

CHELSEA PROPERTY GROUP INC  
Form 10-Q  
August 13, 2003

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

**For the quarterly period ended June 30, 2003**

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

**Commission File No. 1-12328**

**CHELSEA PROPERTY GROUP, INC.**  
*(Exact name of registrant as specified in its charter)*

**Maryland**  
*(State or other jurisdiction  
of incorporation or organization)*

**22-3251332**  
*(I.R.S. Employer  
Identification No.)*

**103 Eisenhower Parkway, Roseland, New Jersey 07068**  
*(Address of principal executive offices - zip code)*

**(973) 228-6111**  
*(Registrant's telephone number, including area code)*

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days Yes  No

Indicate by check mark whether the registrant is an accelerated filer.  
Yes  No

The number of shares outstanding of the registrant's common stock, \$0.01 par value was 43,179,850 at August 1, 2003.

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**Chelsea Property Group, Inc.**

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**Chelsea Property Group, Inc.**  
**Consolidated Balance Sheets**  
(In thousands, except per share data)

	June 30, 2003	Decemb 2
	-----	-----
<b>Assets:</b>		
Rental properties:		
Land.....	\$ 285,424	\$ 26
Depreciable property.....	1,675,145	1,57
	-----	-----
Total rental property.....	1,960,569	1,83
Accumulated depreciation.....	(313,794)	(28
	-----	-----
Rental properties, net.....	1,646,775	1,55
Cash and cash equivalents.....	21,306	2
Restricted cash-escrows.....	4,525	
Tenant accounts receivable (net of allowance for doubtful accounts of \$2,317 in 2003 and \$2,593 in 2002).....	2,559	
Deferred rent receivable.....	21,778	1
Investments in unconsolidated affiliates.....	72,774	4
Notes receivable-related parties.....	2,728	

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Deferred costs, net.....	14,475	1
Other assets.....	29,695	3
	-----	-----
Total assets.....	<b>\$1,816,615</b>	\$ 1,70
	=====	=====
Liabilities and stockholders' equity:		
Liabilities:		
Unsecured bank debt.....	\$83,035	\$ 10
Unsecured notes.....	621,584	62
Mortgage debt.....	363,348	30
Construction payables.....	6,964	
Accounts payable and accrued expenses.....	44,226	4
Obligation under capital lease.....	1,191	
Accrued dividend and distribution payable.....	28,284	
Other liabilities.....	21,342	1
	-----	-----
Total liabilities.....	<b>1,169,974</b>	1,10
Commitments and contingencies		
Minority interest.....	<b>137,974</b>	13
Stockholders' equity:		
8.375% series A cumulative redeemable preferred stock, \$0.01 par value, authorized 5,000 shares, issued and outstanding 797 in 2003 and 2002 (aggregate liquidation preference of \$39,847 in 2003 and 2002).....	8	
Common stock, \$0.01 par value, authorized 100,000 shares, 43,078 in 2003 and 41,485 in 2002.....	431	
Paid-in-capital.....	629,052	57
Officer loan.....	(488)	
Distributions in excess of net income .....	(114,920)	(11
Accumulated other comprehensive loss.....	(5,416)	(
	-----	-----
Total stockholders' equity.....	<b>508,667</b>	45
	-----	-----
Total liabilities and stockholders' equity.....	<b>\$1,816,615</b>	\$1,70
	=====	=====

The accompanying notes are an integral part of the financial statements.

**Chelsea Property Group, Inc.**  
**Condensed Consolidated Statements of Income**  
**for the Three and Six Months Ended June 30, 2003, and 2002**  
**(Unaudited)**  
*(In thousands, except per share data)*

	Three Months Ended June 30, 2003	Three Months Ended June 30, 2002	Six Months Ended June 2003	
	-----	-----	-----	-----
<b>Revenues:</b>				
Base rent.....	\$60,001	\$43,181	\$119,751	\$
Percentage rent.....	4,993	4,465	9,178	
Expense reimbursements.....	20,596	14,485	39,328	
Other income.....	1,816	2,711	3,291	
	-----	-----	-----	-----
<b>Total revenues.....</b>	<b>87,406</b>	64,842	171,548	1
	-----	-----	-----	-----
<b>Expenses:</b>				
Operating and maintenance.....	24,516	18,135	47,440	

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Depreciation and amortization.....	17,258	14,222	34,872
General and administrative.....	2,468	1,921	4,669
Other.....	1,632	1,085	3,068
<b>Total expenses.....</b>	<b>45,874</b>	<b>35,363</b>	<b>90,049</b>
<b>Income before unconsolidated investments, interest expense, minority interest and discontinued operations.....</b>	<b>41,532</b>	<b>29,479</b>	<b>81,499</b>
Income from unconsolidated investments.....	2,495	2,982	3,946
Loss from Chelsea Interactive.....	(905)	(3,776)	(1,742)
Interest expense.....	(16,553)	(10,843)	(33,187)
<b>Income from continuing operations before minority interest.....</b>	<b>26,569</b>	<b>17,842</b>	<b>50,516</b>
Minority interest attributed to continuing operations.....	(5,114)	(3,671)	(9,908)
Income from continuing operations.....	21,455	14,171	40,608
Income from discontinued operations, net of minority interest.....	76	86	170
Gain on sale of discontinued operations, net of minority interest.....	4,008	-	4,008
<b>Net income.....</b>	<b>25,539</b>	<b>14,257</b>	<b>44,786</b>
Preferred dividend.....	(834)	(849)	(1,668)
<b>Net income available to common shareholders.....</b>	<b>\$24,705</b>	<b>\$13,408</b>	<b>\$43,118</b>
<b>Basic:</b>			
Income from continuing operations.....	\$0.49	\$0.35	\$0.93
Income from discontinued operations.....	-	-	-
Gain on sale of discontinued operations.....	0.10	-	0.10
<b>Net income per common share.....</b>	<b>\$0.59</b>	<b>\$0.35</b>	<b>\$1.03</b>
<b>Weighted average common shares outstanding.....</b>	<b>42,041</b>	<b>37,877</b>	<b>41,801</b>
<b>Diluted:</b>			
Income from continuing operations.....	\$0.47	\$0.34	\$0.89
Income from discontinued operations.....	-	-	-
Gain on sale of discontinued operations.....	0.09	-	0.10
<b>Net income per common share.....</b>	<b>\$0.56</b>	<b>\$0.34</b>	<b>\$0.99</b>
<b>Weighted average common shares outstanding.....</b>	<b>43,997</b>	<b>39,375</b>	<b>43,655</b>

*The accompanying notes are an integral part of the financial statements.*

**Chelsea Property Group, Inc.**  
**Condensed Consolidated Statements of Cash Flows**  
**for the Six Months Ended June 30, 2003 and 2002**  
**(Unaudited)**  
*(In thousands)*

	2003	2002
<b>Cash flows from operating activities</b>		
Net income.....	\$44,786	\$27,048

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Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization.....	34,901	27,184
Equity-in-earnings of unconsolidated investments in excess of distributions received.....	(1,240)	(974)
Loss from Chelsea Interactive.....	-	6,476
Loss on interest rate swap.....	514	-
Gain on sale of discontinued operations.....	(4,008)	-
Minority interest in net income.....	9,938	7,140
Proceeds from non-compete receivable.....	-	4,300
Amortization of non-compete revenue.....	-	(2,568)
Additions to deferred leasing costs.....	(439)	(228)
Other operating activities.....	(116)	(446)
Changes in assets and liabilities:		
Straight-line rent receivable.....	(3,597)	(1,448)
Due from affiliates.....	(340)	(1,617)
Other assets.....	8,135	6,511
Deferred incentive compensation.....	-	(14,401)
Accounts payable and accrued expenses.....	134	(4,482)
Net cash provided by operating activities.....	88,668	52,495
<b>Cash flows from investing activities</b>		
Additions to rental properties.....	(65,381)	(76,955)
Net proceeds from sale of center.....	7,198	4,224
Additions to investments in unconsolidated affiliates.....	(22,451)	(18,501)
Distributions from investments in unconsolidated affiliates in excess of earnings.....	-	337
Additions to deferred development costs.....	(321)	(2,844)
Payments from related parties.....	18	1,104
Loans to related parties.....	-	(550)
Net cash used in investing activities.....	(80,937)	(93,185)
<b>Cash flows from financing activities</b>		
Debt proceeds.....	-	177,324
Repayment of debt.....	(27,107)	(89,806)
Net proceeds from sale of common stock.....	53,461	5,001
Distributions.....	(34,632)	(25,177)
Redemption of preferred stock.....	-	(9,010)
Additions to deferred financing costs.....	(698)	(389)
Net cash (used in) provided by financing activities.....	(8,976)	57,943
Net (decrease) increase in cash and cash equivalents.....	(1,245)	17,253
Cash and cash equivalents, beginning of period.....	22,551	24,604
Cash and cash equivalents, end of period.....	\$21,306	\$41,857
<b>Supplemental information :</b>		
Non-cash investing activities:		
Additions to rental properties on consolidation of property previously held as a 50% investment in unconsolidated affiliates	-	\$68,938
Non-cash financing activities:		
Assumption of construction loan payable on consolidation of property previously held as a 50% investment in unconsolidated affiliates	-	\$59,360
Assumption of mortgage debt	\$60,747	-

*The accompanying notes are an integral part of the financial statements.*

**Chelsea Property Group, Inc.**  
**Notes to Condensed Consolidated Financial Statements**  
**(Unaudited)**

**1. Organization and Basis of Presentation**

Chelsea Property Group, Inc. (the "Company") is a self-administered and self-managed real estate investment trust ("REIT"). The Company is the managing general partner of CPG Partners, L.P., (the "Operating Partnership" or "OP"), an operating partnership that specializes in owning, developing, leasing, marketing and managing upscale and fashion-oriented manufacturers' outlet centers. As of June 30, 2003, the Company wholly or partially owned 59 centers in 31 states and Japan containing approximately 14.9 million square feet of gross leasable area ("GLA"). The Company's portfolio is comprised of 28 premium outlet centers containing 9.3 million square feet of GLA (the "Premium Properties") and 31 other retail centers containing approximately 5.6 million square feet of GLA ("Other Properties") (collectively the "Properties"). The Company's Premium Properties generated approximately 77% and 88% of the Company's retail real estate net operating income for the six months ended June 30, 2003, and 2002, respectively. The Premium Properties generally are located near metropolitan areas including New York City, Los Angeles, Boston, Washington, D.C., San Francisco, Sacramento, Cleveland, Atlanta, Dallas, Portland (Oregon), Tokyo and Osaka, Japan. Some Premium Properties are also located within 20 miles of major tourist destinations including Palm Springs, the Napa Valley, Orlando, and Honolulu.

Virtually all of the Company's assets are held by, and all of its operations conducted through, the Operating Partnership. Due to the Company's ability, as the sole general partner, to exercise financial and operational control over the Operating Partnership, the Operating Partnership is consolidated in the accompanying financial statements. All significant intercompany transactions and accounts have been eliminated in consolidation.

Common ownership of the OP as of June 30, 2003, was approximately as follows:

Company	85.3%	43,078,000	units
Unitholders	<u>14.7%</u>	<u>7,438,000</u>	units
<b>Total</b>	<b>100.0%</b>	<b>50,516,000</b>	

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for fair presentation have been included. Operating results for the six month period ended June 30, 2003, are not necessarily indicative of the results that may be expected for the year ending December 31, 2003. The balance sheet at December 31, 2002 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. These financial statements should be read in conjunction with the consolidated financial statements and accompanying notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2002.

Certain information in the prior year financial statements have been reclassified to conform to current year presentation.

**Notes to Condensed Consolidated Financial Statements**  
**(Unaudited)**

**1. Organization and Basis of Presentation (continued)**

In August 2001, the FASB issued Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143") which is effective January 1, 2003. SFAS 143 requires the recording of the fair value of a liability for an asset retirement obligation in the period in which it is incurred. See note 4 to financial statements for discussion related to the estimated future costs to be incurred in connection with the future operations of Chelsea Interactive.

In November 2002, the FASB issued Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others ("FIN 45"). FIN 45 requires certain guarantees to be recorded at fair value, instead of recording a liability only when a loss is probable and reasonably estimatable, as those terms are defined in FASB Statement No. 5, Accounting for Contingencies. FIN 45 also requires a guarantor to make significant new disclosures, even when the likelihood of making any payments under the guarantee is remote. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. The Company adopted the disclosure provisions of FIN 45 effective December 31, 2002. FIN 45's initial recognition and initial measurement provisions are applicable on a prospective basis to guarantees issued or modified after December 31, 2002.

In January of 2003, the FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities ("FIN 46"). FIN 46 clarifies the application of existing accounting pronouncements to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. The provisions of FIN 46 will be immediately effective for all variable interests in variable interest entities created after January 31, 2003, and the Company will need to apply its provisions to any existing variable interests in variable interest entities by no later than September 30, 2003. The Company does not believe that FIN 46 will have a significant impact on the Company's financial statements.

## **2. Stock Option Plan**

The Company elected Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees ("APB No. 25") and related Interpretations in accounting for its employee stock options. Under APB No. 25, no compensation expense is recognized because the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant.

Pro forma information regarding net income and earnings per share is required by SFAS No. 123, and has been determined as if the Company had accounted for its employee stock options under the fair value method. The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions for 2003 and 2002 respectively: risk-free interest rate of 4% for 2003 and 5% for 2002; volatility factor of the expected market price of the Company's common stock based on historical results of 0.166 for 2003 and 0.236 for 2002, and dividend yield of 6% in 2003 and 2002, and an expected option life of four years. On March 13, 2003, the Company granted options to acquire 45,000 shares at an exercise price of \$36.20 that will expire in 2013.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and changes in the subjective input assumptions can materially affect the fair value estimate, management believes the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting period. The Company's pro forma information is as follows (in thousands except for earnings per share information):

**Notes to Condensed Consolidated Financial Statements  
(Unaudited)**

**2. Stock Option Plan (continued)**

	Three Months Ended June 30,		Six Months E June 30
	2003	2002	2003
Net income to common shareholders; as reported.....	\$24,705	\$13,408	\$43,118
Add: Stock based employee expense included in reported net income.....	-	-	-
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of minority interest..	(366)	(521)	(733)
Pro forma net income.....	\$24,339	\$12,887	\$42,385
Earnings per share: .....			
Basic - as reported.....	\$0.59	\$0.35	\$1.03
Basic - proforma.....	0.58	0.34	1.01
Diluted - as reported.....	\$0.56	\$0.34	\$0.99
Diluted - proforma.....	0.55	0.33	0.97

**3. Acquisitions and Dispositions****Acquisitions**

On June 12, 2003, the Company purchased The Crossings Factory Stores, a 390,000 square-foot outlet center located in Tannersville, Pennsylvania for \$111.3 million, including closing costs, and assumed a \$60.7 million 5.85% mortgage loan due 2013. An additional \$5.0 million will be due to the sellers upon the completion of a 21,000 square-foot expansion scheduled to open in late summer 2004, subject to permits. The Company is in the process of finalizing the purchase price allocation and is considering the fair value of the mortgage assumed, the in-place leases, land and building.

**Dispositions**

On June 2, 2003, the Company sold a 23,000 square-foot Premium Outlet Center located in St. Helena, California for \$7.4 million resulting in a gain of approximately \$4.7 million. The center partially secured a mortgage note due April 2010 and \$5.0 million of the sales proceeds were used to pay down the mortgage loan. The aggregate revenues and net income of the sold property were \$0.2 million and \$0.1 million for the three months ended June 30, 2003, and \$0.4 million and \$0.2 million for the six months ended June 30, 2003.

**4. Investments in Affiliates**

The Company holds several non-controlling interests in domestic and international joint ventures accounted for under the equity method. Equity in earnings or losses of these affiliates and related management advisory, license, leasing and guarantee fees earned are included in income from unconsolidated investments in the accompanying financial



statements.

As of June 30, 2003, the Company's interests in joint ventures included a 40% interest in Chelsea Japan Co., Ltd. ("Chelsea Japan"), a 50% interest in two Premium Outlet Centers with Simon Property Group, Inc. ("Simon"), a 50% interest in a strategic alliance with Sordo Madaleno y Asociados and Mr. Carlos Peralta of Mexico City ("Chelsea Mexico"), minority interests in various outlet centers and development projects in Europe operated by Value Retail PLC ("Value Retail") and 100% of the non-voting preferred stock and 50% of the non-voting common stock of Chelsea Interactive, representing 40% of the total common stock.

#### **Notes to Condensed Consolidated Financial Statements (Unaudited)**

#### **4. Investments in Affiliates (continued)**

In March 2003, Chelsea Japan opened the 180,000 square-foot first phase of Sano Premium Outlets, located 40 miles north of Tokyo. Chelsea Japan has two other centers: Gotemba Premium Outlets, located to the west of Tokyo, a 220,000 square-foot center, was expanded by an additional 170,000 square feet in July 2003; Rinku Premium Outlets, located near Osaka, is a 250,000 square-foot center including a 70,000 square-foot second phase that opened in March 2002.

In June 2002, the Company and Simon entered into a 50/50 joint venture to develop and operate Las Vegas Premium Outlets, a 435,000 square-foot single-phase outlet center located in Las Vegas, Nevada, which opened on August 1, 2003. The Company is responsible for financing its 50% share of development costs, or approximately \$48.0 million. As of June 30, 2003, the Company had contributed \$36.6 million and capitalized interest and other costs of \$2.3 million.

In August 2002, the Company and Simon entered into a 50/50 joint venture to develop and operate Chicago Premium Outlets, a 438,000 square-foot single-phase outlet center located in Aurora, Illinois, scheduled to open in mid-2004. The Company is responsible for financing its 50% share of the development costs, or approximately \$46.0 million. As of June 30, 2003, the Company had contributed \$12.8 million and capitalized interest and other costs of \$1.2 million.

At June 30, 2003, the Company had incurred approximately \$1.9 million related to pre-development costs and formation of the Chelsea Mexico joint venture.

At June 30, 2003, the Company had minority interests ranging from 3% to 8% in several outlet centers and outlet development projects in Europe.

At December 31, 2002, the Company recognized an impairment loss equal to the net book value of its investment in Chelsea Interactive. The Company believes that it will not be able to recover the net book value of its investment in Chelsea Interactive through future cash flows before reaching the Company's \$60.0 million funding limit. Through June 30, 2003, the Company had funded \$54.1 million and anticipates that the \$5.9 million funding balance may be used to further develop the platform and/or to fund operating cash shortfalls and potential costs related to the disposal or discontinuance of the business. A \$0.9 million and \$1.7 million funding loss was reported for the three and six months ended June 30, 2003, respectively. Future funding by the Company will be reported as a loss in the period funding is required. The Company has signed a joint venture agreement with a third party to restructure Chelsea Interactive, subject to the satisfaction of certain conditions. There can be no assurance that this joint venture will be successful or that Chelsea Interactive will be able to continue as a going concern.

The following is a summary of investments in and amounts due from affiliates at June 30, 2003 (in thousands):

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	Chelsea Japan	Simon- Ventures	Chelsea Mexico	Other	
Balance December 31, 2002	\$12,471	\$31,919	\$ -	\$3,607	\$4
Additional investment	487	20,956	1,912	25	2
Income from unconsolidated investments	3,946	-	-	-	-
Distribution and fees	(2,706)	-	-	-	(
Advances (net)	98	59	-	-	-
Balance June 30, 2003	<b>\$14,296</b>	<b>\$52,934</b>	<b>\$1,912</b>	<b>\$3,632</b>	<b>\$7</b>

**Notes to Condensed Consolidated Financial Statements  
(Unaudited)**

**4. Investments in Affiliates (continued)**

The Company's share of income (loss) before depreciation, depreciation expense and income (loss) from unconsolidated investments for the three and six months ended June 30, 2003, and 2002, are as follows (in thousands):

	For the Three Months Ended June 30,					
	2003			2002		
	Income (loss) before Depreciation	Depr.	Income (loss) from Unconsol. Investments	Income (loss) before Depreciation	Depr.	Income (loss) from Unconsol. Investments
Chelsea Japan	\$3,189	\$694	\$2,495	\$1,595	\$ 433	\$1,162
F/C (1)	-	-	-	2,546	726	1,820
<b>Total</b>	<b>\$3,189</b>	<b>\$694</b>	<b>\$2,495</b>	<b>\$4,141</b>	<b>\$1,159</b>	<b>\$2,982</b>
Chelsea Interactive	(\$ 905)	\$ -	(\$ 905)	(\$1,716)	\$2,060	(\$3,776)

	For the Six Months Ended June 30,					
	2003			2002		
	Income (loss) before Depreciation	Depr.	Income (loss) from Unconsol. Investments	Income (loss) before Depreciation	Depr.	Income (loss) from Unconsol. Investments
Chelsea Japan	\$5,239	\$1,293	\$3,946	\$2,887	\$832	\$2,055
F/C (1)	-	-	-	4,809	1,447	3,362
Simon- Orlando (2)	-	-	-	1,833	523	1,310
Other	-	-	-	25	-	25
<b>Total</b>	<b>\$5,239</b>	<b>\$1,293</b>	<b>\$3,946</b>	<b>\$9,554</b>	<b>\$2,802</b>	<b>\$6,752</b>
Chelsea						

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Interactive.....	(\$1,742)	\$ -	(\$1,742)	(\$2,908)	\$3,568	(\$6,476)
	=====	=====	=====	=====	=====	=====

- (1) During the three and six months ended June 30, 2002, the Company had a 49% interest in a joint venture, F/C Acquisition, that owns four Premium Outlet centers. In August 2002, the Company became the sole owner of F/C Acquisition by acquiring the remaining 51% undivided ownership interest from the joint venture partner, and consolidated the operations and balance sheet from the buyout date.
- (2) During the three months ended March 31, 2002, the Company had a 50% interest in Orlando Premium Outlets through a 50/50 joint venture with Simon. In April 2002, the Company became the sole owner of Orlando Premium Outlets by acquiring the remaining 50% undivided ownership interest from Simon, and consolidated the operations and balance sheet from the buyout date.

**Notes to Condensed Consolidated Financial Statements  
(Unaudited)**

**4. Investments in Affiliates (continued)**

Condensed financial information as of June 30, 2003, and December 31, 2002, and for the three and six months ended June 30, 2003, and 2002 for investments in unconsolidated affiliates is as follows:

	Retail	Chelsea Interactive
	-----	-----
<b>Property, plant and equipment (net)</b>		
June 30, 2003.....	\$210,246	\$ -
December 31, 2002 (3).....	140,057	-
<b>Total assets</b>		
June 30, 2003.....	265,634	-
December 31, 2002 (3).....	190,157	-
<b>Long term debt</b>		
June 30, 2003.....	95,082	-
December 31, 2002.....	75,139	-
<b>Total liabilities</b>		
June 30, 2003.....	154,947	1,656
December 31, 2002.....	119,886	1,548
<b>Net income (loss)</b>		
Three months ended:		
June 30, 2003.....	2,448	-
June 30, 2002 (1).....	4,055	(3,776)
<b>Six months ended:</b>		
June 30, 2003.....	3,100	-
June 30, 2002 (1) (2).....	9,047	(7,337)
<b>Company's share of net income (loss)</b>		
Three months ended:		
June 30, 2003.....	979	(905)
June 30, 2002 (1).....	1,865	(3,776)
Six months ended:		

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June 30, 2003.....	1,240	(1,742)
June 30, 2002 (1) (2) .....	4,284	(6,476)
<b>Fee income</b>		
Three months ended:		
June 30, 2003.....	1,516	-
June 30, 2002 (1) .....	1,117	-
Six months ended:		
June 30, 2003.....	2,706	-
June 30, 2002 (1) (2) .....	2,468	-

- (1) During the three and six months ended June 30, 2002, the Company had a 49% interest in a joint venture, F/C Acquisition, that owns four Premium Outlet centers. In August 2002, the Company became the sole owner of F/C Acquisition by acquiring the remaining 51% undivided ownership interest from the joint venture partner, and consolidated the operations and balance sheet from the buyout date.
- (2) During the three months ended March 31, 2002, the Company had a 50% interest in Orlando Premium Outlets through a 50/50 joint venture with Simon. In April 2002, the Company became the sole owner of Orlando Premium Outlets by acquiring the remaining 50% undivided ownership interest from Simon, and consolidated the operations and balance sheet from the buyout date.
- (3) At December 31, 2002, Chelsea Interactive recorded an impairment loss equal to the carrying amount of its net assets.

### Notes to Condensed Consolidated Financial Statements (Unaudited)

#### 5. Non-Compete Agreement

The Company recognized income from its non-compete agreement with The Mills Corporation of \$1.3 and \$2.6 million during the three and six months ended June 30, 2002, which is included in other income in the accompanying financial statements.

#### 6. Debt

##### Unsecured Bank Debt

The Company has a \$200.0 million senior unsecured bank line of credit (the "Senior Credit Facility") with an expiration date of March 31, 2005, which the Company has the right to extend until March 31, 2006. The Senior Credit Facility bears interest on the outstanding balance, payable monthly, at a rate equal to the London Interbank Offered Rate ("LIBOR") plus 1.05% (2.21% at June 30, 2003) or the prime rate, at the Company's option. The LIBOR rate spread ranges from 0.85% to 1.50% depending on the Company's Senior Debt rating. The Company received a debt rating upgrade in July 2003, resulting in a reduction of the LIBOR rate spread to 0.95% from 1.05%. At June 30, 2003, \$78.0 million was outstanding under the Senior Credit Facility.

The Company also has a \$5.0 million term loan that carries the same interest rate and maturity as the Senior Credit Facility.

##### Unsecured Notes

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A summary of the terms of the unsecured notes outstanding at June 30, 2003, and December 31, 2002, is as follows (in thousands):

	June 30, 2003	December 31, 2002	Effective Yield (1)
8.375% Unsecured Notes due August 2005.....	\$ 49,937	\$ 49,922	8.44%
7.25% Unsecured Notes due October 2007.....	124,857	124,841	7.39
8.625% Unsecured Notes due August 2009.....	49,938	49,933	8.76
8.25% Unsecured Notes due February 2011.....	148,890	148,817	8.40
6.875% Unsecured Notes due June 2012.....	99,869	99,825	6.90
6.00% Unsecured Notes due January 2013.....	148,093	147,992	6.18
<b>Total</b>	<b>\$621,584</b>	<b>\$621,330</b>	

(1) Including discount on the notes

**Notes to Condensed Consolidated Financial Statements  
(Unaudited)**

**6. Debt (continued)**

**Mortgage Debt**

A summary of the terms of the mortgage debt outstanding at June 30, 2003, and December 31, 2002, and the related interest rate and Net Book Value ("NBV") of the associated collateral as of June 30, 2003, are as follows (in thousands):

	June 30, 2003	December 31, 2002	Effective Interest Rate	NBV
Due July 2008 (1)	\$166,236	\$167,723	7.26%	\$255,043
Due April 2010 (2)	61,975	67,250	7.26%	68,352
Due December 2012 (3)	70,974	71,482	7.67%	74,948
Due March 2013 (4)	64,163	-	5.10%	114,426
	<b>\$363,348</b>	<b>\$306,455</b>		<b>\$512,769</b>

(1) The mortgage loan due July 2008 was consolidated as part of the August 2002 buyout of a joint venture partner's 51% interest in the F/C Acquisition joint venture. The mortgage calls for a \$1.2 million fixed monthly debt service payment based on a 26-year amortization schedule. During the six months ended June 30, 2003, the Company recognized \$67,000 in debt discount amortization that is included in interest expense in the accompanying financial statements.

(2) Chelsea Financing entered into a \$70.0 million mortgage loan due April 2010 originally secured by its four properties. On June 2, 2003 the Company sold one of the encumbered properties for \$7.4 million with a NBV of \$2.5 million. Proceeds of \$5.0 million were used to pay down the mortgage loan. The loan bears interest equal to LIBOR plus 1.50% (2.82% at June 30, 2003) or prime rate plus 1.0% and calls for quarterly principal

amortization of \$0.25 million through April 2005 and thereafter \$0.45 million per quarter until maturity. In December 2000, the Company entered into an interest rate swap agreement to hedge against unfavorable fluctuations in LIBOR rates by fixing the interest rate at 7.26% until January 2006. During the six months ended June 30, 2003, and 2002, the Company recognized interest expense of \$1.5 million on the hedge that is included in interest expense in the accompanying financial statements.

- (3) The mortgage loan due December 2012 was assumed as part of a September 2001 acquisition. The loan calls for a \$0.5 million fixed monthly debt service payment based on a 26-year amortization schedule. During the six months ended June 30, 2003, and 2002, the Company recognized \$0.2 million in debt premium amortization that is included in interest expense in the accompanying financial statements.
- (4) The mortgage loan due March 2013 was assumed as part of a June 2003 acquisition. The stated interest rate of 5.85% was greater than that available to the Company for comparable debt. Accordingly, the Company recorded a \$3.4 million debt premium that will be amortized over the period of the loan which reduces the effective interest rate to 5.10%. The loan calls for a \$0.4 million fixed monthly debt service payment on a 25-year amortization schedule.

Interest and loan costs of approximately \$1.3 million and \$0.6 million were capitalized as development costs during the three months ended June 30, 2003, and 2002, respectively; and approximately \$2.2 million and \$1.3 million during the six months ended June 30, 2003, and 2002, respectively.

**Notes to Condensed Consolidated Financial Statements  
(Unaudited)**

**7. Financial Instruments: Derivatives and Hedging**

The Company employs interest rate and foreign currency forwards or purchased options to hedge qualifying anticipated transactions. Gains and losses are deferred and recognized in net income in the same period that the underlying hedged transaction affects net income, expires or is otherwise terminated or assigned.

At June 30, 2003 the Company's interest rate swap was reported at its fair value and classified as an other liability of \$6.9 million. At June 30, 2003, there were \$6.4 million in deferred losses, recorded in accumulated other comprehensive loss, a shareholder's equity account, and minority interest. During the three months ended June 30, 2003, the Company reclassified \$0.5 million of other comprehensive loss to other expense as a result of its \$5.0 million pay down of swapped mortgage debt in June 2003.

Hedge Type	Notional Value	Rate	Maturity	Fair Value
Swap, Cash Flow	\$67.0 million	5.7625%	1/1/06	(\$6.9 million)

The notional value and fair value of the above hedge provides an indication of the extent of the Company's involvement in financial derivative instruments at June 30, 2003, but does not represent exposure to credit, interest rate, foreign exchange or market risk.

**Notes to Condensed Consolidated Financial Statements  
(Unaudited)**

**8. Stockholders' Equity**

Following is a statement of stockholders' equity at June 30, 2003, (in thousands):

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	Preferred Stock At Par Value	Common Stock At Par Value	Paid- in Capital	Officer Loan	Distrib. in Excess of Net Income	Accum. Other Comp. (Loss) Income	To Stoc E
<b>Balance December 31, 2002.....</b>	<b>\$8</b>	<b>\$415</b>	<b>\$574,352</b>	<b>(\$488)</b>	<b>(\$112,648)</b>	<b>(\$5,808)</b>	<b>\$45</b>
Net income.....	-	-	-	-	44,786	-	4
Other comprehensive loss							
Foreign currency translation..	-	-	-	-	-	(41)	
Interest rate swap.....	-	-	-	-	-	433	
Total comprehensive income.....							4
Preferred dividend.....	-	-	-	-	(1,668)	-	(
Cash distributions declared							
(\$1.07 per common share).....	-	-	-	-	(45,390)	-	(4
Exercise of stock options.....	-	3	3,923	-	-	-	
Shares issued (net of cost).....	-	12	49,370	-	-	-	4
Shares issued in exchange for units of the OP.....	-	1	1,254	-	-	-	
Shares issued through Employee Stock Purchase Plan (net of costs).....	-	-	153	-	-	-	
<b>Balance June 30, 2003.....</b>	<b>\$8</b>	<b>\$431</b>	<b>\$629,052</b>	<b>(\$488)</b>	<b>(\$114,920)</b>	<b>(\$5,416)</b>	<b>\$5</b>

On June 18, 2003, the Company sold 1.2 million shares of common stock at a price of \$42.10 per share, yielding net proceeds after expenses of \$49.4 million, which were used to repay borrowings under the Company's Senior Credit Facility associated with the Company's Tannersville acquisition.

## 9. Dividends

On June 5, 2003, the Board of Directors of the Company declared a \$0.535 per share dividend to shareholders of record on June 30, 2003. The dividend, totaling \$23.0 million, was paid on July 14, 2003. The OP simultaneously paid a \$0.535 per unit cash distribution, totaling \$4.0 million, to its minority unitholders.

## 10. Income Taxes

At June 30, 2003, the Company was in compliance with all REIT requirements under Section 856(c) of the Internal Revenue Code of 1986, as amended, and as such, was not subject to federal income taxes.

## 11. Net Income Per Common Share

Basic earnings per common share is computed using the weighted average number of shares outstanding. Diluted earnings per common share is computed using the weighted average number of shares outstanding adjusted for the incremental shares attributed to outstanding options to purchase common stock of 2.0 million and 1.5 million shares for the three months ended June 30, 2003 and 2002, respectively; and 1.9 million and 1.4 million for the six months ended June 30, 2003, and 2002, respectively.

### Notes to Condensed Consolidated Financial Statements (Unaudited)

**11. Net Income Per Common Share (continued)**

The following table sets forth the computation of basic and diluted earnings per share for the periods indicated:

(In thousands, except per share amounts)	Three Months Ended June 30,		Six Months Ended June	
	2003	2002	2003	2002
<b>Numerator</b>				
Numerator for basic and diluted earnings per share - net income available to common shareholders.....	\$24,705	\$13,408	\$43,118	\$22,816
<b>Denominator</b>				
Denominator for basic earnings per share- Weighted average shares.....	42,041	37,877	41,801	37,877
Effect of dilutive securities- Stock options.....	1,956	1,498	1,854	1,498
Denominator for diluted earnings per share- Adjusted weighted average shares assumed conversions.....	43,997	39,375	43,655	39,375
<b>Per share amounts:</b>				
Net income - basic.....	\$0.59	\$0.35	\$1.03	\$0.60
Net income - diluted.....	\$0.56	\$0.34	\$0.99	\$0.58

**12. Commitments and Contingencies**

In connection with the Simon joint ventures, the Company has committed to provide 50% of the development costs, or approximately \$48.0 million for Las Vegas Premium Outlets and \$46.0 million for Chicago Premium Outlets. As of June 30, 2003, the Company had contributed \$36.6 million and \$12.8 million to the Las Vegas and Chicago projects, respectively.

Borrowings related to Chelsea Japan for which the Company and the OP have provided guarantees for repayment of debt as of June 30, 2003, are as follows:

Total Facility		Outstanding		Due Date	Interest Rate
Yen	US \$ Equivalent	Yen	US \$ Equivalent		
4.0 billion (1)	\$33.4 million	10.9 billion	\$7.9 million	2004	1.41%
3.8 billion (2)	31.7 million	13.4 billion	28.1 million	2015	2.20%
0.6 billion (2)	5.0 million	10.5 billion	4.5 million	2012	1.50%

- Facility entered into by an equity investee of the Company that has a one-year extension option until April 1, 2005.
- Facilities entered into by Chelsea Japan, secured by Gotemba and Rinku and 40% severally guaranteed by the Company.

In May 2002, the Company entered into a 50/50 joint venture agreement with Sordo Madaleno y Asociados and Mr. Carlos Peralta of Mexico City to jointly develop premium outlet centers in Mexico. Subject to leasing and entitlements, construction on the 232,000 square-foot first phase of the outlet project is scheduled to commence later in 2003 and open in late 2004. The site can support a second phase containing approximately 165,000 square feet of GLA. Once Phase I of the project has been approved, the Company will be committed to fund approximately \$14



million which is 50% of the development costs.

### **Notes to Condensed Consolidated Financial Statements (Unaudited)**

#### **12. Commitments and Contingencies (continued)**

As of June 30, 2003, the Company had provided limited debt service guarantees of approximately \$17.3 million to Value Retail and affiliates, under a standby facility for loans provided to Value Retail and affiliates to construct outlet centers in Europe. The standby facility, which has a maximum limit of \$22.0 million, expired in November 2001 and outstanding guarantees shall not survive more than five years after project completion.

At June 30, 2003, other assets includes \$9.4 million and accrued expenses and other liabilities include \$12.8 million related to the 2002 deferred unit incentive program which may be paid to certain key officers in 2007.

The Company is not presently involved in any material litigation nor, to its knowledge, is any material litigation threatened against the Company or its properties, other than routine litigation arising in the ordinary course of business. Management believes the cost incurred by the Company related to any of its litigation will not be material and have been adequately provided for in the consolidated financial statements.

#### **13. Related Party Information**

In 1999, the OP established a \$6.0 million secured loan facility that will expire in June 2004 for the benefit of certain unitholders. Each borrower issued a note that is secured by OP units, bears interest at a rate of LIBOR plus 200 basis points per annum payable quarterly and is due by the facility expiration date. At June 30, 2003, loans made to two unitholders, who are also officers of the Company, totaled \$3.2 million, \$0.5 million of which was used to exercise Company stock options and is reflected as a reduction to stockholder's equity in the accompanying financial statements. Effective June 2002, the Company changed its policy to eliminate new loans to directors and officers.

In August 1997, the Company and one of its directors entered into a Consulting Agreement pursuant to which the director agreed to perform services for the Company in connection with the development and operation of manufacturer's outlet centers in Japan and Hawaii. The agreement provided for payments to the director of \$10,000 per month and was terminated by the Company in December 1999. During the term of the agreement and for four years after the termination of the agreement, the director will be entitled to deferred compensation of 1% of the development costs, up to a maximum amount of \$0.5 million per project, on all projects in which he was involved in Japan or Hawaii either directly or as a result of Mitsubishi and/or Nissho Iwai committing to develop such project with the Company in Japan. Fees paid under this agreement totaled \$0.3 million for the six months ended June 30, 2003. These fees are included in investment in affiliates in the accompanying financial statements.

#### **14. Segment Information**

The Company is principally engaged in the development, ownership, acquisition and operation of manufacturers' outlet centers and has determined that under SFAS No.131 "Disclosures About Segments of an Enterprise and Related Information" it has three reportable retail real estate segments: Premium domestic, other domestic and international. The Company evaluates real estate performance and allocates resources based on Net Operating Income ("NOI") defined as total revenue less operating and maintenance expense. The primary sources of revenue are generated from tenant base rents, percentage rents and reimbursement revenue. Operating expenses primarily consist of common area maintenance, real estate taxes and promotional expenses. The retail real estate business segments meet the quantitative threshold for determining reportable segments.

**Notes to Condensed Consolidated Financial Statements  
(Unaudited)**

**14. Segment Information (continued)**

(in thousands)	Premium Domestic	Other Domestic	International	Other	Total
		(1)	(2)	(3)	
<b>Total revenues</b>					
Three months ended:					
June 30, 2003.....	\$64,605	\$23,248	\$ -	\$ (447)	\$87,406
June 30, 2002.....	50,924	12,555	-	1,363	64,842
Six months ended:					
June 30, 2003.....	126,770	45,193	-	(415)	171,548
June 30, 2002.....	94,799	23,784	-	2,740	121,323
<b>Interest income</b>					
Three months ended:					
June 30, 2003.....	252	10	-	61	323
June 30, 2002.....	257	40	-	78	375
Six months ended:					
June 30, 2003.....	507	14	-	93	614
June 30, 2002.....	540	64	-	171	775
<b>Income from unconsolidated investments</b>					
Three months ended:					
June 30, 2003.....	-	-	2,495	(905)	1,590
June 30, 2002.....	1,819	-	1,163	(3,776)	(794)
Six months ended:					
June 30, 2003.....	-	-	3,946	(1,742)	2,204
June 30, 2002.....	4,672	-	2,080	(6,476)	276
<b>NOI</b>					
Three months ended:					
June 30, 2003.....	46,738	15,525	4,102	(4,278)	62,087
June 30, 2002.....	40,453	6,017	2,148	(1,819)	46,799
Six months ended:					
June 30, 2003.....	92,005	29,988	6,516	(7,135)	121,374
June 30, 2002.....	77,039	10,947	3,851	(2,563)	89,274
<b>Fixed asset additions</b>					
Six months ended:					
June 30, 2003.....	6,711	61,424	-	661	68,796
June 30, 2002.....	47,036	29,088	-	831	76,955
<b>Total assets</b>					
June 30, 2003.....	1,147,618	620,863	17,928	30,206	1,816,615
December 31, 2002.....	1,262,190	394,984	16,077	29,779	1,703,030

- (1) Approximately 15% and 25% of the GLA is occupied by and approximately 7% and 13% of annualized base rent is derived from one tenant during the 2003 and 2002 periods, respectively.
- (2) Principally comprised of the Company's interest in Chelsea Japan.
- (3) Includes corporate overhead assets and results from Chelsea Interactive.

**Notes to Condensed Consolidated Financial Statements  
(Unaudited)**

**14. Segment Information (continued)**

Following is a reconciliation of net operating income to net income for the three and six months ended June 30, 2003, and 2002 (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Segment NOI.....	\$62,087	\$46,799	\$121,374	\$89,274
Interest expense - consolidated.....	(16,553)	(10,843)	(33,187)	(20,593)
Interest expense - unconsolidated investments.....	(189)	(139)	(333)	(267)
Depreciation and amortization expense - consolidated...	(17,269)	(14,243)	(34,901)	(27,184)
Depreciation and amortization expense - unconsolidated investments.....	(694)	(1,159)	(1,293)	(2,802)
Depreciation and amortization expense - Chelsea Interactive.....	-	(2,060)	-	(3,568)
Income tax - unconsolidated investments.....	(724)	(413)	(944)	(672)
Gain on sale of discontinued operations.....	4,008	-	4,008	-
Minority interest.....	(5,127)	(3,685)	(9,938)	(7,140)
Net income.....	<b>\$25,539</b>	<b>\$14,257</b>	<b>\$44,786</b>	<b>\$27,048</b>

**15. Fair Value of Financial Instruments**

The following disclosures of estimated fair value were determined by management, using available market information and appropriate valuation methodologies. Considerable judgment is necessary to interpret market data and develop estimated fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize on disposition of the financial instruments. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

Cash equivalents, accounts receivable, accounts payable, and revolving credit facilities balances reasonably approximate their fair values due to the short maturities of these items. Mortgage debt and the unsecured notes payable have an estimated fair value based on discounted cash flow models of approximately \$1.0 billion, which exceeds the book value by \$0.1 billion. Unsecured bank debt is carried at an amount which reasonably approximates its fair value since it is a variable rate instrument whose interest rate reprices frequently.

Disclosure about fair value of financial instruments is based on pertinent information available to management as of June 30, 2003. Although management is not aware of any factors that would significantly affect the reasonable fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since such date and current estimates of fair value may differ significantly from the amounts presented herein.

**16. Subsequent Events**

On August 1, 2003, the Company acquired Belz Factory Outlet World Las Vegas, a 477,000 square-foot outlet center in Las Vegas, Nevada for \$104.0 million including the assumption of a \$24.4 million 8.12% mortgage loan due 2012. As part of the same transaction, the Company acquired Belz Factory Outlet World Lakeland, a 319,000 square-foot outlet center near Memphis, Tennessee for an additional \$3.5 million. The Lakeland property is expected to be marketed for sale shortly after closing. The approximately \$84.0 million cash portion of the overall transaction was financed through a \$100 million one-year bridge loan facility at an annual interest rate of LIBOR plus 0.80% that is due on July 31, 2004 and extendible for six months until January 31, 2005 at the Company's option. The LIBOR rate spread ranges from 0.70% to 1.35% depending on the Company's Senior Debt rating. Surplus proceeds from the

financing of approximately \$16.0 million will be used for general corporate purposes.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in connection with the accompanying unaudited condensed consolidated financial statements and notes thereto. These financial statements include all adjustments, which in the opinion of management are necessary to reflect a fair statement of results for all interim periods presented, and all such adjustments are of a normal recurring nature.

### General Overview

From July 1, 2002 to June 30, 2003, the Company has grown rental revenue by \$39.8 million to \$128.9 million. This was achieved by increasing rents, expanding three wholly-owned centers and acquiring seven centers in 2002 and one center in 2003. These increases were partially offset by rent decreases from selling three non-core centers. Increasing rents at operating centers resulted in base rent growth of \$1.6 million. The Company re-leased or renewed approximately 1.2 million square feet of Premium Property GLA during the twelve months ended June 30, 2003, for which initial contractual cash rents under new leases were 12% higher than expiring leases. The expansion of three wholly-owned centers increased base rents by \$0.8 million. The acquisition of eight centers increased rental revenue by \$17.4 million. In addition, the purchase of ownership interests in the five centers previously held as unconsolidated investments resulted in rental revenue growth of \$19.5 million and a decrease in income from unconsolidated investments of \$2.8 million. Income from unconsolidated investments for Chelsea Japan grew due to higher earnings, increased fees, the expansion of Rinku Premium Outlets in March 2002 and the opening of Sano Premium Outlets in March 2003.

At June 30, 2003, the Company wholly or partially-owned 14.9 million square feet of GLA. Since July 1, 2002, the Company has added 2.2 million square feet ("sf") of net GLA and details are as follows:

Net GLA added since July 1, 2002 is detailed as follows:

	12 months ended June 30, 2003	6 months ended June 30, 2003	6 months ended December 31, 2002
<b>Changes in GLA (sf in 000's):</b>			
<b>New centers developed:</b>			
Sano Premium Outlets (40% owned) .....	180	180	-
<b>Centers expanded:</b>			
Desert Hills Premium Outlets.....	23	-	23
Liberty Village Premium Outlets.....	23	-	23
Other.....	(31)	(22)	(9)
<b>Total centers expanded.....</b>	<b>15</b>	<b>(22)</b>	<b>37</b>
<b>Centers acquired:</b>			
The Crossings Factory Stores.....	390	390	-
Factory Outlet Village Osage Beach .....	391	-	391
St. Augustine Premium Outlets .....	329	-	329
Outlets at Albertville.....	305	-	305
Factory Merchants Branson.....	300	-	300
Jackson Outlet Village.....	292	-	292
Johnson Creek Outlet Center.....	278	-	278
<b>Total centers acquired.....</b>	<b>2,285</b>	<b>390</b>	<b>1,895</b>

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<b>Centers sold:</b>			
St. Helena Premium Outlets.....	(23)	(23)	-
Three Other Properties.....	(256)	-	(256)
	-----	-----	-----
<b>Total centers sold.....</b>	<b>(279)</b>	<b>(23)</b>	<b>(256)</b>
<b>Net GLA added during the period.....</b>	<b>2,201</b>	<b>525</b>	<b>1,676</b>
<b>GLA at end of period.....</b>	<b>14,911</b>	<b>14,911</b>	<b>14,386</b>

**Results of Operations**

*Comparison of the three months ended June 30, 2003, to the three months ended June 30, 2002.*

Income from continuing operations before minority interest, increased \$8.7 million, or 48.9 %, to \$26.6 million for the three months ended June 30, 2003, from \$17.9 million for the three months ended June 30, 2002. This increase was primarily the result of the buyout of ownership interests in four centers in 2002, the acquisition of six centers in 2002 and one center in 2003, higher rents from releasing and renewals, and a decrease in the loss from Chelsea Interactive, partially offset by increases in general and administrative, interest and other expenses.

Base rentals increased \$16.8 million, or 39.0%, to \$60.0 million for the three months ended June 30, 2003, from \$43.2 million for the three months ended June 30, 2002, due to the buyout of ownership interests in four centers in 2002 and the acquisition of six centers in 2002 and one center in 2003, higher average rents on releasing and renewals, and the expansion of two wholly-owned centers in late 2002.

Percentage rents increased \$0.5 million, or 11.8%, to \$5.0 million for the three months ended June 30, 2003, from \$4.5 million for the three months ended June 30, 2002, primarily due to the buyout of ownership interests in four centers in 2002 and the acquisition of six centers in 2002.

Expense reimbursements, representing contractual recoveries from tenants of certain common area maintenance, operating, real estate tax, promotional and management expenses, increased \$6.1 million, or 42.2%, to \$20.6 million for the three months ended June 30, 2003, from \$14.5 million for the three months ended June 30, 2002, due to the recovery of operating and maintenance costs from increased GLA. The average recovery of reimbursable expenses for the Premium Portfolio was 90% for the three months ended June 30, 2003, compared to 88% for the three months ended June 30, 2002. The average recovery of reimbursable expenses for the Other Retail Centers was 70% for the three months ended June 30, 2003, compared to 55% for the three months ended June 30, 2002. The increase in average recovery on the Other Retail Centers is a result of the centers acquired in 2002.

Other income decreased \$0.9 million or 33.0% to \$1.8 million for the three months ended June 30, 2003, from \$2.7 million for the three months ended June 30, 2002, primarily due to the expiration of the non-compete agreement which included income recognition of \$1.3 million in 2002 partially offset by a \$0.3 million gain on an outparcel sale in 2003.

Operating and maintenance expenses increased \$6.4 million, or 35.2%, to \$24.5 million for the three months ended June 30, 2003, from \$18.1 million for the three months ended June 30, 2002. The increase was primarily due to costs related to increase in GLA.

Depreciation and amortization expense increased \$3.1 million, or 21.3% to \$17.3 million for the three months ended June 30, 2003, from \$14.2 million for the three months ended June 30, 2002. The increase was due to depreciation of the increased GLA.

General and administrative expense increased \$0.6 million or 28.5% to \$2.5 million for the three months ended June 30, 2003, from \$1.9 million for the three months ended June 30, 2002, primarily due to increases in deferred unit incentive program accrual, salaries and professional fees.

Other expenses increased \$0.5 million or 50.4% to \$1.6 million for the three months ended June 30, 2003, from \$1.1 million for the three months ended June 30, 2002, due to a non-cash charge of \$0.5 million on an interest rate swap resulting from the pay down of a hedged mortgage loan in June 2003 related to the sale of St. Helena Premium Outlets.

Income from unconsolidated investments decreased \$0.5 million or 16.3% to \$2.5 million for the three months ended June 30, 2003, from \$3.0 million for the three months ended June 30, 2002, due to the buyout of ownership interest in four centers which were previously held as unconsolidated investments partially offset by higher income and fees including a one-time leasing fee of \$0.6 million from Chelsea Japan.

The loss from Chelsea Interactive decreased \$2.9 million or 76.0% to \$0.9 million for the three months ended June 30, 2003, from \$3.8 million for the three months ended June 30, 2002, due to the write-off of the Company's investment at December 31, 2002. The June 30, 2003 loss represents second quarter funding to Chelsea Interactive.

Interest expense increased \$5.7 million or 52.7% to \$16.5 million for the three months ended June 30, 2003, from \$10.8 million for the three months ended June 30, 2002, due to higher debt that partially financed acquisitions and the buyouts of partner's interests.

Income from discontinued operations of \$0.1 million for the three months ended June 30, 2003 and 2002, and gain on sale of discontinued operations of \$4.0 million, net of minority interest of \$0.7 million for the three months ended June 30, 2003, relates to the June 2003 sale of St. Helena Premium Outlets, a 23,000 square-foot Premium Property.

## **Results of Operations**

### ***Comparison of the six months ended June 30, 2003, to the six months ended June 30, 2002.***

Income from continuing operations before minority interest, increased \$16.6 million, or 48.8%, to \$50.5 million for the six months ended June 30, 2003, from \$34.0 million for the six months ended June 30, 2002. This increase was primarily the result of the buyouts of ownership interests in five centers in 2002, the acquisition of seven centers in 2002 and one center in 2003, higher rents from releasing and renewals and decrease in the loss from Chelsea Interactive, partially offset by increases in general and administrative, interest and other expenses.

Base rentals increased \$38.2 million, or 46.8%, to \$119.8 million for the six months ended June 30, 2003, from \$81.6 million for the six months ended June 30, 2002, due to the buyouts of ownership interests in five centers in 2002, the acquisition of seven centers in 2002 and one center in 2003, higher average rents on releasing and renewals, and the expansion of two wholly-owned centers in late 2002.

Percentage rents increased \$1.7 million, or 22.1%, to \$9.2 million for the six months ended June 30, 2003, from \$7.5 million for the six months ended June 30, 2002, primarily due to the buyouts of ownership interests in five centers in 2002 and the acquisition of seven centers in 2002.

Expense reimbursements, representing contractual recoveries from tenants of certain common area maintenance, operating, real estate tax, promotional and management expenses, increased \$12.3 million, or 45.6%, to \$39.3 million for the six months ended June 30, 2003, from \$27.0 million for the six months ended June 30, 2002, due to the recovery of operating and maintenance costs from increased GLA. The average recovery of reimbursable expenses for the Premium Portfolio was 89% for the six months ended June 30, 2003 compared to 88% for the six months ended June 30, 2002. The average recovery of reimbursable expenses for the Other Retail Centers was 69% for the six

months ended June 30, 2003, compared to 54% for the six months ended June 30, 2002. The increase in average recovery on the Other Retail Centers is a result of the centers acquired in 2002.

Other income decreased \$1.9 million or 36.9% to \$3.3 million for the six months ended June 30, 2003, from \$5.2 million for the six months ended June 30, 2002, primarily due to the expiration of the non-compete agreement which included income recognition of \$2.6 million in 2002 partially offset by an increase in ancillary operating income and gain from an outparcel sale in 2003.

Operating and maintenance expenses increased \$13.1 million, or 38.4%, to \$47.4 million for the six months ended June 30, 2003, from \$34.3 million for the six months ended June 30, 2002. The increase was primarily due to costs related to increase in GLA.

Depreciation and amortization expense increased \$7.7 million, or 28.5% to \$34.9 million for the six months ended June 30, 2003, from \$27.2 million for the six months ended June 30, 2002. The increase was due to depreciation of the increased GLA.

General and administrative expense increased \$1.3 million or 35.8% to \$4.7 million for the six months ended June 30, 2003, from \$3.4 million for the six months ended June 30, 2002, primarily due to increases in deferred unit incentive program accrual, salaries and professional fees.

Other expenses increased \$0.9 million or 40.0% to \$3.1 million for the six months ended June 30, 2003, from \$2.2 million for the six months ended June 30, 2002, due to a non-cash charge of \$0.5 million on an interest rate swap resulting from the pay down of a hedged mortgage loan in June 2003 related to the sale of St. Helena Premium Outlets, and increased reserve for bad debt and center rent expense.

Income from unconsolidated investments decreased \$2.8 million or 41.6% to \$3.9 million for the six months ended June 30, 2003, from \$6.7 million for the six months ended June 30, 2002, due to the buyouts of ownership interests in five centers in 2002 which were previously held as unconsolidated investments partially offset by higher income and fees including one-time leasing fees of \$1.1 million from Chelsea Japan.

The loss from Chelsea Interactive decreased \$4.8 million or 73.1% to \$1.7 million for the six months ended June 30, 2003, from \$6.5 million for the six months ended June 30, 2002, due to the write-off of the Company's investment at December 31, 2002. The loss represents funding to Chelsea Interactive during the six months ended June 30, 2003.

Interest expense increased \$12.6 million or 61.2% to \$33.2 million for the six months ended June 30, 2003, from \$20.6 million for the six months ended June 30, 2002, due to higher debt that partially financed acquisitions and the buyouts of partner's interests.

Income from discontinued operations of \$0.2 million for the six months ended June 30, 2003 and 2002, and gain on sale of discontinued operations of \$4.0 million, net of minority interest of \$0.7 million for the six months ended June 30, 2003, relates to the June 2003 sale of St. Helena Premium Outlets, a 23,000 square-foot Premium Property.

### **Liquidity and Capital Resources**

The Company believes it has adequate financial resources to fund operating expenses, distributions, and planned development, construction and acquisition activities over the short term, which is less than 12 months and the long term, which is 12 months or more. Operating cash flow for the year ended December 31, 2002, of \$128.2 million is expected to increase with a full year of operations from the five joint venture buyout centers and the 1.8 million square feet of GLA added during 2002 as well as scheduled openings of approximately 800,000 square feet of new joint venture GLA in 2003 and recent acquisition activity. The Company has adequate funding sources to complete and open all current development projects from available cash, credit facilities and secured construction financing. The

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Company also has access to the public markets through its \$1.55 billion debt and equity shelf registration for funding or refinancing requirements.

Operating cash flow is expected to provide sufficient funds for dividends and distributions in accordance with REIT federal income tax requirements. In addition, the Company anticipates retaining sufficient operating cash to fund re-tenanting and lease renewal tenant improvement costs, as well as capital expenditures to maintain the quality of its centers, meet funding requirements of Chelsea Interactive and partially fund development projects.

Common distributions declared and recorded in 2003 were \$53.4 million, or \$1.07 per share or unit. The Company's dividend payout ratio as a percentage of net income before minority interest, gain or loss on sale or writedown of assets and depreciation and amortization (reduced by amortization of deferred financing costs, depreciation of non-real estate assets and preferred dividends ("FFO")) was 65.8%. The Company's senior unsecured bank line of credit ("Senior Credit Facility") limits aggregate dividends and distributions to the lesser of (i) 90% of FFO on an annual basis or (ii) 100% of FFO for any two consecutive quarters.

The Company's \$200 million Senior Credit Facility expires in March 2005 (unless extended until March 2006), bears interest on the outstanding balance at an annual rate equal to the London Interbank Offered Rate ("LIBOR") plus 1.05% (2.21% at June 30, 2003) or the prime rate, at the Company's option, and has an annual facility fee of 0.125%. The LIBOR rate spread ranges from 0.85% to 1.50% depending on the Company's Senior Debt rating. The Company received a debt rating upgrade in July 2003, resulting in a reduction of the LIBOR rate spread to 0.95% from 1.05%. At June 30, 2003, \$78.0 million was outstanding under the Senior Credit Facility.

During 2003, the Company completed two acquisition transactions valued at approximately \$219 million. On June 12, 2003, the Company purchased The Crossings Factory Stores, a 390,000 square-foot outlet center located in Tannersville, Pennsylvania, for \$111.3 million, including closing costs, and assumed a \$60.7 million 5.85% mortgage loan due 2013. In conjunction with the Crossings Factory Stores acquisition, the Company completed an offering of 1.2 million shares of common stock at a price of \$42.10 per share on June 18, 2003. Net proceeds after expenses of \$49.4 million were used to fund substantially the entire cash portion of the acquisition.

On August 1, 2003, the Company acquired Belz Factory Outlet World Las Vegas, a 477,000 square-foot outlet center in Las Vegas, Nevada for \$104.0 million including the assumption of a \$24.4 million 8.12% mortgage loan due 2012. As part of the same transaction, the Company acquired Belz Factory Outlet World Lakeland, a 319,000 square-foot outlet center near Memphis, Tennessee for an additional \$3.5 million. The Lakeland property is expected to be marketed for sale shortly after closing. The approximately \$84.0 million cash portion of the overall transaction was financed through a \$100 million one-year bridge loan facility at an annual interest rate of LIBOR plus 0.80% that is due on July 31, 2004 and extendible for six months until January 31, 2005 at the Company's option. The LIBOR rate spread ranges from 0.70% to 1.35% depending on the Company's Senior Debt rating. Surplus proceeds from the financing of approximately \$16.0 million will be used for general corporate purposes.

A summary of the maturity of the Company's contractual debt obligations (at par) as of June 30, 2003, is as follows (in thousands):

	Total	Less than One Year	1 to 3 Years	4 to 5 Years	After 5 Years
Unsecured bank debt	\$83,035	\$ -	\$83,035	\$ -	\$ -
Unsecured notes	625,000	-	50,000	125,000	450,000
Mortgage debt	354,662	3,126	13,206	166,634	171,696
<b>Total</b>	<b>\$1,062,697</b>	<b>\$3,126</b>	<b>\$146,241</b>	<b>\$291,634</b>	<b>\$621,696</b>



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Construction projects underway at June 30, 2003 included a 170,000 square-foot second phase at Gotemba Premium Outlets, which opened on July 8, 2003; and the 435,000 square-foot Las Vegas Premium Outlets, which opened on August 1, 2003. The 180,000 square-foot first phase of Sano Premium Outlets, located north of Tokyo, Japan opened March 14, 2003. The Company is also under construction on the 438,000 square-foot Chicago Premium Outlets in Aurora, Illinois, scheduled to open in mid-2004, and the 124,000 square-foot third phase of Outlets at Albertville, scheduled to open in March 2004. The Gotemba and Sano projects are developments of Chelsea Japan Co., Ltd., the Company's 40%-owned Japanese joint venture. The Las Vegas and Chicago projects are 50/50 joint ventures with Simon. Other projects in various stages of development are expected to open in 2004 and beyond. There can be no assurance that these projects will be completed or opened, or that there will not be delays in opening or completion. All current development activity is fully financed either through project specific secured construction financing, the yen denominated line of credit, available cash or through the Senior Credit Facility. The Company will seek to obtain permanent financing once the projects are completed and income has been stabilized.

In connection with the Simon joint ventures, the Company has committed to provide 50% of the development costs, which are expected to be approximately \$48.0 million for Las Vegas Premium Outlets and \$46.0 million for Chicago Premium Outlets. As of June 30, 2003, the Company had contributed \$36.6 million and \$12.8 million to the Las Vegas and Chicago projects, respectively.

The Company has an agreement with Mitsubishi Estate Co., Ltd. and Nissho Iwai Corporation to jointly develop, own and operate premium outlet centers in Japan under the joint venture Chelsea Japan. Borrowings related to Chelsea Japan for which the Company and the OP have provided guarantees as of June 30, 2003, are as follows:

Total Facility		Outstanding				
Yen	US \$ Equivalent	Yen	US \$ Equivalent	US \$ Guarantee	Due Date	Interest Rate
4.0 billion (1)	\$33.4 million	0.9 billion	\$7.9 million	\$7.9 million	2004	1.41%
3.8 billion (2)	31.7 million	3.4 billion	28.1 million	11.2 million	2015	2.20%
0.6 billion (2)	5.0 million	0.5 billion	4.5 million	1.8 million	2012	1.50%

- 1) Facility entered into by an equity investee of the Company that has a one-year extension option until April 1, 2005.
- 2) Facilities entered into by Chelsea Japan, secured by Gotemba and Rinku and 40% severally guaranteed by the Company.

In May 2002, the Company, through an affiliated entity, entered into a 50/50 strategic alliance with Sordo Madaleno y Asociados and Mr. Carlos Peralta of Mexico City to jointly develop premium outlet centers in Mexico. Subject to leasing and entitlements, construction on a 232,000 square-foot first phase of an outlet project north of Mexico City is expected to commence later in 2003 and to open in late 2004. The site can support a second phase containing approximately 165,000 square feet of GLA. Once phase one of the project has been approved, the Company will be committed to fund approximately \$14 million which is 50% of the development costs. As of June 30, 2003, the Company had incurred costs of approximately \$1.9 million related to predevelopment costs and formation of the joint venture.

At December 31, 2002, the Company recognized an impairment loss equal to the net book value of its investment in Chelsea Interactive. The Company believes that it will not be able to recover the net book value of its investment in Chelsea Interactive through future cash flows before reaching the Company's \$60.0 million funding limit. Through June 30, 2003, the Company had funded \$54.1 million and anticipates that the \$5.9 million funding balance may be

used to further develop the platform and to finance operating cash shortfalls and potential costs related to the disposal or discontinuance of the business. A \$0.9 million and \$1.7 million funding loss was reported for the three and six months ended June 30, 2003 respectively. Future funding by the Company will be reported as a loss in the period funding is required. The Company has signed an agreement with a third party to restructure Chelsea Interactive, subject to the satisfaction of certain conditions. There can be no assurance that this joint venture will be successful or that Chelsea Interactive will be able to continue as a going concern.

The Company has minority interests ranging from 3% to 8% in several outlet centers and outlet development projects in Europe operated by Value Retail. The Company's total investment in Europe as of June 30, 2003, was \$3.6 million. The Company has also provided \$17.3 million in limited debt service guarantees under a standby facility for loans arranged by Value Retail to construct outlet centers in Europe. The standby facility for new guarantees, which has a maximum of \$22.0 million, expired in November 2001 and outstanding guarantees shall not survive more than five years after project completion.

To achieve planned growth and favorable returns in both the short and long-term, the Company's financing strategy is to maintain a strong, flexible financial position by: (i) maintaining a conservative level of leverage; (ii) extending and sequencing debt maturity dates; (iii) managing exposure to floating interest rates; and (iv) maintaining liquidity. Management believes these strategies will continue to enable the Company to access a broad array of capital sources, including bank or institutional borrowings and secured and unsecured debt and equity offerings, subject to market conditions.

Net cash provided by operating activities was \$88.7 million and \$52.5 million for the six months ended June 30, 2003, and 2002, respectively. The increase was primarily due to increased operating cash flow generated on the growth of the Company's GLA and decreased losses from Chelsea Interactive offset by the payout of the deferred incentive compensation in March 2002 and the receipt in January 2002 of the final non-compete installment. Net cash used in investing activities decreased to \$80.9 million from \$93.2 for the six months ended June 30, 2003, and 2002, respectively primarily as a result of a decrease in joint venture and wholly-owned property acquisition activity and an increase in proceeds from sale of a center. Net cash used in financing activities increased to \$9.0 million from cash provided of \$57.9 million for the six months ended June 30, 2003, and 2002, respectively. The increase was primarily a result of decreased debt proceeds and repayments offset by common stock issuance in 2003, preferred stock redemptions in 2002 and increased distributions in 2003.

### **Funds from Operations**

Management believes that funds from operations ("FFO") should be considered in conjunction with net income, as presented in the statements of income included elsewhere herein, to facilitate a clearer understanding of the operating results of the Company. The White Paper on Funds from Operations approved by the Board of Governors of NAREIT in October 1999 defines FFO as net income (loss) (computed in accordance with GAAP), excluding gains (or losses) from debt restructuring and sales of properties, plus real estate related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures. The Company believes that FFO is helpful to investors as a measure of the performance of an equity REIT because, along with cash flow from operating activities, financing activities and investing activities, it provides investors with an indication of the ability of the Company to incur and service debt, to make capital expenditures and to fund other cash needs. The Company computes FFO in accordance with the current standards established by NAREIT which may not be comparable to FFO reported by other REITS that do not define the term in accordance with current NAREIT definition or that interpret the current NAREIT definition differently than the Company. FFO does not represent cash generated from operating activities in accordance with GAAP and should not be considered as an alternative to net income (determined in accordance with GAAP) as an indication of the Company's financial performance or to cash flow from operating activities (determined in accordance with GAAP) as a measure of the Company's liquidity, nor is it indicative of funds available to fund the Company's cash needs, including its ability to make cash distributions.

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	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Net income to common shareholders.....	\$24,705	\$13,408	\$43,118	\$25,700
Add (deduct):				
Depreciation and amortization - wholly owned.....	17,269	14,243	34,901	27,113
Depreciation and amortization - joint ventures.....	694	1,159	1,293	2,113
Amortization of deferred financing costs and depreciation of non-rental real estate assets.....	(583)	(616)	(1,183)	(1,113)
Gain on sale of discontinued operations.....	(4,008)	-	(4,008)	-
Preferred units distribution.....	(1,462)	(1,462)	(2,924)	(2,924)
Minority interest.....	5,127	3,685	9,938	7,113
<b>FFO.....</b>	<b>\$41,742</b>	<b>\$30,417</b>	<b>\$81,135</b>	<b>\$58,000</b>
Average diluted shares/units outstanding .....	51,439	45,656	51,156	45,656
Dividends declared per share.....	\$0.535	\$0.485	\$1.07	\$0.97

### Recent Accounting Pronouncements

In November 2002, the FASB issued Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others ("FIN 45"). FIN 45 requires certain guarantees to be recorded at fair value, instead of recording a liability only when a loss is probable and reasonably estimatable, as those terms are defined in FASB Statement No. 5, Accounting for Contingencies. FIN 45 also requires a guarantor to make significant new disclosures, even when the likelihood of making any payments under the guarantee is remote. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. The Company adopted the disclosure provisions of FIN 45 effective December 31, 2002. FIN 45's initial recognition and initial measurement provisions are applicable on a prospective basis to guarantees issued or modified after December 31, 2002.

In January of 2003, the FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities ("FIN 46"). FIN 46 clarifies the application of existing accounting pronouncements to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. The provisions of FIN 46 will be immediately effective for all variable interests in variable interest entities created after January 31, 2003, and the Company will need to apply its provisions to any existing variable interests in variable interest entities by no later than September 30, 2003. The Company does not believe that FIN 46 will have a significant impact on the Company's financial statements.

### Critical Accounting Policies and Estimates

The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The Company believes the following critical accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

### **Bad Debt**

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its tenants to make required rent payments. If the financial condition of the Company's tenants were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. The Company's allowance for doubtful accounts included in tenant accounts receivable totaled \$2.3 million and \$2.6 million at June 30, 2003, and December 31, 2002, respectively.

### **Valuation of Investments**

On a periodic basis, management assesses whether there are any indicators that the value of real estate properties, including joint venture properties, may be impaired. If the carrying amount of the property is greater than the estimated expected future cash flow (undiscounted and without interest charges) of the asset, impairment has occurred. The Company will then record an impairment loss equal to the difference between the carrying amount and the fair value of the asset. The Company does not believe that the value of any of its rental properties were impaired at June 30, 2003. The Company currently believes that it will not be able to recover the net book value of its investment in Chelsea Interactive through future cash flows unless Chelsea Interactive is able to achieve positive cash flow before reaching the \$60.0 million funding limit. Due to current market conditions and the costs of operating the platform, future funding by the Company will be reported as a loss in the period funding occurs. As of June 30, 2003, \$54.1 million had been funded and \$0.9 million and \$1.7 million has been reported as a loss for the three and six month periods then ended.

### **Economic Conditions**

Substantially all leases contain provisions, including escalations of base rents and percentage rentals calculated on gross sales, to mitigate the impact of inflation. Inflationary increases in common area maintenance and real estate tax expenses are substantially reimbursed by tenants.

Virtually all tenants have met their lease obligations and the Company continues to attract and retain quality tenants. The Company intends to reduce operating and leasing risks by continually improving its tenant mix, rental rates and lease terms and by pursuing contracts with creditworthy upscale and national brand-name tenants.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

The Company is exposed to changes in interest rates primarily from its floating rate debt arrangements. In December 2000, the Company implemented a policy to protect against interest rate and foreign exchange risk. The Company's primary strategy is to protect against this risk by using derivative transactions as appropriate to minimize the variability that floating rate interest and foreign currency fluctuations could have on cash flow. In December 2000, a wholly-owned subsidiary of the Company entered into an interest rate swap agreement effective January 2, 2001 with a financial institution for a notional amount of \$69.3 million amortizing to \$64.1 million to hedge against unfavorable fluctuations in the LIBOR rates of its secured mortgage loan facility. The hedge effectively produces a fixed rate of 7.2625% on the notional amount until January 1, 2006.

At June 30, 2003, a hypothetical 100 basis point adverse move (increase) in US Treasury and LIBOR rates applied to unhedged debt would adversely affect the Company's annual interest cost by approximately \$0.8 million annually.

Following is a summary of the Company's debt obligations at June 30, 2003, (in thousands):

	Expected Maturity Date						Total	Fair
	2004	2005	2006	2007	2008	Thereafter		
Fixed Rate Debt:	-	\$49,937	-	\$124,857	\$166,236	\$581,927	\$922,957	\$1,04
Average Interest Rate:	-	8.38%	-	7.25%	6.99%	7.14%	7.19%	
Variable Rate Debt:	-	\$83,035	-	-	-	\$61,975	\$145,010	\$ 14
Average Interest Rate:	-	2.21%	-	-	-	2.82%	2.47%	

#### Item 4. Controls and Procedures

Our chief executive officer and chief financial officer evaluated the effectiveness of our disclosure controls and procedures (as defined in rule 13a-14(c) under the Securities Exchange Act of 1934, as amended) as of June 30, 2003 and, based on that evaluation, concluded that, as of the end of the period covered by this report, we had sufficient controls and procedures for recording, processing, summarizing and reporting information that is required to be disclosed in our reports under the Securities Exchange Act of 1934, as amended, within the time periods specified in the SEC's rules and forms.

During the quarter ended June 30, 2003, there have not been any significant changes to our internal controls including any corrective actions with regard to significant deficiencies and material weaknesses or other factors that could significantly affect these controls.

### Chelsea Property Group, Inc.

#### Part II. Other Information

##### Item 4. Submission of Matters to a Vote of Security Holders

The Company held an annual meeting of stockholders on June 5, 2003, at which the following matters were voted upon:

1. Election of three directors
2. Approval of the Amendment to Employee Stock Purchase Plan
3. Approval of appointment of Ernst & Young LLP as independent auditors for the fiscal year ending December 31, 2003

The results of the meeting were as follows:

	For	Against	Abstain	Broker Non-Votes
	---	-----	-----	-----
Proposal 1:				
William D. Bloom	33,907,125	2,011,140	-	-
Robert Frommer	34,086,230	1,832,035	-	-
Reuben S. Leibowitz	34,073,631	1,844,634	-	-
Proposal 2:				
Amendment to Employee Stock Purchase Plan	35,166,399	414,568	337,298	
Proposal 3:				
Independent Auditors	34,160,207	1,360,337	397,721	

Messrs. David C. Bloom, Brendan T. Byrne, Barry Ginsburg and Philip Kaltenbacher continued as directors after the meeting.

**Item 6. Exhibits and Reports on Form 8-K**

	<u>Exhibit No.</u>	<u>Description</u>
(a)	31	Section 302 Certifications
	32	Section 906 Certifications
(b)		Current Report on Form 8K reporting under Items 7 and 9 on an event that occurred May 6, 2003.

**Signatures**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

CHELSEA PROPERTY GROUP, INC.

By: /s/ Michael J. Clarke  
Michael J. Clarke  
Chief Financial Officer

Date: August 12 , 2003