

CENTER TRUST INC
Form 10-Q
May 15, 2002

Table of Contents

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2002

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 number 1-12588

Center Trust, Inc.

(Exact name of registrant as specified in charter)

Maryland

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

**3500 Sepulveda Boulevard,
Manhattan Beach, California**

(Address of principal executive offices)

95-4444963

*(I.R.S. Employer
Identification Number)*

90266

(Zip Code)

(310) 546-4520

(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 at least the past 90 days. Yes No

As of May 10, 2002, 27,856,455 shares of Common Stock, Par Value \$.01 Per Share, were outstanding.

TABLE OF CONTENTS

CONSOLIDATED BALANCE SHEETS

CONSOLIDATED STATEMENTS OF OPERATIONS

CONSOLIDATED STATEMENTS OF CASH FLOWS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

PART II -- OTHER INFORMATION

SIGNATURES

Table of Contents

CENTER TRUST, INC.

FORM 10-Q INDEX

| | <u>Page</u> |
|-------------------|---|
| Part I | Financial Information |
| Item 1. | Financial Statements |
| | Consolidated Balance Sheets as of March 31, 2002 (unaudited) and December 31, 2001 |
| | 2 |
| | Consolidated Statements of Operations (unaudited) for the three months ended March 31, 2002 and 2001 |
| | 3 |
| | Consolidated Statements of Cash Flows (unaudited) for the three months ended March 31, 2002 and 2001 |
| | 4 |
| | Notes to Consolidated Financial Statements (unaudited) |
| | 5 |
| Item 2. | Management's Discussion and Analysis of Financial Condition and Results of Operations |
| | 6 |
| Part II | Other Information |
| | 10 |
| Signatures | 11 |

Table of Contents**CENTER TRUST, INC.****CONSOLIDATED BALANCE SHEETS**

| | March 31, 2002 | December 31, 2001 |
|---|-------------------|----------------------|
| (In thousands, except share data) | | |
| (Unaudited) | | |
| ASSETS | | |
| Rental properties | \$ 735,528 | \$ 732,818 |
| Accumulated depreciation and amortization | (153,493) | (149,185) |
| Rental properties, net | 582,035 | 583,633 |
| Cash and cash equivalents | 6,060 | 6,816 |
| Tenant receivables, net | 8,354 | 7,668 |
| Other receivables | 7,152 | 5,161 |
| Restricted cash securities | 14,174 | 13,282 |
| Deferred charges, net | 16,846 | 16,636 |
| Other assets | 2,605 | 3,877 |
| Total | \$ 637,226 | \$ 637,073 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Liabilities: | | |
| Secured debt | \$ 401,732 | \$ 402,377 |
| Accrued dividends and distributions | 1,741 | 1,160 |
| Accrued interest | 1,924 | 2,057 |
| Accounts payable and other accrued expenses | 12,430 | 11,309 |
| Accrued construction costs | 634 | 1,059 |
| Tenant security and other deposits | 1,780 | 2,233 |
| Total liabilities | 420,241 | 420,195 |
| Minority Interests: | | |
| Operating Partnership (1,323,504 and 1,338,644 units issued as of March 31, 2002 and December 31, 2001, respectively) | 9,703 | 9,696 |
| Other minority interests | 1,313 | 1,529 |
| Total minority interests | 11,016 | 11,225 |
| Commitments and Contingencies: | | |
| Stockholders Equity: | | |
| Common stock (\$.01 par value, 100,000,000 shares authorized; 27,856,455 and 27,656,405 shares issued and outstanding as of March 31, 2002 and December 31, 2001, respectively) | 279 | 276 |
| Additional paid-in capital | 366,603 | 365,474 |
| Accumulated distributions and deficit | (160,913) | (160,097) |
| Total stockholders equity | 205,969 | 205,653 |
| Total | \$ 637,226 | \$ 637,073 |

Edgar Filing: CENTER TRUST INC - Form 10-Q

See Notes to Consolidated Financial Statements.

Table of Contents

CENTER TRUST, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

| | Three Months Ended March 31, | |
|---|--|----------------|
| | 2002 | 2001 |
| | (In thousands, except per share amounts) (Unaudited) | |
| Revenues: | | |
| Rental revenues | \$ 17,067 | \$ 17,739 |
| Expense reimbursements | 5,808 | 5,942 |
| Percentage rents | 401 | 521 |
| Other income | 1,132 | 1,426 |
| | <u>24,408</u> | <u>25,628</u> |
| Total revenues | | |
| Expenses: | | |
| Interest | 6,967 | 9,688 |
| Property Operating Costs: | | |
| Common Area | 4,328 | 4,366 |
| Property taxes | 2,471 | 2,520 |
| Leasehold rentals | 276 | 265 |
| Marketing | 271 | 183 |
| Other operating | 1,313 | 1,181 |
| Depreciation and amortization | 5,249 | 5,239 |
| General and administrative | 1,130 | 1,365 |
| Transactional Costs | 343 | |
| | <u>22,348</u> | <u>24,807</u> |
| Total expenses | | |
| Income from Operations Before Other Items | 2,060 | 821 |
| Gain on Sale of Rental Properties | | 900 |
| Minority Interests: | | |
| Operating Partnership | (92) | (52) |
| Other minority interests | (66) | (29) |
| | <u>1,902</u> | <u>1,640</u> |
| Net Income Before Extraordinary Item | | |
| Extraordinary Loss on Early Extinguishment of Debt | | (819) |
| | <u>\$ 1,902</u> | <u>\$ 821</u> |
| Net Income | | |
| Basic and Diluted Income Per Share: | | |
| Income before extraordinary item | \$ 0.07 | \$ 0.06 |
| Extraordinary loss on early extinguishment of debt | | (0.03) |
| | <u>\$ 0.07</u> | <u>\$ 0.03</u> |
| Net Income | | |
| Weighted Average Basic and Diluted Shares Outstanding | <u>27,666</u> | <u>27,024</u> |

See Notes to Consolidated Financial Statements.

Table of Contents

CENTER TRUST, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Three Months Ended March 31, | |
|--|---------------------------------|-----------------|
| | 2002 | 2001 |
| | (In thousands) (Unaudited) | |
| Cash Flows from Operating Activities: | | |
| Net income | \$ 1,902 | \$ 821 |
| Adjustment to reconcile net income to net cash Provided by operating activities: | | |
| Depreciation and amortization | 5,249 | 5,239 |
| Amortization of deferred financing costs | 1,020 | 1,030 |
| Amortization of deferred compensation | 33 | 162 |
| Extraordinary loss on early extinguishment of debt | | 819 |
| Net gain on sale of rental properties | | (900) |
| Minority interests in operations | 158 | 81 |
| Net changes in operating assets and liabilities | (2,023) | (1,910) |
| Net cash provided by operating activities | <u>6,339</u> | <u>5,342</u> |
| Cash Flows from Investing Activities: | | |
| Construction and development costs | (2,710) | (2,835) |
| Net proceeds from sale of rental property | | 33,545 |
| Net cash (used in) provided by investing activities | <u>(2,710)</u> | <u>30,710</u> |
| Cash Flows from Financing Activities: | | |
| Principal payments on notes payable | (645) | (136,371) |
| Borrowings on secured line of credit | | 133,369 |
| Repayment of secured line of credit | | (28,627) |
| Costs of obtaining financing | (1,661) | |
| Increase in restricted cash | (892) | (295) |
| Dividends to shareholders | (1,187) | (5,597) |
| Distributions to minority interests | | (508) |
| Net cash used in financing activities | <u>(4,385)</u> | <u>(38,029)</u> |
| Net Decrease in Cash and Cash Equivalents | (756) | (1,977) |
| Cash and Cash Equivalents, at Beginning of Period | <u>6,816</u> | <u>6,164</u> |
| Cash and Cash Equivalents, at End of Period | <u>\$ 6,060</u> | <u>\$ 4,187</u> |

See Notes to Consolidated Financial Statements.

Table of Contents

CENTER TRUST, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis Of Presentation

Center Trust, Inc., (the Company), a Maryland Corporation, is a self-administered and self-managed real estate investment trust (REIT). The Company engages in the ownership, management, leasing, acquisition, development and redevelopment of open air retail shopping centers in the western United States. As of March 31, 2002, the Company owned 35 retail shopping centers (the Properties) comprising 7.9 million square feet of total shopping center gross leasable area (GLA).

The accompanying financial statements and related notes of the Company are unaudited; however, they have been prepared in accordance with generally accepted accounting principles for interim financial reporting and the instructions to Form 10-Q and the rules and regulations of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures normally included in financial statements prepared under generally accepted accounting principles have been condensed or omitted pursuant to such rule. In the opinion of management, all normal and recurring adjustments considered necessary for fair presentation of the Company's financial position, results of operations and cash flows have been included. These financial statements should be read in conjunction with the Company's Form 10-K for the year ended December 31, 2001.

2. Secured Debt

During the quarter, the Company executed an amendment of its existing line of credit with General Electric Capital Real Estate and Fleet Bank. The amendment reduced the total commitment to \$150 million from \$170 million and has a maturity date of April 1, 2004, with a one-year extension option through April 1, 2005. To facilitate this amendment, the Company incurred a one-percent commitment fee which is included in deferred charges. Interest on the line of credit is incurred at 250 basis points over LIBOR (4.4% as of March 31, 2002). As of March 31, 2002, the Company had an outstanding balance of \$114.5 million and \$23 million of availability under the line of credit.

3. Per Share Data

In accordance with SFAS No. 128 (Earnings Per Share), basic earnings per share (EPS) is based on the weighted average number of shares of common stock outstanding during the period and diluted EPS is based on the weighted average number of shares of common stock outstanding combined with the incremental weighted average shares that would have been outstanding if all dilutive potential common shares had been issued as of the beginning of the period. The weighted average number of shares of common stock used in the computation of basic and diluted EPS for the three-month periods ended March 31, 2002 and 2001 were 27,666,000 and 27,024,000, respectively. Units held by limited partners in the Operating Partnership may be exchanged for shares of common stock of the Company on a one-for-one basis, in certain circumstances, and therefore are not dilutive.

On April 22, 2002, the Company paid a \$0.06 dividend per share to shareholders of record as of March 29, 2002.

Table of Contents

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

Overview

The following discussion should be read in conjunction with the accompanying consolidated financial statements and notes thereto.

Forward Looking Statements

The following discussion of financial condition and results of operations contains certain forward-looking statements that are subject to risk and uncertainty. In particular, statements pertaining to our capital resources, portfolio performance and results of operations contain forward-looking statements. Likewise, all our statements regarding anticipated growth in our funds from operations and anticipated market conditions, demographics and results of operations are forward-looking statements. Forward looking statements involve numerous risks and uncertainties and you should not rely on them as predictions of future events. Forward-looking statements depend on assumptions, data or methods which may be incorrect or imprecise and we may not be able to realize them. We do not guarantee that the transactions and events described will happen as described, or that they will happen at all. You can identify forward-looking statements by the use of forward-looking terminology such as believes, expects, may, will, should, would, seeks, approximately, intends, plans, pro forma, estimates, anticipates, or similar words or phrases. You can also identify forward-looking statements by discussions of strategy, plans or intentions. The following factors, among others, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements:

- defaults on or non-renewal of leases by tenants;
- increased interest rates and operations costs;
- our failure to obtain necessary outside financing;
- difficulties in identifying properties to acquire and completing acquisitions;
- difficulties in disposing of properties;
- our failure to successfully operate acquired properties and operations;
- our failure to successfully develop property;
- our failure to maintain our status as a REIT;
- environmental uncertainties and risks related to natural disasters;
- financial market fluctuations; and
- changes in real estate and zoning laws and increases in real property tax rates.

Our success also depends upon economic trends generally, as well as income tax laws, governmental regulation, legislation, population changes and other matters discussed above. We caution you, however, that any list of risk factors may not be exhaustive.

Results of Operations

Comparison of the three months ended March 31, 2002 to the three months ended March 31, 2001.

Rental revenues decreased by \$0.6 million to \$17.1 million for the three months ended March 31, 2002 from \$17.7 million for the three months ended March 31, 2001. Revenues decreased \$1.1 million as a result of the sale of four community shopping centers and two single tenant facilities in 2001. This was partially offset by an increase in revenues at the remaining properties in the portfolio.

Edgar Filing: CENTER TRUST INC - Form 10-Q

Property operating costs increased by \$0.2 million to \$8.7 million for the three months ended March 31, 2002 from \$8.5 million for the three months ended March 31, 2001. The increase is primarily due to the higher cost of insurance partially offset by a \$0.3 million decrease in expenses due to sold properties.

Table of Contents

Interest expense decreased by \$2.7 million for the three months ended March 31, 2002 to \$7.0 million from \$9.7 million for the three months ended March 31, 2001. The decrease resulted from lower average debt outstanding and lower effective interest rates in the first quarter of 2002 compared to the same period in 2001. The lower average debt outstanding was due to the repayment of the \$128.5 million 7 1/2% Convertible Subordinated Debentures on January 15, 2001 and the reduction of the outstanding balance on the Company's Secured Credit Facility through the use of proceeds from the sale of assets during the first half of 2001.

General and administrative costs decreased by \$0.3 million to \$1.1 million for the three months ended March 31, 2002 from \$1.4 million for the three months ended March 31, 2001. The decrease is the result of the full realization of cost savings in the first quarter of 2002 related to the Company's reorganization at the end of the second quarter of 2001.

During the first quarter of 2002, the Company recorded a transactional expense of \$0.3 million. The transaction expense was incurred in connection with an extensive strategic review and marketing effort of the alternatives available to achieve maximum shareholder value.

The Company reported a net income of \$1.9 million and \$0.8 million for the three months ended March 31, 2002 and 2001, respectively. The increase in net income was primarily due to the decrease in interest expense partially offset by a decrease in net operating income as a result of the sale of assets in 2001.

Selected Property Financial Information

Net operating income (defined as revenues, less property operating costs) for the Company's properties is as follows:

| | Three Months Ended March 31, | |
|--|---|-------------------|
| | 2002 | 2001 |
| Retail Properties (35 in 2002 and 37 in 2001): | | |
| Regional Malls | \$ 4,337 | \$ 4,424 |
| Open Air Centers | 11,097 | 12,057 |
| Single Tenants | 280 | 475 |
| Other income | 35 | 157 |
| | <u> </u> | <u> </u> |
| Net Operating Income | \$ 15,749 | \$ 17,113 |
| | <u> </u> | <u> </u> |

The following summarizes the percentage of leased GLA (excluding non-owned GLA) as of:

| | March 31, 2002 | December 31, 2001 |
|--|-----------------------|--------------------------|
| Retail Properties (35 in 2002 and 37 in 2001): | | |
| Open Air Centers | 88.6% | 91.8% |
| Regional Malls | 92.8 | 94.4 |
| Single Tenants | 100.0 | 100.0 |
| Aggregate Portfolio | 89.8 | 92.6 |

Funds from Operations

The Company considers funds from operations (FFO) to be an alternative measure of the performance of an equity REIT since such measure does not recognize depreciation and amortization expenses as operating expenses. FFO is defined, as outlined in the October 1999 White Paper, by the National Association of Real Estate Investment Trusts (NAREIT) as net income plus depreciation and amortization of real estate, less gains or losses on sales of properties. Additionally, the definition also permits FFO to be adjusted for significant non-recurring items. Funds from operations do not represent cash flows from operations as defined by generally accepted accounting principles and should not be considered as an alternative to those indicators in evaluating the Company's operating performance or liquidity. Further, the methodology for

computing FFO

Table of Contents

utilized by the Company may differ from that utilized by other equity REITs and, accordingly may not be comparable to such other REITs.

The Company computes FFO on both a basic and diluted basis. The diluted basis assumes the conversion of the convertible and exchangeable debentures into shares of common stock. The following table summarizes the Company's computation of FFO and provides certain additional disclosures (dollars in thousands):

| | Three Months Ended March 31, | |
|---|---|-------------------|
| | 2002 | 2001 |
| Funds from Operations | | |
| Net income | \$ 1,902 | \$ 821 |
| Adjustments to reconcile net income to funds from operations: | | |
| Depreciation and Amortization: | | |
| Buildings and improvements | 3,115 | 3,232 |
| Tenant improvements and allowances | 1,190 | 1,096 |
| Leasing costs | 728 | 708 |
| Minority Interests | 25 | (119) |
| Extraordinary loss - early extinguishment of debt | | 819 |
| Gain on Sale of Assets | | (900) |
| Other | 46 | 161 |
| | <u> </u> | <u> </u> |
| Funds from operations, basis and diluted | <u>\$ 7,006</u> | <u>\$ 5,818</u> |

Funds from operations, on a basic basis, increased to \$7.0 million for the three months ended March 31, 2002, as compared to \$5.8 million for the same period in 2001. The increase in funds from operations are principally a result of the reasons stated above under Results of Operations adjusted for the items outlined in the above table.

Funds from operations do not represent cash flows from operations as defined by Generally Accepted Accounting Principles and should not be considered as an alternative to net income as an indicator of Center Trust's operating performance or to cash flows as a measure of liquidity.

Liquidity Sources and Requirements

During the quarter, the Company executed an amendment of its existing line of credit with General Electric Capital Real Estate and Fleet Bank. The amendment reduced the total commitment to \$150 million from \$170 million and has a maturity date of April 1, 2004, with a one-year extension option through April 1, 2005. To facilitate this amendment, the Company incurred a one-percent commitment fee. The spread is 250 basis points over LIBOR. As of March 31, 2002, the Company had an outstanding balance of \$114.5 million and \$23 million of availability under the line of credit.

During 2002, the Company has debt maturities of \$59.1 million. Of this balance, three mortgages totaling \$50.2 million each have three one-year extensions available to the Company. The remaining balance of \$8.9 million represents one non-recourse mortgage secured by Date Palm Center located in Cathedral City, California. We are currently negotiating with the lender to modify the terms of this non-recourse agreement and anticipate that we will be able to successfully execute an extension and amendment to this loan before it matures.

Cash Flows

Net cash provided by operating activity increased by \$1.0 million to \$6.3 million for the three months ended March 31, 2002 from \$5.3 million for the same period of 2001. The increase resulted primarily from lower interest costs for the quarter ended 2002.

Table of Contents

Net cash from investment activities was a use of cash of \$2.7 million for the three months ended March 31, 2002 as compared to cash provided by of \$30.7 million for the three month period ended March 31, 2001. The decrease was the result of proceeds received from the sale of four community shopping centers and two single tenant facilities in 2001 compared to no sales of assets in 2002. Financing activities used cash of \$4.4 million for the three months ended March 31, 2002 as compared to \$38.0 million for the three months ended March 31, 2001. During the period ended 2001, the cash used by financing activities is the result of repayments on the line of credit from proceeds received from the sale of assets.

Inflation

Center Trust's long term leases contain provisions designed to mitigate the adverse impact of inflation on its results from operations. Such provisions include clauses enabling Center Trust to receive percentage rents based upon tenants' gross sales, which generally increase as prices rise, and/or, in certain cases, escalation clauses are often related to increases in the CPI or similar inflation indices. In addition, many of Center Trust's leases are for terms of less than ten years, which permits Center Trust to seek to increase rents upon re-rental at market rates if rents are below then existing market rates. Many of Center Trust's leases require the tenants to pay a pro rata share of operating expenses, including common area maintenance, real estate taxes, insurance and utilities, thereby reducing Center Trust's exposure to increases in costs and operating expenses from inflation.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company is exposed to market risk primarily due to fluctuations in interest rates. Specifically, the risk resulting from increasing LIBOR-based interest rates as interest on the Company's Credit Facility of \$114.5 million as well as mortgage notes of \$75.2 million are tied to various LIBOR interest rates. The Credit Facility matures March 31, 2004. The Company is also subject to market risk resulting from fluctuations in the general level of U.S. interest rates as \$176.0 million of the Company's debt is based on a weighted average fixed rate of 8.0%. As a result, the Company will be obligated to pay contractually agreed upon rates on interest on its fixed rate debt, unless management refinances its existing fixed rate debt and potentially incurs substantial prepayment penalties. The \$36 million of tax-exempt certificates of participation are tied to a general index of AAWA-rated tax-free municipal bonds.

The following table provides information about the Company's interest rate sensitivity financial instruments, including, amounts due at maturity, principal amortization, weighted average interest rates and fair market values as of March 31, 2002 (dollars in thousands):

| As of March 31, 2002 | 2002 | 2003 | 2004 | 2005 | 2006 | Thereafter | Total | Fair Market Value |
|--------------------------------------|--------------|--------------|--------------|------|----------|------------|---------------|-------------------------|
| Interest Rate Sensitive Liabilities: | | | | | | | | |
| Credit Facility | | | \$114,548 | | | | \$114,548 | \$114,548 |
| Interest Rate | | | LIBOR +2.50% | | | | LIBOR +2.50% | |
| Variable Rate | | | | | | | | \$75,185 |
| Debt | \$50,185 | \$25,000 | | | | | \$75,185 | |
| Interest Rate | LIBOR +2.30% | LIBOR +2.50% | | | | | LIBOR +2.367% | |
| Fixed Rate | | | | | | | | \$202,288 |
| Debt | \$8,888 | \$14,768 | | | \$12,947 | \$139,396 | \$175,999 | |
| Weighted Average | | | | | | | | |
| Interest Rate | 10.450% | 10.375% | | | 10.631% | 7.393% | 8.036% | |
| Tax Exempt | | | | | | | | \$36,000 |
| Certificates | | | | | | \$36,000 | \$36,000 | |
| Weighted Average | | | | | | | | |
| Interest Rate | | | | | | 2.995% | 2.995% | |

Table of Contents

PART II OTHER INFORMATION

Item 1: *Legal Proceedings*

None

Item 2: *Changes in Securities*

None

Item 3: *Defaults Upon Senior Securities*

None

Item 4: *Submission of Matters to a Vote of Security Holders*

None

Item 5: *Other Information*

None

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

(a) Exhibits

None

(b) Reports on Form 8-K

On May 8, 2002, the Company filed a report on Form 8-K to make available additional financial and operational information concerning the Company and properties owned as of March 31, 2002.

Table of Contents

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.

CENTER TRUST RETAIL PROPERTIES, INC.

By: */s/ EDWARD A. STOKX*

Edward A. Stokx
Chief Financial Officer and Secretary
(Principal Financial Officer)

By: */s/ SIDNEY M. SHIBATA*

Sidney M. Shibata
Controller
(Principal Accounting Officer)

Dated: May 14, 2002