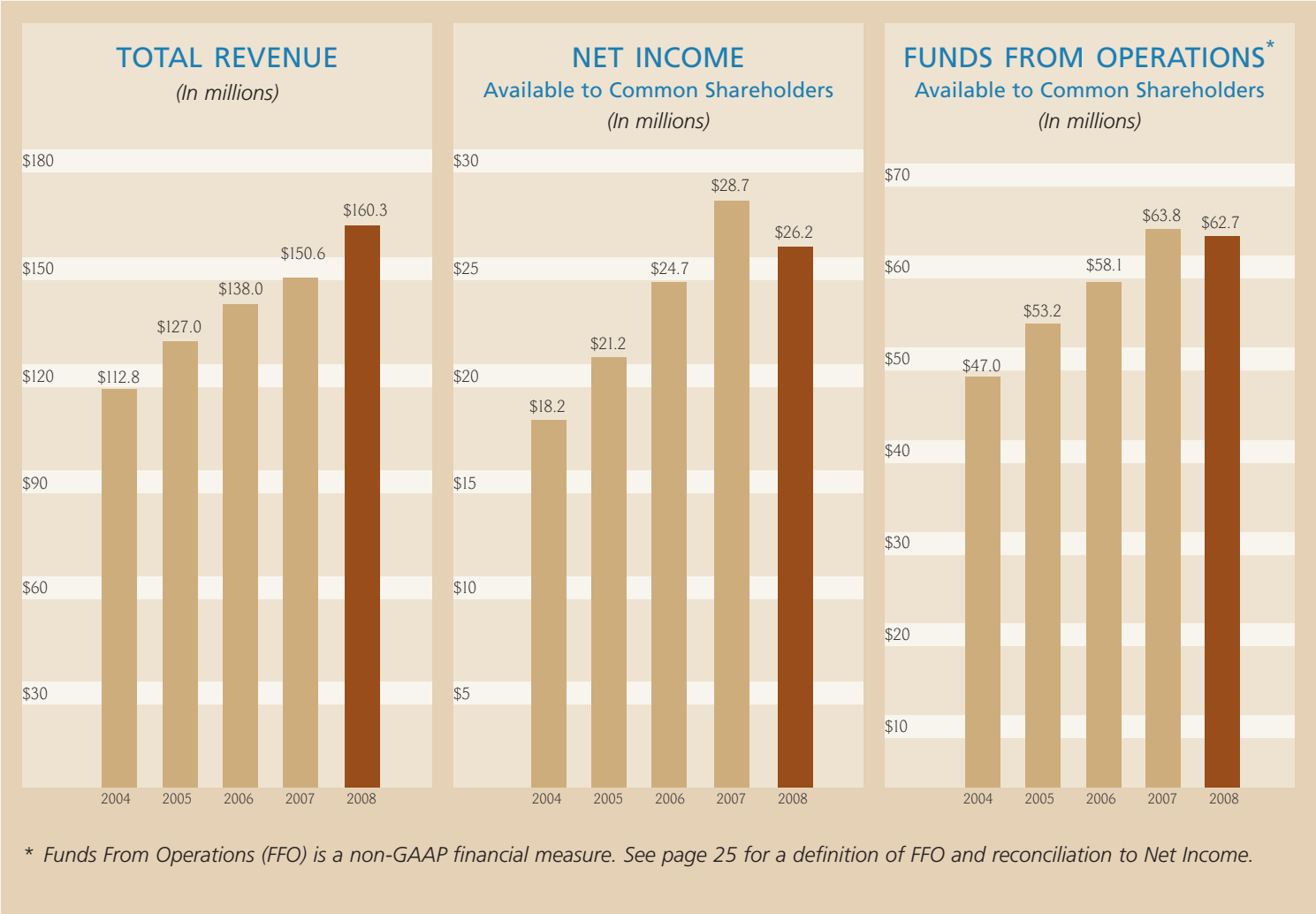


Saul Centers

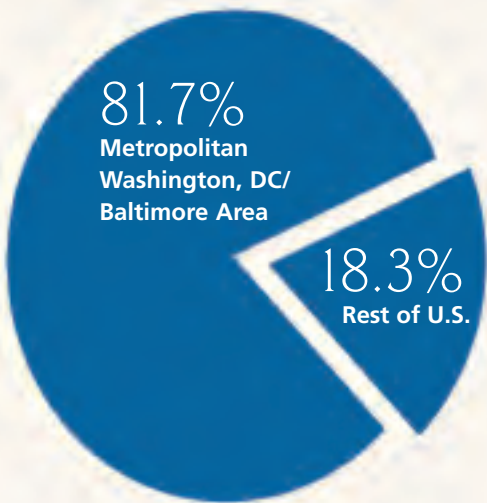
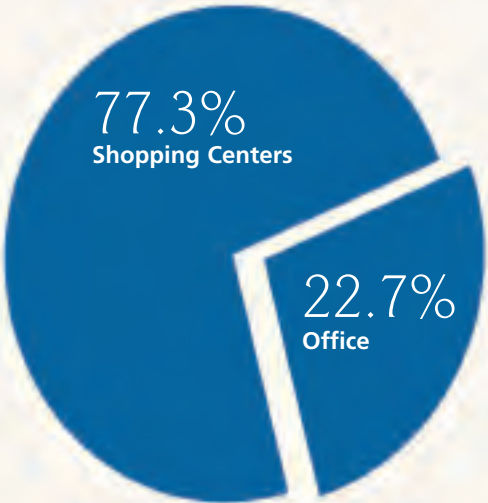
2008 Annual Report



HISTORIC OPERATING PERFORMANCE



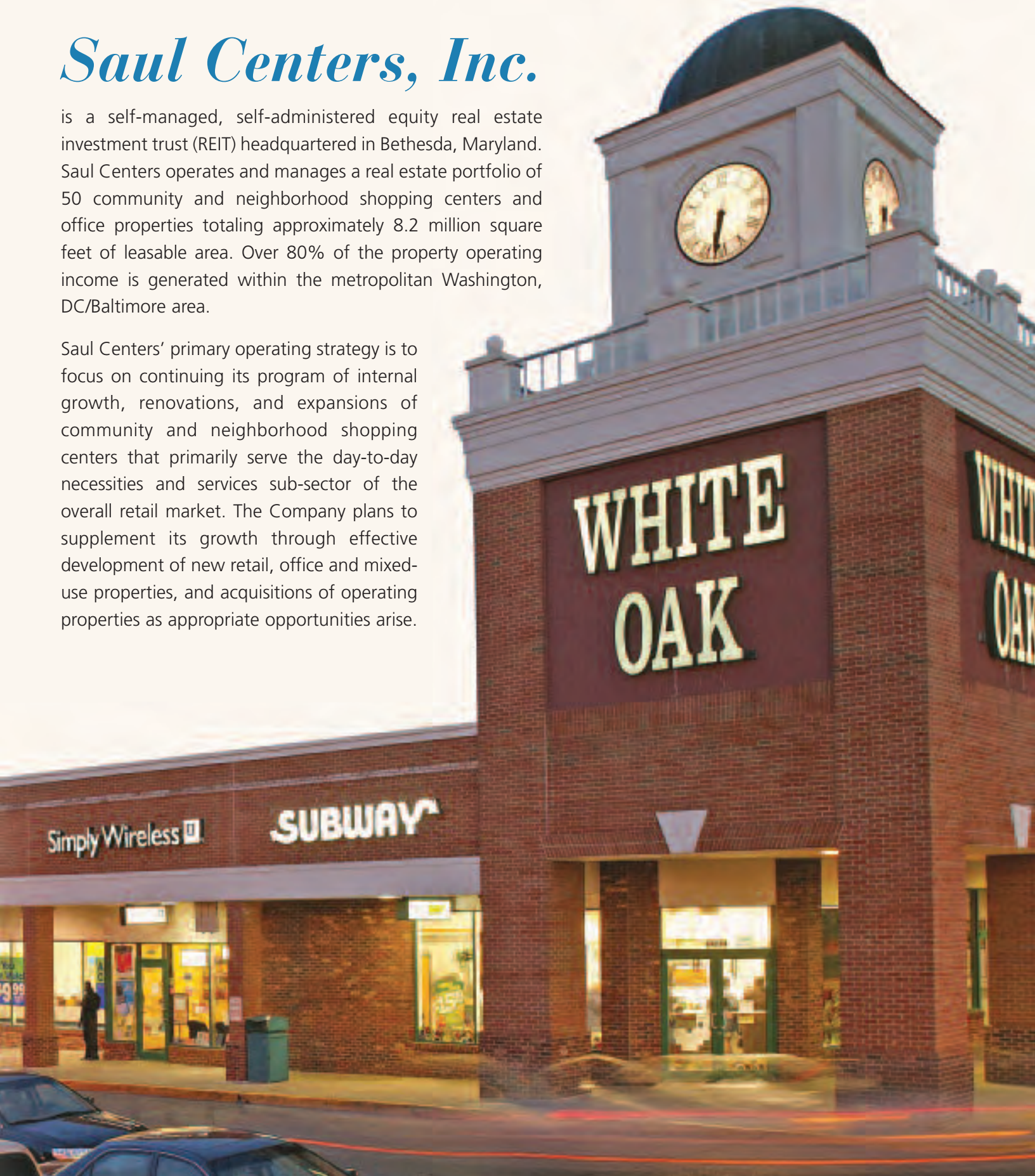
PORTFOLIO COMPOSITION Based on 2008 Property Operating Income



Saul Centers, Inc.

is a self-managed, self-administered equity real estate investment trust (REIT) headquartered in Bethesda, Maryland. Saul Centers operates and manages a real estate portfolio of 50 community and neighborhood shopping centers and office properties totaling approximately 8.2 million square feet of leasable area. Over 80% of the property operating income is generated within 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 that primarily serve 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 retail, office and mixed-use properties, and acquisitions of operating properties as appropriate opportunities arise.



Year ended December 31,

2008

2007

2006

2005

2004

Summary Financial Data

Total Revenue	\$160,345,000	\$150,585,000	\$137,978,000	\$127,015,000	\$112,842,000
Net Income Available to Common Stockholders	\$26,241,000	\$28,703,000	\$24,680,000	\$21,227,000	\$18,174,000
FFO Available to Common Shareholders	\$62,695,000	\$63,846,000	\$58,121,000	\$53,222,000	\$47,031,000
Weighted Average Common Stock Outstanding	17,961,000	17,769,000	17,233,000	16,770,000	16,211,000
Weighted Average Shares and Units Outstanding	23,377,000	23,185,000	22,628,000	22,003,000	21,405,000
Net Income Available to Common Stockholders Per Share (Diluted)	\$1.46	\$1.62	\$1.43	\$1.27	\$1.12
FFO Available to Common Shareholders Per Share (Diluted)	\$2.68	\$2.75	\$2.57	\$2.42	\$2.20
Common Dividend as a Percentage of FFO (Per Share)	70%	64%	65%	66%	71%
Interest Expense Coverage ^a	3.33	3.23	3.14	3.15	3.14

Property Data

Number of Properties ^b	50	48	47	44	40
Total Portfolio Square Feet	8,194,000	8,009,000	7,904,000	7,376,000	7,217,000
Shopping Center Square Feet	6,988,000	6,803,000	6,698,000	6,170,000 ^c	6,012,000
Office Square Feet	1,206,000	1,206,000	1,206,000	1,206,000	1,205,000
Average Percentage Leased ^d	95%	96%	97%	95%	94%

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

(b) Excludes development parcels (Clarendon Center, Ashland Square Phase II, Lexington Center, Westview Village, Northrock and New Market).

(c) During 2005, approximately 301,000 square feet of space was taken out of service at Lexington for a future redevelopment of the center.

(d) Average percentage leased would have been 96% for both 2005 and 2004 if the Lexington redevelopment space was excluded from the calculation for the entire year.



SHOPS AT MONOCACY



THRUWAY

2008

was marked by a troubled economy characterized by a declining housing market, higher unemployment, a virtual shut down of the debt and equity markets and historic lows in consumer confidence. The year ended with our country experiencing one of the deepest recessions in modern history. With a decline in overall consumer spending, retailers continue to struggle with declining sales and limited access to capital. Store closings are on the increase and retailers who were expanding their store count have pulled back. Despite these conditions, our portfolio continues to deliver steady performance. We attribute this largely to the location of our core portfolio of grocery anchored shopping centers and office properties in the Washington, DC metropolitan area. While down from our historical 5-year average growth of 2.8% annually, same property operating income for the retail and office portfolio increased by 0.9%. Though our overall portfolio leasing percentage ended the year at 94.2%, a decrease from 95.3% at year end 2007, rental rate growth across the entire portfolio continued to be strong, with spaces relet at average initial cash rental rates of 8.6% over rents paid on expiring leases. Weaknesses in the portfolio are largely centered in small shop closures in both our Loudoun County, Virginia and Florida shopping centers. Small in-line restaurants were particularly hard hit, although consumer spending at our 28 grocery stores that reported sales increased by 2.0% in 2008.

A total of 220 new leases or lease renewals for 1,165,000 square feet of retail and office space were executed, compared to the 223 leases for 1,035,000 square feet executed in 2007. Funds From Operations (FFO) per share declined by 2.5% in 2008, largely as a result of our preferred stock offering in March 2008. We completed this capital offering in order to strengthen the balance sheet and increase liquidity as we prepared for a potentially prolonged economic downturn. At year end 2008, 97% of our debt was fixed-rate, amortizing, non-recourse mortgage loans, none of which mature until December 2011.



601 PENNSYLVANIA AVENUE



WASHINGTON SQUARE

Balance Sheet Highlights

In March 2008, we issued \$79 million in preferred stock in order to pay down all of our credit line balances and to fund development and redevelopment activity. This was one of the last REIT preferred offerings to be completed before the credit markets' rapid deterioration. We also completed two construction financings in the second quarter of 2008, totaling \$179 million, to fund development of our Harris Teeter anchored Northrock shopping center and the mixed-use Clarendon Center project adjacent to the Clarendon Metro station. As of December 31, 2008, we had no debt maturities prior to December 2011. The mortgage maturing December 2011 will have a remaining balance of \$62,233,000, or only 54% of the original amount borrowed, as a result of loan principal repaid monthly over the term of the loan. We had no outstanding borrowings on our \$150 million credit line as of December 31, 2008. The weighted average interest rate of our debt outstanding was 6.56% and our interest expense coverage was 3.3 times for the year. We maintained leverage of approximately 33.7% debt to total capitalization at December 31, 2008. In January 2009, with credit market conditions continuing to deteriorate and economic growth continuing to slow, we chose to reduce our quarterly common stock dividend by approximately 17%. While it was a difficult decision to lower the payout to our stockholders, we felt that retaining capital in a very uncertain economic climate was the prudent business strategy.

2008 Financial Performance

Operating income increased in 2008 as operating results continued to improve at the newly developed Lansdowne Town Center and rental rates grew at Southdale and several other shopping centers. These increases were offset in part by an increase in credit loss reserves and increased property operating expenses and real estate taxes, net of tenant recoveries.



LANDSDOWNE TOWN CENTER



SOUTHDALE



SEVEN CORNERS

For the year 2008, total revenue increased 6.5% to \$160,345,000 compared to \$150,585,000 for 2007. Operating income increased 2.2% to \$46,365,000. The increase in operating income was more than offset by an increase in preferred stock dividends of \$5,453,000 in 2008. As a result, net income available to common stockholders decreased to \$26,241,000 or \$1.46 per diluted share in 2008 compared to \$1.62 per diluted share in 2007. FFO available to common shareholders (after deducting preferred stock dividends) decreased 1.8% to \$62,695,000 from \$63,846,000 in 2007. Per share FFO available to common shareholders for 2008 decreased 2.5% to \$2.68 in 2008, from \$2.75 per diluted share in 2007.

Retail Performance

We acquired three shopping centers in early 2008 to increase our retail portfolio to 45 community and neighborhood shopping centers totaling 7.0 million square feet of space. The retail portfolio leasing percentage was negatively impacted by the economic contraction, declining by 1.4% to end 2008 at 93.9%. New or renewal retail leases were signed at average cash rental rates of approximately 10.1% over rents paid on expiring leases for the 933,000 square feet of same space lease rollovers or renewals, down slightly from the 11% in 2007. Of the 1,149,000 square feet of retail leases expiring in 2008, approximately 66% of the square footage was renewed. This retention rate is below our preceding 5-year average of 73%.

While retailers generally are, and will likely continue to be, stressed by current economic conditions, our primarily in-fill Washington, DC metropolitan area grocery anchored shopping centers continue to perform relatively well. Our shopping centers generally provide convenient grocery, pharmacy, banking, medical and other necessary and non-discretionary goods and services. On a same store basis, the grocers in our portfolio increased sales by 2.0% during 2008 from a \$458 per square foot average in 2007 to \$467 per square foot in 2008. Weakness is, however, seen in several of the other anchor categories and small shop uses, as evidenced by an overall retail same store sales decrease of approximately 1.0% from 2007 levels.

BEACON CENTER



Shopping center same property operating income increased 1.2%. The rate of increase slowed as a result of increased small shop vacancy and higher credit loss reserves for tenants struggling to make rental payments. This compares to an average increase in same property shopping center operating income of 2.9% annually over the preceding 5 years.

As of March 1, 2009, a total of 54% of the approximately 798,000 square feet of 2009 retail lease expirations have been successfully renewed or released, generally consistent with the 56% of 2008 lease expiration releasing achieved at the same time a year ago.

Office Results

Over 97% of the operating income from our 1.2 million square feet of office space is produced from properties in Washington, DC or in adjacent suburban submarkets. The overall leasing percentage of our office portfolio was 95.8% at year end 2008, compared to 95.2% at the end of 2007. The Washington, DC metropolitan area unemployment rate of approximately 4.7% as of December 2008 remains among the lowest of the country's major metropolitan areas. The new political administration and the currently developing government economic stimulus plan should continue to keep unemployment relatively low in the Washington, DC metropolitan area.

Our office properties produced same property operating income of \$27,742,000 in 2008, a decrease of 0.2% from 2007 levels. The office assets represented 22.7% of our total property operating income in 2008. As of March 1, 2009, only 68,000 square feet of office space is scheduled to expire during the balance of 2009.

Acquisitions

During early 2008, we acquired a portfolio containing three shopping centers, the first of which was the 92,000 square foot Great Falls Center located in Great Falls, Virginia. The center is anchored by a Safeway grocery store and a CVS pharmacy, and it serves one of the premier residential sub-markets in the Washington, DC metropolitan area with household incomes averaging over \$263,000 within a 3-mile radius.

The second property in the portfolio was a 116,000 square foot single tenant property leased to the BJ's Wholesale Club. Its location in Alexandria, Virginia is characterized by strong demographics and high traffic volumes, with 100,000 average daily vehicular trips passing the site.



After renovation

HUNT CLUB CORNERS (before and after renovation)



The third property acquired was the 22,000 square foot Marketplace at Sea Colony, located in Bethany Beach, Delaware. This center is 100% leased by restaurants and retailers serving both permanent residents and visitors to this Atlantic Coast vacation community.

Development and Redevelopment Activity

Construction of two of our three development properties was nearing completion at year end 2008, while our major mixed-use Clarendon Center project is proceeding on schedule toward a late 2010 completion. These three projects will add over 600,000 square feet, or approximately 7.5% to our portfolio size. In addition, we are completing two renovation projects at our Smallwood and Boulevard shopping centers, and have modernized the façade at our Hunt Club Corners center in metropolitan Orlando, Florida.

Developments

Westview Village

In late 2007, we purchased a 10.4 acre site in the Westview mixed-use development in Frederick, Maryland. Our portion of the development consists of approximately 105,000 square feet of commercial space, including 60,000 square feet of retail shop space, 15,000 square feet of retail pads and 30,000 square feet of professional office space. Construction is scheduled for completion in spring 2009. We have executed leases for 19,673 square feet, or 26% of the total retail space.

Northrock

In January 2008, we acquired 15.4 acres of land in Warrenton, Virginia, conveniently located along U.S. Route 29. We are currently constructing the 103,000 square foot Northrock shopping center. The Harris Teeter supermarket chain has leased 52,700 square feet to anchor the center. Additionally, we have leased a bank pad and have signed 7,896 square feet of small shop leases, bringing the development to 62% pre-leased. Construction is projected for completion in spring 2009, and Harris Teeter has announced an early June opening.



Clarendon Center

Early 2008 marked another significant milestone in our development of the two block, mixed-use Clarendon Center project adjacent to the Clarendon Metro station in Arlington, Virginia. We closed a \$157.5 million construction loan in May 2008 and commenced excavation and site construction. At year end 2008, construction had reached the bottom of the south block's four level sub-grade parking deck, and garage deck concrete pours are in progress. Demolition of the north block was completed in late 2008 and excavation has begun. Upon completion in late 2010, the project will include approximately 45,000 square feet of retail space, 170,000 square feet of office space and 244 residential apartments.

Redevelopments

In early 2008, we commenced construction of a capital improvement project at our recently acquired Smallwood Village Center in Waldorf, Maryland. The work includes improving access to the site, reconfiguring some of the buildings, and upgrading the façade and common areas. Substantial completion of these improvements is March 2009.

Also in 2008, we redeveloped a portion of the Boulevard shopping center in Fairfax, Virginia. A vacant pad building, previously occupied by a furniture store, was demolished. The center's in-line shop space was expanded by approximately 8,000 square feet and a new Chevy Chase Bank branch opened on the site of the demolished structure. Two new small shop tenants totaling 3,040 square feet also opened in early 2009.

CLARENDON CENTER
(artist's rendering)



SMALLWOOD VILLAGE CENTER



We completed an upgrade at our recently acquired Hunt Club Corners shopping center in metropolitan Orlando, Florida. The center was originally built in 1980 and the architecture was dated. The improvements provide more visible tenant signage, brightened under canopy walkways, and a newly constructed attractive building façade.

We have prepared for what appears to be a very uncertain and turbulent year ahead of us. Our strong balance sheet, with no 2009 or 2010 debt maturities, is one of our greatest strengths today. We believe that our property types and market focus position us well with 86% of our retail property operating income coming from grocery anchored shopping centers, and over 81% of our total property operating income generated from assets located in the Washington, DC/Baltimore metropolitan area. We are proud of our core portfolio and our team of long tenured professionals who have been collectively tested through prior periods of economic stress, and we remain confident that we can meet the challenges of 2009.

For the Board

B. Francis Saul II
March 12, 2009



GREAT FALLS CENTER



AS OF DECEMBER 31, 2008, SAUL CENTERS' PORTFOLIO PROPERTIES WERE LOCATED IN VIRGINIA, MARYLAND, WASHINGTON, DC, NORTH CAROLINA, DELAWARE, FLORIDA, GEORGIA, KENTUCKY, NEW JERSEY AND OKLAHOMA. PROPERTIES IN THE METROPOLITAN WASHINGTON, DC/BALTIMORE AREA REPRESENT OVER 70% OF THE PORTFOLIO'S GROSS LEASABLE AREA.

PORTFOLIO PROPERTIES

PROPERTY/LOCATION GROSS LEASABLE SQUARE FEET

Shopping Centers

ASHBURN VILLAGE, ASHBURN, VA	221,687
ASHLAND SQUARE, PHASE I, MANASSAS, VA	3,650
BEACON CENTER, ALEXANDRIA, VA	356,115
BJ'S WHOLESALE CLUB, ALEXANDRIA, VA	115,660
BELVEDERE, BALTIMORE, MD	54,941
BOCA VALLEY PLAZA, BOCA RATON, FL	121,269
BOULEVARD, FAIRFAX, VA	49,140
BRIGGS CHANEY MARKETPLACE, SILVER SPRING, MD	194,347
BROADLANDS VILLAGE I, II & III, ASHBURN, VA	159,734
COUNTRYSIDE, STERLING, VA	141,696
CRUSE MARKETPLACE, CUMMING, 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	134,317
GREAT EASTERN, DISTRICT HEIGHTS, MD	255,398
GREAT FALLS CENTER, GREAT FALLS, VA	91,666
HAMPSHIRE LANGLEY, TAKOMA PARK, MD	131,700
HUNT CLUB CORNERS, APOPKA, FL	101,522
JAMESTOWN PLACE, ALTAMONTE SPRINGS, FL	96,372
KENTLANDS SQUARE, GAITHERSBURG, MD	114,381
KENTLANDS PLACE, GAITHERSBURG, MD	40,648
LANSDOWNE TOWN CENTER, LEESBURG, VA	189,210
LEESBURG PIKE, BAILEYS CROSSROADS, VA	97,752
LEXINGTON PADS, LEXINGTON, KY	13,646
LUMBERTON PLAZA, LUMBERTON, NJ	193,044

PROPERTY/LOCATION GROSS LEASABLE SQUARE FEET

SHOPS AT MONOCACY, FREDERICK, MD	109,144
OLDE FORTE VILLAGE, FT. WASHINGTON, MD	143,062
OLNEY, OLNEY, MD	53,765
ORCHARD PARK, DUNWOODY, GA	87,782
PALM SPRINGS CENTER, ALTAMONTE SPRINGS, FL	126,446
RAVENWOOD, BALTIMORE, MD	93,328
SEABREEZE PLAZA, PALM HARBOR, FL	146,673
MARKETPLACE AT SEA COLONY, BETHANY BEACH, DE	21,677
SEVEN CORNERS, FALLS CHURCH, VA	568,831
SHOPS AT FAIRFAX, FAIRFAX, VA	68,743
SMALLWOOD VILLAGE CENTER, WALDORF, MD	172,817
SOUTHDAL, GLEN BURNIE, MD	484,115
SOUTHSIDE PLAZA, RICHMOND, VA	373,651
SOUTH DEKALB PLAZA, ATLANTA, GA	163,418
THRUWAY, WINSTON-SALEM, NC	354,416
VILLAGE CENTER, CENTREVILLE, VA	143,109
WEST PARK, OKLAHOMA CITY, OK	76,610
WHITE OAK, SILVER SPRING, MD	480,156

TOTAL SHOPPING CENTERS 6,987,829

Office Properties

AVENEL BUSINESS PARK, GAITHERSBURG, MD	390,579
CROSTOWN BUSINESS CENTER, TULSA, OK	197,135
601 PENNSYLVANIA AVE., WASHINGTON, DC	226,604
VAN NESS SQUARE, WASHINGTON, DC	156,493
WASHINGTON SQUARE, ALEXANDRIA, VA	235,042

TOTAL OFFICE PROPERTIES 1,205,853

TOTAL PORTFOLIO 8,193,682

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SELECTED FINANCIAL DATA

	Years Ended December 31,				
	2008	2007	2006	2005	2004
<i>(In thousands, except per share data)</i>					
Operating Data					
Total revenue	\$ 160,345	\$ 150,585	\$ 137,978	\$ 127,015	\$ 112,842
Operating expenses	113,980	105,203	97,505	89,990	79,135
Operating income	46,365	45,382	40,473	37,025	33,707
Non-operating income					
Gain on property dispositions	1,301	139	–	–	572
Income before minority interests	47,666	45,521	40,473	37,025	34,279
Minority interests	(7,972)	(8,818)	(7,793)	(7,798)	(8,105)
Net income	39,694	36,703	32,680	29,227	26,174
Preferred dividends	(13,453)	(8,000)	(8,000)	(8,000)	(8,000)
Net income available to common stockholders	\$ 26,241	\$ 28,703	\$ 24,680	\$ 21,227	\$ 18,174
Per Share Data (diluted)					
Net income available to common stockholders	\$ 1.46	\$ 1.62	\$ 1.43	\$ 1.27	\$ 1.12
Basic and diluted shares outstanding					
Weighted average common shares - basic	17,816	17,589	17,075	16,663	16,154
Effect of dilutive options	145	180	158	107	57
Weighted average common shares - diluted	17,961	17,769	17,233	16,770	16,211
Weighted average convertible limited partnership units	5,416	5,416	5,395	5,233	5,194
Weighted average common shares and fully converted limited partnership units - diluted	23,377	23,185	22,628	22,003	21,405
Dividends Paid					
Cash dividends to common stockholders ⁽¹⁾	\$ 33,450	\$ 31,026	\$ 28,579	\$ 26,542	\$ 25,061
Cash dividends per share	\$ 1.88	\$ 1.77	\$ 1.68	\$ 1.60	\$ 1.56
Balance Sheet Data					
Real estate investments (net of accumulated depreciation)	\$ 774,718	\$ 657,258	\$ 627,651	\$ 567,417	\$ 501,388
Total assets	853,873	727,443	700,537	631,469	583,396
Total debt, including accrued interest	570,184	535,319	525,125	484,902	455,925
Preferred stock	179,328	100,000	100,000	100,000	100,000
Total stockholders' equity (deficit)	224,920	148,779	132,091	111,414	100,964
Other Data					
Cash flow provided by (used in):					
Operating activities	\$ 73,101	\$ 71,197	\$ 62,174	\$ 58,674	\$ 50,686
Investing activities	(115,070)	(52,036)	\$ (65,699)	\$ (73,805)	\$ (113,467)
Financing activities	49,210	(21,457)	\$ 3,579	\$ (10,423)	\$ 51,098
Funds from operations ⁽²⁾					
Net income	\$ 39,694	\$ 36,703	\$ 32,680	\$ 29,227	\$ 26,174
Minority Interests	7,972	8,818	7,793	7,798	8,105
Real estate depreciation and amortization	29,783	26,464	25,648	24,197	21,324
Gain on property dispositions	(1,301)	(139)	–	–	(572)
Funds from operations	76,148	71,846	66,121	61,222	55,031
Preferred dividends	(13,453)	(8,000)	(8,000)	(8,000)	(8,000)
Funds from operations available to common shareholders	\$ 62,695	\$ 63,846	\$ 58,121	\$ 53,222	\$ 47,031

(1) For the years 2008, 2007, 2006, 2005 and 2004, shareholders reinvested \$3,941, \$18,725, \$14,842, \$15,330 and \$13,774, in newly issued common stock by operation of the Company's dividend reinvestment plan, respectively.

(2) Funds from operations (FFO) is a non-GAAP financial measure. For a definition of FFO, see page 25.

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 15, discusses the Company's results of operations for the past two years. Beginning on page 19, 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. Finally, on page 25, 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.

The MD&A should be read in conjunction with the other sections of this Annual Report, including the consolidated financial statements and notes thereto, and Risk Factors included in Item 1A of the Form 10-K. Historical results set forth in Selected Financial Information and the Financial Statements 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 investments.

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.

In light of the current capital constrained market, management believes acquisition and development opportunities for investment in existing and new shopping center and office properties are limited. However, management believes that the Company is positioned to take advantage of these opportunities when market conditions change because of its conservative capital structure. It is management's view that several of the sub-markets in which the Company operates have very attractive supply/demand characteristics. The Company will continue to evaluate acquisition, development and redevelopment as an integral part of its overall business plan.

Although there has been a downturn in the national real estate market, to date, the effects on the office and retail markets in the metropolitan Washington, D.C. area, where the majority of the Company's properties are located, have been less severe. However, continued deterioration in the local economies where the Company's properties are located may lead to increased tenant bankruptcies, increased vacancies and decreased rental rates.

With a severe decline in overall consumer spending, retailers continue to struggle with declining sales and limited access to capital. Store closings are on the increase and retailers expanding their store count have disappeared. Vacancies have increased from a year ago. Our overall portfolio leasing percentage ended the year at 94.2%, a decrease from 95.3% at year end 2007. Weakness was largely centered in small shop closures in both our Loudoun County, Virginia and Florida shopping centers. Small in-line restaurants were particularly hard hit, although consumer's spending at grocery stores increased by 2% in 2008 at our 28 grocery stores which reported sales.

In addition, because of the Company's conservative capital structure, the Company has not been significantly affected by the recent turmoil in the credit markets. First, the Company maintains a ratio of total debt to total assets of under 50%, which allows the Company to obtain additional secured borrowings if necessary. Second, as of December 31, 2008, fixed rate debt represented approximately 97% of the Company's notes payable, thus minimizing the effect of increased interest rates on the Company's financial condition. Third, the Company's earliest significant fixed rate debt maturity is not until 2011. Finally, as of December 31, 2008, the Company has loan availability of more than \$149,000,000 on its \$150,000,000 unsecured revolving line of credit.

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 and the southeastern region of the United States, 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 addition to investing in properties in the Washington, DC/Baltimore metropolitan area, from 2006 through 2008, the Company also acquired a grocery-anchored neighborhood shopping center in Florida, totaling 102,000 square feet and a grocery-anchored neighborhood shopping center in Georgia totaling 88,000 square feet.

CRITICAL ACCOUNTING POLICIES

The Company's accounting policies are in conformity with U.S. generally accepted accounting principles ("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 the notes to the Consolidated Financial Statements.

Real Estate Investments

Real estate investment properties are stated at historic cost basis less depreciation. The Company intends to own its real estate investment properties over a long-term. No real estate investment properties have been sold since the Company's formation in 1993. Management believes that these assets have generally appreciated in value since their acquisition 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 U.S. GAAP, they do not report the current value of the Company's 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 above and 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 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.

If there is an event or change in circumstance that indicates an impairment in the value of a real estate investment property, the Company prepares an impairment analysis to assess that the carrying value of the real estate investment property does not exceed its estimated fair value. The Company considers both quantitative and qualitative factors including recurring operating losses, significant decreases in occupancy, and significant adverse changes in legal factors and business climate. If impairment indicators are present the Company performs a comparison of the projected cash flows of the property over its remaining useful life, on an undiscounted basis, to the carrying value of that property. The Company assesses its undiscounted projected cash flows based upon estimated capitalization rates, historic operating results and market conditions that may affect the property. If such carrying value is greater than the undiscounted projected cash flows, the Company would recognize an impairment loss equivalent to an amount required to adjust the carrying amount to its then estimated fair market value. The value of any property is sensitive to the actual results of any of the aforementioned estimated factors, either individually or taken as a whole. Should the actual results differ from management's projections, the valuation could be negatively or positively affected.

When incurred, the Company capitalizes the cost of improvements that extend the useful life of property and equipment. All repair and maintenance expenditures are expensed when incurred. In addition, we capitalize leasehold improvements when certain criteria are met, including when we

supervise construction and will own the improvement. Tenant improvements we own are depreciated over the life of the respective lease or the estimated useful life of the improvements, whichever is shorter.

Interest, real estate taxes, development related salary costs 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.

Deferred Leasing 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. Deferred 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 successful 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. In addition, deferred leasing costs include amounts attributed to in-place leases associated with acquisition properties as determined pursuant to the application of SFAS No.141.

Revenue Recognition

Rental and interest income is accrued as earned except when doubt exists as to collectibility, in which case the accrual is discontinued. Recognition of rental income commences when

control of the space has been given to the tenant. 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 revenue, known as percentage rent, is accrued when a tenant reports sales that exceed a specified breakpoint specified in the lease agreement.

Allowance for Doubtful Accounts – Current and Deferred Receivables

Accounts receivable primarily represent amounts accrued and unpaid from tenants in accordance with the terms of the respective leases, subject to the Company's revenue recognition policy. 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 its 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, 2008	2007	2006	2008 to 2007	2007 to 2006
Base rent	\$ 124,999	\$ 118,806	\$ 110,121	5.2%	7.9%
Expense recoveries	29,066	26,090	22,636	11.4%	15.3%
Percentage rent	1,509	1,497	1,767	0.8%	(15.3)%
Other	4,771	4,192	3,454	13.8%	21.4%
Total revenue	\$ 160,345	\$ 150,585	\$ 137,978	6.5%	9.1%

Note: (Dollars in thousands) Base rent includes \$753, \$1,672 and \$2,089, for the years 2008, 2007 and 2006, respectively, to recognize base rent on a straight-line basis. In addition, base rent includes \$1,445, \$472 and \$408, for the years 2008, 2007 and 2006, respectively, to recognize income from the amortization of in-place leases in accordance with SFAS No. 141.

Total revenue increased 6.5% for the 2008 year compared to 2007 primarily due to (1) the contribution of operating revenue from three operating properties acquired during 2008 (Great Falls Center, BJ's Wholesale Club and Marketplace at Sea Colony), an operating property acquired July 2007 (Orchard Park) and a development property (Ashland Square, Phase I) placed in service during the fourth quarter of 2007 together defined as the "2008/2007 Development and Acquisition Properties" whose operating results are included in 2008's operating income but not fully in the previous year's results. The 2008/2007 Development and Acquisition Properties contributed \$4,943,000 or 50.6% of the increase in revenue. Also contributing to the 2008 revenue increase was a revenue increase of \$1,575,000 or 16.1% from the stabilization of Lansdowne Town Center. The balance of 2008's revenue growth resulted from rental rate growth, increased parking revenue and increased lease termination fees in the remainder of the Company's Current Portfolio Properties (the "Core Properties").

Total revenue increased 9.1% for the 2007 year compared to 2006 primarily due to (1) the contribution of operating revenue from three development properties (Lansdowne Town Center, Broadlands Village III and Ashland Square Phase I) and an acquisition property (Orchard Park) placed in service during 2007 and two operating properties acquired during 2006, (Hunt Club Corners and Smallwood Village Center) together defined as the "2007/2006 Development and Acquisition Properties" whose operating results are included in 2007's operating income but not fully in the previous year's results. The 2007/2006 Development and Acquisition Properties contributed \$7,013,000 or 55.6% of the increase in revenue. Also contributing to the 2007 revenue increase was rental rate growth in the remainder of the Company's Core Properties and increased lease termination fees. A discussion of the components of revenue follows.

Base Rent

The \$6,193,000 increase in base rent for 2008 versus 2007 was primarily attributable (68.8% or approximately \$4,258,000) to leases in effect at the 2008/2007 Development and Acquisition Properties and the stabilization of Lansdowne Town Center (18.1% or approximately \$1,123,000). The balance of the increase was provided by rental rate growth in the Core Properties, particularly Southdale, Seven Corners and Leesburg Pike shopping centers, offset in part by base rent decreases at Broadlands Village, South Dekalb Plaza and Ashburn Village resulting from tenant vacancies.

The \$8,685,000 increase in base rent for 2007 versus 2006 was primarily attributable (68.5% or approximately \$5,950,000) to leases in effect at the 2007/2006 Development and Acquisition Properties. New leases at higher base rental rates than the predecessor leases at certain other properties accounted for the balance of the increase.

Expense Recoveries

Expense recoveries represent a portion of property operating expenses billable to tenants, including common area maintenance, real estate taxes and other recoverable costs. The largest single contributor to the \$2,976,000 increase in expense recovery income in 2008 compared to 2007, resulted from billings to tenants for their share of increased real estate tax expense in the Core Properties (58.0% or approximately \$1,727,000). The operation of the 2008/2007 Development and Acquisition Properties (21.5% or approximately \$639,000) and property operating expenses (20.5% or approximately \$610,000) throughout the Core Properties accounted the balance of the increase.

The largest portion of the \$3,454,000 increase in expense recovery income from 2006 to 2007 resulted from recovery of increased real estate tax resulting from higher assessed valuations in the Core Properties, and to a lesser extent the payment of taxes at 2007/2006 Development and Acquisition Properties (40.6% or approximately \$1,402,000). Increased property operating expenses, particularly snow removal costs, at the Core Properties (39.4% or approximately \$1,360,000) and 2007/2006 Development and Acquisition Properties (20.0% or approximately \$692,000) contributed to the balance of the increase.

Percentage Rent

Percentage rent is rental revenue calculated on the portion of a tenant's sales revenue that exceeds a specified breakpoint. Percentage rent increased slightly for 2008 compared to 2007.

Percentage rent decreased \$270,000 in 2007 versus 2006 primarily as a result of timing differences in the submission of sales reports used to calculate percentage rent by two retail tenants (50.7% or approximately \$137,000, each).

Other Revenue

Other revenue consists primarily of parking revenue at three of the Office Properties, temporary lease rental income, payments associated with early termination of leases and interest income from the investment of cash balances. The increase in other revenue for 2008 compared to 2007 resulted primarily from increased parking revenue primarily at 601 Pennsylvania Avenue (38.2% or approximately \$221,000), increased lease termination fees (29.7% or approximately \$172,000), and interest income resulting from the investment of increased cash balances (23.7% or approximately \$137,000).

Other revenue increased \$738,000 during 2007 versus 2006 as a result of increased lease termination fees (62.3% or approximately \$460,000), increased interest income from short-term investments (16.3% or approximately \$120,000), and increased parking revenue in the office portfolio (11.7% or approximately \$86,000).

Operating Expenses					
(Dollars in thousands)	For the year ended December 31,			Percentage Change	
	2008	2007	2006	2008 to 2007	2007 to 2006
Property operating expenses	\$ 19,877	\$ 18,758	\$ 16,278	6.0%	15.2%
Provision for credit losses	1,113	376	400	196.0%	(6.0)%
Real estate taxes	16,608	14,084	12,503	17.9%	12.6%
Interest expense and amortization of deferred debt	34,278	33,855	32,534	1.2%	4.1%
Depreciation and amortization	29,783	26,464	25,648	12.5%	3.2%
General and administrative	12,321	11,666	10,142	5.6%	15.0%
Total operating expenses	\$ 113,980	\$ 105,203	\$ 97,505	8.3%	7.9%

Property Operating Expenses

Property operating expenses consist primarily of repairs and maintenance, utilities, payroll, insurance and other property related expenses. The largest single item contributing to the \$1,119,000 increase in 2008 property operating expenses compared to the 2007 year was utility expense in the Core Properties (41.4% or approximately \$463,000), a 10.8% increase over the prior year's amount. The operation of the 2008/2007 Development and Acquisition Properties contributed 32.3% or approximately \$361,000. The balance of the 2008 increase represents a 2.0% increase in repairs and maintenance, payroll, insurance and other property related expenses for the Core Properties.

The \$2,480,000 increase in 2007 versus 2006 property operating expenses was caused primarily by the operation of the 2007/2006 Development and Acquisition Properties (47.9% or approximately \$1,188,000) and increased snow removal costs due to winter storms experienced during the 2007 year (22.1% or approximately \$549,000). The balance of the increase represents a 4.9% increase in property operating expenses for the Core Properties.

Provision for Credit Losses

The provision for credit losses represents the Company's estimation that amounts previously included in income and owed by tenants may not be collectible. The largest contributor to the \$737,000 credit loss increase in 2008 versus 2007 was a provision established for a rent dispute with a major tenant (55.5% or approximately \$409,000). The Company established credit loss reserves for tenant rents receivable, the majority of which were independent, small shop retailers, primarily at the Company's Loudoun County, Northern Virginia shopping centers. The provision for credit losses of approximately seven tenths of one percent (0.7%) and three tenths of one percent (0.3%), of total revenue for 2008 and 2007, respectively, reflects the deteriorating impact of the declining housing conditions and frozen credit market.

The provision for credit losses was virtually unchanged from the prior year, a decrease of \$24,000 for 2007 versus 2006. The provision for credit losses is less than three tenths of one percent (0.3%) of total revenue for each year, a reflection of the relative credit quality of the Company's tenants.

Real Estate Taxes

The \$2,524,000 increase in real estate taxes for 2008 versus 2007 was primarily due to a same property shopping center increase of \$1,619,000 (64.1% of total real estate tax increase), a 16.5% increase over 2007's amount, impacted largely by increased expense at several of the Company's Northern Virginia shopping centers. The Office Properties, particularly Van Ness Square and 601 Pennsylvania Avenue, contributed toward the increase (22.3% or approximately \$564,000), a 13.6% increase over 2007's amount, as well as the 2008/2007 Development and Acquisition Properties (13.6% or approximately \$341,000).

The \$1,581,000 increase in real estate taxes for 2007 versus 2006 was largely impacted by an increased value assessment at 601 Pennsylvania Avenue (35.8% or approximately \$566,000). The 2007/2006 Development and Acquisition Properties also contributed to the increase (24.0% or approximately \$380,000). In addition, several of the Company's properties (Ashburn Village, Beacon Center, Countryside, The Glen and White Oak) received increases in assessed values during 2007 resulting in increased tax expense (together 28.3% or approximately \$447,000).

Interest and Amortization of Deferred Debt

Interest expense increased \$423,000 in 2008 versus 2007 due to increased borrowing for the 2008/2007 Development and Acquisition Properties offset in part by increased capitalized interest on development projects. Average outstanding borrowing increased approximately \$35,785,000 (average fixed rate borrowings increased approximately \$38,678,000 while average variable rate borrowings (revolving credit line and construction loans) decreased approximately \$2,893,000). The new borrowing reduced the average interest rate by approximately 0.13%. The combined impact of the new

borrowings, at a lower average rate, resulted in an approximately \$1,700,000 increase in interest expense. Interest capitalized as a cost of construction and development projects increased during 2008 compared to 2007 which resulted in a decrease of interest expense by approximately \$1,270,000 (\$4,159,000 versus \$2,889,000) resulting primarily from construction activity at Clarendon Center, Northrock and Westview Village. Increased deferred debt cost amortization increased interest expense by approximately \$13,000 (\$1,162,000 versus \$1,149,000).

Interest expense increased \$1,261,000 and deferred debt cost amortization increased \$60,000 in 2007 versus 2006. Interest expense increased primarily due to the placement of a new permanent 15-year fixed rate mortgage on Lansdowne Town Center. During 2006, interest on Lansdowne's construction borrowings were capitalized while those dollars were largely expensed in 2007 as the property became fully operational. On a portfolio wide basis, the average outstanding borrowings from 2006 to 2007 increased approximately \$13,000,000 (approximately \$871,000 increase in interest expense). Additionally, interest capitalized as a cost of construction and development projects decreased during 2007 compared to 2006 (\$784,000 increase in interest expense). The change in capitalized interest is the equivalent of approximately \$11,500,000 in construction borrowings converted to operating property debt. Offsetting these increases in interest expense was an approximately 8 basis point decrease in the average interest rate for the loan portfolio resulting from Lansdowne's permanent mortgage rate being lower than the variable rate borrowings the permanent loan replaced (\$394,000 decrease in interest expense). Deferred debt cost amortization expense was \$1,149,000 and \$1,089,000, for the 2007 and 2006 periods, respectively, (\$60,000 increase in interest expense).

Depreciation and Amortization

The \$3,319,000 increase in depreciation and amortization of deferred leasing costs resulted primarily from asset retirements in conjunction with the redevelopment of Smallwood Village Center and Clarendon Center development (42.4% or approximately \$1,406,000) and the commencement of depreciation on the 2008/2007 Development and Acquisition Properties placed in service during the preceding twelve months (22.0% or approximately \$729,000). The write-off of deferred leasing costs and undepreciated leasehold improvements from tenants terminating their leases prior to their contractual lease expiration dates contributed to the increase in depreciation and amortization of deferred leasing costs.

The \$816,000 increase in depreciation and amortization expense resulted primarily from the 2007/2006 Development and Acquisition Properties placed in service during 2007 and 2006, and reflects the Company's reduced level of acquisition activity compared to the 2004 and 2005 years.

General and Administrative

General and administrative expenses consists of payroll, administrative and other overhead expenses. The \$655,000 increase in general and administrative expenses for 2008 compared to 2007 resulted from increased staff expenses (88.9% or approximately \$582,000) and real estate tax on land held for investment (31.0% or approximately \$203,000), offset in part by reduced professional fees.

The \$1,524,000 increase in general and administrative expenses for 2007 versus 2006 was largely attributable to increased payroll and employee benefit expenses for staff over 2006 levels and to the addition of several new administrative staff members (49.1% or approximately \$748,000), the write-off of costs related to an abandoned acquisition of a land parcel (31.8% or approximately \$484,000) and an increase in non-cash expense related to the issue of options to the Company's directors and officers (19.4% or approximately \$296,000).

Gain on Property Disposition

In 2008, the Company recognized a gain of approximately \$1,096,000, arising from insurance proceeds related to minor fire damage sustained at two shopping centers. The insurance proceeds are expected to fund substantially all of the restoration. The gain recognized was measured as the difference between insurance proceeds and the depreciated carrying value of the assets replaced. Additionally, the Company recognized a gain on property dispositions of approximately \$205,000 representing proceeds from an insurance settlement for HVAC units vandalized at the Company's West Park shopping center in Oklahoma City, Oklahoma.

The Company recognized a gain on the disposition of real estate of \$139,000 in 2007. The 2007 gain represents additional condemnation proceeds recognized 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. Original proceeds from the condemnation were received in 2004. There were no property dispositions in 2006.

Impact of Inflation

Inflation has remained relatively low during 2008 and 2007, with the exception of energy costs which fluctuated widely during 2008. Rising energy prices caused increases in utility expense, primarily gas and electric costs. The impact of rising operating expenses on the operating performance of the Company's portfolio however, has been mitigated by terms of substantially all of the Company's leases which contain provisions designed to increase revenues to offset 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.

In addition, substantially all of the Company's properties are leased to tenants under long-term leases, which provide for reimbursement of operating expenses by tenants. These 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 \$13,006,000 and \$5,765,000 at December 31, 2008 and 2007, respectively. The changes in cash and cash equivalents during the years ended December 31, 2008 and 2007 were attributable to operating, investing and financing activities, as described below.

(Dollars in thousands)	Year Ended December 31,	
	2008	2007
Cash provided by operating activities	\$ 73,101	\$ 71,197
Cash used in investing activities	(115,070)	(52,036)
Cash provided by (used in) financing activities	49,210	(21,457)
Increase (decrease) in cash	\$ 7,241	\$ (2,296)

Operating Activities

Cash provided by operating activities increased \$1,904,000 to \$73,101,000 for the year ended December 31, 2008 compared to \$71,197,000 for the year ended December 31, 2007 primarily reflecting increased operating income of the 2008/2007 Development and Acquisition Properties as well as positive contributions from the core portfolio. 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 \$63,034,000 to \$115,070,000 for the year ended December 31, 2008 compared to \$52,036,000 for the year ended December 31, 2007. Investing activities for 2008 primarily reflects the acquisition of properties (Great Falls Center, BJ's Wholesale Club and Marketplace at Sea Colony), the construction of new and renovated shopping center properties (Clarendon Center, Northrock and Westview Village developments and the Smallwood Village Center and Boulevard renovations), tenant improvements and property capital expenditures throughout the portfolio. Investing activities for 2007 primarily reflects the development and construction of new properties (Lansdowne Town Center, Ashburn Village V, Ashland Square and Clarendon Center), the acquisition of properties (Orchard Park and the

Westview land parcel), other construction in progress, tenant improvements and property capital expenditures throughout the portfolio. Tenant improvement and property capital expenditures totaled \$9,986,000 and \$7,302,000, for 2008 and 2007, respectively.

Financing Activities

Cash provided by financing activities for the year ended December 31, 2008 was \$49,210,000 and cash used by financing activities for the year ended December 31, 2007 was \$21,457,000. Cash provided by financing activities for the year ended December 31, 2008 primarily reflects:

- proceeds from the issuance of Series B preferred stock (net of issuance costs) totaling \$76,321,000;
- amounts borrowed from the revolving credit facility totaling \$19,000,000;
- proceeds received from five new mortgage notes payable totaling \$49,005,000; and
- \$4,543,000 of proceeds received from the issuance of common stock under the dividend reinvestment program and from the exercise of stock options;

which was partially offset by:

- the scheduled repayment (amortization) of mortgage notes payable totaling \$16,585,000;
- the repayments of the revolving credit facility totaling \$27,000,000;
- distributions made to common stockholders and holders of convertible limited partnership units in the Operating Partnership during the year totaling \$43,633,000;
- distributions made to preferred stockholders during the year totaling \$11,668,000; and
- payments of \$773,000 for financing costs of five new mortgage loans during 2008.

Cash used in financing activities for the year ended December 31, 2007 primarily reflects:

- the repayment of borrowings on mortgage notes payable totaling \$14,717,000;
- amounts repaid under the revolving credit facility totaling \$47,000,000;
- distributions made to common stockholders and holders of convertible limited partnership units in the Operating Partnership during the year totaling \$40,613,000;
- distributions made to preferred stockholders during the year totaling \$8,000,000; and
- payments of \$2,085,000 for financing costs of the revolving credit facility and two mortgage loans during 2005.

which was partially offset by:

- \$52,000,000 of proceeds received from mortgage notes payable incurred during the year;
- amounts borrowed from the revolving credit facility totaling \$20,000,000; and
- \$18,958,000 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.

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 consist 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 redevelop certain of the Current Portfolio Properties,
- may develop additional freestanding outparcels or expansions within certain of the Shopping Centers,
- will continue to develop its construction in progress properties.

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, 2008, the Company had unfunded contractual payment obligations of approximately \$75.1 million, excluding operating obligations, due within the next 12 months. The table below specifies the total contractual payment obligations as of December 31, 2008.

Contractual Obligations					
(Dollars in thousands)	Payments Due By Period				
	Total	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Notes Payable	\$ 567,495	\$ 18,054	\$ 121,729	\$ 160,059	\$ 267,653
Operating Leases (1)	11,101	165	342	352	10,242
Corporate Headquarters Lease (1)	2,638	807	1,688	143	—
Development Obligations	115,831	56,081	59,750	—	—
Total Contractual Cash Obligations	\$ 697,065	\$ 75,107	\$ 183,509	\$ 160,554	\$ 277,895

(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 cash flow from operations and its capital resources, which at December 31, 2008 included cash balances of \$13.0 million, borrowing availability of approximately \$150.0 million on its revolving line

of credit and borrowing availability of approximately \$160.0 million on its two construction loans will be sufficient to meet its contractual obligations for the foreseeable future.

Preferred Stock Issues

On March 20, 2008, the Company filed a shelf registration statement with the SEC relating to the future offering of up to an aggregate of \$140 million of preferred stock and depositary shares. On March 27, 2008, the Company sold 3,000,000 depositary shares, each representing 1/100th of a share of 9% Series B Cumulative Redeemable Preferred Stock, providing net cash proceeds of \$72.1 million. The underwriters exercised an over-allotment option, purchasing an additional 173,115 depositary shares providing additional net cash proceeds of \$4.2 million.

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 March 15, 2013. The depositary shares will pay an annual dividend of \$2.25 per share, equivalent to 9% of the \$25.00 liquidation preference. The first dividend was paid on July 15, 2008 and covered the period from March 27, 2008 through June 30, 2008. The Series B 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.

Net proceeds from the issuance of approximately \$76.3 million were used to fully repay \$22.0 million then outstanding under the Company's revolving credit facility and approximately \$31.5 million was used to acquire three operating shopping center properties on March 28, 2008 (\$61.1 million acquisition cost less financing proceeds of \$29.6 million from loans secured by the acquisition properties). The remaining \$22.8 million was initially invested in short-term certificates of deposit and subsequently used to fund certain of the Company's development and redevelopment projects.

On July 16, 2003, the Company filed a 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 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 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 74,215 and 381,662 shares under the Plan at a weighted average discounted price of \$47.44 and \$48.11 per share during the years ended December 31, 2008 and 2007, respectively. The Company also credited 9,605 and 7,535 shares to directors pursuant to the reinvestment of dividends specified by the Directors' Deferred Compensation Plan at a weighted average discounted price of \$43.71 and \$49.13 per share, during the years ended December 31, 2008 and 2007, 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, 2008.

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.

The following is a summary of notes payable as of December 31, 2008 and 2007:

Notes Payable				
(Dollars in thousands)	December 31,		Interest Rate *	Scheduled Maturity *
	2008	2007		
Fixed rate mortgages:	\$ 78,489 (a)	\$ 83,078	8.00%	Dec-2011
	115,271 (b)	119,340	7.67%	Oct-2012
	10,846 (c)	11,022	6.12%	Jan-2013
	28,837 (d)	30,041	7.88%	Jan-2013
	7,919 (e)	8,131	5.77%	Jul-2013
	15,576 (f)	12,935	5.40%	May-2014
	18,987 (g)	11,930	7.45%	Jun-2015
	38,263 (h)	39,099	6.01%	Feb-2018
	43,413 (i)	44,495	5.88%	Jan-2019
	14,043 (j)	14,395	5.76%	May-2019
	19,391 (k)	19,878	5.62%	Jul-2019
	19,195 (l)	19,661	5.79%	Sep-2019
	17,165 (m)	17,601	5.22%	Jan-2020
	12,337 (n)	12,535	5.60%	May-2020
	11,576 (o)	11,858	5.30%	Jun-2020
	9,925 (p)	10,139	5.81%	Feb-2021
	6,791 (q)	6,884	6.01%	Aug-2021
	39,198 (r)	39,740	5.62%	Jun-2022
	11,817 (s)	11,964	6.08%	Sep-2022
	12,655 (t)	–	6.43%	Apr-2023
	16,571 (u)	–	6.19%	Feb-2024
Total fixed rate	548,265	524,726	6.67%	7.6 Years
Variable rate loan:				
Revolving credit facility	– (v)	8,000	LIBOR + 1.40%	Dec-2010
Northrock construction loan	12,817 (w)	–	LIBOR + 1.60%	May-2011
Clarendon construction loan	6,413 (x)	–	LIBOR + 2.50%	Nov-2011
Total variable rate	19,230	8,000	3.33%	2.4 Years
Total notes payable	\$ 567,495	\$ 532,726	6.56%	7.5 Years

* Interest rate and scheduled maturity data presented as of December 31, 2008. Totals computed using weighted averages.

(a) 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 final payment of \$63,153,000 at loan maturity. Principal of \$4,589,000 was amortized during 2008.

(b) 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 final payment of \$97,403,000 at loan maturity. Principal of \$4,069,000 was amortized during 2008.

(c) The loan is collateralized by Smallwood Village Center and requires equal monthly principal and interest payments of \$71,000 based upon a 30-year amortization schedule and a final payment of \$10,071,000 at loan maturity. Principal of \$176,000 was amortized during 2008.

(d) 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 final payment of \$22,961,000 at loan maturity. Principal of \$1,204,000 was amortized during 2008.

(e) 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 final payment of \$6,830,000 at loan maturity. Principal of \$212,000 was amortized during 2008.

- (f) The loan is collateralized by Seabreeze Plaza. During 2008, the Company increased the mortgage and borrowed an additional \$3,000,000. The combination of the original note and the 2008 note requires equal monthly principal and interest payments totaling \$102,000 based upon a weighted average 26-year amortization schedule and a final payment of \$13,278,000 is due at loan maturity. Principal of \$359,000 was amortized during 2008.
- (g) The loan is collateralized by Shops at Fairfax and Boulevard shopping centers. During 2008, the Company increased the mortgage and borrowed an additional \$7,500,000. The combination of the original note and the 2008 note required equal monthly principal and interest payments totaling \$156,000 based upon a weighted average 23-year amortization schedule and a final payment of \$15,168,000 is due at loan maturity. Principal of \$443,000 was amortized during 2008.
- (h) 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 final payment of \$28,012,000 at loan maturity. Principal of \$836,000 was amortized during 2008.
- (i) The loan, consisting of two notes dated December 2003 and two notes dated February and December 2004, is currently collateralized by three shopping centers, Broadlands Village (Phases I, II & III), The Glen and Kentlands Square, and requires equal monthly principal and interest payments of \$306,000 based upon a 25-year amortization schedule and a final payment of \$28,393,000 at loan maturity. Principal of \$1,082,000 was amortized during 2008.
- (j) 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 final payment of \$8,985,000 at loan maturity. Principal of \$352,000 was amortized during 2008.
- (k) 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 final payment of \$12,288,000 at loan maturity. Principal of \$487,000 was amortized during 2008.
- (l) The loan is collateralized by Briggs Chaney MarketPlace and requires equal monthly principal and interest payments of \$133,000 based upon a 25-year amortization schedule and a final payment of \$12,192,000 at loan maturity. Principal of \$466,000 was amortized during 2008.
- (m) 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 final payment of \$10,568,000 at loan maturity. Principal of \$436,000 was amortized during 2008.
- (n) The loan is collateralized by Boca Valley Plaza and requires equal monthly principal and interest payments of \$75,000 based upon a 30-year amortization schedule and a final payment of \$9,149,000 at loan maturity. Principal of \$198,000 was amortized during 2008.
- (o) The loan is collateralized by Palm Springs Center and requires equal monthly principal and interest payments of \$75,000 based upon a 25-year amortization schedule and a final payment of \$7,075,000 at loan maturity. Principal of \$282,000 was amortized during 2008.
- (p) The loan is collateralized by Jamestown Place and requires equal monthly principal and interest payments of \$66,000 based upon a 25-year amortization schedule and a final payment of \$6,102,000 at loan maturity. Principal of \$214,000 was amortized during 2008.
- (q) The loan is collateralized by Hunt Club Corners and requires equal monthly principal and interest payments of \$42,000 based upon a 30-year amortization schedule and a final payment of \$5,018,000 at loan maturity. Principal of \$93,000 was amortized during 2008.
- (r) The loan is collateralized by Lansdowne Town Center and requires equal monthly principal and interest payments of \$230,000 based upon a 30-year amortization schedule and a final payment of \$28,177,000 at loan maturity. Principal of \$542,000 was amortized during 2008.
- (s) The loan is collateralized by Orchard Park and requires equal monthly principal and interest payments of \$73,000 based upon a 30-year amortization schedule and a final payment of \$8,628,000 at loan maturity. Principal of \$147,000 was amortized during 2008.
- (t) The loan is collateralized by BJ's Wholesale Club and requires equal monthly principal and interest payments of \$80,000 based upon a 30-year amortization schedule and a final payment of \$9,305,000 at loan maturity. Principal of \$95,000 was amortized during 2008.
- (u) The loan, consisting of two notes dated February 2004 and April 2008, is collateralized by Great Falls Center. The 2004 note requires equal monthly principal and interest payments of \$83,000 based upon a 20-year amortization schedule. The 2008 note of \$6,525,000 requires interest only payments of \$37,000 based upon and interest rate of 6.8% until May 2009, at which time the loan requires equal monthly principal and interest payments of \$43,000 based upon a 30-year amortization schedule. Both loans mature February 1, 2024 at which time a final payment of \$1,378,000 will be due. Principal of \$303,000 was amortized during 2008.
- (v) The loan is an unsecured revolving credit facility totaling \$150,000,000. Interest expense during 2008 was calculated based upon the 1 month LIBOR rate plus a spread of 1.475% (reduced to 1.40% effective April 1, 2008) 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. Monthly payments, if applicable, are interest only and vary depending upon the amount outstanding and the applicable interest rate for any given month.
- (w) The loan is a secured construction loan facility totaling \$21,822,000 to fund the development of Northrock shopping center. Interest charges are funded by the construction loan and are calculated based upon the 1 month LIBOR rate plus a spread of 1.60%. The loan may be extended two years, at the Company's option, subject to the completion of construction and certain debt coverage requirements. Interest charges of approximately \$247,000 accrued and were capitalized as costs of construction during 2008.
- (x) The loan is a secured construction loan facility totaling \$157,500,000 to fund the development of Clarendon Center. Interest charges are funded by the construction loan and are calculated based upon the 1 month LIBOR rate plus a spread of 2.50%. The loan may be extended for two additional 9-month periods, subject to the satisfaction of certain conditions. Interest charges of approximately \$105,000 accrued and were capitalized as costs of construction during 2008.

The December 31, 2008 and 2007 depreciation adjusted cost of properties collateralizing the mortgage notes payable totaled \$693,205,000 and \$557,820,000, respectively. The Company's credit facility requires the Company and its subsidiaries to maintain certain financial covenants. As of December 31, 2008, the material covenants required the Company, on a consolidated basis, to:

- limit the amount of debt so as to maintain a gross asset value, as defined in the loan agreement, in excess of liabilities of at least \$600 million plus 90% of the Company's future net equity proceeds;
- limit the amount of debt as a percentage of gross asset value, as defined in the loan agreement, to less than 60% (leverage ratio);
- limit the amount of debt so that interest coverage will exceed 2.5 to 1 on a trailing 12-full calendar month basis;
- limit the amount of debt so that interest, scheduled principal amortization and preferred dividend coverage exceeds 1.6 to 1; and
- limit the amount of variable rate debt and debt with initial loan terms of less than five years to no more than 40% of total debt.

As of December 31, 2008, the Company was in compliance with all such covenants.

2008 Financing Activity

On February 29, 2008, the Company closed on a \$7,500,000 increase to a fixed-rate mortgage secured by Shops at Fairfax and Boulevard shopping centers. The loan matures June 1, 2015 (same as the original financing), requires monthly interest only payments of \$38,000, based upon a 6.08% interest rate, and requires a final principal payment of \$7,500,000 at maturity. The Company has initially guaranteed \$1,875,000 of this loan until the Boulevard redevelopment is completed and until certain debt service coverage tests are achieved.

On March 23, 2008, the Company closed on a \$3,000,000 increase to a fixed-rate mortgage secured by Seabreeze Plaza. The loan matures May 1, 2014 (same as the original financing), requires equal monthly principal and interest payments of \$17,794, based upon a 5.90% interest rate and 30-year principal amortization, and requires a final principal payment of approximately \$2,738,000 at maturity.

On March 28, 2008, the Company assumed a fully amortizing fixed-rate mortgage loan in the amount of approximately \$10,349,000, secured by the acquisition property, Great Falls Center. The loan matures February 1, 2024 and requires equal monthly principal and interest payments of \$83,113, based upon a 5.80% interest rate and 20-year principal amortization. Management determined the mortgage loan was fairly valued at acquisition because the terms of the loan were not materially different from current market terms.

On March 31, 2008, the Company closed on a new 15-year, fixed-rate mortgage loan in the amount of \$12,750,000, secured by the BJ's Wholesale Club center. The loan matures April 1, 2023, requires equal monthly principal and interest payments of \$80,003, based upon a 6.43% interest rate and 30-year principal amortization, and requires a final principal payment of approximately \$9,255,000 at maturity.

In April 2008, the Company closed on a \$10,825,000 additional financing secured by the Great Falls Center. Funding in the amount of \$6,525,000 occurred on April 6, 2008, payable at an interest rate of 6.80%, interest only for the first year, after which amortization will commence on a 30-year amortization schedule, requiring monthly payments of principal and interest totaling \$42,538. A final principal payment of approximately \$1,274,000 will be due at maturity on February 1, 2024. The Company has initially guaranteed \$2,000,000 of this loan, with the amount of any additional advance to also be guaranteed until certain debt service coverage tests are achieved. The balance totaling \$4,300,000 is a forward commitment to be funded prior to March 31, 2009, subject to achieving certain re-leasing requirements.

In May 2008, the Company closed on a \$21,822,000 secured construction loan, to fund the development of Northrock shopping center in Warrenton, Virginia. Funding in the amount of approximately \$6,495,000 occurred at closing. The loan accrues interest, payable at an interest rate of LIBOR plus 1.6%. The loan matures on May 1, 2011, with one 2-year extension option, exercisable at the Company's option subject to completion of improvements and certain debt service coverage requirements. The loan is 100% guaranteed by the Company until such time as the construction is complete, at which time the guarantee will be limited to 50% of the total principal outstanding. Approximately \$12,817,000 was outstanding as of December 31, 2008.

Also in May 2008, the Company closed a \$157,500,000 secured construction loan to finance the development of Clarendon Center, a mixed-use development adjacent to the Clarendon Metro station in Arlington, Virginia. The Company has guaranteed the loan, with the guarantee to be reduced subject to certain conditions related to pre-leasing, completion of construction and net operating income from the project. The loan accrues interest at an interest rate of LIBOR plus 2.5% and matures on November 14, 2011, which term may be extended by the Company for two additional 9-month periods, subject to the satisfaction of certain conditions. Approximately \$6,413,000 was outstanding as of December 31, 2008.

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, revenue or expenses, results of operations, liquidity, capital expenditures or capital resources.

FUNDS FROM OPERATIONS

In 2008, the Company reported Funds From Operations (FFO)¹ available to common shareholders (common stockholders and limited partner unitholders) of \$62,695,000 representing a 1.8% decrease compared to 2007 FFO available to common shareholders of \$63,846,000. The following table presents a reconciliation from net income to FFO available to common shareholders for the periods indicated:

Funds from Operations					
(Dollars in thousands)	2008	For the Year Ended December 31,			
		2007	2006	2005	2004
Net income	\$ 39,694	\$ 36,703	\$ 32,680	\$ 29,227	\$ 26,174
Subtract:					
Gain on property dispositions	(1,301)	(139)	–	–	(572)
Add:					
Minority interests	7,972	8,818	7,793	7,798	8,105
Real estate depreciation and amortization	29,783	26,464	25,648	24,197	21,324
FFO	76,148	71,846	66,121	61,222	55,031
Preferred dividends	(13,453)	(8,000)	(8,000)	(8,000)	(8,000)
FFO available to common shareholders	\$ 62,695	\$ 63,846	\$ 58,121	\$ 53,222	\$ 47,031
Average shares and units used to compute FFO per share	23,377	23,185	22,628	22,003	21,405

¹ The National Association of Real Estate Investment Trusts (NAREIT) developed FFO as a relative non-GAAP financial measure of performance of an equity REIT in order to recognize that income-producing real estate historically has not depreciated on the basis determined under GAAP. FFO is defined by NAREIT 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 Company's 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 a indicator of the Company's operating performance, or as an alternative to cash flows as a measure of liquidity. Management considers FFO a meaningful supplemental measure of operating performance because it primarily excludes the assumption that the value of the real estate assets diminishes predictably over time (i.e. depreciation), which is contrary to what we believe occurs with our assets, and because industry analysts have accepted it as a performance measure. 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: (i) may redevelop certain of the Current Portfolio Properties, (ii) may develop additional freestanding outparcels or expansions within certain of the Shopping Centers, and (iii) will continue to develop its construction in progress properties. 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, development, 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 Broadlands Village, Smallwood Village Center, Boulevard and Hunt Club Corners. The following describes the acquisitions, developments, redevelopments and renovations which affected the Company's financial position and results of operations in 2008, 2007 and 2006.

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 1,700 acre planned community consisting of 3,500 residences, approximately 90% of which are constructed and 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. Construction of a 30,000 square foot second phase was substantially completed in 2004. The Company's total development costs of both phases, including the land acquisition, were approximately \$22 million. During the second quarter of 2006, the Company substantially completed construction of a third phase of this development, totaling approximately 22,000 square feet of shop space and two pad site locations. Development costs for this phase totaled approximately \$7.1 million. The center was 89.3% leased and fully operational at December 31, 2008.

Ashland Square

On December 15, 2004, the Company acquired a 19.3 acre parcel of land in Manassas, Prince William County, Virginia for a purchase price of \$6.3 million. The Company has plans to develop the parcel into a grocery-anchored neighborhood shopping center. The Company received site plan approval during the third quarter of 2006 to develop approximately 125,000 square feet of retail space. A site plan for an additional 35,000 square feet of commercial space is under review by Prince William County. During the fourth quarter of 2007, the Company completed preliminary site work consisting of clearing, grading and site utility construction. A ground lease has been executed with Chevy Chase Bank, which built a branch on a pad site. The bank branch opened for business October 2007. The balance of the center is being marketed to grocers and other retail businesses, with a development timetable yet to be finalized.

New Market

On March 3, 2005, the Company acquired a 7.1 acre parcel of land located in New Market, Maryland for a purchase price of \$500,000. On September 8, 2005, the Company acquired a 28.4 acre contiguous parcel for a purchase price of \$1.5 million. Together, these parcels will accommodate a neighborhood shopping center development in excess of 120,000 square feet of leasable space. The Company had contracted to purchase one additional parcel with the intent to assemble additional acreage for further retail development near this I-70 interchange, east of Frederick, Maryland. During December 2007, the Company abandoned the acquisition of this final parcel and wrote-off to general and administrative expense all costs related to this parcel.

Lansdowne Town Center

During the first quarter of 2005, the Company received approval of a zoning submission to Loudoun County which allowed the development of a neighborhood shopping center named Lansdowne Town Center, within the Lansdowne Community in northern Virginia. On March 29, 2005, the Company finalized the acquisition of an additional 4.5 acres of land to bring the total acreage of the development parcel to 23.4 acres (including the 18.9 acres acquired in 2002). The additional purchase price was approximately \$1.0 million. In late 2006, the Company substantially completed construction of an approximately 189,000 square foot retail center. A lease was executed with Harris Teeter for a 55,000 square foot grocery store, which opened in November 2006. Project costs totaled approximately \$41.5 million. As of December 31, 2008, the project was fully operational and 98.5% leased.

Smallwood Village Center

On January 27, 2006, the Company acquired the 198,000 square foot Smallwood Village Center, located on 25 acres within the St. Charles planned community of Waldorf, Maryland. The center was acquired for a purchase price of \$17.5 million subject to the assumption of an \$11.3 million mortgage loan, and was 77.1% leased at December 31, 2008. The Company commenced construction during the first quarter of 2008 on a capital improvement project to improve access to the center, reconfigure portions of the center and upgrade the center's façade and common areas. The redeveloped center will total approximately 173,000 square feet. Substantial completion is projected in the first quarter of 2009. Project costs are expected to total approximately \$6.8 million.

Hunt Club Corners

On June 1, 2006, the Company completed the acquisition of the 101,500 square foot Publix-anchored Hunt Club Corners shopping center located in Apopka, Florida (metropolitan Orlando). The center was 95% leased at December 31, 2008 and was acquired for a purchase price of \$11.1 million. The Company completed a façade renovation of Hunt Club Corners during 2008 for a total cost of approximately \$0.9 million.

Clarendon Center

The Company owns an assemblage of land parcels (including its Clarendon and Clarendon Station operating properties) totaling approximately 1.5 acres adjacent to the Clarendon Metro station in Arlington, Virginia. In June 2006, the Company obtained zoning approvals for a mixed-use development project to include up to approximately 45,000 square feet of retail space, 170,000 square feet of office space and 244 residential units. The total development costs are expected to be approximately \$195.0 million, a portion of which will be funded with the \$157.5 million construction loan that the Company closed in May 2008. Pouring of the concrete base and lower parking levels is continuing on the southern block of the two parcels. Both tower cranes have been erected. Demolition of the northern block was completed and excavation commenced in October 2008. The Company estimates substantial completion of shell construction in late 2010.

Westview Village

In November 2007, the Company purchased a 10.4 acre site in the Westview development on Buckeystown Pike (MD Route 85) in Frederick, Maryland. The purchase price was \$5.0 million. The Company has commenced building construction for Westview Village shopping center, a neighborhood shopping center totaling approximately 105,000 square feet of commercial space, comprised of 60,000 square feet of retail shop space, 15,000 square feet of retail pads and 30,000 square feet of professional office space. The Company is currently marketing the space and has executed leases for 19,673 square feet, or 26% of the total retail space. The Company commenced construction in early 2008 and anticipates total construction and development costs, including land, to be

approximately \$26.5 million. Substantial completion of the building shell is scheduled for the first quarter of 2009.

Great Eastern Plaza Land Parcel

On June 6, 2007, the Company acquired 8.0 acres of undeveloped land adjacent to its Great Eastern Plaza shopping center in District Heights, Maryland, for a purchase price of \$1.3 million. The Company is analyzing options to expand the existing shopping center onto this parcel at some future date.

Orchard Park

On July 19, 2007, the Company completed the acquisition of the 88,000 square foot Kroger-anchored Orchard Park shopping center located in Dunwoody, Georgia. The center is 92.5% leased as of December 31, 2008 and was acquired for a purchase price of \$17.0 million.

Northrock

In January 2008, the Company acquired approximately 15.4 acres of undeveloped land in Warrenton, Virginia, located at the southwest corner of the U. S. Route 29/211 and Fletcher Drive intersection. The Company has commenced building construction for Northrock shopping center, a neighborhood shopping center totaling approximately 103,000 square feet of leasable area. Approximately 62% of the project is pre-leased as of December 31, 2008. The Harris Teeter supermarket chain has executed a lease for a 52,700 square foot grocery store to anchor the center. Additionally, the Company has executed a lease with Chevy Chase Bank for a pad building and has executed leases for 7,896 square feet of shop space. The land purchase price was \$12.5 million, and the Company anticipates total construction and development costs, including land, to be approximately \$27.9 million. A portion of these total development costs will be funded with the \$21.8 million construction loan the Company closed in May 2008. Substantial completion of construction is anticipated for the spring of 2009.

Great Falls Center

On March 28, 2008, the Company completed the acquisition of the Safeway-anchored Great Falls Center located in Great Falls, Virginia. The center was 94.9% leased at December 31, 2008 and was acquired for a purchase price of \$36.6 million, subject to the assumption of a \$10.3 million mortgage loan.

BJ's Wholesale Club

On March 28, 2008, the Company completed the acquisition of the single tenant property anchored by BJ's Wholesale Club, located in Alexandria, Virginia. The center was 100% leased at December 31, 2008 and was acquired for a purchase price of \$21.0 million.

Marketplace at Sea Colony

On March 28, 2008, the Company completed the acquisition of Marketplace at Sea Colony, located in Bethany Beach, Delaware. The center was 100% leased at December 31, 2008 and was acquired for a purchase price of \$3.0 million.

Boulevard

During the second quarter of 2008, permits were issued for the redevelopment of a portion of the Boulevard shopping center located in Fairfax, Virginia. A vacant pad building totaling approximately 18,800 square feet and previously occupied by a furniture store has been demolished. The center's in-line shop space will be expanded by approximately 8,000 square feet for

small shop retail and a new pad building will replace the demolished structure. A ground lease has been executed with Chevy Chase Bank for the pad building, and a total of 3,040 square feet, or 38.2% of the small shop space is leased to two tenants. The Company anticipates total construction and development costs to be approximately \$2.8 million, with substantial completion anticipated in the first quarter of 2009.

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
2008	45	5	6,988,000	1,206,000	93.9%	95.8%
2007	43	5	6,803,000	1,206,000	95.3%	95.2%
2006	42	5	6,698,000	1,206,000	96.1%	97.3%

The 2008 same property leasing percentages decreased due to a net decrease of approximately 99,000 square feet of leased space. The largest contributor to the leasing decrease, approximately 29,000 square feet, occurred at South Dekalb Plaza in Atlanta, Georgia. Leasing also decreased approximately 14,000 square feet at Village Center, approximately 13,000 square feet at Broadlands Village and approximately 10,000 square feet at Ashburn Village, located in the Northern Virginia

suburbs of Washington, DC. The 2007 leasing percentages decreased due to a net 67,000 square foot decrease in leased space, 42,000 in the shopping center portfolio and 25,000 in the office portfolio. The shopping center decrease in leased space occurred due to a 22,000 square foot decrease at Smallwood Village, prior to the Company's 2008 redevelopment and a 20,000 square foot decrease at South Dekalb Plaza.

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 assessment, the Company's management has concluded that, as of December 31, 2008,

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 30 in this Annual Report.

Board of Directors and Stockholders
Saul Centers, Inc.

We have audited Saul Centers, Inc.'s internal control over financial reporting as of December 31, 2008, 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 included in the accompanying Assessment of Effectiveness of Internal Control Over Financial Reporting. Our responsibility is to express an opinion on 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, assessing the risk that a material weakness exists, 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, Saul Centers, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, 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, 2008 and 2007, the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2008 of Saul Centers, Inc. and our report dated March 13, 2009 expressed an unqualified opinion thereon.

Ernst & Young LLP
McLean, Virginia

March 13, 2009

Board of Directors and Stockholders
Saul Centers, Inc.

We have audited the accompanying consolidated balance sheets of Saul Centers, Inc. as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2008. Our audits also included the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule 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, 2008 and 2007, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 2 to the consolidated financial statements, in 2006 the Company adopted the provisions of U.S. Securities and Exchange Commission Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements," pursuant to which the Company recorded a cumulative adjustment to retained earnings as of January 1, 2006 to correct prior period misstatements in recording rental income.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Saul Centers, Inc.'s internal control over financial reporting as of December 31, 2008, 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 13, 2009 expressed an unqualified opinion thereon.

Ernst & Young LLP
McLean, Virginia

March 13, 2009

	December 31, 2008	December 31, 2007
<i>(Dollars in thousands, except per share amounts)</i>		
Assets		
Real estate investments		
Land	\$ 215,407	\$ 167,007
Buildings and equipment	713,154	673,328
Construction in progress	98,920	49,592
	1,027,481	889,927
Accumulated depreciation	(252,763)	(232,669)
	774,718	657,258
Cash and cash equivalents	13,006	5,765
Accounts receivable and accrued income, net	37,495	33,967
Deferred leasing costs, net	16,901	16,190
Prepaid expenses, net	2,981	2,571
Deferred debt costs, net	5,875	6,264
Other assets	2,897	5,428
Total assets	\$ 853,873	\$ 727,443
Liabilities		
Mortgage notes payable	\$ 567,495	\$ 524,726
Revolving credit facility outstanding	–	8,000
Dividends and distributions payable	12,864	12,887
Accounts payable, accrued expenses and other liabilities	22,394	13,159
Deferred income	23,233	15,147
Total liabilities	625,986	573,919
Minority interests	2,967	4,745
Stockholders' equity		
Preferred stock, 1,000,000 shares authorized:		
Series A Cumulative Redeemable, 40,000 shares issued and outstanding	100,000	100,000
Series B Cumulative Redeemable, 31,731 shares issued and outstanding as of December 31, 2008	79,328	–
Common stock, \$0.01 par value, 30,000,000 shares authorized, 17,863,214 and 17,747,529 shares issued and outstanding, respectively	179	178
Additional paid-in capital	164,278	161,618
Accumulated deficit	(118,865)	(113,017)
Total stockholders' equity	224,920	148,779
Total liabilities and stockholders' equity	\$ 853,873	\$ 727,443

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS of Operations

	For The Year Ended December 31,		
(Dollars in thousands, except per share amounts)	2008	2007	2006
Revenue			
Base rent	\$ 124,999	\$ 118,806	\$ 110,121
Expense recoveries	29,066	26,090	22,636
Percentage rent	1,509	1,497	1,767
Other	4,771	4,192	3,454
Total revenue	160,345	150,585	137,978
Operating expenses			
Property operating expenses	19,877	18,758	16,278
Provision for credit losses	1,113	376	400
Real estate taxes	16,608	14,084	12,503
Interest expense and amortization of deferred debt	34,278	33,855	32,534
Depreciation and amortization of deferred leasing costs	29,783	26,464	25,648
General and administrative	12,321	11,666	10,142
Total operating expenses	113,980	105,203	97,505
Operating income before minority interests and gain on property dispositions	46,365	45,382	40,473
Non-operating item: Gain on property dispositions	1,301	139	—
Net operating income before minority interests	47,666	45,521	40,473
Minority interests			
Minority share of income	(7,972)	(8,818)	(7,793)
Net income	39,694	36,703	32,680
Preferred dividends	(13,453)	(8,000)	(8,000)
Net income available to common stockholders	\$ 26,241	\$ 28,703	\$ 24,680
Per share net income available to common stockholders			
Basic	\$ 1.47	\$ 1.63	\$ 1.45
Diluted	\$ 1.46	\$ 1.62	\$ 1.43
Distributions declared per common share outstanding	\$ 1.80	\$ 1.82	\$ 1.68

The accompanying notes are an integral part of these statements.

	Preferred Stock	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Total
<i>(Dollars in thousands, except per share amounts)</i>					
Stockholders' equity:					
Balance, December 31, 2005	\$ 100,000	\$ 169	\$ 123,339	\$ (112,094)	\$ 111,414
Issuance of 464,197 shares of common stock:					
358,563 shares due to dividend reinvestment plan	—	4	14,838	—	14,842
105,634 shares due to employee stock options and directors' deferred stock plan and stock option awards	—	—	3,377	—	3,377
Net income	—	—	—	32,680	32,680
Cumulative effect of SAB 108 adjustment (see Note 2)				6,551	6,551
Preferred stock distributions, Series A	—	—	—	(6,000)	(6,000)
Distributions payable preferred stock, Series A (\$50.00 per share)	—	—	—	(2,000)	(2,000)
Common stock distributions	—	—	—	(21,490)	(21,490)
Distributions payable common stock (\$0.42 per share)	—	—	—	(7,283)	(7,283)
Balance, December 31, 2006	100,000	173	141,554	(109,636)	132,091
Issuance of 406,088 shares of common stock:					
389,197 shares due to dividend reinvestment plan	—	5	18,720	—	18,725
16,891 shares due to employee stock options and directors' deferred stock plan and stock option awards	—	—	1,344	—	1,344
Net income	—	—	—	36,703	36,703
Preferred stock distributions, Series A	—	—	—	(6,000)	(6,000)
Distributions payable preferred stock, Series A (\$50.00 per share)	—	—	—	(2,000)	(2,000)
Common stock distributions	—	—	—	(23,743)	(23,743)
Distributions payable common stock (\$0.47 per share)	—	—	—	(8,341)	(8,341)
Balance, December 31, 2007	100,000	178	161,618	(113,017)	148,779
Issuance of 31,731 shares of Series B preferred stock	79,328	—	(3,007)	—	76,321
Issuance of 115,685 shares of common stock:					
83,820 shares due to dividend reinvestment plan	—	1	3,940	—	3,941
31,865 shares due to employee stock options and directors' deferred stock plan and stock option awards	—	—	1,727	—	1,727
Net income	—	—	—	39,694	39,694
Distributions of preferred stock:					
Series A	—	—	—	(6,000)	(6,000)
Series B	—	—	—	(3,668)	(3,668)
Common stock distributions	—	—	—	(25,122)	(25,122)
Distributions payable preferred stock:					
Series A, \$50.00 per share	—	—	—	(2,000)	(2,000)
Series B, \$56.25 per share	—	—	—	(1,785)	(1,785)
Distributions payable common stock (\$0.39 per share)	—	—	—	(6,967)	(6,967)
Balance, December 31, 2008	\$ 179,328	\$ 179	\$ 164,278	\$ (118,865)	\$ 224,920

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS of Cash Flows

(Dollars in thousands)	For the Year Ended December 31,		
	2008	2007	2006
Cash flows from operating activities:			
Net income	\$ 39,694	\$ 36,703	\$ 32,680
Adjustments to reconcile net income to net cash provided by operating activities:			
Gain on property dispositions	(1,301)	(139)	–
Minority interests	7,972	8,818	7,793
Depreciation and amortization of deferred leasing costs	29,783	26,464	25,648
Amortization of deferred debt costs	1,162	1,149	1,089
Non cash compensation costs from stock grants and options	1,125	1,111	1,166
Provision for credit losses	1,113	376	400
Increase in accounts receivable and accrued income	(3,850)	(1,095)	(3,650)
Increase in deferred leasing costs	(3,382)	(2,692)	(2,256)
(Increase) decrease in prepaid expenses	(410)	(64)	33
Decrease (increase) in other assets	2,531	177	(1,219)
(Decrease) Increase in accounts payable, accrued expenses and other liabilities	(698)	598	1,008
Decrease in deferred income	(638)	(209)	(518)
Net cash provided by operating activities	73,101	71,197	62,174
Cash flows from investing activities:			
Acquisitions of real estate investments, net*	(63,406)	(23,744)	(17,318)
Additions to real estate investments	(9,986)	(7,302)	(10,145)
Additions to development and redevelopment activities	(42,513)	(20,990)	(38,236)
Proceeds from property disposition	835	–	–
Net cash used in investing activities	(115,070)	(52,036)	(65,699)
Cash flows from financing activities:			
Proceeds from notes payable	49,005	52,000	17,500
Repayments on notes payable	(16,585)	(14,717)	(13,322)
Proceeds from revolving credit facility	19,000	20,000	31,000
Repayments on revolving credit facility	(27,000)	(47,000)	(6,500)
Additions to deferred debt costs	(773)	(2,085)	(542)
Proceeds from the issuance of:			
Series B preferred stock, net of issuance of costs	76,321	–	–
Common Stock	4,543	18,958	17,053
Convertible limited partnership units in the Operating Partnership	–	–	4,001
Distributions to:			
Series A preferred stockholders	(8,000)	(8,000)	(8,000)
Series B preferred stockholders	(3,668)	–	–
Common stockholders	(33,450)	(31,026)	(28,579)
Convertible limited partnership units in the Operating Partnership	(10,183)	(9,587)	(9,032)
Net cash provided by (used in) financing activities	49,210	(21,457)	3,579
Net increase (decrease) in cash and cash equivalents	7,241	(2,296)	54
Cash and cash equivalents, beginning of year	5,765	8,061	8,007
Cash and cash equivalents, end of year	\$ 13,006	\$ 5,765	\$ 8,061
Supplemental disclosure of cash flow information:			
Cash paid for interest	\$ 37,179	\$ 35,684	\$ 34,906

* Supplemental discussion of non-cash investing and financing activities:

The 2008 real estate acquisition costs of \$63,406 are presented exclusive of a mortgage loan assumed of \$10,349.

The 2006 real estate acquisition costs of \$17,318 are presented exclusive of a mortgage loan assumed of \$11,334 and a \$300 seller rent deficiency reimbursement.

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"). The Company is required to annually distribute at least 90% of its REIT taxable income (excluding net capital gains) to its stockholders and meet 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 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.

The following table lists the properties acquired and/or developed by the Company since December 31, 2005. All of the following properties are operating shopping centers.

Name of Property	Location	Date of Acquisition/Development
Acquisitions		
Smallwood Village Center	Waldorf, MD	2006
Hunt Club Corners	Apopka, FL	2006
Orchard Park	Dunwoody, GA	2007
Great Falls Center	Great Falls, VA	2008
BJ's Wholesale Club	Alexandria, VA	2008
Marketplace at Sea Colony	Bethany Beach, DE	2008
Developments		
Broadlands Village Phase III	Ashburn, VA	2006
Lansdowne Town Center	Leesburg, VA	2006
Ashland Square Phase I	Manassas, VA	2007

As of December 31, 2008, the Company's properties (the "Current Portfolio Properties") consisted of 45 operating shopping center properties (the "Shopping Centers"), five predominantly office operating properties (the "Office Properties") and six (non-operating) development 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. As of December 31, 2008, thirty of the Shopping Centers were anchored by a grocery store and offer primarily day-to-day necessities and services. Only two retail tenants, Giant Food (4.4%), a tenant at eight Shopping Centers, and Safeway (3.1%), a tenant at eight Shopping Centers, and one office tenant, the United States Government (2.7%), a tenant at seven properties, individually accounted for more than 2.5% of the Company's total revenue for the year ended December 31, 2008.

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 U.S. generally accepted accounting principles 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 revenue 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 above and 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 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. The Company has never recorded a customer relationship intangible asset.

If there is an event or change in circumstance that indicates an impairment in the value of a real estate investment property, the Company prepares an impairment analysis to assess that the carrying value of the real estate investment property does not exceed its estimated fair value. The Company considers both quantitative and qualitative factors including recurring operating losses, significant decreases in occupancy, and significant adverse changes in legal factors and business climate. If impairment indicators are present the Company performs a comparison of the projected cash flows of the property over its remaining useful life, on an undiscounted basis, to the carrying value of that property. The Company assesses its undiscounted projected cash flows based upon estimated capitalization rates, historic operating results and market conditions that may affect the property. If such carrying value is greater than the undiscounted projected cash flows, the Company would recognize an impairment loss equivalent to an amount required to adjust the carrying amount to its then estimated fair market value. The value of any property is sensitive to the actual results of any of the aforementioned estimated factors, either individually or taken as a whole. Should the actual results differ from management's projections, the valuation could be negatively or positively affected. The Company has not recognized an impairment loss in 2008, 2007 or 2006 on any of its real estate.

Interest, real estate taxes, development related salary costs 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. Interest expense capitalized totaled \$4,159,000, \$2,889,000 and \$3,673,000, for 2008, 2007 and 2006, 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 that extend the useful lives. In addition, we capitalize leasehold improvements when certain criteria are met, including when we supervise construction and will own the improvement. Tenant 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. Depreciation expense and amortization of leasehold improvements for the years ended December 31, 2008, 2007 and 2006 was \$24,761,000, \$21,638,000 and \$20,236,000, respectively. Repairs and maintenance expense totaled \$9,106,000, \$8,926,000 and \$7,364,000, for 2008, 2007 and 2006, respectively, and is included in property operating expenses in the accompanying consolidated financial statements.

Deferred Leasing 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 \$16,901,000 and \$16,190,000, net of accumulated amortization of \$15,196,000 and \$14,457,000 as of December 31, 2008 and 2007, respectively. Amortization expense, included in depreciation and amortization in the consolidated statements of operations, totaled \$5,022,000, \$4,826,000 and \$5,412,000, for the years ended December 31, 2008, 2007 and 2006, respectively. Capitalized leasing costs consist of commissions paid to third party leasing agents as well as internal direct costs for successful leases such as employee compensation and payroll related fringe benefits directly related to time spent performing such 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, 2008 and 2007 are as follows:

Construction in Progress		
	December 31,	
(In thousands)	2008	2007
Clarendon Center	\$ 49,836	\$ 27,323
Northrock	21,656	–
Westview Village	17,240	6,382
Smallwood Village Center	6,290	–
Boulevard	2,925	–
Ashland Square Phase II	–	10,851
Lexington Center	–	2,813
Other	973	2,223
Total	\$ 98,920	\$ 49,592

As of January 1, 2008, the carrying cost capitalization associated with development at Ashland Square Phase II and Lexington Center was suspended. All development costs for these properties were removed from construction in progress and reclassified to land and buildings and equipment, while awaiting sufficient leasing activity to warrant the resumption of active development.

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 \$914,000 and \$387,000, at December 31, 2008 and 2007, respectively.

Allowance for Doubtful Accounts

	For the Year Ended December 31,	
(In thousands)	2008	2007
Beginning Balance	\$ 387	\$ 479
Provision for Credit Losses	1,113	376
Charge-offs	(586)	(468)
Ending Balance	\$ 914	\$ 387

In addition to rents due currently, the account also includes \$25,766,000 and \$25,013,000, at December 31, 2008 and 2007, 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 \$155,000 and \$52,000, respectively, for tenants whose rent payment history or financial condition cast doubt upon the tenant's ability to perform under its lease obligations.

On September 13, 2006, the SEC staff published Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements in Current Year Financial Statements ("SAB 108"). SAB 108 addresses how the effects of a prior year uncorrected misstatement must be considered in quantifying misstatements in the current year financial statements and provides guidance on the correction of misstatements. SAB 108 offers a transition provision for correcting immaterial prior period misstatements that were uncorrected as of the beginning of the fiscal year of adoption. SAB 108 was effective for fiscal years ending after November 15, 2006. It was the Company's policy, for leases entered into prior to 1998, to recognize rental revenue on a straight-line basis when rental payments due under leases varied, because of free rent periods or fixed rent increases (excluding those increases which approximate inflationary increases). It was the Company's policy that annual scheduled base rent increases of 3% or less were determined to approximate inflationary increases and were not recognized ratably over the life of the lease. Subsequent to 1998, the Company has annually analyzed these uncorrected misstatements and determined that the uncorrected misstatement was immaterial for all reporting periods. The Company has determined that less than 5% of its leases were not recognizing base rent on a straight-line basis and that the cumulative under-reporting of straight-line rental income related to these long term leases totaled approximately \$6,551,000. According to the provisions of SAB 108, the Company recorded an accumulated accounts receivable balance of \$6,551,000 for these leases and recorded a corresponding increase to Stockholders' Equity as of January 1, 2006. Commencing in 2006 and pursuant to the accounting for recognizing rental income on a straight-line basis, a portion of the \$6,551,000 receivable was amortized as a non-cash

reduction of rental income, \$257,000, \$203,000 and \$136,000 in 2008, 2007 and 2006. The remaining unamortized balance of \$5,955,000 as of December 31, 2008 will be amortized as a non-cash reduction of base rent over the remaining life of the affected leases.

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 on a straight-line basis over the terms of the respective loans or agreements, which approximates the effective interest method. Deferred debt costs totaled \$5,875,000 and \$6,264,000, net of accumulated amortization of \$5,079,000 and \$5,393,000, at December 31, 2008 and 2007, 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. In addition, deferred income includes the fair value of a below market lease component associated with acquisition properties as determined pursuant to the application of SFAS 141 "Business Combinations".

Revenue Recognition

Rental and interest income is accrued as earned except when doubt exists as to collectibility, in which case the accrual is discontinued. Recognition of rental income commences when control of the space has been given to the tenant. 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 U.S. generally accepted accounting principles. 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 revenue ("percentage rent") is accrued when a tenant reports sales that exceed a specified breakpoint, pursuant to the terms of their respective leases.

Income Taxes

The Company made an election to be treated, and intends to continue operating so as to qualify as a REIT under the Code, commencing with its taxable year ended December 31, 1993. A REIT generally will not be subject to federal income taxation, provided that distributions to its stockholders equal or exceed its REIT taxable income and complies with certain other requirements. Therefore, no provision has been made for federal income taxes in the accompanying consolidated financial statements.

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). FIN 48 is an interpretation of FASB Statement No. 109, "Accounting for Income Taxes." The Company adopted the provisions of FIN 48 on January 1, 2007. The adoption of FIN 48 did not impact the Company's financial condition or results of operations. Further, as of December 31, 2008, the Company had no material unrecognized tax benefits and there exist no potentially significant unrecognized tax benefits which are reasonably expected to occur within the next twelve months. The Company recognizes penalties and interest accrued related to unrecognized tax benefits, if any, as general and administrative expense. No penalties and interest have been accrued in years 2007 and 2008. The tax basis of the Company's real estate investments was approximately \$745,700,000 and \$677,400,000, as of December 31, 2008 and 2007, respectively. With few exceptions, the Company is no longer subject to U.S. federal, state, and local tax examinations by tax authorities for years before 2004.

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" and accounts for stock based compensation according to SFAS No. 123R, "Accounting for Stock-Based Compensation". The Company had no options eligible for valuation prior to the grant of options in 2003. The fair value of options granted is 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. Expected volatility is determined using the most recent trading history of the Company's common stock (month-end closing prices) corresponding to the average expected term of the options, (2) Average Expected Term. The options are assumed to be outstanding for a term calculated considering prior exercise history, scheduled vesting and the 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 amortizes the value of options granted, ratably over the vesting period, and includes the amounts as compensation 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 additional shares remained 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. The exercise price of \$24.91 per share was the closing market price of the Company's common stock on the date of the award.

At the annual meeting of the Company's stockholders in 2004, the stockholders approved the adoption of the 2004 stock plan for the purpose of attracting and retaining executive officers, directors and other key personnel. The 2004 stock plan was subsequently amended by the Company's stockholders at the 2008 Annual Meeting (the "Amended 2004 Plan"). The Amended 2004 Plan provides for grants of options to purchase up to 1,000,000 shares of common stock as well as grants of up to 200,000 shares of common stock to directors. The Amended 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. The termination date of the Amended 2004 Plan is April 2018.

Effective April 26, 2004, the Compensation Committee granted options to purchase a total of 152,500 shares (27,500 shares from incentive stock options and 125,000 shares from 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 were immediately exercisable. The exercise price of \$25.78 per share was the closing market price of the Company's common stock on the date of the award. Using the Black-Scholes model, the Company determined the total fair value of the 2004 Options

to be \$360,000, of which \$293,000 and \$67,000 were the values assigned to the officer options and director options, respectively. Because the directors' options vest immediately, the entire \$67,000 was expensed as of the date of grant. The expense of the officers' options is being recognized as compensation expense monthly during the four years the options vest. The 2004 Options are due to expire April 25, 2014.

Effective May 6, 2005, the Compensation Committee granted options to purchase a total of 162,500 shares (35,500 shares from incentive stock options and 127,000 shares from nonqualified stock options) to twelve Company officers and to twelve Company directors (the "2005 Options"). The officers' 2005 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 were immediately exercisable. The exercise price of \$33.22 per share was the closing market price of the Company's common stock on the date of the award. Using the Black-Scholes model, the Company determined the total fair value of the 2005 Options to be \$484,500, of which \$413,400 and \$71,100 were the values assigned to the officer options and director options, respectively. Because the directors' options vest immediately, the entire \$71,100 was expensed as of the date of grant. The expense of the officers' options is being recognized as compensation expense monthly during the four years the options vest. The 2005 Options are due to expire May 5, 2015.

Effective May 1, 2006, the Compensation Committee granted options to purchase a total of 30,000 shares (all nonqualified stock options) to twelve Company directors (the "2006 Options"). The options were immediately exercisable. The exercise price of \$40.35 per share was the closing market price of the Company's common stock on the date of the award. Using the Black-Scholes model, the Company determined the total fair value of the 2006 Options to be \$143,400. Because the directors' options vest immediately, the entire \$143,400 was expensed as of the date of grant. The 2006 Options are due to expire April 30, 2016. No options were granted to the Company's officers in 2006.

Effective April 27, 2007, the Compensation Committee granted options to purchase a total of 165,000 shares (27,560 shares from incentive stock options and 137,440 shares from nonqualified stock options) to thirteen Company officers and twelve Company Directors (the "2007 options"). The officers' 2007 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 were immediately exercisable. The exercise price of \$54.17 per share was the closing market price of the Company's common stock on the date of award. Using the Black-Scholes model, the Company determined the total fair value of the 2007 Options to be \$1,544,148, of which \$1,258,848 and \$285,300 were the

values assigned to the officer options and director options, respectively. Because the directors' options vest immediately, the entire \$285,300 was expensed as of the date of grant. The expense for the officers' options is being recognized as compensation expense monthly during the four years the options vest. The 2007 Options are due to expire April 26, 2017.

Effective April 25, 2008, the Compensation Committee granted options to purchase a total of 30,000 shares (all nonqualified stock options) to twelve Company directors (the "2008 Options"). The options were immediately exercisable. The exercise price of \$50.15 per share was the closing market price of the Company's common stock on the date of the award. Using the Black-Scholes model, the Company determined the total fair value of the 2008 Options to be \$254,700. Because the directors' options vest immediately, the entire \$254,700 was expensed as of the date of grant. The 2008 Options are due to expire April 24, 2018. No options were granted to the Company's officers in 2008.

Pursuant to the Amended 2004 Plan, the Compensation Committee established a Deferred Compensation Plan for Directors for the benefit of its directors and their beneficiaries, which replaced a previous Deferred Compensation and Stock Plan for Directors. A director may make an annual election 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 common stock's closing market price on the first trading day of the following quarter to determine the number of shares to be allocated to the director. As of December 31, 2008, 232,000 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 shares, for each of the years ended December 31, 2008, 2007 and 2006. 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 \$120,000, \$130,000 and \$97,000, for the years ended December 31, 2008, 2007 and 2006, respectively.

Minority Interests

Saul Centers is the sole general partner of the Operating Partnership, owning a 76.7% common interest as of December 31, 2008. Minority Interests in the Operating Partnership are comprised of limited partnership units owned by The Saul Organization. Minority Interests as reflected on the Balance Sheets are increased for earnings allocated to limited

partnership interests, distributions reinvested in additional units and in certain situations for distributions to minority interests in excess of earnings allocated, and are decreased for limited partner distributions. Minority Interests as reflected on the Statements of Operations represent earnings allocated to limited partnership interests. Amounts distributed in excess of the limited partners' share of earnings, net of limited partner reinvestments of distributions, also increase minority interests expense in the respective period and are classified on the Statements of Operations as Distributions in excess of earnings to the extent such distributions in excess of earnings exceed the carrying amount of minority interests.

Per Share Data

Per share data is calculated in accordance with SFAS 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, 2008, 2007 and 2006 certain options are dilutive because the average share price of the Company's common stock exceeded the exercise prices. The treasury stock method was used to measure the effect of the dilution.

Basic and Diluted Shares Outstanding			
(In thousands)	December 31		
	2008	2007	2006
Weighted average common shares outstanding – Basic	17,816	17,589	17,075
Effect of dilutive options	145	180	158
Weighted average common shares outstanding – Diluted	17,961	17,769	17,233
Average Share Price	\$ 45.98	\$ 52.22	\$ 43.04

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, the results of operations or liquidity. 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.

Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157 "Fair Value Measurement" ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in

generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 applies to accounting pronouncements that require or permit fair value measurements, except for share-based payments under SFAS No. 123(R). The adoption of SFAS No. 157 is required for the year beginning January 1, 2008. The Company does not have any assets or liabilities recorded at fair value, and therefore the adoption of this statement on January 1, 2008 did not have a material impact on the Company's consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115" ("SFAS No. 159"). This standard permits entities to choose to measure many financial instruments and certain other items at fair value and is effective for the first fiscal year beginning after November 15, 2007. The Company has not elected the fair value option for any assets or liabilities, and therefore the adoption of the statement did not have a material impact on its consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, "Non-controlling Interest in Consolidated Financial Statements" ("SFAS No. 160"). SFAS 160 is effective for fiscal years beginning on or after December 15, 2008. SFAS No. 160 establishes consistent accounting and reporting standards for the non-controlling (or minority) interest in a subsidiary and for the deconsolidation of a subsidiary. Management has assessed the impact of adopting the statement and does not expect the adoption of SFAS No. 160 to have a material impact on the Company's financial condition or results of operations.

On December 4, 2007, the FASB issued SFAS No. 141 (Revised 2007), "Business Combinations" ("SFAS No. 141(R)"). SFAS No. 141(R) will change the accounting for business combinations. Under SFAS No. 141(R), an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. Transaction costs will no longer be included in the measurement of the business acquired. Instead, these items will be expensed as incurred. SFAS No. 141(R) also includes a substantial number of new disclosure requirements. SFAS No. 141(R) applies prospectively to business combinations occurring during fiscal years beginning on or after December 15, 2008, which for the Company begins with the 2009 calendar year. SFAS No. 141(R) will impact the Company's financial statements dependent on the level of acquisition activity in the year 2009 and beyond. The Company currently expects the most significant impact of this statement to be the treatment of transaction costs, which will be expensed as a period cost upon the adoption of this statement.

On June 16, 2008, the FASB issued FASB Staff Position EITF 03-6-1 ("EITF 03-6-1"). This guidance clarifies the accounting for unvested share-based payment awards that contain

non-forfeitable rights to dividends or dividend equivalents by proscribing that such awards be included in the computation of earnings per share ("EPS") pursuant to the two-class method. EITF 03-6-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008. The Company believes the adoption of EITF 03-6-1 will not have a material impact on its EPS calculation.

3. REAL ESTATE ACQUIRED

New Market

On March 3, 2005 and September 8, 2005, the Company acquired two parcels of land located in New Market, Maryland, for a purchase price of \$500,000 and \$1,500,000, respectively. The Company had contracted to purchase an adjacent third parcel with the intent to assemble additional acreage for further retail development near this I-70 interchange, east of Frederick, Maryland. During December 2007, the Company abandoned the acquisition of the third parcel and wrote-off to general and administrative expense all costs related to that parcel.

Smallwood Village Center

On January 27, 2006, the Company acquired the Smallwood Village Center, located within the St. Charles planned community of Waldorf, Maryland, a suburb of metropolitan Washington, DC, through a wholly-owned subsidiary of its operating partnership. The center was acquired for a purchase price of \$17.5 million subject to the assumption of an \$11.3 million mortgage loan.

Hunt Club Corners

On June 1, 2006, the Company completed the acquisition of the Publix-anchored Hunt Club Corners shopping center located in Apopka, FL. The center was acquired for a purchase price of \$11.1 million.

Great Eastern Plaza Land Parcel

On June 6, 2007, the Company acquired an additional parcel of undeveloped land adjacent to its Great Eastern Plaza shopping center in District Heights, Maryland, for a purchase price of \$1.3 million.

Orchard Park

On July 19, 2007, the Company completed the acquisition of the Kroger-anchored Orchard Park shopping center located in Dunwoody, GA. The center was acquired for a purchase price of \$17.0 million.

Westview Village

In November 2007, the Company purchased a land parcel in the Westview development on Buckeystown Pike (MD Route 85) in Frederick, Maryland. The purchase price was \$5.0 million. Construction is nearing completion for a neighborhood shopping center.

Northrock

In January 2008, the Company acquired an undeveloped land parcel in Warrenton, Virginia, located at the southwest corner of the U.S. Route 29/211 and Fletcher Drive intersection. The land purchase price was \$12.5 million. The Company is nearing completion of construction of a neighborhood shopping center. The Harris Teeter supermarket chain has executed a lease for a grocery store to anchor the center.

Great Falls Center

On March 28, 2008, the Company completed the acquisition of the Safeway-anchored Great Falls Center located in Great Falls, Virginia. The center was acquired for a purchase price of \$36.6 million subject to the assumption of a \$10.3 million mortgage loan. As of the date of acquisition, management determined the mortgage loan was fairly valued because the terms of the loan were not materially different from market terms.

BJ's Wholesale Club

On March 28, 2008, the Company completed the acquisition of the single tenant property anchored by BJ's Wholesale Club, located in Alexandria, Virginia. The property was acquired for a purchase price of \$21.0 million.

Marketplace at Sea Colony

On March 28, 2008, the Company completed the acquisition of Marketplace at Sea Colony, located in Bethany Beach, Delaware. The center was acquired for a purchase price of \$3.0 million.

Application of SFAS 141, "Business Combinations", for Real Estate Acquired

The Company accounts for the acquisition of operating properties using the purchase method of accounting in accordance with SFAS 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 \$61,100,000 total cost of the operating property acquisitions in 2008, which exclude undeveloped land acquisitions, and \$17,077,000 in 2007, of which both amounts include the properties' purchase price and closing costs, a total of \$2,351,000 and \$805,000, was allocated as lease intangible assets and included in lease acquisition costs at December 31, 2008 and December 31, 2007, respectively. Each year's lease intangible assets are being amortized over the remaining periods of the leases acquired, a weighted average term of 16 and 26 years, for 2008 and 2007, respectively. The value of below market leases totaling \$8,724,000 and \$3,105,000, are being amortized over a weighted average term of 20 and 30 years, for 2008 and 2007, respectively, and are included in deferred income. The value of above market leases totaling \$148,000 and \$37,000, are being amortized over a weighted average term of 5 and one year, for

2008 and 2007, respectively, and are included as a deferred asset in accounts receivable.

As of December 31, 2008 and 2007, the gross carrying amount of lease intangible assets included in deferred leasing costs was \$13,736,000 and \$11,385,000, respectively, and accumulated amortization was \$9,506,000 and \$7,598,000, respectively. Total amortization of these assets was \$1,908,000, \$1,918,000 and \$2,592,000, for the years ended December 31, 2008, 2007 and 2006, respectively. As of December 31, 2008 and 2007, the gross carrying amount of below market lease intangible liabilities included in deferred income was \$18,402,000 and \$9,678,000, respectively, and accumulated amortization was \$3,151,000 and \$1,599,000, respectively. Total amortization of these liabilities was \$1,552,000, \$580,000 and \$604,000, for the years ended December 31, 2008, 2007 and 2006, respectively. As of December 31, 2008 and 2007, the gross carrying amount of above market lease intangible assets included in accounts receivable was \$874,000 and \$726,000, and accumulated amortization was \$670,000 and \$564,000 respectively. Total amortization of these assets was \$106,000, \$107,000 and \$158,000, for the years ended December 31, 2008, 2007 and 2006, respectively.

As of December 31, 2008, the scheduled amortization of intangible assets and deferred income related to in-place leases are as follows:

Amortization of Intangible Assets and Deferred Income Related to In-place Leases				
<i>(In thousands)</i>	Lease acquisition costs	Above market leases	Below market leases	Total
2009	\$ (1,197)	\$ (75)	\$ 1,323	\$ 51
2010	(761)	(62)	1,087	264
2011	(446)	(30)	865	389
2012	(278)	(25)	771	468
2013	(202)	(12)	714	500
Thereafter	(1,346)	–	10,491	9,145
Total	\$ (4,230)	\$ (204)	\$15,251	\$ 10,817

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, 2008 and 2007, respectively, as if the above described operating property acquisitions had occurred on January 1, 2008 and 2007, 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, 2008 and 2007, respectively.

Pro-Forma Consolidated Condensed Statement of Operations		
	Year Ended December 31,	
<i>(In thousands, except per share data)</i>	2008	2007
Real estate revenue	\$161,610	\$155,353
Net income available to common shareholders	\$ 26,337	\$ 28,264
Net income per common share – basic	\$ 1.48	\$ 1.61
Net income per common share – diluted	\$ 1.47	\$ 1.59

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

The Saul Organization has a 23.3% limited partnership interest, represented by 5,416,000 convertible limited partnership units in the Operating Partnership, as of December 31, 2008. These convertible limited partnership units are convertible into shares of Saul Centers' common stock, at the option of the unit holder, on a one-for-one basis provided that, in accordance with the Saul Centers, Inc. Articles of Incorporation, the rights may not be exercised at any time that The Saul Organization beneficially owns, directly or indirectly, in the aggregate more than 39.9% of the value of the outstanding common stock and preferred stock of Saul Centers (the "Equity Securities").

The impact of The Saul Organization's 23.3% 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, 2008, 2007 and 2006, were 23,377,000, 23,185,000 and 22,628,000, respectively.

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

The Company's outstanding debt, including amounts owed under the Company's revolving credit facility, totaled \$567,495,000 at December 31, 2008, of which \$548,265,000 was fixed rate debt and \$19,230,000 was variable rate debt. At the prior year's end, December 31, 2007, notes payable totaled \$532,726,000, of which \$524,726,000 was fixed rate debt and \$8,000,000 was variable rate debt. At December 31, 2008, the Company had a \$150 million unsecured revolving credit facility with no outstanding borrowings. Saul Centers and certain consolidated subsidiaries of the Operating Partnership have guaranteed the payment obligations of the Operating Partnership under the revolving credit facility which provides for a \$150,000,000 revolving credit facility maturing on December 19, 2010, which term may be extended by the Company for

one additional year subject to the Company's satisfaction of certain conditions. Letters of credit may be issued under the revolving credit facility. On December 31, 2008, of the \$150,000,000 available for borrowing, approximately \$177,000 was committed for letters of credit, and the resulting balance of approximately \$149,823,000 was available to borrow for working capital, operating property acquisitions or development projects. Interest rate pricing under the facility is primarily determined by operating income from the Company's existing unencumbered properties and to a lesser extent, certain leverage tests. As of December 31, 2008, operating income from the unencumbered properties determined the interest rate for up to \$103,000,000 of the line's available borrowings, with interest expense to be calculated based upon the 1, 2, 3 or 6 month LIBOR plus a spread of 1.40% to 1.60% or upon the bank's reference rate, at the Company's option. The remaining \$47,000,000 of the line's availability is determined based upon the Company's consolidated operating income after debt service. On this portion of the facility, interest accrues at a rate of LIBOR plus a spread of 1.70% to 2.25%, determined by certain leverage tests, or upon the bank's reference rate plus a spread of 0.575%, at the Company's option.

Saul Centers is the guarantor of the revolving credit facility, portions of two mortgage notes totaling \$3,875,000 and the two construction loans totaling \$19,230,000. The Operating Partnership is the borrower for all of the notes for which Saul Centers is the guarantor. The remainder of the mortgage notes payable, \$544,390,000, are non-recourse debt.

On February 29, 2008, the Company closed on a \$7,500,000 increase to a fixed-rate mortgage secured by Shops at Fairfax and Boulevard shopping centers. The loan matures June 1, 2015 (same as the original financing), requires monthly interest only payments of \$38,000, based upon a 6.08% interest rate, and requires a final principal payment of \$7,500,000 at maturity. The Company has initially guaranteed \$1,875,000 of this loan until the Boulevard redevelopment is completed and until certain debt service coverage tests are achieved.

On March 23, 2008, the Company closed on a \$3,000,000 increase to a fixed-rate mortgage secured by Seabreeze Plaza. The loan matures May 1, 2014 (same as the original financing), requires equal monthly principal and interest payments of \$17,794, based upon a 5.90% interest rate and 30-year principal amortization, and requires a final principal payment of approximately \$2,738,000 at maturity.

On March 28, 2008, the Company assumed a fully amortizing fixed-rate mortgage loan in the amount of approximately \$10,349,000, secured by the acquisition property, Great Falls Center. The loan matures February 1, 2024 and requires equal monthly principal and interest payments of \$83,113, based upon a 5.80% interest rate and 20-year principal amortization. Management determined the mortgage loan was fairly valued at acquisition because the terms of the loan were not materially different from current market terms.

On March 31, 2008, the Company closed on a new 15-year, fixed-rate mortgage loan in the amount of \$12,750,000, secured by the BJ's Wholesale Club center. The loan matures April 1, 2023, requires equal monthly principal and interest payments of \$80,003, based upon a 6.43% interest rate and 30-year principal amortization, and requires a final principal payment of approximately \$9,255,000 at maturity.

In April 2008, the Company closed on a \$10,825,000 additional financing secured by the Great Falls Center. Funding in the amount of \$6,525,000 occurred on April 6, 2008, payable at an interest rate of 6.80%, interest only for the first year, after which amortization will commence on a 30-year amortization schedule, requiring monthly payments of principal and interest totaling \$42,538. A final principal payment of approximately \$1,274,000 will be due at maturity on February 1, 2024. The Company has initially guaranteed \$2,000,000 of this loan, with the amount of any additional advance to also be guaranteed until certain debt service coverage tests are achieved. The balance totaling \$4,300,000 is a forward commitment to be funded prior to March 31, 2009, subject to achieving certain re-leasing requirements.

In May 2008, the Company closed on a \$21,822,000 secured construction loan, to fund the development of Northrock shopping center in Warrenton, Virginia. Funding in the amount of approximately \$6,495,000 occurred at closing. The loan accrues interest, payable at an interest rate of LIBOR plus 1.6%. The loan matures on May 1, 2011, with one 2-year extension option, exercisable at the Company's option subject to completion of improvements and certain debt service coverage requirements. The loan is 100% guaranteed by the Company until such time as the construction is complete, at which time the guarantee will be limited to 50% of the total principal outstanding. Approximately \$12,817,000 was outstanding as of December 31, 2008.

Also in May 2008, the Company closed a \$157,500,000 secured construction loan to finance the development of Clarendon Center, a mixed-use development adjacent to the Clarendon Metro station in Arlington, Virginia. The Company has guaranteed the loan, with the guarantee to be reduced subject to certain conditions related to pre-leasing, completion of construction and net operating income from the project. The loan accrues interest at an interest rate of LIBOR plus 2.5% and matures on November 14, 2011, which term may be extended by the Company for two additional 9-month periods, subject to the satisfaction of certain conditions. Approximately \$6,413,000 was outstanding as of December 31, 2008.

During 2007, the Company obtained two new fixed-rate, non-recourse financings. On August 15, 2007, the Company closed on a new 15-year, fixed-rate mortgage financing in the amount of \$12,000,000, secured by Orchard Park. The loan matures September 5, 2022, requires equal monthly principal and interest payments of \$72,565, based upon a 6.08% interest rate and 30-year principal amortization, and requires a final

principal payment of \$8,555,000 at maturity. On May 30, 2007, the Company closed on a new 15-year, fixed-rate mortgage financing in the amount of \$40,000,000, secured by Lansdowne Town Center. The loan matures June 10, 2022, requires equal monthly principal and interest payments of

\$230,137, based upon a 5.62% interest rate and 30-year principal amortization, and requires a final principal payment of \$27,947,000 at maturity.

The following is a summary of notes payable as of December 31, 2008 and 2007:

Notes Payable				
(Dollars in thousands)	December 31,		Interest Rate *	Scheduled Maturity *
	2008	2007		
Fixed rate mortgages:	\$ 78,489 (a)	\$ 83,078	8.00%	Dec-2011
	115,271 (b)	119,340	7.67%	Oct-2012
	10,846 (c)	11,022	6.12%	Jan-2013
	28,837 (d)	30,041	7.88%	Jan-2013
	7,919 (e)	8,131	5.77%	Jul-2013
	15,576 (f)	12,935	5.40%	May-2014
	18,987 (g)	11,930	7.45%	Jun-2015
	38,263 (h)	39,099	6.01%	Feb-2018
	43,413 (i)	44,495	5.88%	Jan-2019
	14,043 (j)	14,395	5.76%	May-2019
	19,391 (k)	19,878	5.62%	Jul-2019
	19,195 (l)	19,661	5.79%	Sep-2019
	17,165 (m)	17,601	5.22%	Jan-2020
	12,337 (n)	12,535	5.60%	May-2020
	11,576 (o)	11,858	5.30%	Jun-2020
	9,925 (p)	10,139	5.81%	Feb-2021
	6,791 (q)	6,884	6.01%	Aug-2021
	39,198 (r)	39,740	5.62%	Jun-2022
	11,817 (s)	11,964	6.08%	Sep-2022
	12,655 (t)	–	6.43%	Apr-2023
	16,571 (u)	–	6.19%	Feb-2024
Total fixed rate	548,265	524,726	6.67%	7.6 Years
Variable rate loan:				
Revolving credit facility	– (v)	8,000	LIBOR + 1.40%	Dec-2010
Northrock construction loan	12,817 (w)	–	LIBOR + 1.60%	May-2011
Clarendon construction loan	6,413 (x)	–	LIBOR + 2.50%	Nov-2011
Total variable rate	19,230	8,000	3.33%	2.4 Years
Total notes payable	\$ 567,495	\$ 532,726	6.56%	7.5 Years

* Interest rate and scheduled maturity data presented as of December 31, 2008. Totals computed using weighted averages.

(a) 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 final payment of \$63,153,000 at loan maturity. Principal of \$4,589,000 was amortized during 2008.

(b) 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 final payment of \$97,403,000 at loan maturity. Principal of \$4,069,000 was amortized during 2008.

(c) The loan is collateralized by Smallwood Village Center and requires equal monthly principal and interest payments of \$71,000 based upon a 30-year amortization schedule and a final payment of \$10,071,000 at loan maturity. Principal of \$176,000 was amortized during 2008.

- (d) 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 final payment of \$22,961,000 at loan maturity. Principal of \$1,204,000 was amortized during 2008.
- (e) 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 final payment of \$6,830,000 at loan maturity. Principal of \$212,000 was amortized during 2008.
- (f) The loan is collateralized by Seabreeze Plaza. During 2008, the Company increased the mortgage and borrowed an additional \$3,000,000. The combination of the original note and the 2008 note requires equal monthly principal and interest payments totaling \$102,000 based upon a weighted average 26-year amortization schedule and a final payment of \$13,278,000 is due at loan maturity. Principal of \$359,000 was amortized during 2008.
- (g) The loan is collateralized by Shops at Fairfax and Boulevard shopping centers. During 2008, the Company increased the mortgage and borrowed an additional \$7,500,000. The combination of the original note and the 2008 note required equal monthly principal and interest payments totaling \$156,000 based upon a weighted average 23-year amortization schedule and a final payment of \$15,168,000 is due at loan maturity. Principal of \$443,000 was amortized during 2008.
- (h) 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 final payment of \$28,012,000 at loan maturity. Principal of \$836,000 was amortized during 2008.
- (i) The loan, consisting of two notes dated December 2003 and two notes dated February and December 2004, is currently collateralized by three shopping centers, Broadlands Village (Phases I, II & III), The Glen and Kentlands Square, and requires equal monthly principal and interest payments of \$306,000 based upon a 25-year amortization schedule and a final payment of \$28,393,000 at loan maturity. Principal of \$1,082,000 was amortized during 2008.
- (j) 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 final payment of \$8,985,000 at loan maturity. Principal of \$352,000 was amortized during 2008.
- (k) 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 final payment of \$12,288,000 at loan maturity. Principal of \$487,000 was amortized during 2008.
- (l) The loan is collateralized by Briggs Chaney MarketPlace and requires equal monthly principal and interest payments of \$133,000 based upon a 25-year amortization schedule and a final payment of \$12,192,000 at loan maturity. Principal of \$466,000 was amortized during 2008.
- (m) 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 final payment of \$10,568,000 at loan maturity. Principal of \$436,000 was amortized during 2008.
- (n) The loan is collateralized by Boca Valley Plaza and requires equal monthly principal and interest payments of \$75,000 based upon a 30-year amortization schedule and a final payment of \$9,149,000 at loan maturity. Principal of \$198,000 was amortized during 2008.
- (o) The loan is collateralized by Palm Springs Center and requires equal monthly principal and interest payments of \$75,000 based upon a 25-year amortization schedule and a final payment of \$7,075,000 at loan maturity. Principal of \$282,000 was amortized during 2008.
- (p) The loan is collateralized by Jamestown Place and requires equal monthly principal and interest payments of \$66,000 based upon a 25-year amortization schedule and a final payment of \$6,102,000 at loan maturity. Principal of \$214,000 was amortized during 2008.
- (q) The loan is collateralized by Hunt Club Corners and requires equal monthly principal and interest payments of \$42,000 based upon a 30-year amortization schedule and a final payment of \$5,018,000 at loan maturity. Principal of \$93,000 was amortized during 2008.
- (r) The loan is collateralized by Lansdowne Town Center and requires monthly principal and interest payments of \$230,000 based on a 30-year amortization schedule and a final payment of \$28,177,000 at loan maturity. Principal of \$542,000 was amortized during 2008.
- (s) The loan is collateralized by Orchard Park and requires equal monthly principal and interest payments of \$73,000 based upon a 30-year amortization schedule and a final payment of \$8,628,000 at loan maturity. Principal of \$147,000 was amortized during 2008.
- (t) The loan is collateralized by BJ's Wholesale Club and requires equal monthly principal and interest payments of \$80,000 based upon a 30-year amortization schedule and a final payment of \$9,305,000 at loan maturity. Principal of \$95,000 was amortized during 2008.
- (u) The loan, consisting of two notes dated February 2004 and April 2008, is collateralized by Great Falls Center. The 2004 note requires equal monthly principal and interest payments of \$83,000 based upon a 20-year amortization schedule. The 2008 note of \$6,525,000 requires interest only payments of \$37,000 based upon and interest rate of 6.8% until May 2009, at which time the loan requires equal monthly principal and interest payments of \$43,000 based upon a 30-year amortization schedule. Both loans mature February 1, 2024 at which time a final payment of \$1,378,000 will be due. Principal of \$303,000 was amortized during 2008.
- (v) The loan is an unsecured revolving credit facility totaling \$150,000,000. Interest expense during 2008 was calculated based upon the 1 month LIBOR rate plus a spread of 1.475% (reduced to 1.40% effective April 1, 2008) 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. Monthly payments, if applicable, are interest only and vary depending upon the amount outstanding and the applicable interest rate for any given month.
- (w) The loan is a secured construction loan facility totaling \$21,822,000 to fund the development of Northrock shopping center. Interest charges are funded by the construction loan and are calculated based upon the 1 month LIBOR rate plus a spread of 1.60%. The loan may be extended two years, at the Company's option, subject to the completion of construction and certain debt coverage requirements. Interest charges of approximately \$247,000 accrued and were capitalized as costs of construction during 2008.
- (x) The loan is a secured construction loan facility totaling \$157,500,000 to fund the development of Clarendon Center. Interest charges are funded by the construction loan and are calculated based upon the 1 month LIBOR rate plus a spread of 2.50%. The loan may be extended for two additional 9-month periods, subject to the satisfaction of certain conditions. Interest charges of approximately \$105,000 accrued and were capitalized as costs of construction during 2008.

The December 31, 2008 and 2007 depreciation adjusted cost of properties collateralizing the mortgage notes payable totaled \$693,205,000 and \$557,820,000, respectively. The Company's credit facility requires the Company and its subsidiaries to maintain certain financial covenants. As of December 31, 2008, the material covenants required the Company, on a consolidated basis, to:

- limit the amount of debt so as to maintain a gross asset value, as defined in the loan agreement, in excess of liabilities of at least \$600 million plus 90% of the Company's future net equity proceeds;
- limit the amount of debt as a percentage of gross asset value, as defined in the loan agreement, to less than 60% (leverage ratio);
- limit the amount of debt so that interest coverage will exceed 2.5 to 1 on a trailing 12-full calendar month basis;
- limit the amount of debt so that interest, scheduled principal amortization and preferred dividend coverage exceeds 1.6 to 1; and
- limit the amount of variable rate debt and debt with initial loan terms of less than five years to no more than 40% of total debt.

As of December 31, 2008, the Company was in compliance with all such covenants.

Notes payable at December 31, 2008 and 2007, totaling \$144,108,000 and \$157,381,000, respectively, are guaranteed by members of The Saul Organization. As of December 31, 2008, 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>	Balloon Payments	Scheduled Principal Amortization	Total
2009	\$ —	\$ 18,054	\$ 18,054
2010	—	19,413	19,413
2011	81,463 ^(a)	20,853	102,316
2012	96,300	15,050	111,350
2013	36,440	9,269	48,709
2014	13,176	9,052	22,228
Thereafter	188,451	56,974	245,425
Total	\$ 418,830	\$ 148,665	\$ 567,495

(a) Includes the Clarendon Center and Northrock construction loan balances as of December 31, 2008, totaling \$19,230.

Interest Expense and Amortization of Deferred Debt Costs

<i>(In thousands)</i>	Year ended December 31,		
	2008 ^(a)	2007	2006
Interest incurred	\$ 37,275	\$ 35,595	\$ 35,118
Amortization of deferred debt costs	1,162	1,149	1,089
Capitalized interest	(4,159)	(2,889)	(3,673)
Total	\$ 34,278	\$ 33,855	\$ 32,534

(a) During the 2008 year, the Company incurred and capitalized as construction in progress, deferred debt costs of approximately \$2,369 related to the Clarendon Center and Northrock construction loans.

6. LEASE AGREEMENTS

Lease income includes primarily base rent arising from noncancelable commercial leases. Base rent (including straight-line rent) for the years ended December 31, 2008, 2007 and 2006, amounted to \$124,999,000, \$118,806,000 and \$110,121,000, respectively. Future contractual payments under noncancelable leases for years ended December 31, (which exclude the effect of straight-line rents), are as follows:

Future Contractual Payments	
<i>(In thousands)</i>	
2009	\$ 121,931
2010	111,960
2011	94,971
2012	77,469
2013	59,401
Thereafter	\$ 268,206
Total	\$ 733,938

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, 2008, 2007 and 2006 amounted to \$29,066,000, \$26,090,000 and \$22,636,000, 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 \$1,509,000, \$1,497,000 and \$1,767,000, for the years ended December 31, 2008, 2007 and 2006, 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, 2008, 2007 and 2006, respectively.

The future minimum rental commitments under these ground leases are as follows:

Ground Lease Rental Commitments							
<i>(In thousands)</i>	2009	2010	Annually 2011	2012	2013	Thereafter	Total
Beacon Center	\$ 53	\$ 53	\$ 57	\$ 60	\$ 60	\$ 2,900	\$ 3,183
Olney	52	56	56	56	56	4,097	4,373
Southdale	60	60	60	60	60	3,245	3,545
Total	\$ 165	\$ 169	\$ 173	\$ 176	\$ 176	\$ 10,242	\$ 11,101

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 3.4% of the underlying land 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 expense for the years ended December 31, 2008, 2007 and 2006 were \$813,000, \$796,000 and \$726,000, respectively. Expenses arising from the lease are included in general and administrative expense (see Note 9 – Related Party Transactions).

8. STOCKHOLDERS' EQUITY AND MINORITY INTERESTS

The consolidated statement of operations for the years ended December 31, 2008, 2007 and 2006 includes a charge for minority interests of \$7,972,000 and \$8,818,000, and \$7,793,000, respectively, representing The Saul Organization's share of the net income for the year.

On July 16, 2003, the Company filed a 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 per share liquidation preference at the Company's option as of November 5, 2008. The depositary shares pay an annual dividend of \$2.00 per share, equivalent to 8% of the \$25.00 per share liquidation preference. 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.

On March 20, 2008, the Company filed a shelf registration statement with the SEC relating to the future offering of up to an aggregate of \$140 million of preferred stock and depositary shares. On March 27, 2008, the Company sold 3,000,000 depositary shares, each representing 1/100th of a share of 9% Series B Cumulative Redeemable Preferred Stock. The underwriters exercised an over-allotment option, purchasing an additional 173,115 depositary shares.

The depositary shares may be redeemed, in whole or in part, at the \$25.00 per share liquidation preference at the Company's option on or after March 15, 2013. The depositary shares pay an annual dividend of \$2.25 per share, equivalent to 9% of the \$25.00 per share liquidation preference. The first dividend was paid on July 15, 2008 and covered the period from March 27, 2008 through June 30, 2008. The Series B 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 as of December 31, 2008, leased space in 20 of the Company's properties. Total rental income from Chevy Chase Bank amounted to \$3,458,000, \$2,946,000 and \$2,220,000, for the years ended December 31, 2008, 2007 and 2006, respectively. As of December 31, 2008 and 2007, current accounts receivable and accrued income included \$25,700 and \$12,200, respectively, from various Chevy Chase Bank leases.

The Company utilizes Chevy Chase Bank for its various checking accounts and as of December 31, 2008 had \$12,847,000 deposited in cash and short-term investment accounts.

The Chairman and Chief Executive Officer, the President, the Senior Vice President-General Counsel and the Vice President-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, with the exception of the Vice President-Chief Accounting Officer whose share of annual compensation allocated to the Company is determined by the shared services agreement (described below).

The Company participates in a multi-employer 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 \$381,000, \$331,000 and \$289,000, for 2008, 2007 and 2006, 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 multi-employer 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 ended December 31, 2008, 2007 and 2006, the Company was required to contribute three times the amount deferred by employees. The Company's expense, included in general and administrative expense, totaled \$203,000, \$106,000 and \$106,000, for the years ended December 31, 2008, 2007 and 2006, respectively. All amounts deferred by employees and the Company are fully vested. The cumulative unfunded liability under this plan was \$1,082,000 and \$857,000, at December 31, 2008 and 2007, 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 head count estimates of usage or estimates of 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 thereunder 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, 2008, 2007 and 2006, which included rental expense for the Company's headquarters lease (see Note 7. Long Term Lease Obligations), totaled \$5,188,000, \$4,890,000 and \$3,963,000, respectively. The amounts are expensed when incurred and are primarily reported as general and administrative expenses or capitalized to specific development projects in these consolidated financial statements. As of December 31, 2008 and 2007, accounts payable, accrued expenses and other liabilities included \$324,000 and \$298,000, respectively, represent billings due to The Saul Organization for the Company's share of these ancillary costs and expenses.

The B. F. Saul Insurance Agency of Maryland, Inc., a subsidiary of the B. F. Saul Company and a member of The Saul Organization, is a general insurance agency that receives commissions and counter-signature fees in connection with our insurance program. Such commissions and fees amounted to approximately \$418,000, \$367,000 and \$381,000, for the years ended December 31, 2008, 2007 and 2006, respectively.

On November 14, 2007, the Company purchased a land parcel in Frederick, Maryland, from a subsidiary of Chevy Chase Bank, a related party, for \$5,000,000. 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 Chevy Chase Bank (see Note 17. Subsequent Events-Sale of Chevy Chase 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.

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 per share 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.

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 per share was the market trading price of the Company's common stock on the date the option was granted.

Effective May 6, 2005, the Compensation Committee granted options to purchase a total of 162,500 shares (35,500 shares of incentive stock options and 127,000 shares of nonqualified stock options) to twelve Company officers and to the twelve Company directors (the "2005 Options"). The officers' 2005 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 \$33.22 per share was the market trading price of the Company's common stock on the date the option was granted.

Effective May 1, 2006, the Compensation Committee granted options to purchase a total of 30,000 shares of nonqualified stock options to the twelve Company directors (the "2006 Options"). The options are exercisable immediately. The exercise price of \$40.35 per share was the market trading price of the Company's common stock on the date the option was granted. No options were granted to the Company's officers in 2006.

Effective April 27, 2007, the Compensation Committee granted options to purchase a total of 165,000 shares (27,560 shares from incentive stock options and 137,440 shares from nonqualified stock options) to thirteen Company officers and twelve Company Directors (the "2007 options"). The officers' 2007 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 were immediately exercisable. The exercise price of \$54.17 per share was the closing market price of the Company's common stock on the date the option was granted.

Effective April 25, 2008, the Compensation Committee granted options to purchase a total of 30,000 shares (all nonqualified stock options) to twelve Company directors (the "2008 Options"). The options were immediately exercisable. The exercise price of \$50.15 per share was the closing market price of the Company's common stock on the date of the award. Using the Black-Scholes model, the Company determined the total fair value of the 2008 Options to be \$254,700. Because the directors' options vest immediately, the entire \$254,700 was expensed as of the date of grant. The 2008 Options are due to expire April 24, 2018. No options were granted to the Company's officers in 2008.

The following table summarizes the amount and activity of each grant, the total value and variables used in the computation and the amount expensed and included in general and administrative expense in the Consolidated Statements of Operations for the years ended December 31, 2008, 2007 and 2006:

Stock Options Issued to Officers							
						Subtotal	
Grant date	05/23/2003	04/26/2004	05/06/2005	04/27/2007			
Total grant	220,000	122,500	132,500	135,000		610,000	
Vested	212,500	115,000	91,875	33,750		453,125	
Exercised	96,422	28,750	6,250	—		131,422	
Forfeited	7,500	7,500	11,250	—		26,250	
Exercisable at Dec. 31, 2008	116,078	86,250	85,625	33,750		321,703	
Remaining unexercised	116,078	86,250	115,000	135,000		452,328	
Exercise price	\$ 24.91	\$ 25.78	\$ 33.22	\$ 54.17			
Volatility	0.175	0.183	0.207	0.233			
Expected life (years)	7.0	7.0	8.0	6.5			
Assumed yield	7.00%	5.75%	6.37%	4.13%			
Risk-free rate	4.00%	4.05%	4.15%	4.61%			
Total value at grant date	\$ 332,200	\$ 292,775	\$ 413,400	\$ 1,258,848		\$ 2,297,223	
Forfeited options	11,325	17,925	35,100	—		64,350	
Expensed in previous years	216,399	122,988	69,000	—		408,387	
Expensed in 2006	76,444	67,220	95,460	—		239,124	
Expensed in 2007	28,032	64,242	91,648	209,808		393,730	
Expensed in 2008	—	20,400	91,644	314,721		426,765	
Future expense	\$ —	\$ —	\$ 30,548	\$ 734,319		\$ 764,867	
Stock Options Issued to Directors and Grand Totals							
						Subtotal	Grand Total
Grant date	04/26/2004	05/06/2005	05/01/2006	04/27/2007	04/25/2008		
Total grant	30,000	30,000	30,000	30,000	30,000	150,000	760,000
Vested	30,000	30,000	30,000	30,000	30,000	150,000	603,125
Exercised	6,200	2,500	—	—	—	8,700	140,122
Forfeited	—	—	—	—	—	—	26,250
Exercisable at Dec. 31, 2008	23,800	27,500	30,000	30,000	30,000	141,300	463,003
Remaining unexercised	23,800	27,500	30,000	30,000	30,000	141,300	593,628
Exercise price	\$ 25.78	\$ 33.22	\$ 40.35	\$ 54.17	\$ 50.15		
Volatility	0.183	0.198	0.206	0.225	0.237		
Expected life (years)	5.0	10.0	9.0	8.0	7.0		
Assumed yield	5.75%	6.91%	5.93%	4.39%	4.09%		
Risk-free rate	3.57%	4.28%	5.11%	4.65%	3.49%		
Total value at grant date	\$ 66,600	\$ 71,100	\$ 143,400	\$ 285,300	\$ 254,700	\$ 821,100	\$ 3,118,323
Forfeited options	—	—	—	—	—	—	64,350
Expensed in previous years	66,600	71,100	—	—	—	137,700	546,087
Expensed in 2006	—	—	143,400	—	—	143,400	382,524
Expensed in 2007	—	—	—	285,300	—	285,300	679,030
Expensed in 2008	—	—	—	—	254,700	254,700	681,465
Future expense	—	—	—	—	\$ —	—	\$ 764,867
Weighted average term of future expense (Officer and Director options)							2.3 yrs

The table below summarizes the option activity for the years 2008, 2007 and 2006:

	2008		2007		2006	
	Shares	Wtd Avg Exercise Price	Shares	Wtd Avg Exercise Price	Shares	Wtd Avg Exercise Price
Outstanding at January 1	586,753	\$ 36.15	430,453	\$ 29.06	513,125	\$ 27.80
Granted	30,000	50.15	165,000	54.17	30,000	40.35
Exercised	(23,125)	26.02	(8,700)	26.85	(86,422)	25.59
Expired/Forfeited	—	—	—	—	(26,250)	28.72
Outstanding December 31	593,628	34.72	586,753	36.15	430,453	29.06
Exercisable at December 31	463,003	30.56	354,878	30.74	241,078	29.09

The intrinsic value of options exercised in 2008, 2007 and 2006 was \$557,000, \$208,775 and \$1,871,000, respectively. The intrinsic value of options outstanding and exercisable at year end 2008 was \$4,098,000 and \$3,914,000, respectively. The intrinsic value measures the price difference between the options' exercise price and the closing share price quoted by the New York Stock Exchange as of the date of measurement. The date of exercise was the measurement date for shares exercised during the period. At December 31, 2008, the final trading day of calendar 2008, the closing price was \$39.50 per share and was used for the calculation of aggregate intrinsic value of options outstanding and exercisable at that date. Options having an exercise price in excess of the December 31, 2008 closing price have no intrinsic value. The weighted average remaining contractual life of the Company's exercisable and outstanding options are 6.1 and 6.5 years, respectively.

11. NON-OPERATING ITEMS

Gain on Property Dispositions

The gain on property dispositions of \$1,301,000 resulted from insurance claims arising from three loss events sustained in 2008. The Company recognized a gain of \$1,096,000, arising from insurance proceeds related to minor fire damage sustained at two shopping centers. The insurance proceeds are expected to fund substantially all of the restoration. The gain recognized was measured as the difference between insurance proceeds and the depreciated carrying value of the assets replaced. Additionally, the Company recognized a gain on property dispositions of \$205,000 representing proceeds from an insurance settlement for HVAC units vandalized at the Company's West Park shopping center in Oklahoma City, Oklahoma.

The gain on property dispositions of \$139,000 in 2007 represents additional condemnation proceeds recognized 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. Original proceeds from the condemnation were received in 2004. There were no property dispositions in 2006.

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 \$548,265,000 and \$524,726,000 carrying value at December 31, 2008 and 2007, respectively. Management estimates that the fair value of these fixed rate notes payable, assuming long term interest rates of approximately 7.15% and 6.27%, would be approximately \$525,285,000 and \$528,894,000, as of December 31, 2008 and 2007, 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 paid common stock distributions of \$1.88 per share, \$1.77 per share and \$1.68 per share, during 2008, 2007 and 2006, respectively, and paid Series A preferred stock dividends of \$2.00 per depositary share during each of the years and two Series B preferred stock dividends totaling \$1.16 in

2008. For the common stock dividends paid, \$1.842, \$1.770 and \$1.445 per share, represented ordinary dividend income for the years 2008, 2007 and 2006. For the common stock dividends paid, \$0.038 and \$0.235 per share, represented return of capital to the shareholders for the years 2008 and 2006, respectively. The 2007 common dividend was 100% taxable. All of the preferred stock dividends paid were considered ordinary dividend income.

The following summarizes distributions paid during the years ended December 31, 2008, 2007 and 2006, and includes activity in the Plan as well as limited partnership units issued from the reinvestment of unit distributions:

(Dollars in thousands)	Total Distributions to			Dividend Reinvestments		
	Preferred Stockholders	Common Stockholders	Limited Partnership Unitholders	Common Stock Shs Issued	Units Issued	Discounted Share Price
Distributions during 2008						
October 31	\$ 3,785	\$ 8,376	\$ 2,546	8,520	—	\$ 34.25
July 31	3,883	8,375	2,546	21,712	—	46.78
April 30	2,000	8,356	2,546	26,915	—	48.73
January 31	2,000	8,343	2,545	26,673	—	49.56
Total 2008	\$ 11,668	\$ 33,450	\$ 10,183	83,820	—	
Distributions during 2007						
October 31	\$ 2,000	\$ 8,323	\$ 2,546	19,828	—	\$ 52.52
July 31	2,000	7,740	2,383	148,651	—	41.92
April 30	2,000	7,679	2,383	113,165	—	51.60
January 31	2,000	7,284	2,275	107,553	—	52.24
Total 2007	\$ 8,000	\$ 31,026	\$ 9,587	389,197	—	
Distributions during 2006						
October 31	\$ 2,000	\$ 7,219	\$ 2,274	126,054	—	\$ 47.14
July 28	2,000	7,145	2,274	153,298	—	38.70
April 28	2,000	7,126	2,254	35,807	50,736	39.66
January 31	2,000	7,089	2,230	43,404	55,421	35.89
Total 2006	\$ 8,000	\$ 28,579	\$ 9,032	358,563	106,157	

In December 2008, 2007 and 2006, the Board of Directors of the Company authorized a distribution of \$0.39, \$0.47 and \$0.42 per common share payable in January 2009, 2008 and 2007, to holders of record on January 16, 2009, January 17, 2008 and January 17, 2007, respectively. As a result, \$6,967,000, \$8,343,000 and \$7,284,000, were paid to common shareholders on January 30, 2009, January 31, 2008 and January 31, 2007, respectively. Also, \$2,112,000, \$2,545,000 and \$2,275,000, were paid to limited partnership unitholders on January 30, 2009, January 31, 2008 and January 31, 2007 (\$0.39, \$0.47 and \$0.42 per Operating Partnership unit), respectively. The Board of Directors authorized preferred

stock dividends of \$0.50 per Series A depositary share, to holders of record on January 5, 2009, January 2, 2008 and January 2, 2007, respectively and \$0.5625 per Series B depositary share to holders of record on January 5, 2009. As a result, \$3,785,000 was paid to preferred shareholders on January 15, 2009, and \$2,000,000 was paid January 15, 2008 and January 12, 2007, 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 2008 and 2007.

<i>(In thousands, except per share amounts)</i>				
2008				
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Revenue	\$ 38,722	\$ 40,105	\$ 40,947	\$ 40,571
Operating income before minority interests and gain on property dispositions	11,073	12,175	11,264	11,853
Net income	9,130	10,229	9,521	10,814
Net income available to common shareholders	7,033	6,443	5,736	7,029
Net income available to common shareholders per share (diluted)	0.39	0.36	0.32	0.39
2007				
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Revenue	\$ 36,684	\$ 37,077	\$ 38,014	\$ 38,810
Operating income before minority interests and gain on property dispositions	11,009	11,077	11,956	11,340
Net income	8,874	8,926	9,624	9,279
Net income available to common shareholders	6,874	6,926	7,624	7,279
Net income available to common shareholders per share (diluted)	0.39	0.39	0.43	0.41

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 Other¹	Consolidated Totals
2008				
Real estate rental operations:				
Revenue	\$ 121,050	\$ 38,704	\$ 591	\$ 160,345
Expenses	(26,636)	(10,962)	–	(37,598)
Income from real estate	94,414	27,742	591	122,747
Interest expense & amortization of deferred debt	–	–	(34,278)	(34,278)
General and administrative	–	–	(12,321)	(12,321)
Subtotal	94,414	27,742	(46,008)	76,148
Depreciation and amortization	(21,657)	(8,126)	–	(29,783)
Gain on property dispositions	1,301	–	–	1,301
Minority interests	–	–	(7,972)	(7,972)
Net income	\$ 74,058	\$ 19,616	\$ (53,980)	\$ 39,694
Capital investment	\$ 94,917	\$ 1,833	\$ 19,155	\$ 115,905
Total assets	\$ 668,493	\$ 120,410	\$ 649,970	\$ 853,873

16. BUSINESS SEGMENTS (continued)

<i>(In thousands)</i>	Shopping Centers	Office Properties	Corporate and Other¹	Consolidated Totals
2007				
Real estate rental operations:				
Revenue	\$ 112,444	\$ 37,687	\$ 454	\$ 150,585
Expenses	(23,325)	(9,893)	–	(33,218)
Income from real estate	89,119	27,794	454	117,367
Interest expense & amortization of deferred debt	–	–	(33,855)	(33,855)
General and administrative	–	–	(11,666)	(11,666)
Subtotal	89,119	27,794	(45,067)	71,846
Depreciation and amortization	(18,320)	(8,144)	–	(26,464)
Gain on property dispositions	139	–	–	139
Minority interests	–	–	(8,818)	(8,818)
Net income	\$ 70,938	\$ 19,650	\$ (53,885)	\$ 36,703
Capital investment	\$ 43,325	\$ 1,387	\$ 7,324	\$ 52,036
Total assets	\$ 569,249	\$ 122,908	\$ 35,286	\$ 727,443
2006				
Real estate rental operations:				
Revenue	\$ 101,460	\$ 36,184	\$ 334	\$ 137,978
Expenses	(20,172)	(9,009)	–	(29,181)
Income from real estate	81,288	27,175	334	108,797
Interest expense & amortization of deferred debt	–	–	(32,534)	(32,534)
General and administrative	–	–	(10,142)	(10,142)
Subtotal	81,288	27,175	(42,342)	66,121
Depreciation and amortization	(17,646)	(8,002)	–	(25,648)
Minority interests	–	–	(7,793)	(7,793)
Net income	\$ 63,642	\$ 19,173	\$ (50,135)	\$ 32,680
Capital investment	\$ 59,679	\$ 3,109	\$ 2,911	\$ 65,699
Total assets	\$ 539,283	\$ 131,317	\$ 29,937	\$ 700,537

¹ Clarendon Center development included because a significant component will be residential.

17. SUBSEQUENT EVENTS**Sale of Chevy Chase Bank**

On December 4, 2008, Capital One Financial Corporation ("Capital One") and the shareholders of Chevy Chase Bank (the "Shareholders") announced they had signed a Stock Purchase Agreement, dated as of December 3, 2008, pursuant to which the Shareholders agreed to sell all of the outstanding shares of common stock of Chevy Chase Bank to Capital One, less certain excluded assets. After all regulatory approvals were received the transaction closed on February 28, 2009. The Saul Organization has no ongoing management or financial involvement with Capital One and Capital One is not affiliated with the Saul Organization in any way, therefore, any transactions with Chevy Chase Bank and/or Capital One will not be considered a related party transaction as of the closing date of the sale.

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
Chief Financial Officer,
Municipal Mortgage & Equity, LLC

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

Mark Sullivan III
Attorney

**The Honorable
James W. Symington**
Of Counsel, O'Connor & Hannan,
Attorneys at Law

John R. Whitmore
Financial Consultant

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

Charles W. Sherren, Jr.
Senior Vice President, Management

Thomas H. McCormick
Senior Vice President,
General Counsel

COUNSEL

Pillsbury Winthrop
Shaw Pittman LLP
Washington, DC 20037

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Ernst & Young LLP
McLean, Virginia 22102

WEB SITE

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 2007, 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

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
October 1, 2008 – December 31, 2008	\$48.94	\$24.67
July 1, 2008 – September 30, 2008	\$51.39	\$44.14
April 1, 2008 – June 30, 2008	\$54.56	\$46.81
January 1, 2008 – March 31, 2008	\$55.41	\$45.06
October 1, 2007 – December 31, 2007	\$62.58	\$50.56
July 1, 2007 – September 30, 2007	\$51.50	\$42.32
April 1, 2007 – June 30, 2007	\$56.31	\$43.95
January 1, 2007 – March 31, 2007	\$60.37	\$52.15
On March 12, 2009, the closing price was \$25.09 per share.		
There were approximately 300 holders of record as of that date.		

The Annual Meeting of Shareholders will be held at 11:00 a.m., local time, on April 24, 2009, 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.)





7501 Wisconsin Avenue, Suite 1500
Bethesda, MD 20814-6522
Phone: (301) 986-6200
Website: www.saulcenters.com