**UNITED STATES**
**SECURITIES AND EXCHANGE COMMISSION**
**WASHINGTON, DC 20549**

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# FORM 10-Q

**Quarterly Report Pursuant to Section 13 or 15(d)**
**of the Securities Exchange Act of 1934**

**For Quarterly Period Ended March 31, 2007**
**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 1-11533**

**Parkway Properties, Inc.**
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Maryland** | **74-2123597** |
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |

**One Jackson Place Suite 1000**
**188 East Capitol Street**
**P. O. Box 24647**
**Jackson, Mississippi 39225-4647**
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code **(601) 948-4091**
Registrant's web site **www.pky.com**

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).
Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes ☐ No ☒

15,888,182 shares of Common Stock, $.001 par value, were outstanding as of May 1, 2007.

**PARKWAY PROPERTIES, INC.**

**FORM 10-Q**

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## Part I. Financial Information



## Part II. Other Information



## Signatures

**PARKWAY PROPERTIES, INC.**
**CONSOLIDATED BALANCE SHEETS**
(In thousands, except share data)

| | March 31 2007 | December 31 2006 |
|---|---|---|
| | (Unaudited) | |
| **Assets** | | |
| Real estate related investments: | | |
| Office and parking properties | $ 1,526,346 | $ 1,517,468 |
| Accumulated depreciation | (225,172) | (211,187) |
| | 1,301,174 | 1,306,281 |
| Land available for sale | 1,467 | 1,467 |
| Investment in unconsolidated joint ventures | 11,087 | 11,179 |
| | 1,313,728 | 1,318,927 |
| Rents receivable and other assets | 103,187 | 107,145 |
| Intangible assets, net | 77,727 | 81,800 |
| Cash and cash equivalents | 8,304 | 4,474 |
| | $ 1,502,946 | $ 1,512,346 |
| **Liabilities** | | |
| Notes payable to banks | $ 172,034 | $ 152,312 |
| Mortgage notes payable | 705,443 | 696,012 |
| Accounts payable and other liabilities | 65,357 | 72,659 |
| Subsidiary redeemable preferred membership interests | 10,741 | 10,741 |
| | 953,575 | 931,724 |
| **Minority Interest** | | |
| Minority Interest – unit holders | 36 | 36 |
| Minority Interest – real estate partnerships | 66,958 | 90,280 |
| | 66,994 | 90,316 |
| **Stockholders' Equity** | | |
| 8.00% Series D Preferred stock, $.001 par value, 2,400,000 shares authorized, issued and outstanding | 57,976 | 57,976 |
| Common stock, $.001 par value, 67,600,000 shares authorized, 15,886,801 and 15,764,799 shares issued and outstanding in 2007 and 2006, respectively | 16 | 16 |
| Excess stock, $.001 par value, 30,000,000 shares authorized, no shares issued | - | - |
| Common stock held in trust, at cost, 111,000 and 115,000 shares in 2007 and 2006, respectively | (3,759) | (3,894) |
| Additional paid-in capital | 452,382 | 449,141 |
| Accumulated other comprehensive income | 591 | 828 |
| Accumulated deficit | (24,829) | (13,761) |
| | 482,377 | 490,306 |
| | $ 1,502,946 | $ 1,512,346 |

See notes to consolidated financial statements.

**PARKWAY PROPERTIES, INC.**
**CONSOLIDATED STATEMENTS OF INCOME**
(In thousands, except per share data)

| | Three Months Ended March 31 2007 | Three Months Ended March 31 2006 |
|---|---|---|
| | (Unaudited) | |
| **Revenues** | | |
| Income from office and parking properties | $ 61,538 | $ 48,661 |
| Management company income | 333 | 362 |
| Total revenues | 61,871 | 49,023 |
| **Expenses** | | |
| Property operating expense | 28,234 | 23,629 |
| Depreciation and amortization | 19,211 | 13,526 |
| Operating expense for other real estate properties | 1 | 1 |
| Management company expenses | 268 | 375 |
| General and administrative | 1,645 | 1,146 |
| Total expenses | 49,359 | 38,677 |
| **Operating income** | 12,512 | 10,346 |
| **Other income and expenses** | | |
| Interest and other income | 146 | 19 |
| Equity in earnings of unconsolidated joint ventures | 305 | 410 |
| Gain on sale of real estate | 50 | - |
| Interest expense | (13,084) | (9,426) |
| **Income (loss) before minority interest and discontinued operations** | (71) | 1,349 |
| Minority interest - real estate partnerships | 471 | 80 |
| **Income from continuing operations** | 400 | 1,429 |
| Discontinued operations: | | |
| Income from discontinued operations | 28 | 312 |
| **Net income** | 428 | 1,741 |
| Change in unrealized loss on equity securities | (4) | (30) |
| Change in market value of interest rate swaps | (234) | 466 |
| **Comprehensive income** | $ 190 | $ 2,177 |
| **Net income available to common stockholders:** | | |
| Net income | $ 428 | $ 1,741 |
| Dividends on preferred stock | (1,200) | (1,200) |
| Dividends on convertible preferred stock | - | (587) |
| **Net loss available to common stockholders** | $ (772) | $ (46) |
| **Net income (loss) per common share:** | | |
| Basic: | | |
| Loss from continuing operations | $ (0.05) | $ (0.02) |
| Discontinued operations | - | 0.02 |
| Net loss | $ (0.05) | $ - |
| Diluted: | | |
| Loss from continuing operations | $ (0.05) | $ (0.02) |
| Discontinued operations | - | 0.02 |
| Net loss | $ (0.05) | $ - |
| **Dividends per common share** | $ 0.65 | $ 0.65 |
| **Weighted average shares outstanding:** | | |
| Basic | 15,616 | 14,049 |
| Diluted | 15,616 | 14,049 |

See notes to consolidated financial statements.

**PARKWAY PROPERTIES, INC.**
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**
(In thousands)

| | Three Months Ended March 31 | |
|---|---|---|
| | **2007** | **2006** |
| | (Unaudited) | |
| **8.34% Series B Cumulative Convertible** | | |
| **Preferred stock, $.001 par value** | | |
| Balance at beginning of period | $ - | $ 28,122 |
| Balance at end of period | - | 28,122 |
| **8.00% Series D Preferred stock, $.001 par value** | | |
| Balance at beginning of period | 57,976 | 57,976 |
| Balance at end of period | 57,976 | 57,976 |
| **Common stock, $.001 par value** | | |
| Balance at beginning of period | 16 | 14 |
| Balance at end of period | 16 | 14 |
| **Common stock held in trust** | | |
| Balance at beginning of period | (3,894) | (4,198) |
| Shares distributed from deferred compensation plan | 135 | 203 |
| Balance at end of period | (3,759) | (3,995) |
| **Additional paid-in capital** | | |
| Balance at beginning of period | 449,141 | 389,971 |
| Stock options exercised | 2,610 | 590 |
| Shares issued – DRIP plan | 289 | - |
| Issuance costs – stock offering | (11) | - |
| Share based compensation expense | 353 | 147 |
| Reclassification upon the adoption of SFAS No. 123R | - | (3,101) |
| Balance at end of period | 452,382 | 387,607 |
| **Unearned compensation** | | |
| Balance at beginning of period | - | (3,101) |
| Reclassification upon the adoption of SFAS No. 123R | - | 3,101 |
| Balance at end of period | - | - |
| **Accumulated other comprehensive income** | | |
| Balance at beginning of period | 828 | 826 |
| Change in unrealized loss on equity securities | (4) | (30) |
| Change in market value of interest rate swaps | (233) | 466 |
| Balance at end of period | 591 | 1,262 |
| **Accumulated deficit** | | |
| Balance at beginning of period | (13,761) | 4,906 |
| Net income | 428 | 1,741 |
| Preferred stock dividends declared | (1,200) | (1,200) |
| Convertible preferred stock dividends declared | - | (587) |
| Common stock dividends declared | (10,296) | (9,200) |
| Balance at end of period | (24,829) | (4,340) |
| **Total stockholders' equity** | $ 482,377 | $ 466,646 |

See notes to consolidated financial statements.

**PARKWAY PROPERTIES, INC.**
**CONSOLIDATED STATEMENTS OF CASH FLOWS**
(In thousands)

| | Three Months Ended March 31 2007 | Three Months Ended March 31 2006 |
|---|---|---|
| | (Unaudited) | |
| **Operating activities** | | |
| Net income | $ 428 | $ 1,741 |
| Adjustments to reconcile net income to cash provided by operating activities: | | |
| Depreciation and amortization | 19,211 | 13,526 |
| Depreciation and amortization – discontinued operations | - | 200 |
| Amortization of above market leases | 352 | 409 |
| Amortization of loan costs | 293 | 282 |
| Share based compensation expense | 353 | 147 |
| Operating distributions from unconsolidated joint ventures | 405 | 357 |
| Loss allocated to minority interests | (471) | (80) |
| Net gain on sale of real estate | (50) | - |
| Equity in earnings of unconsolidated joint ventures | (305) | (410) |
| Changes in operating assets and liabilities: | | |
| Decrease in receivables and other assets | 2,226 | 2,907 |
| Decrease in accounts payable and other liabilities | (7,374) | (6,153) |
| **Cash provided by operating activities** | 15,068 | 12,926 |
| **Investing activities** | | |
| Purchases of real estate related investments | (2,119) | (1,456) |
| Improvements to real estate related investments | (6,364) | (7,310) |
| **Cash used in investing activities** | (8,483) | (8,766) |
| **Financing activities** | | |
| Principal payments on mortgage notes payable | (22,069) | (3,594) |
| Proceeds from long-term financing | 31,500 | - |
| Net proceeds from bank borrowings | 19,489 | 14,389 |
| Debt financing costs | (293) | (54) |
| Stock options exercised | 2,610 | 590 |
| Dividends paid on common stock | (10,219) | (9,138) |
| Dividends paid on preferred stock | (1,200) | (1,787) |
| Contributions from minority interest partners | 1,313 | 375 |
| Distributions to minority interest partners | (24,164) | (303) |
| Proceeds from DRIP Plan | 289 | - |
| Issuance costs from stock offerings | (11) | - |
| **Cash (used in) provided by financing activities** | (2,755) | 478 |
| **Change in cash and cash equivalents** | 3,830 | 4,638 |
| **Cash and cash equivalents at beginning of period** | 4,474 | 3,363 |
| **Cash and cash equivalents at end of period** | $ 8,304 | $ 8,001 |

See notes to consolidated financial statements.

**Parkway Properties, Inc.**
**Notes to Consolidated Financial Statements (Unaudited)**
**March 31, 2007**

## (1) Basis of Presentation

The consolidated financial statements include the accounts of Parkway Properties, Inc. ("Parkway" or "the Company"), its wholly-owned subsidiaries and joint ventures in which the Company has a controlling interest. Third party equity interests in the consolidated joint ventures are reflected as minority interests in the consolidated financial statements. Parkway also consolidates subsidiaries where the entity is a variable interest entity and Parkway is the primary beneficiary, as defined in FASB Interpretation 46R, *Consolidation of Variable Interest Entities* ("FIN 46R"). All significant intercompany transactions and accounts have been eliminated.

The Company determines consolidation for joint ventures based on standards set forth in EITF 96-16, *Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights;* EITF 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights;* Statement of Position 78-9, *Accounting for Investments in Real Estate Ventures;* and FIN 46R. Based on the guidance set forth in these pronouncements, the Company consolidates certain joint ventures where it exercises significant control over major operating and management decisions, or where the Company is the sole general partner and the limited partners do not possess kick-out rights or other substantive participating rights or where the entity is a variable interest entity and Parkway is the primary beneficiary. The equity method of accounting is used for those joint ventures that do not meet the criteria for consolidation under these pronouncements.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

The accompanying financial statements reflect all adjustments which are, in the opinion of management, necessary for a fair statement of the results for the interim periods presented. All such adjustments are of a normal recurring nature. Operating results for the three months ended March 31, 2007 are not necessarily indicative of the results that may be expected for the year ended December 31, 2007. The financial statements should be read in conjunction with the annual report and the notes thereto.

The balance sheet at December 31, 2006 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

On January 1, 2007, the Company adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 clarifies the accounting for uncertain income tax positions recognized in a company's financial statements and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Company has evaluated its tax positions and found that the adoption of FIN 48 has not had a material impact on income from continuing operations, net income, cash flow from operations, cash flow from financing activities or basic and diluted earnings per share.

## (2) Net Income Per Common Share

Basic earnings per share ("EPS") are computed by dividing income (loss) available to common stockholders by the weighted-average number of common shares outstanding for the period. In arriving at income available to common stockholders, preferred stock dividends are deducted. Diluted EPS reflects the potential dilution that could occur if share equivalents such as employee stock options, restricted shares, deferred incentive share units, warrants and 8.34% Series B cumulative convertible preferred stock were exercised or converted into common stock that then shared in the earnings of Parkway.

The computation of diluted EPS is as follows (in thousands, except per share data):

| | Three Months Ended March 31 | |
|---|---|---|
| | **2007** | **2006** |
| Numerator: | | |
| Basic and diluted net loss available to common stockholders | $ (772) | $ (46) |
| Denominator: | | |
| Basic weighted average shares | 15,616 | 14,049 |
| Diluted weighted average shares | 15,616 | 14,049 |
| Diluted earnings per share | $ (0.05) | $ 0.00 |

The computation of diluted EPS for the three months ended March 31, 2007 and 2006 did not include the effect of share equivalents because their inclusion would have been anti-dilutive.

## (3) Supplemental Cash Flow Information and Schedule of Non-Cash Investing and Financing Activity

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

| | Three Months Ended March 31 | |
|---|---|---|
| | **2007** | **2006** |
| | (in thousands) | |
| Supplemental cash flow information: | | |
| Cash paid for interest | $ 12,419 | $ 8,518 |
| Income taxes paid | 29 | 2 |
| Supplemental schedule of non-cash investing and financing activity: | | |
| None | - | - |

## (4) Discontinued Operations

All current and prior period income from the following office property dispositions are included in discontinued operations for the three months ended March 31, 2007 and 2006 (in thousands).

| Office Property | Location | Square Feet | Date of Sale | Gross Sales Price | Net Book Value of Real Estate | Gain (Loss) on Sale |
|---|---|---|---|---|---|---|
| The Park on Camelback | Phoenix, Arizona | 102 | 09/09/05 | $ 17,500 | $ 12,526 | $ 4,419 |
| 250 Commonwealth | Greenville, South Carolina | 46 | 09/14/05 | 4,020 | 4,104 | (238) |
| 2005 Dispositions | | 148 | | $ 21,520 | $ 16,630 | $ 4,181 |
| Central Station Building | St. Petersburg, Florida | 133 | 08/02/06 | $ 15,000 | $ 14,338 | $ 211 |
| Richmond Centre | Houston, Texas | 92 | 11/29/06 | 6,906 | 4,551 | 2,018 |
| Ashford II | Houston, Texas | 59 | 12/07/06 | 5,250 | 2,185 | 2,854 |
| 2006 Dispositions | | 284 | | $ 27,156 | $ 21,074 | $ 5,083 |

The amount of revenue and expense for these five office properties reported in discontinued operations for the three months ended March 31, 2007 and 2006 is as follows (in thousands):

| | Three Months Ended March 31 | |
|---|---|---|
| | **2007** | **2006** |
| **Income Statement:** | | |
| **Revenues** | | |
| Income from office and parking properties | $ 1 | $ 1,036 |
| | 1 | 1,036 |
| **Expenses** | | |
| Property operating expense | (27) | 524 |
| Depreciation and amortization | - | 200 |
| | (27) | 724 |
| **Income from discontinued operations** | $ 28 | $ 312 |

## (5) Investment in Unconsolidated Joint Ventures

As of March 31, 2007, the Company was invested in four unconsolidated joint ventures with unrelated investors. These joint ventures are accounted for using the equity method of accounting, as Parkway does not control but has the ability to significantly influence the operations of these joint ventures and is not the primary beneficiary, as that term is defined in FIN 46R. As a result, the assets and liabilities of the joint ventures are not included in Parkway's consolidated balance sheet. Information relating to the unconsolidated joint ventures at March 31, 2007 is detailed below (in thousands).

| Joint Ventures | Property Name | Location | Parkway's Ownership Interest | Square Feet | Percentage Leased |
|---|---|---|---|---|---|
| Wink-Parkway Partnership | Wink Building | New Orleans, LA | 50.0% | 32 | 100.0% |
| Parkway Joint Venture, LLC ("Jackson JV") | UBS Building/River Oaks | Jackson, MS | 20.0% | 167 | 81.8% |
| RubiconPark I, LLC ("Rubicon JV") | Lakewood/Falls Pointe<br>Carmel Crossing | Atlanta, GA<br>Charlotte, NC | 20.0% | 551 | 99.3% |
| RubiconPark II, LLC ("Maitland JV") | Maitland 200 | Orlando, FL | 20.0% | 203 | 93.2% |
| | | | | 953 | 95.0% |

Cash distributions from unconsolidated joint ventures are made to each partner based on their percentage of ownership in each entity. Cash distributions made to partners in joint ventures where the percentage of debt assumed is disproportionate to the ownership percentage in the venture is distributed based on each partner's share of cash available for distribution before debt service, based on their ownership percentage, less the partner's share of debt service based on the percentage of debt assumed by each partner.

Parkway provides management, construction and leasing services for all of the unconsolidated joint ventures except for the Wink-Parkway Partnership, and receives market based fees for these services. The portion of fees earned on unconsolidated joint ventures attributable to Parkway's ownership interest is eliminated in consolidation.

Balance sheet information for the unconsolidated joint ventures is summarized below as of March 31, 2007 and December 31, 2006 (in thousands):

**Balance Sheet Information**

| | March 31, 2007 | | | | | |
|---|---|---|---|---|---|---|
| | **Viad JV** | **Wink Building** | **Jackson JV** | **Rubicon JV** | **Maitland JV** | **Combined Total** |
| **Unconsolidated Joint Ventures (at 100%):** | | | | | | |
| Real Estate, Net | $ - | $ 1,208 | $ 16,345 | $ 67,658 | $ 28,936 | $ 114,147 |
| Other Assets | 318 | 240 | 1,243 | 6,352 | 765 | 8,918 |
| Total Assets | $ 318 | $ 1,448 | $ 17,588 | $ 74,010 | $ 29,701 | $ 123,065 |
| Mortgage Debt (a) | $ - | $ 251 | $ 12,600 | $ 52,000 | $ 18,951 | $ 83,802 |
| Other Liabilities | 12 | 30 | 670 | 1,157 | 507 | 2,376 |
| Partners' and Shareholders' Equity | 306 | 1,167 | 4,318 | 20,853 | 10,243 | 36,887 |
| Total Liabilities & Partners'/Shareholders' Equity | $ 318 | $ 1,448 | $ 17,588 | $ 74,010 | $ 29,701 | $ 123,065 |
| **Parkway's Share of Unconsolidated Joint Ventures** | | | | | | |
| Real Estate, Net | $ - | $ 604 | $ 3,269 | $ 13,532 | $ 5,787 | $ 23,192 |
| Mortgage Debt | $ - | $ 125 | $ 2,520 | $ 7,200 | $ - | $ 9,845 |
| Investment in Joint Ventures | $ - | $ 584 | $ (171) | $ 5,551 | $ 5,123 | $ 11,087 |

| | December 31, 2006 | | | | | |
|---|---|---|---|---|---|---|
| | **Viad JV** | **Wink Building** | **Jackson JV** | **Rubicon JV** | **Maitland JV** | **Combined Total** |
| **Unconsolidated Joint Ventures (at 100%):** | | | | | | |
| Real Estate, Net | $ - | $ 1,214 | $ 16,431 | $ 68,053 | $ 28,980 | $ 114,678 |
| Other Assets | 190 | 256 | 1,083 | 6,355 | 663 | 8,547 |
| Total Assets | $ 190 | $ 1,470 | $ 17,514 | $ 74,408 | $ 29,643 | $ 123,225 |
| Mortgage Debt (a) | $ - | $ 275 | $ 12,600 | $ 52,000 | $ 19,061 | $ 83,936 |
| Other Liabilities | 26 | 113 | 493 | 1,333 | 489 | 2,454 |
| Partners' and Shareholders' Equity | 164 | 1,082 | 4,421 | 21,075 | 10,093 | 36,835 |
| Total Liabilities & Partners'/Shareholders' Equity | $ 190 | $ 1,470 | $ 17,514 | $ 74,408 | $ 29,643 | $ 123,225 |
| **Parkway's Share of Unconsolidated Joint Ventures** | | | | | | |
| Real Estate, Net | $ - | $ 607 | $ 3,286 | $ 13,611 | $ 5,796 | $ 23,300 |
| Mortgage Debt | $ - | $ 137 | $ 2,520 | $ 7,200 | $ - | $ 9,857 |
| Investment in Joint Ventures | $ - | $ 541 | $ (150) | $ 5,676 | $ 5,112 | $ 11,179 |

(a) The mortgage debt, all of which is non-recourse, is collateralized by the individual real estate properties within each venture.

In most cases the Company's share of debt related to its unconsolidated joint ventures is the same as its ownership percentage in the venture. However, in the case of the Rubicon Joint Venture and Maitland Joint Venture, the Company's share of debt is disproportionate to its ownership percentage. The disproportionate debt structure was created to meet the Company's partner's financing criteria. In the Rubicon Joint Venture, Parkway owns a 20% interest in the venture but assumed 13.85% of the debt. In the Maitland Joint Venture, the Company owns a 20% interest in the venture and assumed none of the debt. The terms related to Parkway's share of unconsolidated joint venture mortgage debt are summarized below (in thousands):

| **Joint Venture** | **Type of Debt Service** | **Interest Rate** | **Maturity** | **Parkway's Share of Debt** | **Monthly Debt Service** | **Loan Balance 03/31/07** | **Loan Balance 12/31/06** |
|---|---|---|---|---|---|---|---|
| Wink-Parkway Partnership | Amortizing | 8.625% | 07/01/09 | 50.00% | $ 5 | $ 125 | $ 137 |
| Maitland JV | Amortizing | 4.390% | 06/01/11 | 0.00% | - | - | - |
| Rubicon JV | Interest Only | 4.865% | 01/01/12 | 13.85% | 30 | 7,200 | 7,200 |
| Jackson JV | Interest Only | 5.840% | 07/01/15 | 20.00% | 12 | 2,520 | 2,520 |
| | | | | | $ 47 | $ 9,845 | $ 9,857 |
| **Weighted average interest rate at end of period** | | | | | | 5.162% | 5.167% |

The following table presents Parkway's proportionate share of principal payments due for mortgage debt in unconsolidated joint ventures as of March 31, 2007 (in thousands):

| | **Wink Partnership** | **Jackson JV** | **Rubicon JV** | **Maitland JV** | **Total** |
|---|---|---|---|---|---|
| 2007 (Remaining nine months ) | $ 38 | $ - | $ - | $ - | $ 38 |
| 2008 | 54 | - | - | - | 54 |
| 2009 | 33 | 13 | 100 | - | 146 |
| 2010 | - | 33 | 114 | - | 147 |
| 2011 | - | 35 | 119 | - | 154 |
| Thereafter | - | 2,439 | 6,867 | - | 9,306 |
| | $ 125 | $ 2,520 | $ 7,200 | $ - | $ 9,845 |

Income statement information for the unconsolidated joint ventures is summarized below for the three months ending March 31, 2007 and 2006 (in thousands):

**Results of Operations**

| | Three Months Ended March 31, 2007 | | | | | |
|---|---|---|---|---|---|---|
| | **Viad JV** | **Wink Building** | **Jackson JV** | **Rubicon JV** | **Maitland JV** | **Combined Total** |
| **Unconsolidated Joint Ventures (100%):** | | | | | | |
| Revenues | $ - | $ 114 | $ 680 | $ 2,584 | $ 1,112 | $ 4,490 |
| Operating Expenses | (25) | (16) | (342) | (881) | (381) | (1,645) |
| Net Operating Income | (25) | 98 | 338 | 1,703 | 731 | 2,845 |
| Interest Expense | - | (6) | (184) | (632) | (208) | (1,030) |
| Loan Cost Amortization | - | (1) | (1) | (16) | (3) | (21) |
| Depreciation and Amortization | - | (6) | (140) | (491) | (157) | (794) |
| Income (Loss) Before Gain on Sale of Real Estate | (25) | 85 | 13 | 564 | 363 | 1,000 |
| Gain on Sale of Real Estate | 166 | - | - | - | - | 166 |
| Net Income | $ 141 | $ 85 | $ 13 | $ 564 | $ 363 | $ 1,166 |
| **Parkway's Share of Unconsolidated Joint Ventures:** | | | | | | |
| Income (Loss) Before Gain on Sale of Real Estate | $ (8) | $ 43 | $ 3 | $ 152 | $ 115 | $ 305 |
| Gain on Sale of Real Estate | 50 | - | - | - | - | 50 |
| Net Income | $ 42 | $ 43 | $ 3 | $ 152 | $ 115 | $ 355 |
| Depreciation and Amortization | $ - | $ 3 | $ 28 | $ 98 | $ 32 | $ 161 |
| Property Management Fees | $ - | $ - | $ 58 | $ 70 | $ 34 | $ 162 |
| Interest Expense | $ - | $ 3 | $ 37 | $ 87 | $ - | $ 127 |
| Loan Cost Amortization | $ - | $ 1 | $ - | $ 2 | $ - | $ 3 |
| **Other Supplemental Information:** | | | | | | |
| Distributions from Unconsolidated JVs | $ - | $ - | $ 23 | $ 278 | $ 104 | $ 405 |

| | Three Months Ended March 31, 2006 | | | | | |
|---|---|---|---|---|---|---|
| | **Viad JV** | **Wink Building** | **Jackson JV** | **Rubicon JV** | **Maitland JV** | **Combined Total** |
| **Unconsolidated Joint Ventures (100%):** | | | | | | |
| Revenues | $ 3,264 | $ 76 | $ 660 | $ 2,421 | $ 1,048 | $ 7,469 |
| Operating Expenses | (1,262) | (26) | (358) | (954) | (410) | (3,010) |
| Net Operating Income | 2,002 | 50 | 302 | 1,467 | 638 | 4,459 |
| Interest Expense | (838) | (8) | (184) | (632) | (212) | (1,874) |
| Loan Cost Amortization | (86) | - | (1) | (16) | (3) | (106) |
| Depreciation and Amortization | (495) | (6) | (125) | (412) | (153) | (1,191) |
| Net Income (Loss) | $ 583 | $ 36 | $ (8) | $ 407 | $ 270 | $ 1,288 |
| **Parkway's Share of Unconsolidated Joint Ventures:** | | | | | | |
| Net Income (Loss) | $ 175 | $ 18 | $ (1) | $ 121 | $ 97 | $ 410 |
| Depreciation and Amortization | $ 148 | $ 3 | $ 25 | $ 82 | $ 31 | $ 289 |
| Property Management Fees | $ 237 | $ - | $ 28 | $ 96 | $ 32 | $ 393 |
| Interest Expense | $ 251 | $ 4 | $ 37 | $ 88 | $ - | $ 380 |
| Loan Cost Amortization | $ 26 | $ - | $ - | $ 2 | $ - | $ 28 |
| **Other Supplemental Information:** | | | | | | |
| Distributions from Unconsolidated JVs | $ 162 | $ - | $ 23 | $ 70 | $ 102 | $ 357 |

## (6) Minority Interest – Real Estate Partnerships

The Company has an interest in two joint ventures that are included in its consolidated financial statements. Information relating to these consolidated joint ventures is detailed below.

| Joint Venture Entity | Property Name | Location | Parkway's Ownership % |
|---|---|---|---|
| Parkway Moore, LLC | Moore Building Associates, LP/ Toyota Center | Memphis, TN | 75.025% |
| Parkway Properties Office Fund, LP | BellSouth Building/Centurion Centre | Jacksonville, FL | 25.000% |
| | Maitland 100/555 Winderley | Orlando, FL | |
| | Chatham Centre | Schaumburg, IL | |
| | Renaissance Center | Memphis, TN | |
| | 100 Ashford Center/Peachtree Ridge | Atlanta, GA | |
| | Overlook II | Atlanta, GA | |

Moore Building Associates, LP ("MBALP") was established for the purpose of owning a commercial office building (the Toyota Center in Memphis, Tennessee). In acting as the general partner, Parkway is committed to providing additional funding to meet partnership operating deficits up to an aggregate amount of $1 million. Parkway receives income from MBALP in the form of interest from a construction note receivable, incentive management fees and property management fees. Parkway also receives interest income on a note receivable from Parkway Moore, LLC ("PMLLC"). Any intercompany asset, liability, revenue and expense accounts between Parkway and MBALP and PMLLC have been eliminated.

Parkway serves as the general partner of Parkway Properties Office Fund, LP (the "Fund") and provides asset management, property management, leasing and construction management services to the Fund, for which it is paid market-based fees. Cash distributions from the Fund are made to each joint venture partner based on their percentage of ownership in the Fund. Since Parkway is the sole general partner and has the authority to make major decisions on behalf of the Fund, Parkway is considered to have a controlling interest under GAAP. Accordingly, Parkway is required to include the Fund in its consolidated financial statements.

Minority interest in real estate partnerships represents the other partners' proportionate share of equity in the partnerships discussed above at March 31, 2007. Income is allocated to minority interest based on the weighted average percentage ownership during the year.

## (7) Share Based Compensation

Effective January 1, 2003, the stockholders of the Company approved Parkway's 2003 Equity Incentive Plan (the "2003 Plan") that authorized the grant of up to 200,000 equity based awards to employees of the Company. At present, it is Parkway's intention to grant restricted shares and/or deferred incentive share units instead of stock options. Restricted shares and deferred incentive share units are valued based on the New York Stock Exchange closing market price of Parkway common shares (NYSE ticker symbol, PKY) as of the date of grant.

Compensation expense, including estimated forfeitures, is recognized over the expected vesting period, which is four to seven years from grant date for restricted shares subject to service conditions and four years from grant date for deferred incentive share units. Certain restricted shares have been granted to officers of the Company where vesting is contingent upon achieving the cumulative goals of the GEAR UP Plan, which began January 1, 2006 and ends December 31, 2008. Compensation expense will not be recorded on the shares that vest based on performance conditions until the Company determines that it is probable that the goal will be achieved. Therefore, no expense has been recorded in 2006 and 2007 for these shares.

Compensation expense related to restricted shares and deferred incentive share units of $353,000 and $147,000 was recognized for the three months ending March 31, 2007 and 2006, respectively. Total compensation expense related to nonvested awards subject to service conditions not yet recognized was $5.1 million as of March 31, 2007. The weighted average period over which this expense is expected to be recognized is approximately 3.3 years. Total potential compensation expense associated with shares that vest based on performance conditions is $1.5 million as of March 31, 2007.

Restricted shares and deferred incentive share units are forfeited if an employee leaves the Company before the vesting date. Shares and/or units that are forfeited become available for future grant under the 2003 Plan.

On January 12, 2007, the Board of Directors approved the grant of 35,874 restricted shares to officers of the Company. The shares were valued at $1.9 million and 34,875 shares will vest four years from grant date and 999 shares will vest subject to achievement of the cumulative goals of the GEAR UP Plan, which will end on December 31, 2008.

A summary of the Company's restricted shares and deferred incentive share unit activity for the three months ended March 31, 2007 is as follows:

| | Restricted Shares | Weighted Average Grant-Date Fair Value | Deferred Incentive Share Units | Weighted Average Grant-Date Fair Value |
|---|---|---|---|---|
| Outstanding at December 31, 2006 | 188,500 | $ 38.60 | 18,806 | $ 46.33 |
| Granted | 35,874 | 52.36 | 30 | 52.36 |
| Forfeited | (3,375) | 46.14 | (1,868) | 46.31 |
| Outstanding at March 31, 2007 | 220,999 | $ 40.72 | 16,968 | $ 46.34 |

**(8) Capital and Financing Transactions**

On February 9, 2007, the Fund placed a $31.5 million ten-year non-recourse first mortgage at an interest rate of 5.61% in connection with the 2006 purchase of Overlook II in Atlanta, Georgia. Payments during the mortgage term will be on an interest only basis and the loan matures on March 1, 2017.

On March 1, 2007, the Company paid off the $18 million first mortgage secured by Citrus Center in Orlando, Florida which was previously scheduled to mature on August 1, 2007.

In connection with the 2006 first mortgage placed on One Illinois Center, located at 111 East Wacker Drive in Chicago, Illinois, the Company delivered $11.3 million in letters of credit to satisfy the various escrow requirements made by the lender. The letters of credit expire June 30, 2007. On April 2, 2007, the Company renewed these letters of credit through June 30, 2008 and reduced the carrying amount from $11.3 million to $3 million. The reduction in the letters of credit is due to the Company funding the lender escrow requirements with cash contributions to the escrow accounts.

**(9) Subsequent Events**

On April 30, 2007, the Company reached agreement with an unrelated purchaser and received $2 million in non refundable earnest money for the sale of two wholly-owned buildings located in Knoxville, Tennessee. These properties represent approximately 549,000 rentable square feet. The estimated gross sales proceeds are expected to be approximately $59 million and the sale is scheduled to be completed in the second quarter of 2007.

**(10) Segment Information**

Parkway's primary business is the ownership and operation of office properties. The Company accounts for each office property or groups of related office properties as an individual operating segment. Parkway has aggregated its individual operating segments into a single reporting segment due to the fact that the individual operating segments have similar operating and economic characteristics.

The Company believes that the individual operating segments exhibit similar economic characteristics such as being leased by the square foot, sharing the same primary operating expenses and ancillary revenue opportunities and being cyclical in the economic performance based on current supply and demand conditions. The individual operating segments are also similar in that revenues are derived from the leasing of office space to customers and each office property is managed and operated consistently in accordance with Parkway's standard operating procedures. The range and type of customer uses of our properties is similar throughout our portfolio regardless of location or class of building and the needs and priorities of our customers do not vary from building to building. Therefore, Parkway's management responsibilities do not vary from location to location based on the size of the building, geographic location or class.

The management of the Company evaluates the performance of the reportable office segment based on funds from operations applicable to common shareholders ("FFO"). Management believes that funds from operations available to common shareholders ("FFO") is an appropriate measure of performance for equity REITs and computes this measure in accordance with the National Association of Real Estate Investment Trusts' ("NAREIT") definition of FFO. Funds from operations is defined by NAREIT as net income (computed in accordance with generally accepted accounting principles "GAAP"), excluding gains or losses from sales of property and extraordinary items under GAAP, plus depreciation and amortization, and after adjustments to derive the Company's pro rata share of FFO of consolidated and unconsolidated joint ventures. Further, the Company does not adjust FFO to eliminate the effects of non-recurring charges. The Company believes that FFO is a meaningful supplemental measure of its operating performance because historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time, as reflected through depreciation and amortization expenses. However, since real estate values have historically risen or fallen with market and other conditions, many industry investors and analysts have considered presentation of operating results for real estate companies that use historical cost accounting to be insufficient. Thus, NAREIT created FFO as a supplemental measure of operating performance for real estate investment trusts that excludes historical cost depreciation and amortization, among other items, from net income, as defined by GAAP. The Company believes that the use of FFO, combined with the required GAAP presentations, has been beneficial in improving the understanding of operating results of real estate investment trusts among the investing public and making comparisons of operating results among such companies more meaningful. FFO as reported by Parkway may not be comparable to FFO reported by other REITs that do not define the term in accordance with the current NAREIT definition. Funds from operations do not represent cash generated from operating activities in accordance with accounting principles generally accepted in the United States and is not an indication of cash available to fund cash needs. Funds from operations should not be considered an alternative to net income as an indicator of the Company's operating performance or as an alternative to cash flow as a measure of liquidity.

The following is a reconciliation of FFO and net income available to common stockholders for office properties and total consolidated entities for the three months ending March 31, 2007 and 2006.

| | As of or for the three months ended March 31, 2007 | | | As of or for the three months ended March 31, 2006 | | |
|---|---|---|---|---|---|---|
| | Office & Parking Properties | Unallocated and Other | Consolidated | Office & Parking Properties | Unallocated and Other | Consolidated |
| | (In thousands) | | | (In thousands) | | |
| Property operating revenues (a) | $ 61,538 | $ - | $ 61,538 | $ 48,661 | $ - | $ 48,661 |
| Property operating expenses (b) | (28,234) | - | (28,234) | (23,629) | - | (23,629) |
| Property net operating income from continuing operations | 33,304 | - | 33,304 | 25,032 | - | 25,032 |
| Management company income | - | 333 | 333 | - | 362 | 362 |
| Interest and other income | - | 146 | 146 | - | 19 | 19 |
| Interest expense (c) | (10,508) | (2,576) | (13,084) | (7,157) | (2,269) | (9,426) |
| Management company expenses | - | (268) | (268) | - | (375) | (375) |
| General and administrative expenses | - | (1,645) | (1,645) | - | (1,146) | (1,146) |
| Other expense | - | (1) | (1) | - | (1) | (1) |
| Equity in earnings of unconsolidated joint ventures | 305 | - | 305 | 410 | - | 410 |
| Adjustment for depreciation and amortization - unconsolidated joint ventures | 161 | - | 161 | 289 | - | 289 |
| Adjustment for depreciation and amortization - discontinued operations | - | - | - | 200 | - | 200 |
| Adjustment for minority interest - real estate partnerships | (1,920) | - | (1,920) | (330) | - | (330) |
| Income from discontinued operations | 28 | - | 28 | 312 | - | 312 |
| Gain on non depreciable assets | 50 | - | 50 | - | - | - |
| Dividends on preferred stock | - | (1,200) | (1,200) | - | (1,200) | (1,200) |
| Dividends on convertible preferred stock | - | - | - | - | (587) | (587) |
| Funds from operations available to common stockholders | 21,420 | (5,211) | 16,209 | 18,756 | (5,197) | 13,559 |
| Depreciation and amortization | (19,211) | - | (19,211) | (13,526) | - | (13,526) |
| Depreciation and amortization - unconsolidated joint ventures | (161) | - | (161) | (289) | - | (289) |
| Depreciation and amortization - discontinued operations | - | - | - | (200) | - | (200) |
| Depreciation and amortization - minority interest - real estate partnerships | 2,391 | - | 2,391 | 410 | - | 410 |
| Net income (loss) available to common stockholders | $ 4,439 | $ (5,211) | $ (772) | $ 5,151 | $ (5,197) | $ (46) |
| Total assets | $ 1,494,761 | $ 8,185 | $ 1,502,946 | $ 1,174,327 | $ 6,183 | $ 1,180,510 |
| Office and parking properties | $ 1,301,174 | $ - | $ 1,301,174 | $ 1,033,958 | $ - | $ 1,033,958 |
| Investment in unconsolidated joint ventures | $ 11,087 | $ - | $ 11,087 | $ 12,995 | $ - | $ 12,995 |
| Capital expenditures | $ 6,364 | $ - | $ 6,364 | $ 7,310 | $ - | $ 7,310 |

(a) Included in property operating revenues are rental revenues, customer reimbursements, parking income and other income.

(b) Included in property operating expenses are real estate taxes, insurance, contract services, repairs and maintenance and property operating expenses.

(c) Interest expense for office properties represents interest expense on property secured mortgage debt and interest on subsidiary redeemable preferred membership interests. It does not include interest expense on the unsecured lines of credit, which is included in “Unallocated and Other”.

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

### Overview

Parkway is a self-administered and self-managed REIT specializing in the acquisition, operations, leasing and ownership of office properties. The Company is geographically focused on the Southeastern and Southwestern United States and Chicago. As of April 1, 2007 Parkway owned or had an interest in 66 office properties located in 11 states with an aggregate of approximately 13.3 million square feet of leasable space. Included in the portfolio are 17 properties totaling 2.5 million square feet that are owned jointly with other investors, representing 19% of the portfolio. Under the Company's GEAR UP Plan, which started January 1, 2006 and ends December 31, 2008, it is the Company's goal to transform its strategy from being an owner-operator to being an operator-owner. The strategy highlights the Company's strength in providing excellent service in the operation of office properties in addition to its direct ownership of real estate assets. Fee-based real estate services are offered through the Company's wholly owned subsidiary, Parkway Realty Services LLC, which also manages and/or leases approximately 1.2 million square feet for third party owners as of April 1, 2007. The Company generates revenue primarily by leasing office space to its customers and providing management and leasing services to third party office property owners (including joint venture interests). The primary drivers behind Parkway's revenues are occupancy, rental rates and customer retention.

*Occupancy*. Parkway's revenues are dependent on the occupancy of its office buildings. As a result of job losses and over supply of office properties during 2001 through 2003, vacancy rates increased nationally and in Parkway's markets. In 2004, the office sector began to recover from high vacancy rates due to improving job creation. As of April 1, 2007, occupancy of Parkway's office portfolio was 90.9% compared to 90.8% as of January 1, 2007 and 89.4% as of April 1, 2006. Not included in the April 1, 2007 occupancy rate are 24 signed leases totaling 147,000 square feet, which commence during the second through third quarters of 2007 and will raise Parkway's percentage leased to 92%. To combat rising vacancy, Parkway utilizes innovative approaches to produce new leases. These include the Broker Bill of Rights, a short-form service agreement and customer advocacy programs which are models in the industry and have helped the Company maintain occupancy around 91% during a time when the national occupancy rate is approximately 87%. Parkway projects occupancy ranging from 91% to 94% during 2007 for its office properties.

*Rental Rates*. An increase in vacancy rates has the effect of reducing market rental rates and vice versa. Parkway's leases typically have three to seven year terms. As leases expire, the Company replaces the existing leases with new leases at the current market rental rate.

*Customer Retention*. Keeping existing customers is important as high customer retention leads to increased occupancy, less downtime between leases, and reduced leasing costs. Parkway estimates that it costs five to six times more to replace an existing customer with a new one than to retain the customer. In making this estimate, Parkway takes into account the sum of revenue lost during downtime on the space plus leasing costs, which rise as market vacancies increase. Therefore, Parkway focuses a great deal of energy on customer retention. Parkway's operating philosophy is based on the premise that it is in the customer retention business. Parkway seeks to retain its customers by continually focusing on operations at its office properties. The Company believes in providing superior customer service; hiring, training, retaining and empowering each employee; and creating an environment of open communication both internally and externally with customers and stockholders. Over the past ten years, Parkway maintained an average 73.7% customer retention rate. Parkway's customer retention for the quarter ending March 31, 2007 was 52.4% compared to 76% for the quarter ending December 31, 2006 and 77.4% for the quarter ending March 31, 2006. The primary driver of the decrease in customer retention for the quarter ending March 31, 2007 is the loss of a 100,000 square foot customer in Richmond, Virginia, and we anticipate that the annual customer retention rate for 2007 will be in the range of 70% to 75%.

*Strategic Planning*. Management continues to see Parkway defined as a focused office REIT with a hands-on, service-oriented approach, a disciplined asset allocation program and a willingness to recycle assets. However, management sees the future transformation taking Parkway from being an owner-operator to being an operator-owner. On January 1, 2006, the Company initiated a new three-year operating plan referred to as the "GEAR UP" Plan that will serve as the spring board to transform Parkway from being first an owner of real estate and secondarily an operator of real estate for others to being first an operator of real estate for others that also owns an interest in the real estate. The goals of the GEAR UP Plan are as follows:

- ***Great People***. Great customer service starts with hiring great people, training them well and retaining them. It will take great people to accomplish the ambitious goals of the Plan.

- ***Equity Opportunities***. Over the last several years management has created a broad array of equity opportunities for Parkway. On the private equity side this includes the use of discretionary funds, such as the Fund with Ohio PERS, and partnerships. The judicious use of private equity provides a greater return on equity to the public shareholders. Parkway intends to contribute assets from its balance sheet to form new joint ventures and expects these subsequent ventures to be similar to discretionary funds in their duration and economics. On the public equity side, this includes the judicious use of common equity and preferred equity to manage the balance sheet and growth.

- ***Asset Recycling***. The Company has demonstrated its willingness in the past to sell assets when management believed the time was right. At the start of the GEAR UP Plan, Parkway identified 25 buildings in twelve markets, totaling approximately 5 million rentable square feet to be part of the asset recycling program. Most of these properties are smaller assets or located in smaller markets that do not fit with the Company strategy of owning larger assets in institutional markets. The dispositions that are planned will help align the Company's portfolio with its current acquisition criteria, which focuses on larger properties in institutional markets. In most cases, Parkway will seek to keep a 10% to 30% joint venture interest in the properties being recycled and retain management and leasing agreements. This is a fluid list of assets based on the Company's evaluation of specific market conditions and review of the portfolio. The other side of Asset Recycling is the reinvestment of proceeds from dispositions into other assets, either owned in the fee-simple format or owned jointly with a partner.

These two goals, ***Equity Opportunities*** and ***Asset Recycling***, are what combine to transform Parkway from being an owner-operator to being an operator-owner. Management strongly believes that these actions will result in Parkway better leveraging its core strength of operating office properties and will be advantageous for the Company's shareholders over the long term.

- ***Retain Customers***. Customer retention remains the cornerstone of the Company's business and is why partners choose to partner with Parkway. The goal is a customer retention rate of 70% to 75%. The average customer retention rate since the inception of the GEAR UP Plan on January 1, 2006 is 68%, and we anticipate that the annual customer retention rate for 2007 will be in the range of 70% to 75%.

- ***Uncompromising Focus on Operations***. Parkway is reaffirming its commitment to do that which it does best, and that is to operate office properties for maximum returns.

- ***Performance***. In the planning process, management first decided what actions to take strategically over the three years of the GEAR UP Plan and secondly, modeled the economic impact of these actions. Given the large component of Asset Recycling in the Plan, management selected a financial metric that would be most appropriate to measure the success of the Plan. This led to the adoption of Cumulative Adjusted Funds Available for Distribution ("Cumulative Adjusted FAD") as the metric for the GEAR UP Plan, with a target of $7.18 per share cumulative over three years. Actual Adjusted FAD for 2006 exceeded the amount projected by the Company by $.29 per diluted share. Additionally, Parkway established a self-imposed limit for the modified fixed charge coverage ratio of 2.5 times as a pledge not to use leverage to achieve Company goals.

For the GEAR UP Plan Parkway is not abandoning Funds from Operations, but rather carrying it a step further to include accountability for capital items and removing the accounting adjustments which are not directly influenced by the operations of its properties. Management believes an Adjusted FAD goal provides an effective alignment with the shareholders by focusing the team on maximizing income from operations while being mindful of capital expenses and ultimately the funds available to cover the dividend. Cumulative Adjusted FAD is calculated as the sum of Adjusted FAD for each of the three years of the plan. The adjustments that will be made to FAD reported each quarter principally include charges for impairment of value and expenses related to the early extinguishment of debt.

Parkway has made progress on its ***Asset Recycling*** and ***Equity Opportunities*** goals in 2006 as follows:

- *Dispositions*. Parkway sold eight office properties for a gross sales price totaling $94.8 million and recorded a total gain on the sales for financial reporting purposes in the amount of $22.8 million.

- *Fund Acquisitions*. The Fund with Ohio PERS purchased seven office properties at an aggregate contract purchase price of $183.7 million.

- *Fee Simple Purchases*. Parkway purchased One Illinois Center in Chicago, Illinois at a contract purchase price of $198 million.

- *Other Purchases*. Parkway purchased an additional interest in Moore Building Associates, LP, which owns the Toyota Center in Memphis, Tennessee, for $1.4 million raising Parkway's total ownership interest to 75.025%.

- *Equity Offering*. On December 18, 2006, the Company sold 600,000 shares of common stock to Banc of America Securities LLC at a gross offering price of $50.25 per share and a net price of $49.37 per share. The Company used the net proceeds of approximately $29.6 million to repay indebtedness outstanding under a $19.3 million mezzanine loan incurred in connection with the purchase of One Illinois Center and to purchase additional investments in office properties.

In accordance with the GEAR UP Plan, the Company projects the following acquisitions and dispositions in 2007.

- Fee simple office property purchases totaling approximately $150 million;

- Fund office property purchases totaling approximately $170 million;

- Contributions of assets to funds or similar ventures where the Company will retain a 25% ownership interest are projected to be made as shown below:

    - Assets in Knoxville, Tennessee totaling 549,000 square feet with an estimated value of $59 million in the second quarter of 2007;

    - Assets in Virginia totaling 883,000 square feet with an estimated value of $97 million in the third quarter of 2007;

    - Three assets in Columbia, South Carolina totaling 867,000 square feet with an estimated value of $106 million in the fourth quarter of 2007; and

    - In connection with the proposed ventures, Parkway may incur debt prepayment penalties and expense of approximately $2.8 million.

*Discretionary Fund*. On July 6, 2005, Parkway, through affiliated entities, entered into a limited partnership agreement forming a $500 million discretionary fund with Ohio PERS for the purpose of acquiring high-quality multi-tenant office properties. Ohio PERS is a 75% investor and Parkway is a 25% investor in the Fund, which will be capitalized with approximately $200 million of equity capital and $300 million of non-recourse, fixed-rate first mortgage debt. The Fund targets acquisitions in the existing core Parkway markets of Memphis, Houston, Phoenix, Atlanta, Chicago, Charlotte, Orlando, Tampa/St. Petersburg, Ft. Lauderdale and Jacksonville. There is approximately $275 million remaining capacity for Fund office investments. The remaining office investments are expected to be funded by approximately $165 million in mortgage debt and $110 million in equity contributions from partners.

The Fund targets properties with an anticipated cash on cash return greater than 7% and an anticipated leveraged internal rate of return of greater than 11%. Parkway serves as the general partner of the Fund and provides asset management, property management, leasing and construction management services to the Fund, for which it will be paid market-based fees. After each partner has received a 10% annual cumulative preferred return and a return of invested capital, 20% of the excess cash flow will be paid to the general partner and 80% will be paid to the limited partners. Through its general partner and limited partner ownership interests, Parkway may receive a distribution of the cash flow equivalent to 40%. Parkway will have three years from the inception date of the Fund to identify and acquire properties (the "Commitment Period"), with funds contributed as needed to close acquisitions. Parkway will exclusively represent the Fund in making acquisitions within the target markets and within certain predefined criteria. Parkway will not be prohibited from making fee-simple or joint venture acquisitions in markets outside of the target markets, acquiring properties within the target markets that do not meet the Fund's specific criteria or selling or joint venturing any currently owned properties. The term of the Fund will be seven years from the expiration of the Commitment Period, with provisions to extend the term for two additional one-year periods.

**Financial Condition**

***Comments are for the balance sheet dated March 31, 2007 compared to the balance sheet dated December 31, 2006.***

*Office and Parking Properties.* In 2007, Parkway continued the application of its strategy of operating and acquiring office properties, joint venturing interests in office assets, as well as liquidating non-core assets and office assets that no longer meet the Company's investment criteria and/or the Company has determined value will be maximized by selling. During the three months ending March 31, 2007, total assets decreased $9.4 million or .6% and office and parking properties (before depreciation) increased $8.9 million or .6%.

*Purchases and Improvements*. Parkway's investment in office and parking properties decreased $5.1 million net of depreciation to a carrying amount of $1.3 billion at March 31, 2007, and consisted of 60 office and parking properties. The primary reason for the decrease in office and parking properties relates to the net effect of the purchase of land, building improvements and depreciation recorded during the quarter.

On February 28, 2007, the Company purchased 2.5 acres of land in Jackson, Mississippi for $1.8 million. This land was purchased as part of the Company's plan to develop the 194,000 square foot Class A+ office building known as The Pinnacle at Jackson Place ("The Pinnacle"), adjacent to the Company's headquarters building. The estimated cost of the development is $42.5 million with expected completion in the fall of 2008. The Company has received commitments to lease approximately 72% of the new office space from four major customers. Parkway will be seeking partners for an 80% ownership interest in the development. The development is designed to utilize benefits available under the Gulf Opportunity Zone Act for new developments in areas affected by Hurricane Katrina. There can be no assurance that the development or joint venture of The Pinnacle will occur.

During the three months ending March 31, 2007, the Company capitalized building improvements and additional purchase expenses of $5.8 million and recorded depreciation expense of $14.5 million related to its office and parking properties.

*Rents Receivable and Other Assets.* Rents receivable and other assets decreased $4 million or 3.7% for the three months ended March 31, 2007. The decrease is primarily attributable to the decrease in escrow bank account balances of $4.4 million, which was caused by the release of funds in connection with expenditures incurred in leasing office properties and payment of property taxes.

*Intangible Assets, Net.* For the three months ended March 31, 2007, intangible assets net of related amortization decreased $4.1 million and was primarily due to the amortization of the existing intangible assets for the period.

*Notes Payable to Banks.* Notes payable to banks increased $19.7 million or 13% during the three months ended March 31, 2007. At March 31, 2007, notes payable to banks totaled $172 million and the increase is primarily attributable to advances under bank lines of credit to purchase land, make improvements to office properties and retire existing mortgage debt.

*Mortgage Notes Payable.* During the three months ended March 31, 2007, mortgage notes payable increased $9.4 million or 1.4% and is due to scheduled principal payments on mortgages of $4.1 million, the prepayment of existing mortgage debt of $18 million and the placement of mortgage debt of $31.5 million described below.

On February 9, 2007, the Fund with Ohio PERS, of which Parkway owns 25%, placed a $31.5 million ten-year non-recourse first mortgage with an interest rate of 5.61% in connection with the 2006 purchase of Overlook II in Atlanta, Georgia. Payments during the mortgage term will be on an interest only basis and the loan matures on March 1, 2017.

The Company expects to continue seeking fixed-rate, non-recourse mortgage financing with maturities from five to ten years typically amortizing over 25 to 30 years on select office building investments as additional capital is needed. The Company targets a debt to total market capitalization rate at a percentage in the range of 45% to 50%. This rate may vary at times pending acquisitions, sales and/or equity offerings. In addition, volatility in the price of the Company's common stock may affect the debt to total market capitalization ratio. However, over time the Company plans to maintain a percentage in the range of 45% to 50%. The Company calculates this ratio by including its proportionate share of any debt on assets held in funds and partnerships. In addition to this debt ratio, the Company monitors interest, fixed charge and modified fixed charge coverage ratios. The interest coverage ratio is computed by comparing the cash interest accrued to earnings before interest, taxes, depreciation and amortization ("EBITDA"). The fixed charge coverage ratio is computed by comparing the cash interest accrued, principal payments made on mortgage loans and preferred dividends paid to EBITDA. The modified fixed charge coverage ratio is computed by comparing cash interest accrued and preferred dividends paid to EBITDA. In accordance with the GEAR UP Plan, Parkway has established a self-imposed limit for the modified fixed charge coverage ratio of 2.5 times as the Company's pledge not to use leverage to achieve Company goals. Management believes the debt to market capitalization, interest coverage, fixed charge coverage and modified fixed charge coverage ratios provide useful information on total debt levels as well as the Company's ability to cover interest, principal and/or preferred dividend payments with current income.

The computation of the interest, fixed charge and modified fixed charge coverage ratios and the reconciliation of net income to EBITDA is as follows for the three months ended March 31, 2007 and 2006 (in thousands):

| | Three Months Ended March 31 | |
|---|---|---|
| | **2007** | **2006** |
| **Net Income** | $ 428 | $ 1,741 |
| **Adjustments to Net Income:** | | |
| Interest expense | 12,915 | 9,144 |
| Amortization of financing costs | 293 | 282 |
| Write off of debt premium assumed on mortgage note payable | (124) | - |
| Depreciation and amortization | 19,211 | 13,726 |
| Amortization of share based compensation | 353 | 147 |
| Gain on real estate | (50) | - |
| Tax expense | 13 | - |
| EBITDA adjustments - unconsolidated joint ventures | 291 | 697 |
| EBITDA adjustments - minority interest in real estate partnerships | (3,629) | (782) |
| **EBITDA (1)** | $ 29,701 | $ 24,955 |
| | | |
| **Interest Coverage Ratio:** | | |
| EBITDA | $ 29,701 | $ 24,955 |
| Interest expense: | | |
| Interest expense | $ 12,915 | $ 9,144 |
| Interest expense - unconsolidated joint ventures | 127 | 380 |
| Interest expense - minority interest in real estate partnerships | (1,203) | (360) |
| Total interest expense | $ 11,839 | $ 9,164 |
| **Interest Coverage Ratio** | 2.51 | 2.72 |
| | | |
| **Fixed Charge Coverage Ratio:** | | |
| EBITDA | $ 29,701 | $ 24,955 |
| Fixed charges: | | |
| Interest expense | $ 11,839 | $ 9,164 |
| Preferred dividends | 1,200 | 1,787 |
| Principal payments (excluding early extinguishment of debt) | 4,051 | 3,594 |
| Principal payments - unconsolidated joint ventures | 12 | 11 |
| Principal payments - minority interest in real estate partnerships | (65) | (118) |
| Total fixed charges | $ 17,037 | $ 14,438 |
| **Fixed Charge Coverage Ratio** | 1.74 | 1.73 |
| | | |
| **Modified Fixed Charge Coverage Ratio:** | | |
| EBITDA | $ 29,701 | $ 24,955 |
| Modified Fixed Charges: | | |
| Interest expense | $ 11,839 | $ 9,164 |
| Preferred dividends | 1,200 | 1,787 |
| Total Modified Fixed Charges | $ 13,039 | $ 10,951 |
| **Modified Fixed Charge Coverage Ratio** | 2.28 | 2.28 |

(1) Parkway defines EBITDA, a non-GAAP financial measure, as net income before interest, income taxes, depreciation, amortization, losses on early extinguishment of debt and other gains and losses. EBITDA, as calculated by us, is not comparable to EBITDA reported by other REITs that do not define EBITDA exactly as we do.

The Company believes that EBITDA helps investors and Parkway's management analyze the Company's ability to service debt and pay cash distributions. However, the material limitations associated with using EBITDA as a non-GAAP financial measure compared to cash flows provided by operating, investing and financing activities are that EBITDA does not reflect the Company's historical cash expenditures or future cash requirements for working capital, capital expenditures or the cash required to make interest and principal payments on the Company's outstanding debt. Although EBITDA has limitations as an analytical tool, the Company compensates for the limitations by only using EBITDA to supplement GAAP financial measures. Additionally, the Company believes that investors should consider EBITDA in conjunction with net income and the other required GAAP measures of its performance and liquidity to improve their understanding of Parkway's operating results and liquidity.

Parkway views EBITDA primarily as a liquidity measure and, as such, the GAAP financial measure most directly comparable to it is cash flows provided by operating activities. Because EBITDA is not a measure of financial performance calculated in accordance with GAAP, it should not be considered in isolation or as a substitute for operating income, net income, cash flows provided by operating, investing and financing activities prepared in accordance with GAAP. The following table reconciles EBITDA to cash flows provided by operating activities for the three months ended March 31, 2007 and 2006 (in thousands):

| | **Three Months Ended March 31** | |
|---|---|---|
| | **2007** | **2006** |
| EBITDA | $ 29,701 | $ 24,955 |
| Amortization of above market leases | 352 | 409 |
| Operating distributions from unconsolidated joint ventures | 405 | 357 |
| Interest expense | (12,915) | (9,144) |
| Write off of debt premium assumed on mortgage note payable | 124 | - |
| Tax expense | (13) | - |
| Decrease in receivables and other assets | 2,226 | 2,907 |
| Decrease in accounts payable and other liabilities | (7,374) | (6,153) |
| Adjustments for minority interests | 3,158 | 702 |
| Adjustments for unconsolidated joint ventures | (596) | (1,107) |
| Cash flows provided by operating activities | $ 15,068 | $ 12,926 |

*Accounts Payable and Other Liabilities.* Accounts payable and other liabilities decreased $7.3 million or 10.1% for the three months ended March 31, 2007 and was primarily due to the decrease in accrued property taxes for the period in the amount of $6.9 million as a result of property tax payments.

*Minority Interest – Real Estate Partnerships.* During the three months ending March 31, 2007, minority interest associated with real estate partnerships decreased $23.3 million or 25.8%. The decrease is attributable to the distribution of the minority interest partner's share of the $31.5 million mortgage notes payable placed by the Fund. The minority interest partner's share of mortgage proceeds was $23.6 million.

*Stockholders' Equity.* Stockholders' equity decreased $7.9 million or 1.6% during the three months ended March 31, 2007, as a result of the following (in thousands):

| | **Increase (Decrease)** |
|---|---|
| Net income | $ 428 |
| Change in unrealized loss on equity securities | (4) |
| Change in market value of interest rate swaps | (233) |
| Comprehensive income | 191 |
| Common stock dividends declared | (10,296) |
| Preferred stock dividends declared | (1,200) |
| Exercise of stock options | 2,610 |
| Share based compensation expense | 353 |
| Shares distributed from deferred compensation plan | 135 |
| Shares issued through DRIP Plan | 289 |
| Stock offering issuance costs | (11) |
| | $ (7,929) |

**Results of Operations**

***Comments are for the three months ended March 31, 2007 compared to the three months ended March 31, 2006.***

Net loss available to common stockholders for the three months ended March 31, 2007, was $772,000 ($0.05 per basic common share) as compared to net loss available to common stockholders of $46,000 ($0.00 per basic common share) for the three months ended March 31, 2006.

*Office and Parking Properties.* The analysis below includes changes attributable to same store properties, acquisitions and dispositions of office properties. Same store properties are those that the Company owned for the current and prior year reporting periods, excluding properties classified as discontinued operations. At March 31, 2007, same store properties consisted of 52 properties comprising 10.1 million square feet. Properties acquired in 2006 that do not meet the definition of same store properties consisted of eight properties with 2.2 million square feet.

The following table represents income from office and parking properties for the three months ended March 31, 2007 and 2006 (in thousands):

| | Three Months Ended March 31 | | | |
|---|---|---|---|---|
| | 2007 | 2006 | Increase (Decrease) | % Change |
| Income from office and parking properties: | | | | |
| Same store properties | $ 48,904 | $ 47,478 | $ 1,426 | 3.0% |
| Properties acquired in 2006 | 12,634 | - | 12,634 | 0.0% |
| Properties disposed | - | 1,183 | (1,183) | -100.0% |
| Total income from office and parking properties | $ 61,538 | $ 48,661 | $ 12,877 | 26.5% |

Income from office and parking properties for same store properties increased $1.4 million for the three months ended March 31, 2007 compared to the same period for 2006. The primary reason for the increase is due to an increase in same store occupancy and average rental rates for same store properties for the three months ended March 31, 2007 compared to March 31, 2006. Average same store occupancy was 91.7% and for the three months ended March 31, 2007 compared to 88.8% for the same period of 2006.

The following table represents property operating expenses for the three months ended March 31, 2007 and 2006 (in thousands):

| | Three Months Ended March 31 | | | |
|---|---|---|---|---|
| | 2007 | 2006 | Increase (Decrease) | % Change |
| Property operating expenses: | | | | |
| Same store properties | $ 22,276 | $ 23,026 | $ (750) | -3.3% |
| Properties acquired in 2006 | 5,940 | - | 5,940 | 0.0% |
| Properties disposed | 18 | 603 | (585) | -97.0% |
| Total property operating expenses | $ 28,234 | $ 23,629 | $ 4,605 | 19.5% |

Property operating expenses for same store properties decreased $750,000 for the three months ended March 31, 2007 compared to the same period for 2006. The primary reason for the decrease is due to decreased repair and maintenance expenditures and utilities.

Depreciation and amortization expense attributable to office and parking properties increased $5.7 million for the three months ended March 31, 2007 compared to the same period for 2006 and is due to the increase in the net investment in office and parking properties due to additional purchases and improvements to properties.

*Share Based Compensation Expense*. Effective January 1, 2006, Parkway adopted FASB Statement No. 123R, Share-Based Payment (“FAS 123R”) using the modified-prospective transition method. In the past the Company had granted stock options for a fixed number of shares to employees and directors with an exercise price equal to or above the fair value of the shares at the date of grant. However, no stock options have been granted to employees since 2002 or to directors since 2003. Since 2003, Parkway has elected to grant restricted shares and deferred incentive share units instead of stock options. Therefore, the adoption of FAS 123R has not had a material impact on income from continuing operations, net income, cash flow from operations, cash flow from financing activities or basic and diluted earnings per share.

On January 12, 2007, the Board of Directors approved the grant of 35,874 shares to officers of the Company. The shares were valued at $1.9 million and 34,875 shares will vest four years from grant date and 999 shares will vest subject to achievement of the cumulative goals of the GEAR UP Plan, which will end December 31, 2008. Compensation expense will not be recorded on the shares that vest based on performance conditions until the Company determines that it is probable that the goal will be achieved. Therefore, no expense has been recorded to date for the shares that vest based on achievement of the cumulative goals of the GEAR UP Plan.

Share based compensation expense of $353,000 and $147,000 was recognized for the three months ended March 31, 2007 and 2006, respectively. Total compensation expense related to nonvested awards subject to service conditions not yet recognized was $5.1 million as of March 31, 2007. The weighted average period over which this expense is expected to be recognized is approximately 3.3 years. Total potential compensation expense associated with shares that vest based on performance conditions is $1.5 million as of March 31, 2007.

*General and Administrative Expense*. General and administrative expense increased $499,000 for the three months ended March 31, 2007 compared to the same period of 2006 and is primarily attributable to increased personnel costs and share based compensation expense.

*Interest Expense.* Interest expense, including amortization, increased $3.7 million or 38.8% for the three months ended March 31, 2007 compared to the same period of 2006 and is comprised of the following (in thousands):

| | Three Months Ended March 31 | | | |
|---|---|---|---|---|
| | **2007** | **2006** | **Increase (Decrease)** | **% Change** |
| Interest expense: | | | | |
| Mortgage interest expense | $ 10,250 | $ 6,810 | $ 3,440 | 50.5% |
| Bank line interest expense | 2,480 | 2,149 | 331 | 15.4% |
| Subsidiary redeemable preferred membership interest | 185 | 185 | - | 0.0% |
| Write off of debt premium assumed on mortgage note payable | (124) | - | (124) | 0.0% |
| Mortgage loan cost amortization | 197 | 162 | 35 | 21.6% |
| Bank loan cost amortization | 96 | 120 | (24) | -20.0% |
| Total interest expense | $ 13,084 | $ 9,426 | $ 3,658 | 38.8% |

Mortgage interest expense increased $3.4 million or 50.5% for the three months ended March 31, 2007 compared to the same period for 2006 and is due to the net effect of new loans placed or assumed in 2007 and 2006 and the early extinguishment of a mortgage in 2007. The average interest rate on mortgage notes payable as of March 31, 2007 and 2006 was 5.8 and 5.7%, respectively.

**Liquidity and Capital Resources**

*Statement of Cash Flows.* Cash and cash equivalents were $8.3 million and $4.5 million at March 31, 2007 and December 31, 2006, respectively. Cash flows provided by operating activities for the three months ended March 31, 2007 were $15.1 million compared to $12.9 million for the same period of 2006. The increase in cash flows from operating activities of $2.2 million is primarily attributable to the effect of the timing of receipt of revenues and payment of expenses.

Cash used in investing activities was $8.5 million for the three months ended March 31, 2007 compared to cash used in investing activities of $8.8 million for the same period of 2006. The decrease in cash used in investing activities of $283,000 is primarily due to decreased office property improvements.

Cash used in financing activities was $2.8 million for the three months ended March 31, 2007 compared to cash provided by financing activities of $478,000 for the same period of 2006. The decrease in cash provided by financing activities of $3.2 million is primarily due to the net effect of an early extinguishment of a mortgage note payable in 2007 offset by proceeds received on a mortgage placement in 2007.

*Liquidity.* The Company plans to continue pursuing the acquisition of additional investments that meet the Company's investment criteria and intends to use bank lines of credit, proceeds from the sale of non-core assets and office properties, proceeds from the sale of portions of owned assets through joint ventures, possible sales of securities and cash balances to fund those acquisitions.

The Company's cash flows are exposed to interest rate changes primarily as a result of its lines of credit used to maintain liquidity and fund capital expenditures and expansion of the Company's real estate investment portfolio and operations. The Company's interest rate risk management objective is to limit the impact of interest rate changes on earnings and cash flows and to lower its overall borrowing costs. To achieve its objectives, the Company borrows at fixed rates, but also utilizes a four-year unsecured revolving credit facility, a five-year unsecured term loan and two one-year unsecured lines of credit.

At March 31, 2007, Parkway had a total of $172 million outstanding under a four-year $140 million unsecured revolving credit facility and a five-year $60 million unsecured term loan, both led by Wachovia Bank and syndicated to nine other banks (the "$200 million line"), a $15 million unsecured line of credit with PNC Bank (the "$15 million line") and a $9 million unsecured line of credit with Trustmark National Bank (the "$9 million line"). The weighted average interest rate on unsecured lines of credit was 6.3% and 5.7% at March 31, 2007 and 2006, respectively.

The $200 million line is comprised of a $60 million term loan maturing in April 2011 and a $140 million revolving loan maturing in April 2010. The interest rate on the $200 million line is based on LIBOR plus 80 to 130 basis points depending upon overall Company leverage, with the current rate set at LIBOR plus 130 basis points as of March 31, 2007. The Company pays an annual administration fee of $35,000 and fees on the unused portion of the revolver ranging between 12.5 and 20 basis points based upon overall Company leverage, with the rate set at 12.5 basis points at March 31, 2007.

The Company's $200 million line requires compliance with a number of restrictive financial covenants, including tangible net worth, fixed charge coverage ratio, unencumbered interest coverage ratio, total debt to total asset ratio, secured debt to total asset value ratio, secured recourse debt to total asset value ratio and unencumbered pool restrictions. As of March 31, 2007 the Company was in compliance with these financial covenants.

The $15 million line matures January 29, 2008, is unsecured and is expected to fund the daily cash requirements of the Company's treasury management system. The interest rate on the $15 million line is based on LIBOR plus 80 to 130 basis points, depending upon overall Company leverage, with the current rate set at LIBOR plus 130 basis points as of March 31, 2007. Under the $15 million line, the Company does not pay annual administration fees or fees on the unused portion of the line.

The $9 million line with Trustmark National Bank is interest only, has a current interest rate equal to the 30-day LIBOR rate plus 132.5 basis points and matures December 7, 2007. The proceeds of the loan were used to finance the construction of the City Centre Garage, which was completed in 2005.

To protect against the potential for rapidly rising interest rates, the Company entered into interest rate swap agreements in 2005 and 2004. The Company designated the swaps as hedges of the variable interest rates on the Company's borrowings under the Wachovia unsecured revolving credit facility. Accordingly, changes in the fair value of the swaps are recognized in accumulated other comprehensive income until the hedged item is recognized in earnings. The Company's interest rate hedge contracts as of March 31, 2007 and 2006 are summarized as follows (in thousands):

| Type of Hedge | Notional Amount | Maturity Date | Reference Rate | Fixed Rate | Fair Market Value March 31 2007 | Fair Market Value March 31 2006 |
|---|---|---|---|---|---|---|
| Swap | $40,000 | 06/30/06 | 1-Month LIBOR | 3.530% | $ - | $ 146 |
| Swap | $40,000 | 12/31/08 | 1-Month LIBOR | 4.360% | 371 | 801 |
| Swap | $20,000 | 12/31/08 | 1-Month LIBOR | 4.245% | 227 | 423 |
| | | | | | $ 598 | $ 1,370 |

At March 31, 2007, the Company had $705.4 million in mortgage notes payable with an average interest rate of 5.8% secured by office properties and $172 million drawn under bank lines of credit. Parkway's pro rata share of unconsolidated joint venture debt was $9.8 million with an average interest rate of 5.2% at March 31, 2007. Based on the Company's total market capitalization of approximately $1.7 billion at March 31, 2007 (using the March 31, 2007 closing price of $52.25 per common share), the Company's debt represented approximately 47.4% of its total market capitalization. The Company targets a debt to total market capitalization rate at a percentage in the range of 45% to 50%. This rate may vary at times pending acquisitions, sales and/or equity offerings. In addition, volatility in the price of the Company's common stock may affect the debt to total market capitalization ratio. However, over time the Company plans to maintain a percentage in the range of 45% to 50%.

In addition to the debt to total market capitalization ratio, the Company also monitors interest, fixed charge and modified fixed charge coverage ratios. The interest coverage ratio is computed by comparing the cash interest accrued to earnings before interest, taxes, depreciation and amortization ("EBITDA"). This ratio for the three months ended March 31, 2007 and 2006 was 2.51 and 2.72 times, respectively. The fixed charge coverage ratio is computed by comparing the cash interest accrued, principal payments made on mortgage loans and preferred dividends paid to EBITDA. This ratio for the three months ended March 31, 2007 and 2006 was 1.74 and 1.73 times, respectively. The modified fixed charge coverage ratio is computed by comparing the cash interest accrued and preferred dividends paid to EBITDA. This ratio for the three months ended March 31, 2007 and 2006 was 2.28 times. In accordance with the GEAR UP Plan, Parkway has established a self-imposed limit for the modified fixed charge coverage ratio of 2.5 times as the Company's pledge not to use leverage to achieve Company goals. Management believes the debt to market capitalization, interest coverage, fixed charge coverage and modified fixed charge coverage ratios provide useful information on total debt levels as well as the Company's ability to cover interest, principal and/or preferred dividend payments with current income.

The table below presents the principal payments due and weighted average interest rates for the mortgage notes payable as of March 31, 2007.

| | Average Interest Rate | Mortgage Notes Payable (In thousands) |
|---|---|---|
| 2007* | 5.8% | $ 12,090 |
| 2008 | 5.9% | 57,120 |
| 2009 | 5.9% | 37,471 |
| 2010 | 5.9% | 98,840 |
| 2011 | 6.1% | 113,129 |
| 2012 | 6.1% | 64,437 |
| Thereafter | 6.3% | 322,356 |
| Total | | $ 705,443 |
| | | |
| Fair value at 03/31/07 | | $ 718,832 |

*Remaining nine months

The Company presently has plans to make additional capital improvements at its office properties in 2007 of approximately $39.4 million. These expenses include tenant improvements, capitalized acquisition costs and capitalized building improvements. Approximately $21.8 million of these improvements relate to upgrades on properties acquired in recent years that were anticipated at the time of purchase. All such improvements are expected to be financed by cash flow from the properties, capital expenditure escrow accounts, advances on the bank lines of credit or contributions from partners.

In 2006, the Company announced the proposed development of a 194,000 square foot Class A+ office building in Jackson, Mississippi known as The Pinnacle at Jackson Place, adjacent to the Company's headquarters building. The estimated cost of the development is $42.5 million with expected completion in the fall of 2008. In 2007, the Company expects to incur approximately $7 million in construction costs. The Company has received commitments to lease approximately 72% of the new office space from four major customers. Parkway will be seeking partners for an 80% ownership interest in the development. The development is designed to utilize benefits available under the Gulf Opportunity Zone Act for new developments in areas affected by Hurricane Katrina. There can be no assurance that the development or joint venture of The Pinnacle will occur.

In accordance with Parkway's strategic plan, GEAR UP, the Company projects the following acquisitions and dispositions in 2007. Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations – Overview – Strategic Planning," includes a full discussion of the GEAR UP Plan.

- Fee simple office property purchases totaling approximately $150 million, which will be funded with proceeds from sales and/or bank lines of credit.

- Fund office property purchases totaling approximately $170 million. Parkway's equity contribution will be approximately $17 million and will be funded with proceeds from sales and/or bank lines of credit.

- Contributions of asset to funds or similar ventures where the Company will retain a 25% ownership interest are projected to be made as shown below:

    - Assets in Knoxville, Tennessee totaling 549,000 square feet with an estimated value of $59 million in the second quarter of 2007;

    - Assets in Virginia totaling 883,000 square feet with an estimated value of $97 million in the third quarter of 2007;

    - Three assets in Columbia, South Carolina totaling 867,000 square feet with an estimated value of $106 million in the fourth quarter of 2007; and

    - In connection with the proposed ventures, Parkway may incur debt prepayment penalties and expense of approximately $2.8 million.

The Company anticipates that its current cash balance, operating cash flows and borrowings (including borrowings under the working capital line of credit) will be adequate to pay the Company's (i) operating and administrative expenses, (ii) debt service obligations, (iii) distributions to shareholders, (iv) capital improvements, and (v) normal repair and maintenance expenses at its properties, both in the short and long term. In addition, the Company may use proceeds from sales of assets, possible sales of securities and borrowings to fund property acquisitions.

**Contractual Obligations**

See information appearing under the caption "Financial Condition – Note Payable to Banks and Mortgage Notes Payable" in Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations for a discussion of changes in long-term debt since December 31, 2006.

**Funds From Operations**

Management believes that funds from operations available to common shareholders ("FFO") is an appropriate measure of performance for equity REITs and computes this measure in accordance with the National Association of Real Estate Investment Trusts' ("NAREIT") definition of FFO. Funds from operations is defined by NAREIT as net income (computed in accordance with generally accepted accounting principles "GAAP"), excluding gains or losses from sales of property and extraordinary items under GAAP, plus depreciation and amortization, and after adjustments to derive the Company's pro rata share of FFO of consolidated and unconsolidated joint ventures. Further, the Company does not adjust FFO to eliminate the effects of non-recurring charges. The Company believes that FFO is a meaningful supplemental measure of its operating performance because historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time, as reflected through depreciation and amortization expenses. However, since real estate values have historically risen or fallen with market and other conditions, many industry investors and analysts have considered presentation of operating results for real estate companies that use historical cost accounting to be insufficient. Thus, NAREIT created FFO as a supplemental measure of operating performance for real estate investment trusts that excludes historical cost depreciation and amortization, among other items, from net income, as defined by GAAP. The Company believes that the use of FFO, combined with the required GAAP presentations, has been beneficial in improving the understanding of operating results of real estate investment trusts among the investing public and making comparisons of operating results among such companies more meaningful. FFO as reported by Parkway may not be comparable to FFO reported by other REITs that do not define the term in accordance with the current NAREIT definition. Funds from operations do not represent cash generated from operating activities in accordance with accounting principles generally accepted in the United States and is not an indication of cash available to fund cash needs. Funds from operations should not be considered an alternative to net income as an indicator of the Company's operating performance or as an alternative to cash flow as a measure of liquidity.

The following table presents a reconciliation of the Company's net income to FFO for the three months ended March 31, 2007 and 2006 (in thousands):

| | **Three Months Ended March 31** | |
|---|---|---|
| | **2007** | **2006** |
| Net income | $ 428 | $ 1,741 |
| Adjustments to derive funds from operations: | | |
| Depreciation and amortization | 19,211 | 13,526 |
| Depreciation and amortization – discontinued operations | - | 200 |
| Minority interest depreciation and amortization | (2,391) | (410) |
| Adjustments for unconsolidated joint ventures | 161 | 289 |
| Preferred dividends | (1,200) | (1,200) |
| Convertible preferred dividends | - | (587) |
| Funds from operations applicable to common shareholders | $ 16,209 | $ 13,559 |

**Inflation**

Except for insurance, inflation has not had a significant impact on the Company because of the relatively low inflation rate in the Company's geographic areas of operation. Additionally, most of the leases require the customers to pay their pro rata share of operating expenses, including common area maintenance, real estate taxes, utilities and insurance, thereby reducing the Company's exposure to increases in operating expenses resulting from inflation. The Company's leases typically have three to seven year terms, which may enable the Company to replace existing leases with new leases at market base rent, which may be higher or lower than the existing lease rate.

*Insurance*. Following the devastating hurricanes of 2004 and 2005, the insurance market for properties located in coastal and wind prone areas of the country has been extremely volatile. Following a mild hurricane season in 2006, insurance premiums moderated and the Company renewed its property and casualty insurance policy on April 1, 2007, with an overall decrease in premium cost compared to the previous 16-month policy period. While most individual properties experienced a decline in premium, properties located in coastal or wind prone areas did experience rate increases. Increases or decreases in insurance costs directly related to each property are passed through to customers to the extent allowed by the lease terms. Upon renewal, the deductible for wind damage for properties located in Florida increased from 2% of replacement cost to 5% of replacement cost and for properties located in Harris and Fort Bend County in Texas, deductibles for wind damage increased from 2% to 3% of replacement cost. The new policy will be in effect until April 1, 2008, at which time these lines of coverage will be renewed under market conditions that exist at that time.

**Forward-Looking Statements**

In addition to historical information, certain sections of this Form 10-Q may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, such as those that are not in the present or past tense, that discuss the Company's beliefs, expectations or intentions or those pertaining to the Company's capital resources, profitability and portfolio performance and estimates of market rental rates. Forward-looking statements involve numerous risks and uncertainties. The following factors, among others discussed herein and in the Company's filings under the Securities Exchange Act of 1934, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements: defaults or non-renewal of leases, increased interest rates and operating costs, failure to obtain necessary outside financing, difficulties in identifying properties to acquire and in effecting acquisitions, the failure to acquire or sell properties as and when anticipated, failure to qualify as a real estate investment trust under the Internal Revenue Code of 1986, as amended, environmental uncertainties, risks related to natural disasters, financial market fluctuations, changes in real estate and zoning laws and increases in real property tax rates. The success of the Company also depends upon the trends of the economy, including interest rates, income tax laws, governmental regulation, legislation, population changes and those risk factors discussed elsewhere in this Form 10-Q and in the Company's filings under the Securities Exchange Act of 1934. Readers are cautioned not to place undue reliance on forward-looking statements, which reflect management's analysis only as the date hereof. The Company assumes no obligation to update forward-looking statements.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

See information appearing under the caption "Liquidity" in Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations.

**Item 4. Controls and Procedures**

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that as of the end of the Company's most recent fiscal quarter, the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic SEC filings.

During the period covered by this report, the Company reviewed its internal controls, and there have been no changes in the Company's internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

## PART II. OTHER INFORMATION

**Item 1A. Risk Factors**

There have been no material changes to the risk factors disclosed in Parkway's Form 10-K for the year ended December 31, 2006.

**Item 6. Exhibits**

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

## 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.

**DATE**: May 9, 2007

**PARKWAY PROPERTIES, INC.**

**BY**: /s/ Mandy M. Pope
Mandy M. Pope, CPA
Senior Vice President and
Chief Accounting Officer