005 and required monthly interest payments, if applicable, at a rate of LIBOR plus a spread of 1.625% to 1.875% (determined by certain debt service coverage and leverage tests) or upon the bank's reference rate at the Company's option. On January 28, 2005, the Company replaced the line with a new three year, \$150 million unsecured revolving credit facility. (See Note 17. Subsequent Events.) Loan availability is determined by operating income from the Company's unencumbered properties, which, as

of December 31, 2004 supported line availability of \$80,000,000, of which \$2,100,000 had been issued under a letter of credit, leaving \$77,900,000 available for working capital uses. An additional \$45,000,000 was available for funding working capital and operating property acquisitions supported by the unencumbered properties' internal cash flow growth and operating income of future acquisitions.

Saul Centers has guaranteed portions of two mortgage notes payable totaling \$7,464,000, the amount of which are considered recourse obligations to Saul Centers as of December 31, 2004. The guarantees are expected to be released upon the completion of improvements and achievement of specified leasing thresholds at these recently developed and acquired properties. Saul Centers is also a guarantor of the revolving credit facility. The operating partnership issued a letter of credit from the revolving credit facility in the amount of \$2,100,000 related to a non-recourse mortgage note to ensure completion of construction at the recently developed Shops at Monocacy. The balance of the mortgage notes payable totaling \$446,182,000 are non-recourse.

During 2004, the Company completed new financings and refinanced several existing mortgage loans to take advantage of favorable financing terms available to the Company. In addition, the Company assumed two mortgages securing real estate properties acquired by the Company during 2004. In February, the Company refinanced Kentlands Square with a new \$10.2 million fixed-rate 15 year mortgage and assumed a \$9.2 million mortgage with the acquisition of Boca Valley Plaza. In March, the Company assumed an \$8.8 million mortgage with the acquisition of Cruse MarketPlace. In April 2004, the Company obtained a new \$15.5 million fixed-rate 15 year mortgage secured by Olde Forte Village, acquired in July 2003. In July 2004, the Company obtained a new \$21.35 million fixed-rate 15 year mortgage secured by Countryside, acquired in February 2004. In August 2004, the Company obtained a new \$21 million fixed-rate 15 year mortgage secured by Briggs Chaney Plaza, acquired in April 2004. In December 2004, the Company obtained a new \$18.75 million fixed-rate 15 year mortgage secured by Shops at Monocacy, a development placed in service during the fourth quarter of 2004. Also in December 2004, the Company obtained a new \$8 million fixed-rate 14 year mortgage secured by Broadlands Village and Broadlands Village II, a development placed in service during the fourth quarter of 2004.

The following is a summary of notes payable as of December 31, 2004 and 2003

**Notes Payable**

(Dollars in thousands)

	December 31,		Interest	Scheduled
	2004	2003	Rate *	Maturity *
Fixed Rate Mortgages:	\$ 129,883 (a)	\$ 132,859	7.67 %	Oct 2012
	94,794 (b)	98,103	8.00 %	Dec 2011
	47,375 (c)	29,800	5.88 %	Jan 2019
	41,324 (d)	41,982	6.01 %	Feb 2018
	33,138 (e)	34,017	7.88 %	Jan 2013
	21,185 (f)	--	5.62 %	Jul 2019
	20,906 (g)	--	5.79 %	Sep 2019
	18,750 (h)	--	5.22 %	Jan 2020
	15,335 (i)	--	5.76 %	May 2019
	13,057 (j)	13,375	8.33 %	Jun 2015
	9,200 (k)	--	6.82 %	Apr 2007
	8,699 (l)	--	5.77 %	Jul 2013
	-- (m)	7,112		
Total Fixed Rate	453,646	357,248	7.03%	9.9 Years
Variable Rate Loan:				
Line of Credit	-- (n)	--	LIBOR plus 1.625%	Aug 2005
Total Variable Rate	--	--	--	--
Total Notes Payable	\$ 453,646	\$ 357,248	7.03 %	9.9 Years

\*Interest rate and scheduled maturity data presented as of December 31, 2004.

Totals computed using weighted averages.

- (a) The loan is collateralized by nine shopping centers (Seven Corners, Thruway, White Oak, Hampshire Langley, Great Eastern, Southside Plaza, Belvedere, Giant and Ravenwood) and requires equal monthly principal and interest payments of \$1,103,000 based upon a 25 year amortization schedule and a balloon payment of \$96,784,000 at loan maturity. Principal of \$2,976,000 was amortized during 2004.
- (b) The loan is collateralized by Avenel Business Park, Van Ness Square, Ashburn Village, Leesburg Pike, Lumberton Plaza and Village Center. The loan has been increased on four occasions since its inception in 1997. The 8.00% blended interest rate is the weighted average of the initial loan rate and additional borrowing rates. The loan requires equal monthly principal and interest payments of \$920,000 based upon a weighted average 23 year amortization schedule and a balloon payment of \$63,153,000 at loan maturity. Principal of \$3,309,000 was amortized during 2004.
- (c) The loan, consisting of two notes dated December 2003 and two notes dated February and December 2004, is currently collateralized by four shopping centers, Broadlands Village (Phases I & II), The Glen and Kentlands Square, and requires equal monthly principal and interest payments of \$306,000 (beginning February 1, 2005; prior to that date, payments totaled \$256,000 per month) based upon a 25 year amortization schedule and a balloon payment of \$28,255,000 at loan maturity. Principal of \$625,000 was amortized during 2004.
- (d) The loan is collateralized by Washington Square and requires equal monthly principal and interest payments of \$264,000 based upon a 27.5 year amortization schedule and a balloon payment of \$27,872,000 at loan maturity. Principal of \$658,000 was amortized during 2004.
- (e) The loan is collateralized by 601 Pennsylvania Avenue and requires equal monthly principal and interest payments of \$294,000 based upon a 25 year amortization schedule and a balloon payment of \$22,808,000 at loan maturity. Principal of \$879,000 was amortized during 2004.

- (f) The loan is collateralized by Countryside and requires equal monthly principal and interest payments of \$133,000 based upon a 25 year amortization schedule and a balloon payment of \$12,231,000 at loan maturity. Principal of \$165,000 was amortized during 2004.
- (g) The loan is collateralized by Briggs Chaney Plaza and requires equal monthly principal and interest payments of \$133,000 based upon a 25 year amortization schedule and a balloon payment of \$12,134,000 at loan maturity. Principal of \$94,000 was amortized during 2004.
- (h) The loan is collateralized by Shops at Monocacy and requires equal monthly principal and interest payments of \$112,000 based upon a 25 year amortization schedule and a balloon payment of \$10,522,000 at loan maturity. Payments commenced February 2005.
- (i) The loan is collateralized by Olde Forte Village and requires equal monthly principal and interest payments of \$98,000 based upon a 25 year amortization schedule and a balloon payment of \$8,942,000 at loan maturity. Principal of \$165,000 was amortized during 2004.
- (j) The loan is collateralized by Shops at Fairfax and Boulevard shopping centers and requires monthly principal and interest payments of \$118,000 based upon a 22 year amortization schedule and a balloon payment of \$7,577,000 at loan maturity. Principal of \$318,000 was amortized during 2004.
- (k) The loan is collateralized by Boca Valley Plaza and requires monthly interest only payments of \$52,000. A balloon payment of \$9,200,000 is due at loan maturity.
- (l) The loan is collateralized by Cruse MarketPlace and requires equal monthly principal and interest payments of \$56,000 based upon an amortization schedule of approximately 24 years and a balloon payment of \$6,797,000 at loan maturity. Principal of \$126,000 was amortized during 2004.
- (m) The \$7,112,000 loan was collateralized by Kentlands Square and was repaid and retired at maturity in February 2004 using proceeds provided by a \$10,200,000 increase to the loan described in (c) above.
- (n) The loan is an unsecured revolving credit facility totaling \$125,000,000. Loan availability for working capital and general corporate uses is determined by operating income from the Company's unencumbered properties, with a portion available only for funding qualified operating property acquisitions. Interest expense is calculated based upon the 1,2,3 or 6 month LIBOR rate plus a spread of 1.625% to 1.875% (determined by certain debt service coverage and leverage tests) or upon the bank's reference rate at the Company's option. The line may be extended one year with payment of a fee of 1/4% at the Company's option. There were no outstanding borrowings as of December 31, 2004. Monthly payments, if applicable, are interest only and will vary depending upon the amount outstanding and the applicable interest rate for any given month. On January 28, 2005, the Company executed a new \$150,000,000 unsecured revolving credit facility to replace the \$125,000,000 line. The new line has a three year term and provides for an additional one year extension at the Company's option, subject to the Company's satisfaction of certain conditions. (see Note 17. Subsequent Events).

The December 31, 2004 and 2003 depreciation adjusted cost of properties collateralizing the mortgage notes payable totaled \$420,320,000 and \$295,506,000, respectively. The Company's credit facility requires the Company and its subsidiaries to maintain certain financial covenants. As of December 31, 2004, the material covenants required the Company, on a consolidated basis, to:

- limit the amount of debt so as to maintain a gross asset value in excess of liabilities of at least \$250 million;
- limit the amount of debt as a percentage of gross asset value (leverage ratio) to less than 60%;
- limit the amount of debt so that interest coverage will exceed 2.1 to 1 on a trailing four quarter basis; and
- limit the amount of debt so that interest, scheduled principal amortization and preferred dividend coverage exceeds 1.6 to 1.

As of December 31, 2004, the Company was in compliance with all such covenants.

Notes payable at December 31, 2004 and 2003, totaling \$163,022,000 and \$166,876,000, respectively, are guaranteed by members of The Saul Organization. As of December 31, 2004, the scheduled maturities of all debt including scheduled principal amortization for years ended December 31, are as follows:

Debt Maturity Schedule		
<i>(In thousands)</i>		
2005	\$	11,349
2006		12,259
2007		22,394
2008		14,176
2009		15,290
Thereafter		378,178
Total	\$	453,646



### Interest Expense and Amortization of Deferred Debt Costs

(In thousands)	Year ended December 31,		
	2004	2003	2002
Interest incurred		\$ 27,154	\$ 25,661
Amortization of deferred debt costs		801	725
Capitalized interest		(1,382)	(548)
Total		\$ 26,573	\$ 25,838

## 6. LEASE AGREEMENTS

Lease income includes primarily base rent arising from noncancelable commercial leases. Base rent (including straight-lined rent) for the years ended December 31, 2004, 2003 and 2002, amounted to \$91,125,000, \$78,167,000 and \$75,699,000, respectively. Future contractual payments under noncancelable leases for years ended December 31, are as follows:

### Base Rent Future Contractual Payments

(In thousands)		
2005	\$	92,181
2006		85,272
2007		77,803
2008		67,674
2009		56,309
Thereafter		290,213
Total	\$	669,452

The majority of the leases also provide for rental increases and expense recoveries based on fixed annual increases or increases in the Consumer Price Index and increases in operating expenses. The expense recoveries generally are payable in equal installments throughout the year based on estimates, with adjustments made in the succeeding year. Expense recoveries for the years ended December 31, 2004, 2003 and 2002 amounted to \$16,712,000, \$14,438,000 and \$12,680,000, respectively. In addition, certain retail leases provide for percentage rent based on sales in excess of the minimum specified in the tenant's lease. Percentage rent amounted to \$1,635,000, \$1,695,000 and \$1,850,000, for the years ended December 31, 2004, 2003 and 2002, respectively.

## 7. LONG-TERM LEASE OBLIGATIONS

Certain properties are subject to noncancelable long-term leases which apply to land underlying the Shopping Centers. Certain of the leases provide for periodic adjustments of the base annual rent and require the payment of real estate taxes on the underlying land. The leases will expire between 2058 and 2068. Reflected in the accompanying consolidated financial statements is minimum ground rent expense of \$164,000 for each of the years ended December 31, 2004, 2003 and 2002, respectively. The future minimum rental commitments under these ground leases are as follows:

### Ground Lease Rental Commitments

(In thousands)	Annually 2005-2009	Total Thereafter
Beacon Center		\$ 3,130
Olney		4,322
Southdale		3,485
Total		\$ 10,937

In addition to the above, Flagship Center consists of two developed out parcels that are part of a larger adjacent community shopping center formerly owned by The Saul Organization and sold to an affiliate of a tenant in 1991. The Company has a 90-year ground leasehold interest which commenced in September 1991 with a minimum rent of one dollar per year. Countryside shopping center was acquired in February, 2004. Because of certain land use considerations, approximately 0.54 of the 16 acres acquired is held under a 99-year ground lease. The lease requires the Company to pay minimum rent of one dollar per year as well as its pro-rata share of the real estate taxes.

The Company's corporate headquarters lease, which commenced in March 2002, is leased by a member of The Saul Organization. The 10-year lease provides for base rent escalated at 3% per year, with payment of a pro-rata share of operating expenses over a base year amount. The Company and The Saul Organization entered into a shared services agreement whereby each party pays an allocation of total rental payments on a percentage proportionate to the number of employees employed by each party. The Company's rent payments for the years ended December 31, 2004, 2003 and 2002 were \$621,000, \$569,000 and \$547,000, respectively. Expenses arising from the lease are included in general and administrative expense (see Note 9 – Related Party Transactions).

## 8. STOCKHOLDERS' EQUITY (DEFICIT) AND MINORITY INTERESTS

The consolidated statement of operations for the year ended December 31, 2004 includes a charge for minority interests of \$8,105,000, consisting of \$6,386,000 related to The Saul Organization's share of the net income for the year and \$1,719,000 related to distributions to minority interests in excess of allocated net income for the year. The charge for the year ended December 31, 2003 of \$8,086,000, consisting of \$6,495,000 related to The Saul Organization's share of the net income for the year and \$1,591,000 related to distributions to minority interests in excess of allocated net income for the year. The charge for the year ended December 31, 2002 of \$8,070,000, consisting of \$7,130,000 related to The Saul Organization's share of the net income for the year and \$940,000 related to distributions to minority interests in excess of allocated net income for the year.

On July 16, 2003, the Company filed a shelf registration statement (the "Shelf Registration Statement") with the SEC relating to the future offering of up to an aggregate of \$100 million of preferred stock and depositary shares. On November 5, 2003, the Company sold 3,500,000 depositary shares, each representing 1/100th of a share of 8% Series A Cumulative Redeemable Preferred Stock. The underwriters exercised an over-allotment option, purchasing an additional 500,000 depositary shares on November 26, 2003.

The depositary shares may be redeemed, in whole or in part, at the \$25.00 liquidation preference at the Company's option on or after November 5, 2008. The depositary shares will pay an annual dividend of \$2.00 per share, equivalent to 8% of the \$25.00 liquidation preference. The first dividend, paid on January 15, 2004, was for less than a full quarter and covered the period from November 5 through December 31, 2003. The Series A preferred stock has no stated maturity, is not subject to any sinking fund or mandatory redemption and is not convertible into any other securities of the Company. Investors in the depositary shares generally have no voting rights, but will have limited voting rights if the Company fails to pay dividends for six or more quarters (whether or not declared or consecutive) and in certain other events.

## 9. RELATED PARTY TRANSACTIONS

Chevy Chase Bank, an affiliate of The Saul Organization, leases space in 14 of the Company's properties. Total rental income from Chevy Chase Bank

amounted to \$1,733,000, \$1,495,000 and \$1,368,000, for the years ended December 31, 2004, 2003 and 2002, respectively.

The Company utilizes Chevy Chase Bank for its various checking accounts and as of December 31, 2004 had \$32.9 million deposited in cash and short-term investment accounts.

The Chairman and Chief Executive Officer, the President and the Chief Accounting Officer of the Company are also officers of various members of The Saul Organization and their management time is shared with The Saul Organization. Their annual compensation is fixed by the Compensation Committee of the Board of Directors.

The Company participates in a multiemployer profit sharing retirement plan with other entities within The Saul Organization which covers those full-time employees who meet the requirements as specified in the plan. Beginning January 1, 2002, only employer contributions are made to the plan. Each participant who is entitled to be credited with at least one hour of service on or after January 1, 2002, shall be 100% vested in his or her employer contribution account and no portion of such account shall be forfeitable. Employer contributions, included in general and administrative expense or property operating expenses in the consolidated statements of operations, at the discretionary amount of up to six percent of the employee's cash compensation, subject to certain limits, were \$269,000, \$199,000 and \$155,000 for 2004, 2003 and 2002, respectively. There are no past service costs associated with the plan since it is of the defined-contribution type.

The Company also participates in a multiemployer nonqualified deferred plan with entities in The Saul Organization which covers those full-time employees who meet the requirements as specified in the plan. The plan, which can be modified or discontinued at any time, requires participating employees to defer 2% of their compensation over a specified amount. For the years ending December 31, 2004, 2003 and 2002, the Company is required to contribute three times the amount deferred by employees. The Company's expense, included in general and administrative expense, totaled \$650,000, \$31,000, and \$8,000 for the years ended December 31, 2004, 2003 and 2002, respectively. All amounts deferred by employees and the Company are fully vested. The cumulative unfunded liability under this plan was \$452,000 and \$92,000 at December 31, 2004 and 2003 respectively, and is included in accounts payable, accrued expenses and other liabilities in the consolidated balance sheets.

The Company has entered into a shared services agreement (the "Agreement") with The Saul Organization that provides for the sharing of certain personnel and ancillary functions such as computer hardware, software, and support services and certain direct and indirect administrative personnel. The method for determining the cost of the shared services is provided for in the Agreement and is based upon estimates of usage or time incurred, as applicable. Senior management has determined that the final allocations of shared costs are reasonable. The terms of the Agreement and the payments made there under are reviewed annually by the Audit Committee of the Board of Directors, which consists entirely of independent directors. Billings by The Saul Organization for the Company's share of these ancillary costs and expenses for the years ended December 31, 2004, 2003 and 2002, which included rental payments for the Company's headquarters lease (see Note 7. Long Term Lease Obligations), totaled \$3,139,000, \$2,628,000 and \$2,574,000, respectively. The amounts are expensed when billed and are primarily reported as general and administrative expense in these consolidated financial statements. As of December 31, 2004 and 2003, accounts payable, accrued expenses and other liabilities included \$259,000 and \$247,000, respectively, represent billings due to The Saul Organization for the Company's share of these ancillary costs and expenses.

On January 23, 2004, the Company purchased a 3.4 acre site, adjacent to the Company's Kentlands Square property, from a subsidiary of Chevy Chase Bank for \$1,425,000. The Company is developing this property into a 41,000 square foot retail/office property known as Kentlands Place. The purchase price of the property was determined by the average of two independent third party appraisals which were contracted, one on behalf of the Company and one on behalf of the Bank.

## 10. STOCK OPTION PLAN

The Company established a stock option plan in 1993 (the "1993 Plan") for the purpose of attracting and retaining executive officers and other key personnel. The 1993 Plan provided for grants of options to purchase a specified number of shares of common stock. A total of 400,000 shares were made available under the 1993 Plan. The 1993 Plan authorizes the Compensation Committee of the Board of Directors to grant options at an exercise price which may not be less than the market value of the common stock on the date the option is granted.

During 1993 and 1994, the Compensation Committee granted options to purchase a total of 180,000 shares (90,000 shares from incentive stock options and 90,000 shares from nonqualified stock options) to five Company officers. The options vested 25% per year over four years, had an exercise price of \$20 per share and a term of ten years, subject to earlier expiration upon termination of employment. No compensation expense was recognized as a result of these grants. As of December 31, 2004, no 1993 and 1994 options remained unexercised.

On May 23, 2003, the Compensation Committee granted options to purchase a total of 220,000 shares (80,000 shares from incentive stock options and 140,000 shares from nonqualified stock options) to six Company officers (the "2003 Options"). The 2003 Options vest 25% per year over four years and have a term of ten years, subject to earlier expiration upon termination of employment. The exercise price of \$24.91 was the market trading price of the Company's common stock at the time of the award. As a result of the 2003 Options grant, no further shares were available under the 1993 Plan.

At the annual meeting of the Company's stockholders in 2004, the stockholders approved the adoption of the 2004 stock plan (the "2004 Plan") for the purpose of attracting and retaining executive officers, directors and other key personnel. The 2004 Plan provides for grants of options to purchase up to 500,000 shares of common stock as well as grants of up to 100,000 shares of common stock to directors. The 2004 Plan authorizes the Compensation Committee of the Board of Directors to grant options at an exercise price which may not be less than the market value of the common stock on the date the option is granted.

Effective April 26, 2004, the Compensation Committee granted options to purchase a total of 152,500 shares (27,500 shares of incentive stock options and 125,000 shares of nonqualified stock options) to eleven Company officers and to the twelve Company directors (the "2004 Options"). The officers' 2004 Options vest 25% per year over four years and have a term of ten years, subject to earlier expiration upon termination of employment. The directors' options are exercisable immediately. The exercise price of \$25.78 was the market trading price of the Company's common stock at the time of the award.



The table below summarizes the status of the 2003 and 2004 option grants and the value of the options expensed and included in general and administrative expense in the Consolidated Statements of Operations

Stock Options	Officers		Directors	Total
Grant date	05/23/2003	04/26/2004	04/26/2004	
Total grant	220,000	122,500	30,000	372,500
Vested	55,000	--	30,000	85,000
Exercised	20,000	--	--	20,000
Remaining unexercised	200,000	122,500	30,000	352,500
Exercise price	\$ 24.91	\$ 25.78	\$ 25.78	
Volatility	0.175	0.183	0.183	
Expected life (years)	7.0	7.0	5.0	
Assumed yield	7.00 %	5.75 %	5.75 %	
Risk-free rate	4.00 %	4.05 %	3.57 %	
Total value	\$ 332,200	\$ 292,775	\$ 66,600	\$ 691,575
Expensed in 2003	50,000	--	--	50,000
Expensed in 2004	83,000	50,000	66,600	199,600
To be expensed (2005-2007)	199,200	242,775	--	441,975

The table below summarizes the option activity for the years 2004, 2003 and 2002

	2004		2003		2002	
	Shares	Wtd Avg Exercise Price	Shares	Wtd Avg Exercise Price	Shares	Wtd Avg Exercise Price
Outstanding at January 1	220,000	\$ 24.91	93,210	\$ 20.00	180,000	\$ 20.00
Granted	152,500	25.78	220,000	24.91	--	--
Exercised	(20,000)	24.91	(93,210)	20.00	(86,790)	20.00
Expired/Forfeited	--	--	--	--	--	--
Outstanding December 31	352,500	25.29	220,000	24.91	93,210	20.00
Exercisable at December 31	65,000	25.31	--	--	93,210	20.00

## 11. NON-OPERATING ITEMS

### Gain on Sale of Property

The gain on sale of property of \$572,000 in 2004 represents the Company's share of the gain recognized as a result of a condemnation of a portion of land at the Company's White Oak shopping center for road improvements. The gain on sale of property of \$182,000 in 2003 represents the gain recognized as a result of a condemnation of a portion of land at the Company's Avenel Business Park property for improvement of an interchange on I-270, adjacent to the property. The gain on sale of property of \$1,426,000 in 2002 represents the final proceeds received upon appeal of the District of Columbia's purchase of the Company's Park Road property as part of an assemblage of parcels for a neighborhood revitalization project.

## 12. FAIR VALUE OF FINANCIAL INSTRUMENTS

Statement of Financial Accounting Standards No. 107, "Disclosure about Fair Value of Financial Instruments," requires disclosure about the fair value of financial instruments. The carrying values of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses are reasonable estimates of their fair value. Based upon management's estimate of borrowing rates and loan terms currently available to the Company for fixed-rate financing, the fair value of the fixed-rate notes payable is in excess of the \$453,646,000 and \$357,248,000 carrying value at December 31, 2004 and 2003, respectively. Management estimates that the fair value of these fixed-rate notes payable, assuming long term interest rates of approximately 5.5% and 6.0%, would be approximately \$474,993,000 and \$386,300,000, as of December 31, 2004 and 2003, respectively.

### 13. COMMITMENTS AND CONTINGENCIES

Neither the Company nor the Current Portfolio Properties are subject to any material litigation, nor, to management's knowledge, is any material litigation currently threatened against the Company, other than routine litigation and administrative proceedings arising in the ordinary course of business. Management believes that these items, individually or in the aggregate, will not have a material adverse impact on the Company or the Current Portfolio Properties.

### 14. DISTRIBUTIONS

In December 1995, the Company established a Dividend Reinvestment and Stock Purchase Plan (the "Plan"), to allow its stockholders and holders of limited partnership interests an opportunity to buy additional shares of common stock by reinvesting all or a portion of their dividends or distributions. The Plan provides for investing in newly issued shares of common stock at a 3% discount from market price without payment of any

brokerage commissions, service charges or other expenses. All expenses of the Plan are paid by the Company. The Operating Partnership also maintains a similar dividend reinvestment plan that mirrors the Plan, which allows limited partnership interests the opportunity to buy additional limited partnership units.

The Company declared and paid common stock distributions of \$1.56 per share during 2004, 2003 and 2002 and paid preferred stock dividends of \$1.811 per depositary share during 2004. No preferred stock dividends were paid during 2003 and 2002. For the common stock dividends paid, \$1.248, \$1.284 and \$1.458 per share, represented ordinary dividend income and \$0.312, \$0.276 and \$0.102 per share, represented return of capital to the shareholders for the years 2004, 2003 and 2002, respectively. All of the preferred stock dividends paid are considered ordinary dividend income. The following summarizes distributions paid during the years ended December 31, 2004, 2003 and 2002, and includes activity in the Plan as well as limited partnership units issued from the reinvestment of unit distributions:

	Total Distributions to			Dividend Reinvestments		
	Preferred Stockholders (In thousands)	Common Stockholders (In thousands)	Limited Partnership Unitholders (In thousands)	Common Stock Shs Issued	Units Issued	Discounted Share Price
<b>Distributions during 2004</b>						
October 31	\$ 2,000	\$ 6,342	\$ 2,028	116,006	2,590	\$ 31.53
July 31	2,000	6,296	2,027	117,334	2,769	29.10
April 30	2,000	6,236	2,026	140,253	3,270	24.25
January 31	1,244	6,187	2,024	123,689	2,928	26.69
	\$ 7,244	\$ 25,061	\$ 8,105	497,282	11,557	
<b>Distributions during 2003</b>						
October 31	\$ --	\$ 6,135	\$ 2,023	129,319	2,919	\$ 26.38
July 31	--	6,088	2,023	126,862	2,847	26.67
April 30	--	6,021	2,020	139,576	3,262	22.88
January 31	--	5,927	2,020	156,413	3,412	21.49
	\$ --	\$ 24,171	\$ 8,086	552,170	12,440	
<b>Distributions during 2002</b>						
October 31	\$ --	\$ 5,839	\$ 2,019	136,107	3,110	\$ 23.18
July 31	--	5,785	2,017	135,603	--	22.94
April 30	--	5,736	2,017	119,772	--	22.94
January 31	--	5,670	2,017	165,390	--	20.39
	\$ --	\$ 23,030	\$ 8,070	556,872	3,110	

In December 2004, 2003 and 2002, the Board of Directors of the Company authorized a distribution of \$0.39 per common share payable in January 2005, 2004 and 2003, to holders of record on January 17, 2005, January 16, 2004 and January 17, 2003, respectively. As a result, \$6,396,000, \$6,187,000 and \$5,927,000, were paid to common shareholders on January 31, 2005, January 30, 2004 and January 31, 2003, respectively. Also, \$2,028,000, \$2,024,000 and \$2,020,000, were paid to limited partnership unitholders on January 31, 2005, January 30, 2004 and January 31, 2003 (\$0.39 per Operating Partnership unit), respectively. The Board of Directors authorized

preferred stock dividends of \$0.50 and \$0.31 per depositary share, to holders of record on January 3, 2005 and January 2, 2004, respectively. As a result, \$2,000,000 and \$1,244,000, were paid to preferred shareholders on January 14, 2005 and January 15, 2004, respectively. These amounts are reflected as a reduction of stockholders' equity in the case of common stock and preferred stock dividends and minority interests deductions in the case of limited partner distributions and are included in dividends and distributions payable in the accompanying consolidated financial statements.

## 15. INTERIM RESULTS (Unaudited)

The following summary presents the results of operations of the Company for the quarterly periods of calendar years 2004 and 2003

(In thousands, except per share amounts)

	2004			
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Revenue	\$ 26,341	\$ 27,888	\$ 29,044	\$ 29,569
Operating income before minority interests and gain on sale of property	8,329	8,329	8,793	8,256
Net income	6,305	6,286	7,355 (a)	6,228
Net income available to common stockholders	4,305	4,286	5,355	4,228
Net income available to common stockholders per share (basic & diluted) (b)	0.27	0.27	0.33	0.26

(a) Includes \$572 gain on land condemnation at White Oak.

(b) The sum of the quarterly net income per common share-diluted, \$1.13, differs from the annual net income per common share-diluted, \$1.12, due to rounding.

	2003			
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Revenue	\$ 23,870	\$ 23,226	\$ 24,659	\$ 26,129
Operating income before minority interests and gain on sale of property	6,539	6,016	7,035	7,556
Net income	4,519	3,996	5,012	5,715 (c)
Net income available to common stockholders	4,519	3,996	5,012	4,471
Net income available to common stockholders per share (basic & diluted)	0.29	0.26	0.32	0.28

(c) Includes \$182 gain on land condemnation at Avenel Business Park.



## 16. BUSINESS SEGMENTS

The Company has two reportable business segments: Shopping Centers and Office Properties. The accounting policies of the segments are the same as those described in the summary of significant accounting policies (see Note 2). The Company evaluates performance based upon income from real estate for the combined properties in each segment.

<i>(In thousands)</i>	Shopping Centers	Office Properties	Corporate and Other	Consolidated Totals
<b>2004</b>				
Real estate rental operations:				
Revenue	\$ 77,906	\$ 34,679	\$ 257	\$ 112,842
Expenses	(14,226)	(8,121)	--	(22,347)
Income from real estate	63,680	26,558	257	90,495
Interest expense & amortization of debt costs	--	--	(27,022)	(27,022)
General and administrative	--	--	(8,442)	(8,442)
Subtotal	63,680	26,558	(35,207)	55,031
Depreciation and amortization	(13,758)	(7,566)	--	(21,324)
Gain on property sale	572	--	--	572
Minority interests	--	--	(8,105)	(8,105)
Net income	\$ 50,494	\$ 18,992	\$ (43,312)	\$ 26,174
Capital investment	\$ 109,637	\$ 4,426	\$ --	\$ 114,063
Total assets	\$ 394,674	\$ 138,273	\$ 50,449	\$ 583,396
<b>2003</b>				
Real estate rental operations:				
Revenue	\$ 66,070	\$ 31,722	\$ 92	\$ 97,884
Expenses	(12,274)	(7,840)	--	(20,114)
Income from real estate	53,796	23,882	92	77,770
Interest expense & amortization of debt costs	--	--	(26,573)	(26,573)
General and administrative	--	--	(6,213)	(6,213)
Subtotal	53,796	23,882	(32,694)	44,984
Depreciation and amortization	(10,429)	(7,409)	--	(17,838)
Gain on property sale	--	182	--	182
Minority interests	--	--	(8,086)	(8,086)
Net income	\$ 43,367	\$ 16,655	\$ (40,780)	\$ 19,242
Capital investment	\$ 42,999	\$ 6,122	\$ --	\$ 49,121
Total assets	\$ 271,565	\$ 138,862	\$ 61,189	\$ 471,616
<b>2002</b>				
Real estate rental operations:				
Revenue	\$ 61,597	\$ 32,261	\$ 105	\$ 93,963
Expenses	(10,675)	(7,882)	--	(18,557)
Income from real estate	50,922	24,379	105	75,406
Interest expense & amortization of debt costs	--	--	(25,838)	(25,838)
General and administrative	--	--	(5,537)	(5,537)
Subtotal	50,922	24,379	(31,270)	44,031
Depreciation and amortization	(11,295)	(6,526)	--	(17,821)
Gain on property sale	1,426	--	--	1,426
Minority interests	--	--	(8,070)	(8,070)
Net income	\$ 41,053	\$ 17,853	\$ (39,340)	\$ 19,566
Capital investment	\$ 23,785	\$ 4,850	\$ 11,534	\$ 40,169
Total assets	\$ 237,990	\$ 135,477	\$ 15,220	\$ 388,687

## 17. SUBSEQUENT EVENTS

On January 28, 2005, the Company executed a \$150 million unsecured revolving credit facility, an expansion of the \$125 million agreement in place as of December 31, 2004. The facility is intended to provide working capital and funds for acquisitions, certain developments and redevelopments. The line has a three year term and provides for an additional one year extension at the Company's option, subject to the Company's satisfaction of certain conditions. Until January 27, 2007, certain or all of the lenders may, upon request by the Company and payment of certain fees, increase the revolving credit facility line by up to \$50,000,000. Letters of credit may be issued under the revolving credit facility. The facility requires monthly interest payments, if applicable, at a rate of LIBOR plus a spread of 1.40% to 1.625% (determined by certain leverage tests) or upon the bank's reference rate at the Company's option.

Loan availability under the facility is determined by operating income from the Company's existing unencumbered properties. Based upon the revised terms of the facility, the unencumbered properties support line availability of \$86,500,000, of which \$2,100,000 has been issued under a letter of credit, leaving \$84,400,000 available for working capital uses. An additional \$63,500,000 is available for funding working capital and operating property acquisitions supported by the unencumbered properties' internal cash flow growth and operating income of future acquisitions. No funds have yet been borrowed from the facility.

On March 3, 2005, the Company acquired the 126,000 square foot Albertson's anchored, Palm Springs Center located in Altamonte Springs, Florida, near Orlando, for a purchase price of \$17.5 million. The Company paid the property's purchase price using available cash balances. The property was approximately 98% leased at the date of acquisition.

Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) begins with the Company's primary business strategy to give the reader an overview of the goals of the Company's business. This is followed by a discussion of the critical accounting policies that the Company believes are important to understanding the assumptions and judgments incorporated in the Company's reported financial results. The next section, beginning on page 40, discusses the Company's results of operations for the past two years. Beginning on page 43, the Company provides an analysis of its liquidity and capital resources, including discussions of its cash flows, debt arrangements, sources of capital and financial commitments. On page 49, the Company discusses funds from operations, or FFO, which is a relative non-GAAP financial measure of performance of an equity REIT used by the REIT industry. Starting on page 50, the Company describes its recent acquisitions, developments and renovations.

The MD&A should be read in conjunction with the other sections of this Annual Report, including the consolidated financial statements and notes thereto. Historical results set forth in Summary Financial Data and the financial statements and this section should not be taken as indicative of the Company's future operations.

## OVERVIEW

The Company's principal business activity is the ownership, management and development of income-producing properties. The Company's long-term objectives are to increase cash flow from operations and to maximize capital appreciation of its real estate.

The Company's primary operating strategy is to focus on its community and neighborhood shopping center business and to operate its properties to achieve both cash flow growth and capital appreciation. Management believes there is potential for growth in cash flow as existing leases for space in the Shopping Centers expire and are renewed, or newly available or vacant space is leased. The Company intends to renegotiate leases where possible and seek new tenants for available space in order to maximize this potential for increased cash flow. As leases expire, management expects to revise rental rates, lease terms and conditions, relocate existing tenants, reconfigure tenant spaces and introduce new tenants with the goal of increasing cash flow. In those circumstances in which leases are not otherwise expiring, management selectively attempts to increase cash flow through a variety of means, or in connection with renovations or relocations, recapturing leases with below market rents and re-leasing at market rates, as well as replacing

financially troubled tenants. When possible, management also will seek to include scheduled increases in base rent, as well as percentage rental provisions, in its leases.

The Company's redevelopment and renovation objective is to selectively and opportunistically redevelop and renovate its properties, by replacing leases with below market rents with strong, traffic-generating anchor stores such as supermarkets and drug stores, as well as other desirable local, regional and national tenants. The Company's strategy remains focused on continuing the operating performance and internal growth of its existing Shopping Centers, while enhancing this growth with selective retail redevelopments and renovations.

Management believes that attractive acquisition and development opportunities for investment in existing and new shopping center properties will continue to be available from time to time. Management believes that the Company's capital structure will enable it to take advantage of these opportunities as they arise. In addition, management believes its shopping center expertise should permit it to optimize the performance of shopping centers once they have been acquired.

Management also believes that opportunities may arise for investment in new office properties. It is management's view that several of the office sub-markets in which the Company operates have attractive supply/demand characteristics. The Company will continue to evaluate new office development and redevelopment as an integral part of its overall business plan.

Although it is management's present intention to concentrate future acquisition and development activities on community and neighborhood shopping centers and office properties in the Washington, DC/Baltimore metropolitan area, the Company may, in the future, also acquire other types of real estate in other areas of the country as opportunities present themselves. While the Company may diversify in terms of property locations, size and market, the Company does not set any limit on the amount or percentage of Company assets that may be invested in any one property or any one geographic area. In February 2004, the Company acquired a 121,000 square foot neighborhood shopping center in Boca Raton, Florida anchored by Publix, the dominant grocer in South Florida. In March 2004, the Company acquired another Publix anchored center, the 79,000 square foot Cruse MarketPlace, located in a suburb of Atlanta, Georgia. In March 2005, the Company acquired the 126,000 square foot Albertson's anchored neighborhood shopping center, Palm Springs Center, located in a suburb of Orlando, Florida.



## CRITICAL ACCOUNTING POLICIES

The Company's accounting policies are in conformity with accounting principles generally accepted in the United States ("GAAP"). The preparation of financial statements in conformity with GAAP requires management to use judgment in the application of accounting policies, including making estimates and assumptions. These judgments affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the Company's financial statements and the reported amounts of revenue and expenses during the reporting periods. If judgment or interpretation of the facts and circumstances relating to various transactions had been different, it is possible that different accounting policies would have been applied resulting in a different presentation of the financial statements. Below is a discussion of accounting policies which the Company considers critical in that they may require judgment in their application or require estimates about matters which are inherently uncertain. Additional discussion of accounting policies which the Company considers significant, including further discussion of the critical accounting policies described below, can be found in Notes To Consolidated Financial Statements.

### Real Estate Investments

Real estate investment properties are stated at historic cost basis less depreciation. Management believes that these assets have generally appreciated in value and, accordingly, the aggregate current value exceeds their aggregate net book value and also exceeds the value of the Company's liabilities as reported in these financial statements. Because these financial statements are prepared in conformity with GAAP, they do not report the current value of the Company's real estate assets. The purchase price of real estate assets acquired is allocated between land, building and in-place acquired leases based on the relative fair values of the components at the date of acquisition. Buildings are depreciated on a straight-line basis over their estimated useful lives of 35 to 50 years. Intangibles associated with acquired in-place leases are amortized over the remaining base lease terms.

If there is an event or change in circumstance that indicates an impairment in the value of a real estate investment property, the Company assesses an impairment in value by making a comparison of the current and projected operating cash flows of the property over its remaining useful life, on an undiscounted basis, to the carrying amount of that property. If such carrying amount is greater than the estimated projected cash flows, the Company would recognize an impairment loss equivalent to an amount required to adjust the carrying amount to its estimated fair market value.

When incurred, the Company capitalizes the cost of improvements that extend the useful life of property and equipment and all repair and maintenance expenditures are expensed.

Interest, real estate taxes and other carrying costs are capitalized on projects under construction. Once construction is substantially complete and the assets are placed in service, rental income, direct operating expenses, and depreciation associated with such properties are included in current operations.

In the initial rental operations of development projects, a project is considered substantially complete and available for occupancy upon completion of tenant improvements, but no later than one year from the cessation of major construction activity. Substantially completed portions of a project are accounted for as separate projects. Depreciation is calculated using the straight-line method and estimated useful lives of 35 to 50 years for base buildings and up to 20 years for certain other improvements. Leasehold improvements are amortized over the lives of the related leases using the straight-line method.

### Lease Acquisition Costs

Certain initial direct costs incurred by the Company in negotiating and consummating successful leases are capitalized and amortized over the initial base term of the leases. Capitalized leasing costs consist of commissions paid to third party leasing agents as well as internal direct costs such as employee compensation and payroll related fringe benefits directly related to time spent performing leasing related activities. Such activities include evaluating prospective tenants' financial condition, evaluating and recording guarantees, collateral and other security arrangements, negotiating lease terms, preparing lease documents and closing transactions.

### Revenue Recognition

Rental and interest income is accrued as earned except when doubt exists as to collectibility, in which case the accrual is discontinued. When rental payments due under leases vary from a straight-line basis because of free rent periods or scheduled rent increases, income is recognized on a straight-line basis throughout the initial term of the lease. Expense recoveries represent a portion of property operating expenses billed to tenants, including common area maintenance, real estate taxes and other recoverable costs. Expense recoveries are recognized in the period when the expenses are incurred. Rental income based on a tenant's revenues, known as percentage rent, is accrued when a tenant reports sales that exceed a specified breakpoint.

## MANAGEMENT'S DISCUSSION & ANALYSIS OF FINANCIAL CONDITION & RESULTS OF OPERATIONS

### Allowance for Doubtful Accounts - Current and Deferred Receivables

Accounts receivable primarily represent amounts currently due from tenants in accordance with the terms of the respective leases. Receivables are reviewed monthly and reserves are established with a charge to current period operations when, in the opinion of management, collection of the receivable is doubtful. In addition to rents due currently, accounts receivable include amounts representing minimum rental income accrued on a straight-line basis to be paid by tenants over the remaining term of their respective leases. Reserves are established with a charge to income for tenants whose rent payment history or financial condition casts doubt upon the tenant's ability to perform under its lease obligations.

### Legal Contingencies

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business. These matters are generally covered by insurance. While the resolution of these matters cannot be predicted with certainty, the Company believes the final outcome of such matters will not have a material adverse effect on the financial position or the results of operations. Once it has been determined that a loss is probable to occur, the estimated amount of the loss is recorded in the financial statements. Both the amount of the loss and the point at which its occurrence is considered probable can be difficult to determine.

## RESULTS OF OPERATIONS

(Dollars in thousands)	REVENUE			Percentage Change	
	For the year ended December 31, 2004	2003	2002	2004 to 2003	2003 to 2002
Base rent	\$ 91,125	\$ 78,167	\$ 75,699	16.6%	3.3%
Expense recoveries	16,712	14,438	12,680	15.8%	13.9%
Percentage rent	1,635	1,695	1,850	(3.5%)	(8.4%)
Other	3,370	3,584	3,734	(6.0%)	(4.0%)
Total	\$112,842	\$ 97,884	\$ 93,963	15.3%	4.2%

Total revenues increased 15.3% for the 2004 year compared to 2003 primarily due to the contribution of operating revenue from three development properties and five acquisition properties placed in service during 2004 or 2003. The developments Broadlands Village II and Shops at Monocacy were placed in service in 2004 and Broadlands Village in 2003. The acquisition properties Boca Valley Plaza, Countryside, Cruse MarketPlace and Briggs Chaney Plaza were acquired in 2004 and Olde Forte Village was acquired in 2003 (the "Development and Acquisition Properties"). The Development and Acquisition Properties contributed \$10,888,000 or 73% of the increase in revenues. The Company's 601 Pennsylvania Avenue office property was fully leased during 2004 and contributed \$2,267,000 or 15% of the year's revenue improvement. A discussion of the components of revenue follows.

### Base rent

The \$12,958,000 increase in base rent for 2004 versus 2003 was primarily attributable (69% or approximately \$8,958,000) to leases in effect at the Development and Acquisition Properties. The lease-up of space at 601

Pennsylvania Avenue (15% or approximately \$1,886,000) and contractual rent increases at other Properties substantially accounted for the balance of the increase.

The increase in base rent for 2003 versus 2002 was primarily attributable to leases in effect at properties acquired and developed in 2003 and 2002: Ashburn Village IV, Kentlands Square and Olde Forte Village (approximately \$1,890,000), the continued lease-up of space at Washington Square (approximately \$1,200,000), and releasing space at several other properties at rental rates higher than expiring rental rates. This increase was partially offset by an approximately \$1,920,000 decrease in base rent at 601 Pennsylvania Avenue resulting from the departure of a major tenant whose lease expired during the first quarter of 2003. The major tenant was also paying higher rent under the terms of a short-term lease extension during the prior year, increasing the magnitude of the variance between periods. By December 31, 2003, the former tenant's space was re-leased and 601 Pennsylvania Avenue was 100% leased.

# MANAGEMENT'S DISCUSSION & ANALYSIS OF FINANCIAL CONDITION & RESULTS OF OPERATIONS

MD&A

## Expense recoveries

Expense recoveries represent a portion of property operating expenses billed to tenants, including common area maintenance, real estate taxes and other recoverable costs. The Development and Acquisition Properties provided the majority (81% or approximately \$1,849,000) of the 2004 versus 2003 increase of \$2,274,000 in expense recovery income. The office properties 601 Pennsylvania Avenue and Van Ness Square were the other large contributors (together, 20% or approximately \$457,000).

The increase in expense recoveries for 2003 versus 2002 was primarily attributable to income resulting from billings to tenants for their share of increased snow removal expenses during 2003 (25% of increase) and the commencement of operations at the newly acquired and developed properties (28% of increase).

## Percentage rent

Percentage rent is rental income calculated on the portion of a tenant's revenues that exceed a specified breakpoint. Percentage rent decreased \$60,000 for 2004 versus 2003 due to a change in major tenant's sales reporting procedures. In years prior to 2004, the tenant voluntarily provided interim sales reports upon which the Company had based its calculations. The tenant has indicated that going forward, it will only provide required annual sales reports per the terms of its lease agreement. Accounting rules prohibit the accrual of percentage rent until the tenant actually

reports sales. Therefore the tenant's sales reporting change impacts only the timing of when the Company recognizes percentage rent. The Company expects to recognize percentage rent for this tenant during the second quarter of years 2005 and beyond.

The decrease in percentage rent for 2003 versus 2002 was primarily attributable to reduced sales reported by the grocery store and a pad building tenant at Beacon Center (27% of decrease) and a drug store tenant at each of Southside (27% of decrease) and Thruway (20% of decrease) paying higher minimum rent in lieu of percentage rent.

## Other income

Other income consists primarily of parking income at three of the Office Properties, kiosk leasing, temporary leases and payments associated with early termination of leases and interest income from the investment of cash balances. The \$214,000 decrease in other income for 2004 versus 2003 resulted primarily from a \$619,000 decrease in lease termination fees from \$1,286,000 in 2003 to \$667,000 in 2004, which was partially offset by an increase in parking income at the Office Properties of \$178,000 and an increase in cash investment income of \$166,000 in 2004.

The decrease in other income for 2003 versus 2002 resulted primarily from a \$365,000 decrease in lease termination payments compared to the prior year due to several large lease termination fees received in 2002.

## OPERATING EXPENSES

(Dollars in thousands)

	For the year ended December 31,			Percentage Change	
	2004	2003	2002	2004 to 2003	2003 to 2002
<b>Operating expenses:</b>					
Property operating expenses	\$ 12,070	\$ 11,363	\$ 10,115	6.2%	12.3%
Provision for credit losses	488	171	421	185.4%	(59.4)%
Real estate taxes	9,789	8,580	8,021	14.1%	7.0%
Interest expense and amortization of deferred debt	27,022	26,573	25,838	1.7%	2.8%
Depreciation and amortization	21,324	17,838	17,821	19.5%	0.1%
General and administrative	8,442	6,213	5,537	35.9%	12.2%
<b>Total</b>	<b>\$ 79,135</b>	<b>\$ 70,738</b>	<b>\$ 67,753</b>	<b>11.9%</b>	<b>4.4%</b>

**Property operating expenses**

Property operating expenses consist primarily of repairs and maintenance, utilities, payroll, insurance and other property related expenses. Property operating expenses increased \$707,000 for 2004 versus 2003. The Development and Acquisition Properties accounted for a \$1,024,000 increase in property operating expenses during 2004 which was offset by an approximately \$591,000 decrease in snow removal expenses at the remainder of the property portfolio due to 2003's unseasonably severe winter weather primarily in the Mid-Atlantic region.

The increase in property operating expenses for 2003 versus 2002 resulted primarily from an increase in snow removal expense of \$650,000 due to unseasonably severe winter weather primarily in the Mid-Atlantic region. The Company also paid increased property insurance premiums of approximately \$190,000 during 2003. In addition, approximately \$130,000 of the increase resulted from the settlement of a dispute with a former tenant at Crosstown Business Park and related legal expenses.

**Provision for credit losses**

The provision for credit losses increased \$317,000 for 2004 versus 2003 primarily due to 2003's absence of any significant tenant bankruptcy or collection difficulties. The 2004 provision for credit loss includes a \$155,000 provision for an anchor tenant at Great Eastern Plaza, a \$113,000 provision for a former tenant at Leesburg Pike, and a \$55,000 provision for a tenant at Seven Corners.

The provision for credit losses decreased for 2003 versus 2002 primarily due to the absence of any significant tenant bankruptcy or collection difficulties in 2003 as compared to 2002 when the Company established reserves for two office tenants in bankruptcy and a reserve for a rent dispute with another office tenant.

**Real estate taxes**

The \$1,209,000 increase in real estate taxes for 2004 versus 2003 was primarily attributable to the commencement of operations at the Development and Acquisition Properties (79% or approximately \$958,000).

The increase in real estate taxes for 2003 versus 2002 was primarily attributable to the commencement of operations at the newly acquired and developed properties (40% of increase) and increased real estate taxes assessed at 601 Pennsylvania Avenue (30% of increase).

**Interest expense and amortization of deferred debt**

Of the \$449,000 increase from 2004 versus 2003, \$322,000 resulted from increased interest expense and \$127,000 resulted from increased amortization of deferred debt expense. Interest expense increased in 2004 versus 2003 due to an increase in average outstanding borrowings of approximately \$22,645,000 (\$1,608,000 interest expense increase) and an increase in the weighted average interest rate of 12 basis points (\$501,000 interest expense increase), reflecting the Company's repayment of all of its short-term line of credit borrowings with proceeds from new 15-year fixed rate mortgages. As a result of the 2004 financing activity, the allocation of the Company's average floating rate notes payable balances as a percentage of total indebtedness decreased from 12% in 2003 to 1% in 2004. The increase in interest expense resulting from the new financings was more than offset by an increase in interest capitalized on costs of construction and development work. During 2004 and 2003, \$3,227,000 and \$1,382,000, was capitalized, respectively (\$1,845,000 interest expense decrease).

The \$735,000 increase in interest expense and amortization of deferred debt for 2003 versus 2002 resulted primarily from the placement of a new \$42.5 million, 15 year, 6.01% fixed rate mortgage replacing Washington Square's construction loan which charged interest at a variable rate averaging 3.5% during the prior year. The increase was partially offset by interest expense savings from lower interest rates on the Company's variable rate debt and the repayment of amounts borrowed under the revolving credit agreement in November 2003 using proceeds from the preferred stock offering. Amortization of deferred debt expense increased \$76,000 in 2003 versus 2002 primarily as a result of the full year's amortization of additional loan costs in 2003 associated with refinancing the Company's revolving credit agreement during the third quarter of 2002.

**Depreciation and amortization**

The increase in depreciation and amortization expense of \$3,486,000 resulted primarily from the Development and Acquisition Properties placed in service during 2003 and 2004.

Depreciation and amortization expense was virtually unchanged from 2002 to 2003. The Company recorded new depreciation expense on developments and acquisitions placed in service during 2002 and 2003, which was offset by a \$1,311,000 charge-off recorded in 2002, resulting from assets retired based upon a comprehensive review of real estate asset records and the Company's revision of the assets' estimated useful lives.



## General and administrative

General and administrative expense consists of payroll, administrative and other overhead expenses. The \$2,229,000 increase in general and administrative expense for 2004 versus 2003 was attributable to increased payroll, retirement and employment expenses (47% or \$1,040,000) primarily resulting from staffing for the Company's acquisitions department and a non-recurring retirement payment to a former executive officer. In addition, accounting fees and other administrative expenses, incurred to comply with new Sarbanes-Oxley documentation and compliance requirements, increased 28% or \$614,000, and the expensing of officer and director stock options increased 6.7% or \$150,000.

The increase in general and administrative expense for 2003 versus 2002 was primarily attributable to increased payroll and employment expenses (57% of increase). Approximately one-half of the increased payroll expense resulted from staffing for the Company's evaluation of property acquisitions. The increase in general and administrative expense resulted also from increased corporate insurance premiums (17% of increase) and increased data processing expenses (14% of increase).

## Gain on Sale of Property

The Company recognized a gain on the sale of real estate of \$572,000 in 2004, \$182,000 in 2003 and \$1,426,000 in 2002. The 2004 gain resulted from the State of Maryland's condemnation and taking of a small strip of unimproved land for a road widening project at White Oak shopping center. The 2003 gain resulted from the State of Maryland's condemnation and purchase of a piece of vacant land at Avenel Business Park for improvement of an interchange on I-270, adjacent to the property. The 2002 gain resulted from the 1999 District of Columbia's condemnation and purchase of the Company's Park Road property as part of an assemblage of parcels for a neighborhood revitalization project. The Company disputed the original purchase price awarded by the District. The 2002 gain represents additional net proceeds the Company was awarded upon settlement of the dispute.

## IMPACT OF INFLATION

Inflation has remained relatively low and has had a minimal impact on the operating performance of the Company's portfolio; however, substantially all of the Company's leases contain provisions designed to mitigate the adverse impact of inflation on the Company's results of operations. These provisions include upward periodic adjustments in base rent due from tenants, usually based on a stipulated increase and to a lesser extent on a factor of the change in the consumer price index, commonly referred to as the CPI.

Substantially all of the Company's properties are leased to tenants under long-term, triple-net leases. Triple-net leases tend to reduce the Company's exposure to rising property expenses due to inflation. Inflation and increased costs may have an adverse impact on the Company's tenants if increases in their operating expenses exceed increases in their revenue.

## LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents were \$33,561,000 and \$45,244,000 at December 31, 2004 and 2003, respectively. The changes in cash and cash equivalents during the years ended December 31, 2004 and 2003 were attributable to operating, investing and financing activities, as described below.

(In thousands)	Year Ended December 31,	
	2004	2003
Cash provided by operating activities	\$ 50,711	\$ 37,363
Cash used in investing activities	(114,063)	(49,121)
Cash provided by financing activities	51,669	55,693
Increase (decrease) in cash	\$ (11,683)	\$ 43,935

**Operating Activities**

Cash provided by operating activities increased \$13,348,000 to \$50,711,000 for the year ended December 31, 2004 compared to \$37,363,000 for the year ended December 31, 2003 primarily reflecting increased operating income of the Development and Acquisition Properties. Cash provided by operating activities represents, in each year, cash received primarily from rental income, plus other income, less property operating expenses, normal recurring general and administrative expenses and interest payments on debt outstanding.

**Investing Activities**

Cash used in investing activities increased \$64,942,000 to \$114,063,000 for the year ended December 31, 2004 compared to \$49,121,000 for the year ended December 31, 2003 and primarily reflects the acquisition of properties (Boca Valley Plaza, Briggs Chaney Plaza, Countryside, Cruse MarketPlace and the Kentlands Place and Ashland Square land parcels in 2004 and the Shops at Monocacy land parcel, and Olde Forte Village in 2003), the construction of new shopping center properties (Broadlands Village II, Shops at Monocacy, Kentlands Place and Olde Forte Village redevelopment in 2004 and Broadlands Village shopping center in 2003), tenant improvements and construction in progress during those years.

**Financing Activities**

Cash provided by financing activities for the years ended December 31, 2004 and 2003, was \$51,669,000 and \$55,693,000, respectively. Cash provided by financing activities for the year ended December 31, 2004 primarily reflects:

- \$94,800,000 of proceeds received from mortgage notes payable incurred during the year; and
- \$15,422,000 of proceeds received from the issuance of common stock under the dividend reinvestment program and from the exercise of stock options, and from the issuance of convertible limited partnership interests in the Operating Partnership;

which was partially offset by:

- the repayment of borrowings on mortgage notes payable totaling \$16,427,000;
- distributions made to common stockholders and holders of convertible limited partnership units in the Operating Partnership during the year totaling \$33,166,000;
- distributions made to preferred stockholders during the year totaling \$7,244,000; and
- payments of \$1,716,000 for financing costs of six mortgage loans during 2004.

The Company also temporarily borrowed and subsequently repaid \$33,000,000 on its revolving credit facility during 2004.

Cash provided by financing activities for the year ended December 31, 2003 primarily reflects:

- \$93,134,000 of proceeds received from mortgage notes payable incurred during the year;
- amounts borrowed from the revolving credit facility totaling \$35,000,000;
- \$96,327,000 of proceeds from the issuance of \$100,000,000 Series A 8% Cumulative Redeemable Preferred Stock after netting issuance costs of \$3,673,000; and
- \$16,018,000 of proceeds received from the issuance of common stock under the dividend reinvestment program and from the exercise of stock options, and from the issuance of convertible limited partnership interests in the Operating Partnership;

which was partially offset by:

- the repayment of borrowings on mortgage notes payable totaling \$69,879,000;
- the repayment of amounts borrowed from the revolving credit facility totaling \$81,750,000;
- distributions made to common stockholders and holders of convertible limited partnership units in the Operating Partnership during the year totaling \$32,257,000; and
- payments of \$900,000 for financing costs of three mortgage loans during 2003.

## Liquidity Requirements

Short-term liquidity requirements consist primarily of normal recurring operating expenses and capital expenditures, debt service requirements (including debt service relating to additional and replacement debt), distributions to common and preferred stockholders, distributions to unit holders and amounts required for expansion and renovation of the Current Portfolio Properties and selective acquisition and development of additional properties. In order to qualify as a REIT for federal income tax purposes, the Company must distribute to its stockholders at least 90% of its "real estate investment trust taxable income," as defined in the Code. The Company expects to meet these short-term liquidity requirements (other than amounts required for additional property acquisitions and developments) through cash provided from operations, available cash and its existing line of credit.

Long-term liquidity requirements consisted primarily of obligations under our long-term debt and dividends paid to our preferred shareholders. We anticipate that long-term liquidity requirements will also include amounts required for property acquisitions and developments. Management anticipates that during the coming year the Company may: i) redevelop certain of

the Current Portfolio Properties, ii) develop additional freestanding outparcels or expansions within certain of the Shopping Centers, iii) acquire existing neighborhood and community shopping centers and/or office properties, and iv) develop new shopping center or office sites. Acquisition and development of properties are undertaken only after careful analysis and review, and management's determination that such properties are expected to provide long-term earnings and cash flow growth. During the coming year, developments, expansions or acquisitions are expected to be funded with available cash, bank borrowings from the Company's credit line, construction and permanent financing, proceeds from the operation of the Company's dividend reinvestment plan or other external debt or equity capital resources available to the Company and proceeds from the sale of properties. Borrowings may be at the Saul Centers, Operating Partnership or Subsidiary Partnership level, and securities offerings may include (subject to certain limitations) the issuance of additional limited partnership interests in the Operating Partnership which can be converted into shares of Saul Centers common stock. The availability and terms of any such financing will depend upon market and other conditions.

## CONTRACTUAL PAYMENT OBLIGATIONS

As of December 31, 2004, the Company had unfunded contractual payment obligations of approximately \$15.3 million, excluding operating obligations, due within the next 12 months. The table below specifies the total contractual payment obligations as of December 31, 2004.

<i>(In thousands)</i> Contractual Obligations	Payments Due By Period				
	Total	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Notes Payable	\$ 453,646	\$ 11,349	\$ 34,653	\$ 29,466	\$ 378,178
Operating Leases (1)	11,757	164	328	328	10,937
Corporate Headquarters Lease (1)	5,077	646	1,350	1,432	1,649
Development Obligations	3,173	3,173	--	--	--
Total Contractual Cash Obligations	\$ 473,653	\$ 15,332	\$ 36,331	\$ 31,226	\$ 390,764

(1) See Note 7 to Consolidated Financial Statements. Corporate Headquarters Lease amounts represent an allocation to the Company based upon employees' time dedicated to the Company's business as specified in the Shared Services Agreement. Future amounts are subject to change as the number of employees, employed by each of the parties to the lease, fluctuate.

Management believes that the Company's capital resources, which at December 31, 2004 included cash balances of \$33.6 million and borrowing availability of \$125 million on its revolving line of credit (\$80 million for general corporate use and \$45 million for qualified future acquisitions), will be sufficient to meet its liquidity needs for the foreseeable future.

#### **Preferred Stock Issue**

On July 16, 2003, the Company filed a shelf registration statement (the "Shelf Registration Statement") with the SEC relating to the future offering of up to an aggregate of \$100 million of preferred stock and depositary shares. On November 5, 2003, the Company sold 3,500,000 depositary shares, each representing 1/100th of a share of 8% Series A Cumulative Redeemable Preferred Stock. The underwriters exercised an over-allotment option, purchasing an additional 500,000 depositary shares on November 26, 2003.

The depositary shares may be redeemed, in whole or in part, at the \$25.00 liquidation preference at the Company's option on or after November 5, 2008. The depositary shares pay an annual dividend of \$2.00 per depositary share, equivalent to 8% of the \$25.00 liquidation preference. The first dividend, paid on January 15, 2004 was for less than a full quarter and covered the period from November 5 through December 31, 2003. The Series A preferred stock has no stated maturity, is not subject to any sinking fund or mandatory redemption and is not convertible into any other securities of the Company. Investors in the depositary shares generally have no voting rights, but will have limited voting rights if the Company fails to pay dividends for six or more quarters (whether or not declared or consecutive) and in certain other events.

#### **Dividend Reinvestments**

In December 1995, the Company established a Dividend Reinvestment and Stock Purchase Plan (the "Plan") to allow its common stockholders and holders of limited partnership interests an opportunity to buy additional shares of common stock by reinvesting all or a portion of their dividends or distributions. The Plan provides for investing in newly issued shares of common stock at a 3% discount from market price without payment of any brokerage commissions, service charges or other expenses. All expenses of the

Plan are paid by the Company. The Company issued 497,282 and 552,170 shares under the Plan at a weighted average discounted price of \$27.70 and \$24.18 per share during the years ended December 31, 2004 and 2003, respectively.

Additionally, the Operating Partnership issued 11,557 and 12,440 limited partnership units under a dividend reinvestment plan mirroring the Plan at a weighted average discounted price of \$27.70 and \$24.18 per unit during the years ended December 31, 2004 and 2003, respectively.

### **CAPITAL STRATEGY AND FINANCING ACTIVITY**

As a general policy, the Company intends to maintain a ratio of its total debt to total asset value of 50% or less and to actively manage the Company's leverage and debt expense on an ongoing basis in order to maintain prudent coverage of fixed charges. Asset value is the aggregate fair market value of the Current Portfolio Properties and any subsequently acquired properties as reasonably determined by management by reference to the properties' aggregate cash flow. Given the Company's current debt level, it is management's belief that the ratio of the Company's debt to total asset value was below 50% as of December 31, 2004.

The organizational documents of the Company do not limit the absolute amount or percentage of indebtedness that it may incur. The Board of Directors may, from time to time, reevaluate the Company's debt capitalization policy in light of current economic conditions, relative costs of capital, market values of the Company property portfolio, opportunities for acquisition, development or expansion, and such other factors as the Board of Directors then deems relevant. The Board of Directors may modify the Company's debt capitalization policy based on such a reevaluation without shareholder approval and consequently, may increase or decrease the Company's debt to total asset ratio above or below 50% or may waive the policy for certain periods of time. The Company selectively continues to refinance or renegotiate the terms of its outstanding debt in order to achieve longer maturities, and obtain generally more favorable loan terms, whenever management determines the financing environment is favorable.



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The following is a summary of notes payable as of December 31, 2004 and 2003

Notes Payable (Dollars in thousands)	December 31,		Interest Rate *	Scheduled Maturity *
	2004	2003		
Fixed Rate Mortgages:	\$ 129,883 (a)	\$ 132,859	7.67 %	Oct 2012
	94,794 (b)	98,103	8.00 %	Dec 2011
	47,375 (c)	29,800	5.88 %	Jan 2019
	41,324 (d)	41,982	6.01 %	Feb 2018
	33,138 (e)	34,017	7.88 %	Jan 2013
	21,185 (f)	--	5.62 %	Jul 2019
	20,906 (g)	--	5.79 %	Sep 2019
	18,750 (h)	--	5.22 %	Jan 2020
	15,335 (i)	--	5.76 %	May 2019
	13,057 (j)	13,375	8.33 %	Jun 2015
	9,200 (k)	--	6.82 %	Apr 2007
	8,699 (l)	--	5.77 %	Jul 2013
	-- (m)	7,112		
Total Fixed Rate	453,646	357,248	7.03%	9.9 Years
Variable Rate Loan:				
Line of Credit	-- (n)	--	LIBOR plus 1.625%	Aug 2005
Total Variable Rate	--	--	--	--
Total Notes Payable	\$ 453,646	\$ 357,248	7.03 %	9.9 Years

\*Interest rate and scheduled maturity data presented as of December 31, 2004.

Totals computed using weighted averages.

- (a) The loan is collateralized by nine shopping centers (Seven Corners, Thruway, White Oak, Hampshire Langley, Great Eastern, Southside Plaza, Belvedere, Giant and Ravenwood) and requires equal monthly principal and interest payments of \$1,103,000 based upon a 25 year amortization schedule and a balloon payment of \$96,784,000 at loan maturity. Principal of \$2,976,000 was amortized during 2004.
- (b) The loan is collateralized by Avenel Business Park, Van Ness Square, Ashburn Village, Leesburg Pike, Lumberton Plaza and Village Center. The loan has been increased on four occasions since its inception in 1997. The 8.00% blended interest rate is the weighted average of the initial loan rate and additional borrowing rates. The loan requires equal monthly principal and interest payments of \$920,000 based upon a weighted average 23 year amortization schedule and a balloon payment of \$63,153,000 at loan maturity. Principal of \$3,309,000 was amortized during 2004.
- (c) The loan, consisting of two notes dated December 2003 and two notes dated February and December 2004, is currently collateralized by four shopping centers, Broadlands Village (Phases I & II), The Glen and Kentlands Square, and requires equal monthly principal and interest payments of \$306,000 (beginning February 1, 2005; prior to that date, payments totaled \$256,000 per month) based upon a 25 year amortization schedule and a balloon payment of \$28,255,000 at loan maturity. Principal of \$625,000 was amortized during 2004.
- (d) The loan is collateralized by Washington Square and requires equal monthly principal and interest payments of \$264,000 based upon a 27.5 year amortization schedule and a balloon payment of \$27,872,000 at loan maturity. Principal of \$658,000 was amortized during 2004.
- (e) The loan is collateralized by 601 Pennsylvania Avenue and requires equal monthly principal and interest payments of \$294,000 based upon a 25 year amortization schedule and a balloon payment of \$22,808,000 at loan maturity. Principal of \$879,000 was amortized during 2004.

- (f) The loan is collateralized by Countryside and requires equal monthly principal and interest payments of \$133,000 based upon a 25 year amortization schedule and a balloon payment of \$12,231,000 at loan maturity. Principal of \$165,000 was amortized during 2004.
- (g) The loan is collateralized by Briggs Chaney Plaza and requires equal monthly principal and interest payments of \$133,000 based upon a 25 year amortization schedule and a balloon payment of \$12,134,000 at loan maturity. Principal of \$94,000 was amortized during 2004.
- (h) The loan is collateralized by Shops at Monocacy and requires equal monthly principal and interest payments of \$112,000 based upon a 25 year amortization schedule and a balloon payment of \$10,522,000 at loan maturity. Payments commenced February 2005.
- (i) The loan is collateralized by Olde Forte Village and requires equal monthly principal and interest payments of \$98,000 based upon a 25 year amortization schedule and a balloon payment of \$8,942,000 at loan maturity. Principal of \$165,000 was amortized during 2004.
- (j) The loan is collateralized by Shops at Fairfax and Boulevard shopping centers and requires monthly principal and interest payments of \$118,000 based upon a 22 year amortization schedule and a balloon payment of \$7,577,000 at loan maturity. Principal of \$318,000 was amortized during 2004.
- (k) The loan is collateralized by Boca Valley Plaza and requires monthly interest only payments of \$52,000. A balloon payment of \$9,200,000 is due at loan maturity.
- (l) The loan is collateralized by Cruse MarketPlace and requires equal monthly principal and interest payments of \$56,000 based upon an amortization schedule of approximately 24 years and a balloon payment of \$6,797,000 at loan maturity. Principal of \$126,000 was amortized during 2004.
- (m) The \$7,112,000 loan was collateralized by Kentlands Square and was repaid and retired at maturity in February 2004 using proceeds provided by a \$10,200,000 increase to the loan described in (c) above.
- (n) The loan is an unsecured revolving credit facility totaling \$125,000,000. Loan availability for working capital and general corporate uses is determined by operating income from the Company's unencumbered properties, with a portion available only for funding qualified operating property acquisitions. Interest expense is calculated based upon the 1,2,3 or 6 month LIBOR rate plus a spread of 1.625% to 1.875% (determined by certain debt service coverage and leverage tests) or upon the bank's reference rate at the Company's option. The line may be extended one year with payment of a fee of 1/4% at the Company's option. There were no outstanding borrowings as of December 31, 2004. Monthly payments, if applicable, are interest only and will vary depending upon the amount outstanding and the applicable interest rate for any given month. On January 28, 2005, the Company executed a new \$150,000,000 unsecured revolving credit facility to replace the \$125,000,000 line. The new line has a three year term and provides for an additional one year extension at the Company's option, subject to the Company's satisfaction of certain conditions. (see Note 17. Subsequent Events).

The December 31, 2004 and 2003 depreciation adjusted cost of properties collateralizing the mortgage notes payable totaled \$420,320,000 and \$295,506,000, respectively. The Company's credit facility requires the Company and its subsidiaries to maintain certain financial covenants. As of December 31, 2004, the material covenants required the Company, on a consolidated basis, to:

- limit the amount of debt so as to maintain a gross asset value in excess of liabilities of at least \$250 million;
- limit the amount of debt as a percentage of gross asset value (leverage ratio) to less than 60%;
- limit the amount of debt so that interest coverage will exceed 2.1 to 1 on a trailing four quarter basis; and
- limit the amount of debt so that interest, scheduled principal amortization and preferred dividend coverage exceeds 1.6 to 1.

As of December 31, 2004, the Company was in compliance with all such covenants.

During 2004, the Company completed new financings and refinanced several existing mortgage loans to take advantage of favorable financing terms available to the Company. In addition, the Company assumed two mortgages securing real estate properties acquired by the Company during 2004. In February, the Company refinanced Kentlands Square with a new \$10.2 million, fixed-rate, 15-year mortgage and assumed a \$9.2 million mortgage with the acquisition of Boca Valley Plaza. In March, the Company assumed an \$8.8 million mortgage with the acquisition of Cruse MarketPlace. In April 2004, the Company placed a new \$15.5 million, fixed-rate, 15-year mortgage secured by Olde Forte Plaza, acquired in July 2003. In July 2004, the Company placed a new \$21.35 million, fixed-rate, 15-year mortgage secured by Countryside, acquired in February 2004. In August 2004, the Company placed a new \$21 million, fixed-rate, 15-year mortgage secured by Briggs Chaney Plaza, acquired in April 2004. In December 2004, the Company placed a new \$18.75 million, fixed-rate, 15-year mortgage secured by Shops at Monocacy, a development placed in service during

## MANAGEMENT'S DISCUSSION & ANALYSIS OF FINANCIAL CONDITION & RESULTS OF OPERATIONS

the fourth quarter of 2004. Also in December 2004, the Company placed a new \$8 million, fixed-rate, 14-year mortgage secured by Broadlands Village and Broadlands Village II, a development placed in service during the fourth quarter of 2004.

On January 28, 2005, the Company executed a \$150 million unsecured revolving credit facility, an expansion of the \$125 million agreement in place as of December 31, 2004. The facility is intended to provide working capital and funds for acquisitions, certain developments and redevelopments. The line has a three-year term and provides for an additional one-year extension at the Company's option, subject to the Company's satisfaction of certain conditions. Until January 27, 2007, certain or all of the lenders may, upon request by the Company and payment of certain fees, increase the revolving credit facility by up to \$50,000,000. Letters of credit may be issued under the revolving credit facility. The facility requires monthly interest payments, if applicable, at a rate of LIBOR plus a spread of 1.40% to 1.625% (determined by certain leverage tests) or upon the bank's reference rate at the Company's option. Loan availability under the facility is determined by operating income from the Company's existing unencumbered properties. Based upon the revised

terms of the facility, the unencumbered properties support line availability of \$86,500,000, of which \$2,100,000 has been issued under a letter of credit, leaving \$84,400,000 available for working capital uses. An additional \$63,500,000 is available for funding working capital and operating property acquisitions supported by the unencumbered properties' internal cash flow growth and operating income of future acquisitions. No funds have yet been borrowed from the facility.

### OFF-BALANCE SHEET ARRANGEMENTS

The Company has no off-balance sheet arrangements that are reasonably likely to have a current or future material effect on the Company's financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

### FUNDS FROM OPERATIONS

In 2004, the Company reported Funds From Operations (FFO)<sup>1</sup> available to common shareholders (common stockholders and limited partner unitholders) of \$47,031,000 representing a 7.5% increase over 2003 FFO available to common shareholders of \$43,740,000.

**The following table presents a reconciliation from net income to FFO available to common shareholders for the periods indicated**

(In thousands)	For the Year Ended December 31,				
	2004	2003	2002	2001	2000
Net income	\$ 26,174	\$ 19,242	\$ 19,566	\$ 17,314	\$ 14,045
Subtract:					
Gain on sale of property	(572)	(182)	(1,426)	--	--
Add:					
Minority interests	8,105	8,086	8,070	8,069	8,069
Depreciation and amortization of real property	21,324	17,838	17,821	14,758	13,534
FFO	55,031	44,984	44,031	40,141	35,648
Preferred dividends	(8,000)	(1,244)	--	--	--
FFO available to common shareholders	\$ 47,031	\$ 43,740	\$ 44,031	\$ 40,141	\$ 35,648
Average shares and units used to compute FFO per share	21,405	20,790	20,059	19,382	18,795

<sup>1</sup> FFO is a widely accepted non-GAAP financial measure of operating performance for REITs. FFO is defined by the National Association of Real Estate Investment Trusts as net income, computed in accordance with GAAP, plus minority interests, extraordinary items and real estate depreciation and amortization, excluding gains or losses from property sales. FFO does not represent cash generated from operating activities in accordance with GAAP and is not necessarily indicative of cash available to fund cash needs, which is disclosed in the Consolidated Statements of Cash Flows for the applicable periods. There are no material legal or functional restrictions on the use of FFO. FFO should not be considered as an alternative to net income, its most directly comparable GAAP measure, as an indicator of the Company's operating performance, or as an alternative to cash flows as a measure of liquidity. Management considers FFO a supplemental measure of operating performance and along with cash flow from operating activities, financing activities and investing activities, it provides investors with an indication of the ability of the Company to incur and service debt, to make capital expenditures and to fund other cash needs. FFO may not be comparable to similarly titled measures employed by other REITs.

## ACQUISITIONS, REDEVELOPMENTS AND RENOVATIONS

Management anticipates that during the coming year the Company may: i) redevelop certain of the Current Portfolio Properties, ii) develop additional freestanding outparcels or expansions within certain of the Shopping Centers, iii) acquire existing neighborhood and community shopping centers and/or office properties, and iv) develop new shopping center or office sites. Acquisition and development of properties are undertaken only after careful analysis and review, and management's determination that such properties are expected to provide long-term earnings and cash flow growth. During the coming year, any developments, expansions or acquisitions are expected to be funded with bank borrowings from the Company's credit line, construction financing, proceeds from the operation of the Company's dividend reinvestment plan or other external capital resources available to the Company.

The Company has been selectively involved in acquisition, redevelopment and renovation activities. It continues to evaluate the acquisition of land parcels for retail and office development and acquisitions of operating properties for opportunities to enhance operating income and cash flow growth. The Company also continues to take advantage of redevelopment, renovation and expansion opportunities within the portfolio, as demonstrated by its recent activities at Olde Forte Village, Broadlands Village, Thruway and The Glen. The following describes the acquisitions, redevelopments and renovations which affected the Company's results of operations in 2003 and 2004.

### Olde Forte Village

In July 2003, the Company acquired Olde Forte Village, a 161,000 square foot neighborhood shopping center located in Fort Washington, Maryland. The center is anchored by a newly constructed 58,000 square foot Safeway supermarket which opened in March 2003, relocating from a smaller store within the center. The center then contained approximately 50,000 square feet of vacant space, consisting primarily of the former Safeway space, which the Company redeveloped in 2004. This former anchor space and some adjoining space was reconfigured into new small shop space totaling approximately 33,000 square feet. The redeveloped center totals 142,000 square feet. The Company has substantially completed site improvements and small shop construction and renovation. Total redevelopment costs, including the initial property acquisition cost, were approximately \$22 million. Olde Forte Village was

70% leased at December 31, 2004. A total of 25,000 square feet of the recently completed small shop space remains available.

### Broadlands Village

The Company purchased 24 acres of undeveloped land in the Broadlands section of the Dulles Technology Corridor of Loudoun County, Virginia in April 2002. Broadlands is a 1,500 acre planned community consisting of 3,500 residences, approximately half of which are constructed and currently occupied. In October 2003, the Company completed construction of the first phase of the Broadlands Village shopping center. The 58,000 square foot Safeway supermarket opened in October 2003 with a pad building and many in-line small shops also opening in the fourth quarter of 2003. The 105,000 square foot first phase is 100% leased. Construction of a 30,000 square foot second phase was substantially completed in November 2004. Total development costs of both phases, including the land acquisition, are expected to total approximately \$22 million. The second phase was 96% leased at December 31, 2004. This second phase added a spacious landscaped courtyard and fountain to the center, and includes Original Steakhouse and Bonefish Grill, both quality restaurants that recently opened.

### Thruway

During the fourth quarter of 2003, the Company commenced a 15,725 square foot expansion of the Thruway shopping center located in Winston Salem, North Carolina. The new development includes replacing a former 6,100 square foot single-tenant pad building with a new multi-tenant building. Leases have been executed for 100% of the new space, including Ann Taylor Loft, JoS. A Banks Clothiers, Chico's and Liz Claiborne. This \$2.1 million expansion was completed in April 2004 with tenant openings beginning in March 2004.

### Shops at Monocacy

In November 2003, the Company acquired 13 acres of undeveloped land in Frederick, Maryland at the southeast corner of Maryland Route 26 and Monocacy Boulevard. Construction commenced in early December 2003 of a 107,000 square foot shopping center anchored by a 57,000 square foot Giant grocery store. Total development costs, including the land acquisition, are expected to be approximately \$22.3 million upon completion of the final leasing. The center was substantially completed and Giant opened for business during October 2004. The property was 84% leased at December 31, 2004.



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### Kentlands Place

In January 2004, the Company purchased 3.4 acres of undeveloped land adjacent to its 109,000 square foot Kentlands Square shopping center in Gaithersburg, Maryland. The Company commenced construction of a 41,300 square foot retail/office property, comprised of 24,400 square feet of in-line retail space and 16,900 square feet of professional office suites, in April 2004. Development costs, including the land acquisition, are projected to total \$7.8 million. The building was substantially completed in January 2005. The property was 39% leased at December 31, 2004 and 58% leased as of March 11, 2005. Additional tenant prospects have been identified and lease negotiations are proceeding for nearly all of the remaining space.

### Boca Valley Plaza

The Company added Publix as one of its grocery tenants with the February 2004 acquisition of Boca Valley Plaza in Boca Raton, Florida. Boca Valley Plaza is a 121,000 square foot neighborhood shopping center on U.S. Highway 1 in South Florida. The center, constructed in 1988 was 91% leased at December 31, 2004 and is anchored by a 42,000 square foot Publix supermarket. The property was acquired for a purchase price of \$17.5 million, subject to the assumption of a \$9.2 million mortgage.

### Countryside

In mid-February 2004, the Company completed the acquisition of the 142,000 square foot Safeway

anchored Countryside shopping center, its fourth neighborhood shopping center investment in Loudoun County, Virginia. The center was 95% leased at December 31, 2004 and was acquired for a purchase price of \$29.7 million.

### Cruse MarketPlace

On March 25, 2004, the Company completed the acquisition of the 79,000 square foot Publix anchored, Cruse MarketPlace located in Forsyth County, Georgia. Cruse MarketPlace was constructed in 2002 and was 97% leased at December 31, 2004. The center was purchased for \$12.6 million, subject to the assumption of an \$8.8 million mortgage.

### Briggs Chaney Plaza

In April 2004, the Company acquired Briggs Chaney Plaza in Silver Spring, Maryland. Briggs Chaney Plaza is a 197,000 square foot neighborhood shopping center on Route 29 in Montgomery County, Maryland. The center, constructed in 1983, was 94% leased at December 31, 2004 and is anchored by a 45,000 square foot Safeway supermarket and a 28,000 square foot Ross Dress For Less. The property was acquired for \$27.3 million. The Company has substantially completed interior construction on a portion of the vacant space totaling approximately 11,000 square feet of leasable area. The space was reconfigured into six small shops, with five currently leased. The Company is also finalizing plans for a substantial facade renovation of the shopping center, projected to be substantially completed in mid-2005.

## PORTFOLIO LEASING STATUS

The following chart sets forth certain information regarding our properties for the periods indicated

As of December 31,	Total Properties		Total Square Footage		Percent Leased	
	Shopping Centers	Office	Shopping Centers	Office	Shopping Centers	Office
2004	35	5	6,012,000	1,205,000	93.5%	95.9%
2003	31	5	5,328,000	1,204,000	94.1%	95.8%
2002	29	5	5,069,000	1,203,000	93.9%	92.9%

The comparative decrease in the year end 2004 leasing percentage is largely attributable to the departure of a 39,000 square foot local grocer at Southside Plaza in suburban Richmond, Virginia. The improvement in the

portfolio's leasing percentage in 2003 compared to 2002 resulted primarily from improved leasing in the Office Properties at 601 Pennsylvania Avenue, Washington Square and Avenel Business Park.

## FORWARD-LOOKING STATEMENTS

This Annual Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements are generally characterized by terms such as “believe”, “expect” and “may”.

Although the Company believes that the expectations reflected in such forward-looking statements are based upon reasonable assumptions, the Company's actual results could differ materially from those given in the forward-looking statements as a result of changes in factors which include among others, the following:

- risks that the Company's tenants will not pay rent;
- risks related to the Company's reliance on shopping center “anchor” tenants and other significant tenants;
- risks related to the Company's substantial relationships with members of The Saul Organization;
- risks of financing, such as increases in interest rates, restrictions imposed by the Company's debt, the Company's ability to meet existing financial covenants and the Company's ability to consummate planned and additional financings on acceptable terms;
- risks related to the Company's development activities;
- risks that the Company's growth will be limited if the Company cannot obtain additional capital;
- risks that planned and additional acquisitions or redevelopments may not be consummated, or if they are consummated, that they will not perform as expected;
- risks generally incident to the ownership of real property, including adverse changes in economic conditions, changes in the investment climate for real estate, changes in real estate taxes and other operating expenses, adverse changes in governmental rules and fiscal policies, the relative illiquidity of real estate and environmental risks; and
- risks related to the Company's status as a REIT for federal income tax purposes, such as the existence of complex regulations relating to the Company's status as a REIT, the effect of future changes in REIT requirements as a result of new legislation and the adverse consequences of the failure to qualify as a REIT.

Saul Centers, Inc. offers a dividend reinvestment plan which enables its shareholders to automatically invest some of or all dividends in additional shares. The plan provides shareholders with a convenient and cost-free way to increase their investment in Saul Centers. Shares purchased under the dividend reinvestment plan are issued at a 3% discount from the closing price of the stock on the dividend payment date. The Plan's prospectus is available for review in the Shareholders Information section of the Company's web site.

To receive more information please call the plan administrator at (800) 509-5586 and request to speak with a service representative or write:

Continental Stock Transfer & Trust Company  
Attention: Saul Centers, Inc. Dividend Reinvestment Plan  
17 Battery Place  
New York, NY 10004

### COMMON STOCK PRICES

Period	Share Price	
	High	Low
Fourth Quarter, 2004	\$39.25	\$31.84
Third Quarter, 2004	\$33.25	\$28.83
Second Quarter, 2004	\$32.41	\$24.70
First Quarter, 2004	\$30.55	\$27.30
Fourth Quarter, 2003	\$29.04	\$26.62
Third Quarter, 2003	\$27.95	\$25.75
Second Quarter, 2003	\$26.55	\$23.59
First Quarter, 2003	\$24.10	\$21.97

On March 11, 2005, the closing price was \$32.82  
There were approximately 390 holders of record as of that date.

**DIRECTORS****B. Francis Saul II**

Chairman & Chief  
Executive Officer

**B. Francis Saul III**

President

**Philip D. Caraci**

Vice Chairman

**The Honorable****John E. Chapoton**

Partner, Brown Investment  
Advisory

**Gilbert M. Grosvenor**

Chairman of the  
Board of Trustees,  
National Geographic Society

**Philip C. Jackson, Jr.**

Adjunct Professor Emeritus,  
Birmingham-Southern  
College

**David B. Kay**

Senior Advisor,  
J.E. Robert Companies

**General Paul X. Kelley**

28th Commandant of  
the Marine Corps

**Charles R. Longworth**

Chairman Emeritus, Colonial  
Williamsburg Foundation

**Patrick F. Noonan**

Chairman Emeritus,  
The Conservation Fund

**The Honorable****James W. Symington**

Of Counsel, O'Connor &  
Hannan, Attorneys at Law

**John R. Whitmore**

Senior Advisor to the  
Bessemer Group, Inc.

**EXECUTIVE OFFICERS****B. Francis Saul II**

Chairman & Chief  
Executive Officer

**B. Francis Saul III**

President

**Scott V. Schneider**

Senior Vice President,  
Chief Financial Officer,  
Treasurer & Secretary

**Kenneth D. Shoop**

Vice President,  
Chief Accounting Officer

**Christopher H. Netter**

Senior Vice President,  
Leasing

**John F. Collich**

Senior Vice President,  
Retail Development

**M. Laurence Millspaugh**

Senior Vice President,  
Acquisitions & Development

**Charles W. Sherren, Jr.**

Senior Vice President,  
Management

**Thomas H. McCormick**

Senior Vice President,  
General Counsel

**COUNSEL**

Shaw Pittman LLP  
Washington, DC 20037

**INDEPENDENT  
REGISTERED PUBLIC  
ACCOUNTING FIRM**

Ernst & Young LLP  
McLean, Virginia 22102

**WEB SITE**

[www.saulcenters.com](http://www.saulcenters.com)

**EXCHANGE LISTING**

New York Stock  
Exchange (NYSE) Symbol:  
Common Stock: BFS  
Preferred Stock: BFS.PrA

**TRANSFER AGENT**

Continental Stock Transfer &  
Trust Company  
17 Battery Place  
New York, NY 10004  
(800) 509-5586

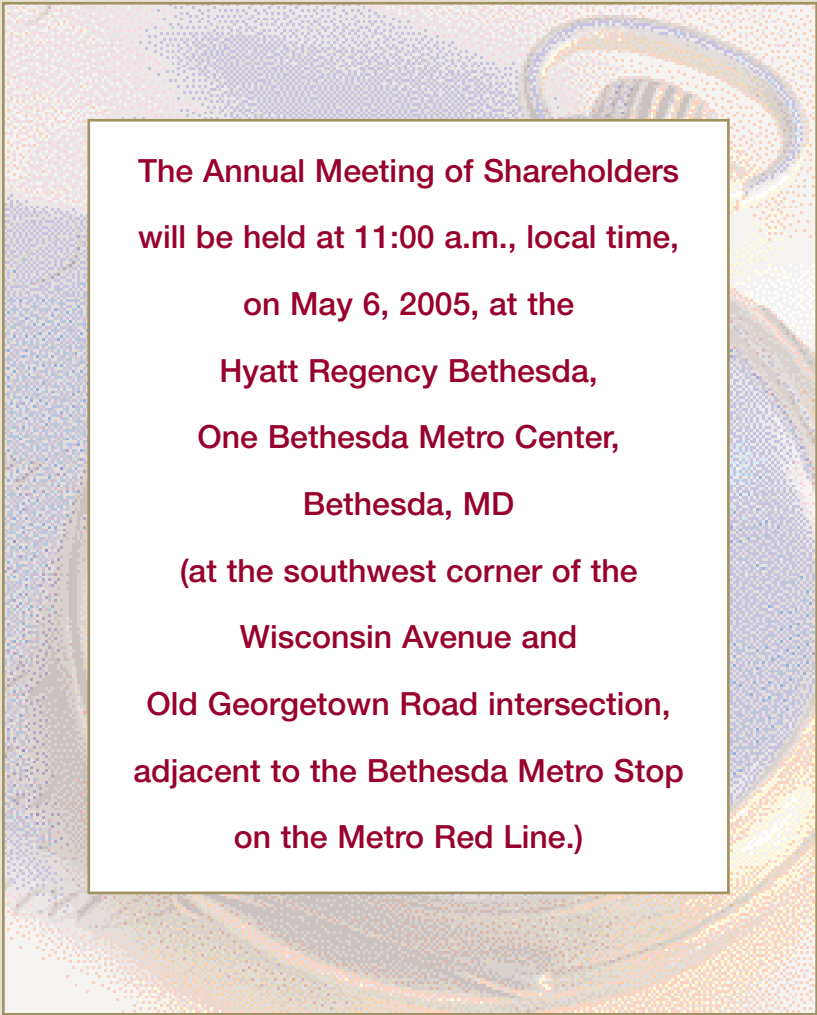
**INVESTOR RELATIONS**

A copy of the Saul Centers, Inc. annual report to the Securities and Exchange Commission on Form 10-K, which includes as exhibits the Chief Executive Officer and Chief Financial Officer Certifications required by Section 302 of the Sarbanes-Oxley Act, may be printed from the Company's web site or obtained at no cost to stockholders by writing to the address below or calling (301) 986-6016. In 2004, the Company filed with the NYSE the Certification of its Chief Executive Officer confirming that he was not aware of any violation by the Company of the NYSE's corporate governance listing standards.

**HEADQUARTERS**

7501 Wisconsin Ave.  
Suite 1500  
Bethesda, MD 20814-6522  
Phone: (301) 986-6200





The Annual Meeting of Shareholders  
will be held at 11:00 a.m., local time,  
on May 6, 2005, at the  
Hyatt Regency Bethesda,  
One Bethesda Metro Center,  
Bethesda, MD  
(at the southwest corner of the  
Wisconsin Avenue and  
Old Georgetown Road intersection,  
adjacent to the Bethesda Metro Stop  
on the Metro Red Line.)

# Saul Centers

7501 Wisconsin Avenue, Suite 1500

Bethesda, MD 20814-6522

Phone: (301) 986-6200

Website: [www.saulcenters.com](http://www.saulcenters.com)