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MISSION WEST PROPERTIES INC

Form 10-Q

May 15, 2002

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 MARCH 31, 2002

COMMISSION FILE NUMBER 1-8383

Mission West Properties, Inc.
(Exact name of registrant as specified in its charter)

Maryland

95-2635431

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer Identification Number)

10050 Bandley Drive
Cupertino, California 95014-2188
(Address of principal executive offices)

Registrant's telephone number, including area code is (408) 725-0700

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 X NO

APPLICABLE ONLY TO CORPORATE ISSUERS

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date:

17,463,329 shares outstanding as of May 14, 2002

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Mission West Properties, Inc.

FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2002

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PART I - FINANCIAL INFORMATION

ITEM 1 CONSOLIDATED FINANCIAL STATEMENTS

MISSION WEST PROPERTIES, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except per share amounts)

	March 31, 2002

	(Unaudited)
ASSETS	
Real estate assets, at cost	
Land	\$231,412
Buildings	710,663

	942,075
Less accumulated depreciation	(52,988)

Net real estate assets	889,087

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Cash and cash equivalents	7,498
Restricted cash	2,715
Deferred rent	16,143
Other assets	15,624

Total assets	\$931,067
	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

Liabilities:

Line of credit (related parties)	\$ 85,089
Unsecured loan	20,000
Mortgage notes payable	126,918
Mortgage notes payable (related parties)	11,300
Interest payable	342
Security deposits	7,600
Prepaid rental income	13,940
Dividends/distributions payable	24,872
Refundable option payment	-
Accounts payable and accrued expenses	4,980

Total liabilities	295,041

Commitments and contingencies (Note 8)

Minority interest 525,173

Stockholders' equity:

Preferred stock, \$.001 par value, 20,000,000 shares authorized, none issued and outstanding	-
Common stock, \$.001 par value, 200,000,000 shares authorized, 17,463,329 and 17,329,779 shares issued and outstanding at March 31, 2002 and December 31, 2001, respectively	17
Paid-in-capital	128,046
Accumulated deficit	(17,210)

Total stockholders' equity	110,853

Total liabilities and stockholders' equity	\$931,067
	=====

The accompanying notes are an integral part of these consolidated financial statements.

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MISSION WEST PROPERTIES, INC
CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in thousands, except share and per share amounts)
(Unaudited)

Three months ended March 31,

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	2002	2001
	-----	-----
Revenues:		
Rental income from real estate	\$32,484	\$29,679
Tenant reimbursements	5,326	3,488
Other income, including interest	497	516
	-----	-----
Total revenues	38,307	33,683
	-----	-----
Expenses:		
Operating expenses	2,275	1,225
Real estate taxes	3,057	2,321
Depreciation of real estate	4,356	4,102
General and administrative	434	318
Interest	2,270	2,209
Interest (related parties)	1,010	1,300
	-----	-----
Total expenses	13,402	11,475
	-----	-----
Income before minority interest and discontinued operations	24,905	22,208
Minority interest	20,769	18,507
	-----	-----
Income from continuing operations	4,136	3,701
	-----	-----
Discontinued operations:		
Gain from disposal of discontinued operations	6,103	3,101
Gain from discontinued operations	287	-
	-----	-----
Net gain from discontinued operations	6,390	3,101
	-----	-----
Net income to minority interest	\$26,094	\$21,090
	=====	=====
Net income to common stockholders	\$ 5,201	\$ 4,219
	=====	=====
Income per share from continuing operations:		
Basic	\$ 0.24	\$ 0.22
	=====	=====
Diluted	\$ 0.23	\$ 0.21
	=====	=====
Income per share from discontinued operations:		
Basic	-	-
	=====	=====
Diluted	-	-
	=====	=====
Net income per share to common stockholders:		
Basic	\$ 0.24	\$ 0.22
	=====	=====
Diluted	\$ 0.23	\$ 0.21
	=====	=====
Weighted average number of shares of common stock outstanding (basic)	17,404,568	17,037,201
	=====	=====
Weighted average number of shares of common stock outstanding (diluted)	17,853,809	17,242,821
	=====	=====

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The accompanying notes are an integral part of these consolidated financial statements.

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MISSION WEST PROPERTIES, INC. CONSOLIDATED STATEMENTS OF CASH FLOWS (Dollars in thousands) (Unaudited) -----

	Thre

	20

Cash flows from operating activities:	
Net income	\$ 5,
Adjustments to reconcile net income to net cash provided by operating activities:	
Minority interest	26,
Depreciation	4,
Gain on sales of real estate	(6,
Other	
Changes in assets and liabilities:	
Deferred rent	
Other assets	(3,
Security deposits	
Prepaid rental income	1,
Accounts payable and accrued expenses	

Net cash provided by operating activities	28,

Cash flows from investing activities:	
Improvements to real estate assets	(18,
Refundable option payment	(31,
Real estate purchase	18,
Proceeds from sales of real estate	15,
Restricted cash	(2,
Restricted cash available	

Net cash used in investing activities	(18,

Cash flows from financing activities:	
Principal payments on mortgage notes payable	(
Principal payments on mortgage notes payable (related parties)	(2,
Net payments under line of credit (related parties)	20,
Proceeds from unsecured loan	
Financing costs	
Proceeds from stock options exercised	(20,
Minority interest distributions	(4,
Dividends paid	

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Net cash used in financing activities	(7,

Net increase/(decrease) in cash and cash equivalents	2,
Cash and cash equivalents, beginning	5,

Cash and cash equivalents, ending	\$ 7,
	=====
Supplemental information:	
Cash paid for interest	\$ 3
	=====
Supplemental schedule of non-cash investing and financing activities:	
Debt incurred in connection with property acquisitions (related parties)	\$ 7
	=====
Assumption of other liabilities in connection with property acquisitions	\$
	=====
Issuance of operating partnership units in connection with property acquisitions	\$ 6
	=====

The accompanying notes are an integral part of these consolidated
financial statements.

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MISSION WEST PROPERTIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except share and per share data)
(Unaudited)

1. Principles of Consolidation and Basis of Presentation

The accompanying consolidated financial statements include the accounts of Mission West Properties, Inc. and its controlled subsidiaries, including the operating partnerships (the "Company"). All significant intercompany balances have been eliminated in consolidation.

Certain prior year amounts have been reclassified to conform to the current year's presentation.

Minority interest represents the separate private ownership of the operating partnerships by the Berg Group (defined as Carl E. Berg, his brother Clyde J. Berg, members of their respective immediate families, and certain entities they control) and other non-affiliate interests. In total, these interests account for approximately 83% of the ownership interests in the real estate operations of the Company as of March 31, 2002. Minority interest in earnings has been calculated by taking the net income of the operating partnerships (on a stand-alone basis) multiplied by the respective minority interest ownership percentage.

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") applicable to interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures normally included in financial

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statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. However, in the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation have been included. The Company presumes that users of the interim financial information have read or have access to the audited financial statements for the preceding fiscal year and that the adequacy of additional disclosure needed for a fair presentation may be determined in that context. The results of operations for the three months ended March 31, 2002 are not necessarily indicative of the results to be expected for the entire year.

The Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long Lived Assets" effective January 1, 2002 (see note 9).

The Company has elected to be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended. Accordingly, no provision has been made for income taxes for the three months ended March 31, 2002.

2. Real Estate

BERG LAND HOLDINGS OPTION AGREEMENT

Under the terms of the Berg land holdings option agreement, the Company, through the operating partnerships, has the option to acquire any future Research & Development ("R&D"), office and industrial buildings developed by the Berg Group on land currently owned, optioned, or acquired for these purposes in the future, directly or indirectly by certain members of the Berg Group. At present, there are approximately 284 acres of Silicon Valley land, including land under development, owned directly or under 50% joint venture entities, by certain members of the Berg Group that are subject to the terms of the Berg land holdings option agreement. The owners of the future R&D property developments may obtain cash or, at their option, operating partnership interests ("O.P. Units") valued at the average closing price of shares of common stock over the 30-trading-day period preceding the acquisition date. As of March 31, 2002, the Company had completed seventeen acquisitions under the Berg land holdings option agreement representing approximately 1,699,000 rentable square feet. Upon the Company's exercise of an option to purchase any of the future R&D property developments under the terms of the Berg land holdings option agreement, the acquisition price will equal the sum of (a) the full construction cost of the building; (b) 10% of the full construction cost of the building; (c) the acquisition value of the parcel as defined in the agreement upon which the improvements are constructed (currently ranging from \$8.50 to \$20.00 per square foot); (d) 10% per annum of the acquisition value of the parcel for the period from January 1, 1998 to the close of escrow; and (e) interest at LIBOR (London Interbank Offer Rate) plus 1.65% per annum on the full construction costs of the building for the period from the date funds were disbursed by the developer to the close of escrow; less (f) any debt encumbering the property, or a lesser amount as approved by the members of the independent directors committee of the Company's board of directors.

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No estimate can be given at this time as to the total cost to the Company to acquire projects under the Berg land holdings option agreement, or the timing of the Company's acquisition of any of such projects. However, the Berg Group currently has four properties under development with a total of approximately 476,000 rentable square feet of R&D properties that the Company has the right to acquire under this agreement. Of the four

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properties, three are joint ventures in which the Berg Group holds approximately a 50% interest. The joint venture properties prospectively represent a total of approximately 311,000 rentable square feet. As of March 31, 2002, the estimated acquisition price to the operating partnerships for these four projects would be approximately \$54,600. The final acquisition price of these four properties could differ significantly from this estimate. In addition to projects currently under development, the Company has the right to acquire future developments by the Berg Group on up to 250 additional acres of land currently controlled by the Berg Group, which could support approximately 3.9 million square feet of new developments. Under the Berg land holdings option agreement, as long as the Berg Group's percentage ownership interest in the Company and the operating partnerships taken as a whole is at least 65%, the Company also has an option to purchase all land acquired, directly or indirectly, by Carl E. Berg or Clyde J. Berg in the future which has not been improved with completed buildings and which is zoned for, intended for or appropriate for research and development, office and/or industrial development or use in the states of California, Oregon and Washington.

PROPERTY DISPOSITION

On March 6, 2002, the Company completed the sale, in a tax-deferred exchange, of a 72,400 square foot R&D property located at 2001 Logic Drive, San Jose, California to Xilinx, Inc., which had exercised a purchase option in the same month. The Company realized a gain of \$6,103 on the total sale price of approximately \$18,503. At March 31, 2002, the proceeds from the sale of this property were classified as restricted cash to be used in tax-deferred property exchanges.

PROPERTY ACQUISITIONS

Effective January 1, 2002, the Company acquired an approximately 125,000 rentable square foot newly constructed R&D building located at 5345 Hellyer Avenue in San Jose, California from the Berg Group under the Berg land holdings option agreement. The total acquisition price for this property was \$13,652. The Company acquired this property by borrowing \$7,500 under the Berg Group line of credit and issuing 502,805 O.P. Units to various members of the Berg Group.

Effective March 8, 2002, the Company acquired three R&D buildings totaling approximately 206,500 rentable square foot located at 2610 and 2630 Orchard Parkway and 55 West Trimble Road in San Jose, California from Silicon Valley Properties, LLC in a tax-deferred exchange transaction involving the Company's former R&D properties located at 2001 Logic Drive and 5713-5729 Fontanoso Way, San Jose, California. The total acquisition price for the properties acquired from Silicon Valley Properties, LLC was approximately \$31,250.

3. Restricted Cash

At March 31, 2002, restricted cash represents the remaining proceeds from a property sale and interest income being held in a separate cash account at a trust company in order to preserve the Company's option of receiving replacement property on a tax-deferred basis.

4. Stock Transactions

During the three months ended March 31, 2002, stock options to purchase 33,550 shares of common stock were exercised at \$4.50 per share. Total proceeds to the Company were \$151. In January 2002, a limited partner of one of the operating partnerships exchanged 100,000 O.P. Units for 100,000 shares of the Company's common stock under the terms of the December 1998 exchange rights agreement among the Company and all limited partners of the operating partnerships.

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5. Net Income Per Share

Basic operating net income per share is computed by dividing net income, excluding gain on sale of real estate, by the weighted-average number of common shares outstanding for the period. Diluted operating net income per share is computed by dividing net income, excluding gain on sale of real estate, by the sum of the weighted-average number of common shares outstanding for the period plus the assumed exercise of all dilutive securities.

The computation for weighted average shares is detailed below:

	Three Months Ended March 31,	
	2002	2001
Weighted average shares outstanding (basic)	17,404,568	17,037,201
Incremental shares from assumed option exercise	449,241	205,620
Weighted average shares outstanding (diluted)	17,853,809	17,242,821

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The outstanding O.P. Units, which are exchangeable at the unit holder's option, subject to certain conditions, for shares of common stock on a one-for-one basis have been excluded from the diluted net income per share calculation, as there would be no effect on the amounts because the minority interests' share of income would also be added back to net income. The total number of O.P. Units outstanding at March 31, 2002 and 2001 was 86,165,346 and 84,547,078, respectively.

6. Related Party Transactions

As of March 31, 2002, the Berg Group owned 78,133,436 O.P. Units. Combined with shares of the Company's common stock owned by the Berg Group, the Berg Group's ownership as of March 31, 2002 represented approximately 75% of the equity interests of the Company, assuming conversion of the 86,165,346 O.P. Units outstanding into the Company's common stock.

As of March 31, 2002, debt in the amount of \$85,089 was due the Berg Group under the line of credit established March 1, 2000. The Berg Group \$100 million line of credit is currently collateralized by eleven properties, bears interest at LIBOR plus 1.30%, and matures in March 2003. The Company believes that the terms of the Berg Group line of credit are more favorable than those available from commercial lenders. As of March 31, 2002, debt in the amount of \$11,300 was due the Berg Group under a mortgage note established May 15, 2000 in connection with the acquisition of a 50% interest in Hellyer Avenue Limited Partnership, the obligor under the mortgage note. The mortgage note bears interest at 7.65%, and is due in 10 years with principal payments amortized over 20 years.

Carl E. Berg has a substantial financial interest in one company that leases space from the operating partnerships. This company occupies 5,862

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square feet at \$0.93 per square foot per month. This lease was in effect prior to the Company's acquisition of its general partnership interests in July 1998. The lease expires in May 2003.

The Company currently leases office space owned by Berg & Berg Enterprises, Inc., an affiliate of Carl E. Berg and Clyde J. Berg. Rental amounts and overhead reimbursements paid to Berg & Berg Enterprises, Inc. were \$23 for each of the three-month periods ended March 31, 2002 and 2001.

7. Subsequent Events

On April 11, 2002, the Company paid dividends of \$0.24 per share of common stock to all common stockholders of record as of March 29, 2002. On the same date, the operating partnerships paid a distribution of \$0.24 per O.P. Unit.

8. Commitments and Contingencies

The Company and the operating partnerships are or may become, from time to time, parties to litigation arising out of the normal course of business. Management is not aware of any litigation against the Company that would have a material adverse effect on the consolidated financial position, results of operations or cash flows of the Company.

Insurance policies currently maintained by the Company do not cover seismic activity, although they do cover losses from fires after an earthquake.

9. Discontinued Operations

Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long Lived Assets" which addresses financial accounting and reporting for the impairment and disposal of long-lived assets. In general, income or loss attributable to the operations and sale of property, and the operations related to property held for sale, are classified as discontinued operations in the statements of operations. Prior period statement of operations have been reclassified to reflect the income or loss related to properties that were sold and presented as discontinued operations during the three months ended March 31, 2002. Additionally, all periods presented will likely require further reclassification in future periods if additional property sales occur.

As of March 31, 2002, there were no properties under contract to be sold or disposed of which would qualify as discontinued operations.

In March 2002, the Company sold one property for a gain of \$6,103. Gain from operation for this property was approximately \$287 and \$430 for the three months ended March 31, 2002 and 2001, respectively. Condensed operations for the three months ended March 31, 2002 and 2001 are as follows:

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Three Months Ended March 31,

2002

2001

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	-----	-----
	(Dollars in thousands)	
Rental income from real estate	\$333	\$500
Tenant reimbursements	293	23
	-----	-----
Total revenues	626	523
	-----	-----
Real estate taxes	293	23
Depreciation	46	70
	-----	-----
Total expenses	339	93
	-----	-----
Net income	\$287	\$430
	=====	=====

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ITEM 2

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the accompanying consolidated financial statements and notes thereto contained herein and the Company's consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K as of and for the year ended December 31, 2001. The results for the three months ended March 31, 2002 are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2002. The following discussion includes forward-looking statements, including but not limited to, statements with respect to the Company's future financial performance, operating results, plans and objectives. Actual results may differ materially from those currently anticipated depending upon a variety of factors, including those described below under the sub-heading, "Forward-Looking Information."

OVERVIEW

Mission West Properties, Inc. (the "Company") acquires, markets, leases, and manages R&D and office properties, primarily located in the Silicon Valley portion of the San Francisco Bay Area. As of March 31, 2002, the Company owned and managed 100 properties totaling approximately 7.0 million rentable square feet through four limited partnerships, or operating partnerships, for which it is the sole general partner. This class of property is designed for research and development and office uses and, in some cases, includes space for light manufacturing operations with loading docks. The Company believes that it has one of the largest portfolios of R&D properties in the Silicon Valley. The four tenants who lease the most square footage from the Company are Microsoft Corporation, JDS Uniphase Corporation, Amdahl Corporation (a subsidiary of Fujitsu Limited), and Apple Computer, Inc. For federal income tax purposes the Company has operated as a self-managed, self-administered and fully integrated real estate investment trust ("REIT") since fiscal 1999.

The Company's acquisition and growth strategy incorporates the following elements:

- working with the Berg Group to take advantage of their abilities and

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resources to pursue development opportunities which we have an option to acquire, on pre-negotiated terms, upon completion and leasing;

- capitalizing on opportunistic acquisitions from third parties of high-quality R&D and office properties that provide attractive initial yields and significant potential for growth in cash-flow;
- focusing on general purpose, single-tenant Silicon Valley R&D and office properties for information technology companies in order to maintain low operating costs, reduce tenant turnover and capitalize on our relationships with these companies and our extensive knowledge of their real estate needs; and
- maintaining prudent financial management principles that emphasize current cash flow while building long-term value, the acquisition of pre-leased properties to reduce development and leasing risks and the maintenance of sufficient liquidity to acquire and finance properties on desirable terms.

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RESULTS OF OPERATIONS

COMPARISON OF THE THREE MONTHS ENDED MARCH 31, 2002 TO THE THREE MONTHS ENDED MARCH 31, 2001.

As of March 31, 2002, the Company, through its controlling interests in the operating partnerships, owned 100 properties totaling approximately 7.0 million square feet compared to 90 properties totaling approximately 6.2 million square feet owned by the Company as of March 31, 2001. This represents a net increase of approximately 13% in total rentable square footage from one year ago. Since March 31, 2001 the Company has acquired the properties listed below and disposed of 77,700 rentable square feet at 5713-5729 Fontanoso Way and 72,400 rentable square feet at 2001 Logic Drive in San Jose, California.

Date of Acquisition	Address	Rentable Square Footage
04/01	245 Caspian Drive (1) (3)	59,400
05/01	855 Branham Lane East (1)	67,912
06/01	5550 Hellyer Avenue	78,794
07/01	5906-65 Silver Creek Valley Rd. I (2)	247,500
08/01	5750 Hellyer Avenue	73,312
10/01	5905-65 Silver Creek Valley Rd. II	98,500
01/02	5345 Hellyer Avenue	125,000
03/02	2630 Orchard Parkway (4)	60,633
03/02	2610 Orchard Parkway (4)	54,093
03/02	55 West Trimble (4)	91,722

		956,866
		=====

- (1) Acquired in a tax-deferred exchange from the sale of R&D property at 4949 Hellyer Avenue, San Jose, California.
- (2) Three buildings were acquired at this location.

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- (3) The lessee at this location will terminate its lease effective May 2002 in a negotiated settlement with us. The building has not been completed for occupancy, which was at the option of the lessee.
- (4) Acquired in a tax-deferred exchange from the sale of R&D properties at 5713-5729 Fontanoso Way and 2001 Logic Drive, San Jose, California.

The following tables reflect the increase in the Company's rental revenues, excluding rental revenues from discontinued operations, for the three months ended March 31, 2002 over rental revenues for the comparable three months in 2001:

	Three Months Ended March 31,			% Change by
	2002	2001	\$ Change	Property Gro
	(Dollars in thousands)			
Same Property (1)	\$25,910	\$28,243	(\$ 2,333)	(8.3%)
2001 Acquisitions (2)	5,534	1,436	4,098	285.4%
2002 Acquisitions	1,040	-	1,040	100.0%
	\$32,484	\$29,679	\$ 2,805	9.4%

- (1) "Same Property" is defined as properties owned as of July 1, 1998 and acquired in 1998, 1999 and 2000 and still owned as of March 31, 2002.
- (2) The figures for "2001 Acquisitions" in year 2001 for some properties do not reflect a full three months of rent due to the timing of the acquisition of the properties during 2001.

RENTAL REVENUE FROM CONTINUING OPERATIONS

For the quarter ended March 31, 2002, rental revenues increased by \$2.8 million from \$29.7 million for the three months ended March 31, 2001 to \$32.5 million for the same period of 2002, which included a decrease of \$1.4 million straight-line rent adjustment. Of the \$2.8 million increase in rental revenues, (\$2.3) million resulted from the Company's "Same Property" portfolio, \$4.1 million resulted from properties acquired in 2001 and \$1.0 million resulted from properties acquired in 2002. Approximately \$0.3 million in rental revenues was generated from a discontinued operation for the three months ended March 31, 2002. The decline in rental revenues from the "same property" portfolio was a result from adverse market conditions and loss of seven tenants due to bankruptcy or cease of operations. The net increase in rental revenues was primarily attributable to new acquisitions.

OTHER INCOME FROM CONTINUING OPERATIONS

Other income, including interest, was approximately \$0.5 million for each of the three-month periods ended March 31, 2002 and 2001.

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EXPENSES FROM CONTINUING OPERATIONS

Tenant reimbursements from continuing operations increased by \$1.8 million, or 51%, from \$3.5 million for the three months ended March 31, 2001 to \$5.3 million for the three months ended March 31, 2002. Operating expenses and real estate

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taxes from continuing operations, on a combined basis, also increased by \$1.8 million, or 51%, from \$3.5 million to \$5.3 million for the three months ended March 31, 2001 and 2002, respectively. Both tenant reimbursements and operating expenses combined with real estate taxes from a discontinued operation were approximately \$0.3 million each for the quarter ended March 31, 2002. The increases in all categories resulted primarily from the increase in the total rentable square footage since March 31, 2001.

Depreciation expense from continuing operations increased by \$0.3 million from \$4.1 million to \$4.4 million for the three months ended March 31, 2001 and 2002, respectively. Depreciation expense from a discontinued operation was approximately \$46,000 for the quarter ended March 31, 2002. The increase was attributable to the acquisition of twelve R&D properties since March 31, 2001.

Interest expense increased by \$0.06 million, or 2.7%, from \$2.21 million for the three months ended March 31, 2001 to \$2.27 million for the three months ended March 31, 2002 from additional debt that the Company incurred under a new \$20.0 million unsecured loan obtained from Citicorp during the first quarter 2002. Interest expense (related parties) decreased by \$0.29 million, or 22.3%, from \$1.30 million for the three months ended March 31, 2001 to \$1.01 million for the three months ended March 31, 2002 due to lower interest rates and repayments on the Berg Group line of credit. As a result, overall interest expense (including amounts to related parties) for the quarter ended March 31, 2002 decreased by \$0.23 million compared to the first quarter a year ago. The twelve R&D property acquisitions increased total debt outstanding, including amounts due related parties, by \$36.02 million, or 17.4%, from \$207.29 million as of March 31, 2001 to \$243.31 million as of March 31, 2002. Management expects interest expense to increase as new debt is incurred in connection with property acquisitions, as the Company draws on the Berg Group line of credit, and as it seeks alternative sources of credit.

MINORITY INTEREST AND NET INCOME

The minority interest portion of income increased by \$4.99 million, or 23.6%, from \$21.10 million for the three months ended March 31, 2001 to \$26.09 million for the three months ended March 31, 2002. Net income to shareholders increased by \$0.98 million, or 23.2%, from \$4.22 million for the three months ended March 31, 2001 to \$5.20 million for the same period in 2002. Minority interest represents the ownership interest of all limited partners in the operating partnerships taken as a whole, which was approximately 83% as of March 31, 2002 and 2001.

RECENT RENTAL MARKET DEVELOPMENTS

All of the Company's properties are located in the Northern California area known as Silicon Valley, which generally consists of portions of Santa Clara County, Southwestern Alameda County, Southeastern San Mateo County and Eastern Santa Cruz County. The Silicon Valley economy and business activity slowed markedly in 2001 and in the first three months of 2002 after fast-paced growth in 1999 and 2000. The Silicon Valley R&D property market has historically fluctuated with the local economy. According to a recent report by BT Commercial Real Estate, vacancy rates for Silicon Valley R&D property increased from approximately 14.8% in late 2001 to 17.3% at the end of the first quarter 2002. Total vacant R&D square footage in Silicon Valley at the end of the first quarter of 2002 amounted to 26.1 million square feet, of which 44%, or 11.5 million square feet, accounted for sublease spaces. Total negative net absorption in 2001 amounted to approximately (15.6) million square feet. During the first three months of 2002, there was total negative net absorption of approximately (3.5) million square feet. The impact of this decline has not been uniform throughout the area, however. The Silicon Valley R&D property market has been characterized by a substantial number of submarkets, with rent and vacancy rates varying considerably by submarket and location within each submarket. The Company's average occupancy rate for the three-month period ended March 31, 2002

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was 95% with approximately 476,000 rentable square feet expiring in 2002. Key tenants could seek the protection of the bankruptcy laws, which could result in the rejection and termination of their leases, thereby causing a reduction in our rental income. For example, during the last six months, six tenants accounting for approximately 458,000 net rentable square feet of R&D properties have either filed petitions under Chapter 11 of the Bankruptcy Code or have discontinued operations. Under the bankruptcy laws, tenants may have the right to reject their leases with us and our claim for rent will be limited to the greater of one year's rent or 15% of the total amount of rent under the leases upon default, but not to exceed three years of rent on the remaining term of the lease following the earlier of the petition filing date or the date on which we gained repossession of the property, as well as any rent that was unpaid on the earlier of those dates. These properties may take anywhere from six to twelve months or longer to re-lease. The Company anticipates its vacancy rate to range between 12-15% by the end of 2002 and renewal rental rates to be the same as or, perhaps, lower than current rents. The Company's operating results and ability to pay dividends at current levels remain subject to a number of material risks, as indicated under the caption "Forward-Looking Information" below and in the section entitled "Risk Factors" in the Company's most recent annual report on Form 10-K.

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CHANGES IN FINANCIAL CONDITION

The most significant changes in the Company's financial condition during the three months ended March 31, 2002 resulted from property acquisitions and exchanges. In addition, debt increased from new acquisitions and stockholders' equity increased from the exercise of stock options and the exchange of O.P. Units for common stock.

At March 31, 2002, real estate assets increased by approximately \$31.5 million from December 31, 2001 because of new acquisitions and one disposition. During the first three months of 2002, the Company acquired one additional property representing approximately 125,000 rentable square feet of R&D property located in Silicon Valley. This property was acquired from the Berg Group under the Berg land holdings option agreement. The aggregate acquisition price for this property was approximately \$13.7 million. The Company financed this acquisition by borrowing \$7.5 million under the Berg Group line of credit and issuing 502,805 O.P. Units. In March 2002, the Company acquired three R&D properties representing approximately 206,500 rentable square feet for approximately \$31.3 million as replacement properties in a tax-deferred exchange in which the Company disposed of former R&D properties at 5713-5729 Fontanoso Way and 2001 Logic Drive in San Jose, California. Pending the purchase of the replacement properties, the proceeds for the Fontanoso Way and Logic Drive properties were classified as restricted cash of which approximately \$2.7 million remained in restricted cash at March 31, 2002. No debt or O.P. Units were issued for these acquisitions. The Company also realized a gain of \$6.1 million on the transaction.

At March 31, 2002, total liabilities increased by approximately \$8.3 million from December 31, 2001 due to mainly debt incurred in connection with R&D property acquisitions.

At March 31, 2002, total stockholders' equity increased by approximately \$2.4 million from December 31, 2001 from reduction of accumulated deficit, stock option exercises and the exchange of O.P. Units for the Company's common stock. During the three months ended March 31, 2002, stock options to purchase 33,550 shares of common stock were exercised at \$4.50 per share. Total proceeds to the

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Company were approximately \$0.15 million. One limited partner of an operating partnership exchanged 100,000 O.P. Units for 100,000 shares of the Company's common stock under the exchange rights agreement among the Company and the limited partners in the operating partnerships, which represented additional paid in capital of approximately \$1.3 million.

LIQUIDITY AND CAPITAL RESOURCES

The Company expects its principal sources of liquidity for distributions to stockholders and unit holders, debt service, leasing commissions and recurring capital expenditures to come from Funds From Operations ("FFO") and/or the Berg Group line of credit and other credit facilities that may be established by the Company with third party financial institutions. The Company expects these sources of liquidity to be adequate to meet projected distributions to stockholders and other presently anticipated liquidity requirements in 2002. The Company expects to meet its long-term liquidity requirements for the funding of property development, property acquisitions and other material non-recurring capital improvements through long-term secured and unsecured indebtedness and the issuance of additional equity securities by the Company. The Company has the ability to meet short-term obligations or other liquidity needs based on the line of credit (related parties). Despite the current weakness in the economy, the Company expects interest expense to increase, but not significantly, as it incurs debt through acquisitions of new properties and as interest rates increase.

The Company is continually evaluating alternative sources of credit to replace the Berg Group \$100 million line of credit, which expires in March 2003. The Company believes that the terms of the Berg Group line of credit are more favorable than those available from institutional lenders. There can be no assurance that the Berg Group will continue to rollover and extend this line of credit, as it has been doing since 1999, or the Company will be able to obtain a line of credit with terms similar to the Berg Group line of credit. Thus, the Company's cost of borrowing could increase substantially after 2002.

On March 1, 2002, the Company obtained a \$20 million unsecured loan from Citicorp USA, Inc. with an interest rate based on LIBOR. The loan, which matures on March 1, 2003, bears a fixed LIBOR interest rate of 4.09% for the first six months and LIBOR plus 2.0% thereafter. The Company paid a loan fee of \$50,000 and expects to use the loan for acquiring new R&D properties.

At March 31, 2002, the Company had total indebtedness of \$243.3 million, including \$126.9 million of fixed rate mortgage debt, \$11.3 million under the Berg Group mortgage note (related parties), \$85.1 million under the Berg Group line of credit (related parties), and \$20.0 million under the Citicorp loan.

As of March 31, 2002, the Company's Debt to Total Market Capitalization ratio was approximately 15.1%, based upon a Total Market Capitalization of approximately \$1.6 billion. The Company computed this ratio by dividing the Company's total debt outstanding by the sum of this debt plus the market value of common stock (based upon the closing price of \$13.10 per share on March 28, 2002) on a fully diluted basis, taking into account the conversion of all O.P. Units into common stock.

On April 11, 2002, the Company paid dividends of \$0.24 per share of common stock to all common stockholders of record as of March 29, 2002. On the same date, the operating partnerships paid a distribution of \$0.24 per O.P. Unit.

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MORTGAGE DEBT

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The following table sets forth information regarding debt outstanding as of March 31, 2002:

Debt Description	Collateral Properties	
		(Dollars)
Line of Credit:		
Berg Group (related parties)	2033-2043 Samaritan Drive, San Jose, CA 2133 Samaritan Drive, San Jose, CA 2233-2243 Samaritan Drive, San Jose, CA 1310-1450 McCandless Drive, Milpitas, CA 1315-1375 McCandless Drive, Milpitas, CA 1650-1690 McCandless Drive, Milpitas, CA 1795-1845 McCandless Drive, Milpitas, CA 5325 Hellyer Avenue, San Jose, CA 5345 Hellyer Avenue, San Jose, CA 2610 N. First Street, San Jose, CA 75 E. Trimble Road, San Jose, CA	-----
Unsecured Loan:		
Citicorp USA, Inc.	Not Available	-----
Mortgage Notes Payable (related parties):	5300 & 5350 Hellyer Avenue, San Jose, CA	-----
Mortgage Notes Payable:		
Prudential Capital Group	20400 Mariani Avenue, Cupertino, CA	
New York Life Insurance Company	10440 Bubb Road, Cupertino, CA	
Home Savings & Loan Association	10460 Bubb Road, Cupertino, CA	
Prudential Insurance Company of America (3)	10300 Bubb Road, Cupertino, CA 10500 N. DeAnza Blvd, Cupertino, CA 4050 Starboard Drive, Fremont, CA 45700 Northport Loop, Fremont, CA 45738 Northport Loop, Fremont, CA 450-460 National Avenue, Mountain View, CA 6311 San Ignacio Avenue, San Jose, CA 6321 San Ignacio Avenue, San Jose, CA 6325 San Ignacio Avenue, San Jose, CA 6331 San Ignacio Avenue, San Jose, CA 6341 San Ignacio Avenue, San Jose, CA 6351 San Ignacio Avenue, San Jose, CA 3236 Scott Blvd, Santa Clara, CA 3560 Bassett Street, Santa Clara, CA 3570 Bassett Street, Santa Clara, CA 3580 Bassett Street, Santa Clara, CA 1135 Kern Avenue, Sunnyvale, CA 1212 Bordeaux Lane, Sunnyvale, CA 1230 E. Arques, Sunnyvale, CA 1250 E. Arques, Sunnyvale, CA 1170 Morse Avenue, Sunnyvale, CA 1600 Memorex Drive, Santa Clara, CA 1688 Richard Avenue, Santa Clara, CA 1700 Richard Avenue, Santa Clara, CA 3540 Bassett Street, Santa Clara, CA 3542 Bassett Street, Santa Clara, CA 3544 Bassett Street, Santa Clara, CA 3550 Bassett Street, Santa Clara, CA	

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Mortgage Notes Payable Subtotal

TOTAL

- (1) The debt owed to the Berg Group under the line of credit carries a variable interest rate equal to LIBOR plus 1.30% and is payable in full in March 2003. The interest rate at March 31, 2002 was 3.632%.
- (2) The unsecured loan from Citicorp USA, Inc. carries a fixed LIBOR interest rate equal to 4.09% for the first six months and LIBOR plus 2.0% thereafter and is payable in full in March 2003.
- (3) John Kontrabecki, one of the limited partners, has guaranteed approximately \$12.0 million of this debt.

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CURRENT PROPERTIES SUBJECT TO OUR ACQUISITION AGREEMENT WITH THE BERG GROUP

The following table presents certain projected information at March 31, 2002 concerning projects for which the Company, through its interests in the operating partnerships, has the right to acquire under the Berg land holdings option agreement.

Property	Number of Buildings	Approximate Rentable Area (Square Feet)	Anticipated Acquisition Date	To Acqui
BERG LAND HOLDINGS OPTION				
UNDER DEVELOPMENT				
Morgan Hill (JV I) (2)	2	160,000	4th Q 2002/Q1 2003	(dol
Morgan Hill (JV II) (2)	1	151,242	4th Q 2002/Q1 2003	
Piercy & Hellyer	1	165,000	3rd Q 2002	
	-	-----		
Subtotal	4	476,242		
AVAILABLE LAND				
Piercy & Hellyer		490,000		
Morgan Hill (2)		368,025		
King Ranch		207,000		
Fremont & Cushing		387,000		
Evergreen		2,480,000		

Subtotal		3,932,025		
TOTAL	4	4,408,267		
	=	=====		

- (1) The estimated acquisition value represents the estimated cash price for acquiring the projects under the terms of the Berg land holdings option

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agreement, which may differ from the actual acquisition cost as determined under GAAP, if O.P. Units or any other securities based on the market value of our common stock are issued in the transaction.

- (2) The Company expects to own an approximate 50% interest in the partnership through one of its operating partnerships. The property will be operated and managed by the other partner in the entity. The rentable area and estimated acquisition value shown above reflect both the Company's and the other partner's combined interest in these properties.

Pursuant to the Berg land holdings option agreement between the Company and the Berg Group, the Company currently has the option to acquire any future R&D, office and industrial property developed by the Berg Group on land it currently owns or has under option, or acquires for these purposes in the future, directly or indirectly by certain members of the Berg Group.

The time required to complete the leasing of developments varies from project to project. The acquisition dates and acquisition costs set forth in the table are only estimates by management. Generally, the Company will not acquire any of the above projects until they are fully completed and leased. There can be no assurance that the acquisition date and final cost to the Company as indicated above would be realized. No estimate can be given at this time as to the Company's total cost to acquire projects under the Berg land holdings option agreement, nor can we be certain of the period in which we will acquire any of the projects.

Although the Company expects to acquire the new properties available to it under the terms of the Berg land holdings option agreement, subsequent to the approval by the independent directors committee, there can be no assurance that the Company actually will consummate any intended transactions, including all of those discussed above. Furthermore, the Company has not yet determined the means by which it would acquire and pay for any such properties or the impact of any of the acquisitions on its business, results of operations, financial condition, FFO or available cash for distribution.

Leasing activity for new build-to-suit and vacated R&D properties has slowed considerably during the past year and the first three months of 2002. Consequently, the Company believes that the projected acquisition dates for other development properties subject to the Berg land holdings option agreement, with the exception of the project at Piercy and Hellyer for approximately 165,000 rentable square feet, may be delayed for the foreseeable future. Such delays could reduce future growth in revenues, operating income and Funds Available for Distribution ("FAD").

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HISTORICAL CASH FLOWS

Net cash provided by operating activities for the three months ended March 31, 2002 was \$28.6 million compared to \$22.3 million for the same period in 2001, a 28% increase. The change was a direct result of increased rent from newly acquired properties.

Net cash used in investing activities was approximately \$18.8 million and \$0.7 million for the three months ended March 31, 2002 and 2001, respectively. Of the \$18.8 million net cash used in investing activities, \$18.5 million were returned to Xilinx, Inc. relating to the purchase option agreement between Xilinx and the Company, and \$0.3 million were applied to Xilinx's monthly rent.

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Net cash used in financing activities was \$7.6 million for the three months ended March 31, 2002 compared to \$26.3 million for the same period in 2001, a 71% decrease. Of the \$7.6 million net cash used in financing activities, \$2.9 million were used to pay outstanding debt, \$20.6 million for minority interest distributions, \$4.2 million for dividend payments, net of \$20.1 million received from the Citicorp unsecured loan and the proceeds of exercised stock options. During the three months ended March 31, 2002, the Company made payments on outstanding debt and distributions to holders of its common stock and O.P. Units by utilizing cash generated from operating activities.

CAPITAL EXPENDITURES

The Company's existing R&D properties require periodic investments of capital for tenant-related capital expenditures and for general capital improvements. For the years ended December 31, 1997 through December 31, 2001, the recurring tenant improvement costs and leasing commissions incurred with respect to new leases and lease renewals of the properties that were owned or controlled by members of the Berg Group prior to July 1, 1998 averaged approximately \$1.75 million annually. The Company expects that the average annual cost of recurring tenant improvements and leasing commissions, related to the properties, will be approximately \$1.3 million during 2002. The Company believes it will recover substantially all of these sums from the tenants under new or renewed leases through increases in rental rates. The Company expects to meet its long-term liquidity requirements for the funding of property development, property acquisitions and other material non-recurring capital improvements through long-term secured and unsecured indebtedness and the issuance of additional equity securities by the Company.

FUNDS FROM OPERATIONS

As defined by the National Association of Real Estate Investment Trusts ("NAREIT"), FFO represents net income (loss) before minority interest of unit holders (computed in accordance with GAAP), excluding gains (or losses) from debt restructuring and sales of property, plus real estate related depreciation and amortization (excluding amortization of deferred financing costs and depreciation of non-real estate assets) and after adjustments for unconsolidated partnerships and joint ventures. Management considers FFO an appropriate measure of performance of an equity REIT because, along with cash flows from operating activities, financing activities and investing activities, it provides investors with an understanding of the Company's ability to incur and service debt, and make capital expenditures. With the recent emphasis on the disclosure of operating earnings per share, we will still continue to use FFO as a measure of the Company's performance. FFO should not be considered as an alternative for net income as a measure of profitability and it is not comparable to cash flows provided by operating activities determined in accordance with GAAP, nor is FFO necessarily indicative of funds available to meet the Company's cash needs, including its need to make cash distributions to satisfy REIT requirements.

The Company's definition of FFO also assumes conversion at the beginning of the period of all convertible securities, including minority interests that might be exchanged for common stock. FFO does not represent the amount available for management's discretionary use as such funds may be needed for capital replacement or expansion, debt service obligations or other commitments and uncertainties.

The minority interest in earnings for unrelated parties are deducted from total minority interest in earnings in calculating FFO.

Furthermore, FFO is not comparable to similarly entitled items reported by other REITs that do not define them exactly as the Company defines FFO. FFO for the three months ended March 31, 2002 and 2001 are summarized in the tables below:

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	Three Months Ended March 31,	
	2002	2001
	(Dollars in thousands)	
Net income	\$ 5,201	\$ 4,219
Add:		
Minority interest (1)	25,933	20,916
Depreciation	4,402	4,102
Less:		
Gain on sale of assets	6,103	3,101
FFO	\$29,433	\$26,136

(1) The minority interest for unrelated parties was deducted from total minority interest in calculating FFO. Distribution Policy

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DISTRIBUTION POLICY

The Company intends to pay distributions to stockholders and O.P. unit holders based upon total Funds Available for Distribution ("FAD"), which is calculated as FFO less adjustment for straight-line rent included in net income, leasing commissions paid and capital expenditures made during the respective period. The calculations of FAD for the three months ended March 31, 2002 and 2001 are as follows:

	Three Months Ended March 31,	
	2002	2001
	(Dollars in thousands)	
FFO	\$29,433	\$26,136
Less:		
Straight-line rents	(780)	2,089
Leasing commissions	140	163
Capital expenditures	-	154
FAD	\$30,073	\$23,730

The Company's board of directors will determine the amount and timing of distributions to our stockholders. The board of directors will consider many factors prior to making any distributions, including the following:

- the amount of cash available for distribution;

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- the Company's financial condition;
- whether to reinvest funds rather than to distribute such funds;
- the Company's committed and projected capital expenditures;
- the effects of new property acquisitions, including acquisitions under existing agreements with the Berg Group;
- the annual distribution requirements under the REIT provisions of the federal income tax laws; and
- such other factors as the board of directors deems relevant.

We cannot assure you that the Company will be able to meet or maintain management's cash distribution objectives.

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IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

The Company does not believe recently issued accounting standards will materially impact the Company's financial statements.

FORWARD-LOOKING INFORMATION

This quarterly report contains forward-looking statements within the meaning of the federal securities laws. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Reform Act of 1995, and is including this statement for purposes of complying with these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of the Company, are generally identifiable by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project" or similar expressions. Additionally, all disclosures under Part I., Item 3 constitutes forward-looking statements. The Company's ability to predict results or the actual effect of future plans or strategies is inherently uncertain.

Factors that could have a material adverse effect on the operations and future prospects of the Company include, but are not limited to, changes in:

- economic conditions generally and the real estate market specifically,
- legislative or regulatory provisions affecting the Company (including changes to laws governing the taxation of REITs),
- availability of capital,
- interest rates,
- competition,
- supply of and demand for R&D, office and industrial properties in the Company's current and proposed market areas,

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- tenant defaults and bankruptcies, and
- general accounting principles, policies and guidelines applicable to REITs.

In addition, the actual timing of development, construction, and leasing on the projects that the Company believes it may acquire in the future under the Berg land holdings option agreement is unknown presently, and reliance should not be placed on the estimates concerning these projects set forth under the caption, "Current Properties Subject to Our Acquisition Agreement with the Berg Group," above. These risks and uncertainties, together with the other risks described from time to time in the Company's reports and other documents filed with the Securities and Exchange Commission, should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements.

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ITEM 3

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We do not generally hold market risk sensitive instruments for trading purposes. We use fixed and variable rate debt to finance our operations. Our exposure to market risk for changes in interest rates relates primarily to our current and future debt obligations. We are vulnerable to significant fluctuations of interest rates on our floating rate debt, and pricing on our future debt. We manage our market risk by monitoring interest rates where we try to recognize the unpredictability of the financial markets and seek to reduce potentially adverse effect on the results of our operations. This takes frequent evaluation of available lending rates and examination of opportunities to reduce interest expense through new sources of debt financing. By attempting to match anticipated cash inflow from our operating and financing activities with anticipated cash outflow to fund debt payments, distributions to shareholders and O.P. Unit holders, capital expenditures and other cash requirements, we expect to minimize the effects on our future earnings and cash flow where interest rate risk is most sensitive. Several factors affecting the interest rate risk include governmental monetary and tax policies, domestic and international economics and other factors that are beyond our control.

The primary market risk we face is the risk of interest rate fluctuations. The Berg Group line of credit, which is tied to a LIBOR based interest rate, was approximately \$85.1 million, or 35%, of the total \$243.3 million of outstanding debt as of March 31, 2002. As a result, we pay lower rates of interest in periods of decreasing interest rates and higher rates of interest in periods of increasing interest rates. At March 31, 2002, we had no interest rate caps or interest rate swap contracts.

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PART II - OTHER INFORMATION

ITEM 6

EXHIBITS AND REPORTS ON FORM 8-K

- a. Exhibits
- None
- b. Reports on Form 8-K

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None

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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 thereto duly authorized.

MISSION WEST PROPERTIES, INC.
(Registrant)

Date: May 14, 2002

By: /s/ Wayne N. Pham

Wayne N. Pham
Vice President of Finance and Controller
(Principal Accounting Officer and Duly
Authorized Officer)

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