

Embracing the Future Owning the Past

As I assume my new role as Executive Chairman of the Board, I am excited about my new position and very optimistic about the future of our company. I will speak more about this transition later, but first let's reflect on our company's many successes in 2009.

Much has already been written about the financial crisis that began in 2008, gained steam in 2009 and severely tested the resiliency of the capital structure that had served our company so well over the past 17 years. As a result of those events, we developed a well-conceived, multi-faceted plan to restore our financial situation to acceptable levels that would inspire investor confidence and position the company to take advantage of future investment opportunities. As a team, we executed on that plan and achieved the following:

- Sold \$320 million of common equity, \$113 million to the Otto Family and \$207 million through the continuous equity program
- Completed \$590 million in asset sales
- Repurchased \$816 million of our senior unsecured notes at a discount to par of \$172 million
- Issued \$300 million in new unsecured corporate debt
- Generated over \$250 million in retained capital from earnings
- Raised over \$600 million in new secured indebtedness, including the first and only Federal Reserve approved new issue TALF CMBS deal in the United States, which was also the first new issue CMBS transaction in the nation following the financial crisis

- Leased over 10.5 million square feet of retail space
- Improved portfolio quality through disposition of non-prime assets
- Reduced capital spending on developments
- Reduced general and administrative expenses
- Increased ancillary income by 30% from 2008 to over \$30 million

Through all of these activities, we reduced total consolidated indebtedness by approximately \$700 million and significantly enhanced our debt maturity schedule. In short, when coupled with our recent issuance of an additional \$400 million in new common equity in 2010, we have reduced indebtedness by over \$1 billion, restored the company to sound financial footing and positioned the company for future growth.

While we accomplished a lot operationally in 2009, in order to deal with the short-term challenges occasioned by the financial crisis, we also spent an extraordinary amount of energy at the Board level to achieve a new long-term strategic plan. With the additions of Dan Hurwitz, Jim Boland, and our two new directors from Germany, Volker Kraft and Thomas Finne, we have an outstanding, talented, engaged, and highly invested Board of Directors to guide us through the next chapter in our history. This next chapter will include the following fundamental changes:

- Transition from a consolidator to an active asset manager with a laser focus on developing a



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portfolio of prime assets that will maximize our opportunity for internal growth

- If and when new ground up developments become desirable in the future, we will pursue them primarily in off balance sheet joint ventures using private equity to fund the great majority of the capital investments required by such projects to minimize the drag that developments inflict on our financial metrics and enhance our return on invested capital
- Evaluate all future investments through a prism that will mandate not only accretion to EBITDA, but also increase net asset value per share
- Continue to seek to generate exceptional growth from our investment in Sonae Sierra Brazil and from our large Puerto Rico portfolio
- Focus our balance sheet strategy not on minimizing current interest expense, but rather on developing a very level long-term debt maturity schedule that minimizes refinancing risk
- Focus on growing EBITDA per share in lieu of a singular focus on FFO as a measure of success
- Target a financial leverage level of 6.5 to 7.5 times EBITDA and seek to maintain consensus investment grade credit ratings at all times to maintain a significant cushion relative to all debt covenants
- Continue to make an extraordinary commitment to developing talent as our human capital is our most precious resource

These adjustments to our strategic plan will ensure that we will protect ourselves to the maximum extent possible from vulnerability to any future financial crisis.

Through our accomplishments in the capital markets during the past year we have positioned ourselves to be a survivor and a leader in our industry. Let me detail exactly where we see the opportunities for the future.

First and foremost, we believe we have assembled a top-of-class prime portfolio of high-quality shopping centers that will perform well in any economic environment. The hallmarks of this portfolio are its profitable tenants, desirable locations, diverse assets, and strong demographics. Another hallmark is the portfolio's emphasis on value and convenience, which caters to consumers' recent and more permanent shifts in shopping habits. Our prime portfolio consists of high-quality, popular-priced retail in healthy markets and is the dominant driver of our growth in net operating income. As noted above, we are committed to proactive portfolio management and we will continue to sell those assets that we expect to underperform and reinvest the proceeds into assets that will meet our very stringent investment criteria for the future.

While we expect our portfolio, when stabilized, to generate consistent organic growth, we have a unique opportunity for more significant growth in the near-term as our portfolio occupancy returns to historic norms. The square footage vacated by recent bankruptcies is high-quality space and we expect that it will lease over the next few years, at a consistent pace. This expected return to a normalized 95% occupancy level portends a one-time increase of nearly 5% in our EBITDA which should be realized over the next few years.

We also will continue to build on our New Business Development Program which generates tens of millions of dollars per year in revenue from initiatives such as short-term seasonal leasing, our solar energy program, and other non-traditional initiatives. Revenues from this program have grown over 40 times in the last 10 years and are expected to continue to grow at a double-digit pace without any significant capital investment as we expand the platform to our portfolio in Brazil.

Our investment in Brazil offers a unique opportunity for outsized growth in the coming years.

Our joint venture with leading European developer Sonae Sierra from Portugal is the third largest landlord of shopping malls in all of Brazil and owns the largest shopping mall in South America. We employ 130 professionals in the home office in Sao Paulo and we have a highly competent development team. We have also been able to capitalize on our position as Wal-Mart's leading landlord to work closely with them on their exceptional appetite for growth in Brazil. We have a robust pipeline of developments and expansions and the investment returns in Brazil far outstrip those available in the US. In addition, the net operating income of our core portfolio has grown at nearly five times the growth rate of our solid United States portfolio and that growth profile is projected to continue for the foreseeable future. As a result, Brazil figures to make a very significant contribution to our earnings growth in the coming years.

On a macro level, we believe that this is the most advantageous time in history to be a well-capitalized publicly traded REIT. External growth opportunities for well-capitalized companies with strong operating platforms will abound in the coming years. It is no secret that the real estate industry as a whole is dramatically over-leveraged. The deleveraging process will be extraordinarily painful for private companies and operators that have traditionally relied on high loan-to-value secured debt and traditional bank loans to fund their investments and operations. On the other hand, capital flows are strong to well-capitalized public companies such as Developers Diversified as evidenced by the nearly \$2 billion of capital that we have raised in the past year. As our balance sheet continues to improve, so will our access to that well-priced capital.

We fully expect that the coming years will feature one of the greatest migrations of high-quality assets from private ownership to public ownership since the early 1990s when a similar liquidity crisis existed for the real estate industry. The difference is that in the early 1990s, that migration featured an endless stream of IPOs as private companies became public companies. This time, there is no necessity for a high volume of IPOs because there are already many well-capitalized public companies in every sector that are well-positioned to bring quality assets onto their

balance sheets with a more appropriate and conservative capital structure. Developers Diversified is committed to take all steps necessary to be a leader in this process without putting our reputation at risk.

As we position ourselves to take advantage of future opportunities, we will do so with some very fundamental changes to our management team. At the beginning of this year Dan Hurwitz was promoted to Chief Executive Officer as I assumed the new role of Executive Chairman. We made this important decision for two very important reasons. First and foremost, Dan Hurwitz will be an outstanding CEO for Developers Diversified. This has been our succession plan for many years and we decided the time was right to make it happen.

The second important reason for the transition was that we concluded that the most appropriate corporate governance model for the future was to separate the position of Chairman of the Board from the position of CEO, recognizing the differences between the two roles and acknowledging the time-consuming and labor-intensive nature of Board activities.

As Executive Chairman, I will be more aligned with the Board in updating our strategic plan and positioned well to ensure that management is executing on that plan. At the same time, I will maintain important responsibilities in the areas of capital markets, strategic transactions, corporate governance, and international operations; areas where, working closely with Dan, I believe I can make the greatest contribution to the company's performance in the future. I look forward to working with Dan and the rest of his management team to do everything in my power to contribute to the success of Developers Diversified. I also look forward to working closely with our outstanding Board of Directors to ensure that our flexible strategic plan is constantly examined and updated to maximize the alignment of our management team with the long-term interests of our shareholders.

It is with great pride that I reflect upon our many accomplishments as a public company since our IPO in 1993. At the time we were a relatively small enterprise consisting of only 82 assets valued at \$480 million. Our assets were primarily Kmart anchored shopping centers located in tertiary markets.

We employed less than 100 people. Our capital structure was comprised of simple mortgage debt and common equity and we had no line of credit available to us at all. All of our senior executives met together every single morning and I was involved in every aspect of our operations.

Today, we are an international enterprise that operates over 600 properties valued at nearly \$18 billion located throughout North and South America and the Caribbean. We employ nearly 1,000 people and our platform features one of the largest, highest-quality and most diversified portfolios of shopping centers in the world. We have assembled a management team that is “best-of-breed” and we are the leading landlord to many of the nation’s most successful retailers. Our capital structure features over \$3 billion in common equity, over \$550 million in preferred equity, \$1.3 billion in unsecured revolving credit facilities, nearly \$2 billion in unsecured corporate bonds, and nearly \$3 billion in private equity in company-managed joint ventures.

Investors in our IPO in 1993 have been rewarded for their confidence. Even after the massive decline in REIT share prices over the last 18 months, an investor in the Developers Diversified IPO today holds 2.21 shares of Developers Diversified for each share purchased in 1993. The value of those shares exceeds the original investment and the investor has also received cash distributions equal to a 230% return. Operating Funds from Operations per share this past year were 87% greater than Funds from Operations per share in 1993. But beyond sheer investment returns and operating metrics, we are most proud of Developers Diversified’s consistent role as a leader and an innovator in our industry over the past 17 years. Whether through the formation of joint ventures with private capital, partnerships with tenants, talent recruitment and development, a commitment to ancillary revenue or groundbreaking financing transactions, we have consistently embraced change in an effort to enhance shareholder value. This commitment to innovation is a trend that we anticipate will continue as we operate in a new environment.

In summary, 2009 was a watershed year for Developers Diversified in many respects. It was a

year of unprecedented challenges. It was also a year of exceptional accomplishment during which we laid a new strong foundation for the future. We want to thank our employees for their hard work in accomplishing so many of our lofty goals for the year. We also want to thank our shareholders for believing in us during this very challenging time. We particularly want to thank the Otto Family for choosing Developers Diversified from the entire universe of publicly traded REITs in the United States as the platform to make their very significant investment in US real estate. We are highly gratified by the confidence that they have placed in our team. Lastly, I want to thank Dan Hurwitz for all of his hard work in helping to make our company successful and I want to pledge to him my complete support and promise that I will do everything I can to ensure that, together, we will reward our shareholders for their confidence with the strongest possible performance in the future. Dan assumes his new role with one of the most powerful shopping center platforms in the world at his disposal. I am confident that he will be an outstanding leader of our team and I am truly excited about our opportunities for the future.



Scott A. Wolstein
Executive Chairman of the Board of Directors