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Principal U.S. Property Separate Account

2008 ANNUAL REPORT | sub-advised by PRINCIPAL REAL ESTATE INVESTORS

Background – Philosophy – Objectives 2
Portfolio Highlights 3
Portfolio Manager Commentary 6
Market Aftershocks and the Road to Recovery 8
U.S. Economic Outlook 9
Space Market Fundamentals 10
U.S. Property Separate Account Performance 13
Capital Markets 17
2008 Transaction Activity 18
Independent Auditors' Report 22
Audited Financial Statements 23

Background | Philosophy | Objectives

Principal U.S. Property Separate Account Background

Since 1982, the U.S. Property Separate Account (the Separate Account) has been made available to pension and retirement plan clients of the Principal Financial Group® (The Principal®) by Principal Life Insurance Company, a member company of The Principal.[1] The Separate Account is a comingled insurance company real estate separate account sponsored by Principal Life and managed by Principal Real Estate Investors, LLC. The Separate Account is a diversified real estate equity account consisting primarily of high quality, well-leased real estate properties in the multi-family, industrial, office, retail, and hotel sectors.

Philosophy

The Principal U.S. Property Separate Account is a core real estate separate account designed to have a low to moderate risk profile compared to other open-end real estate funds. This risk profile has two components: 1) a low to moderate real estate property risk profile; and 2) a low to moderate risk fund-level operating profile. Low to moderate real estate property risk is accomplished by investing primarily in well-leased properties on an unleveraged basis. Low to moderate fund level risk is accomplished by operating with a strong focus on client diversification and by managing fund-level obligations.

Objectives

The Principal U.S. Property Separate Account has two primary objectives: 1) to invest in a well-diversified real estate portfolio that reflects the overall performance of the U.S. commercial real estate market; and 2) to provide clients with private real estate returns that meet or exceed over a market cycle a) the open-end fund component of the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index at the property level and b) the NCREIF Fund Index Open-end Diversified Core Equity (NFI-ODCE) at the portfolio level.

1 The Account is available through group annuity contracts issued by Principal Life Insurance Company to plans meeting the requirements for qualification under Section 401(a) of the Internal Revenue Code of 1986 (“Code”), as amended, and governmental plans meeting the requirements of Section 457 of the Code, as amended.

Portfolio Highlights

KEY STATISTICS		DECEMBER 31, 2008	
Inception Date	January, 1982	Number of Investors	over 15,200
Gross Asset Value	$6.9 billion	Institutional Investors > $5M	67
Net Asset Value	$4.9 billion	2008 Client Contributions	$1,247 million
Number of Investments	149	2008 Client Distributions	$1,977 million
Number of Markets	46	Leverage Ratio[1]	26.1%
Size	40.1 million sf	Portfolio Occupancy	82%
Cash to Gross Assets	1.1%	Occupancy Excluding Value-added Properties[2]	90%
Redemption Queue	$837.8 million		

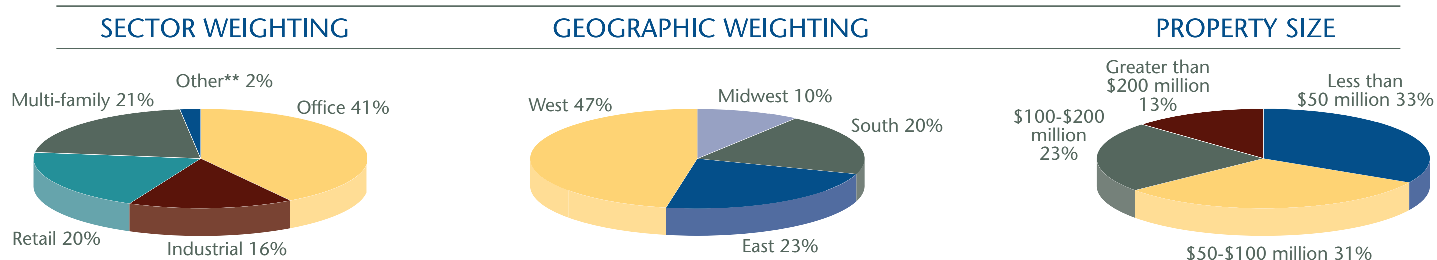
SECTOR	CURRENT ALLOCATION[3]	NCREIF ALLOCATION	TARGET ALLOCATION
Office	41%	38%	30% - 45%
Multi-family	21%	24%	15% - 25%
Retail	20%	21%	10% - 20%
Industrial	16%	15%	15% - 25%
Other (Hotel, Land)	2%	2%	0 % - 4%

PERFORMANCE	GROSS PORTFOLIO[4]	NET PORTFOLIO[5]	PORTFOLIO BENCHMARK[6]	PROPERTY[7]	PROPERTY BENCHMARK[8]
4Q 2008	-10.8%	-11.0%	-11.6%	-8.5%	-8.8%
1 year	-12.2%	-13.2%	-10.3%	-8.9%	-8.0%
3 year	5.5%	4.3%	6.5%	6.6%	6.9%
5 year	9.9%	8.6%	10.4%	10.5%	10.5%
10 year	9.6%	8.4%	9.7%	10.1%	9.6%
Since Inception	8.2%	7.0%	7.8%	8.6%	7.7%

1 Total debt (both property and portfolio) divided by total assets.
2 Value-added properties include those that are acquired at less than 85% occupancy, are under development or include the sale of individual condominium units.
3 Diversification is based upon the Separate Account's gross market value of real estate assets and mortgage loans receivable.
4 Gross portfolio returns are levered and pre-fee.
5 Net portfolio level returns are shown after deduction for fund expenses including the investment management fee, which is 1.15% annually from July 1, 2002 through the present. Net fund level returns prior to July 1, 2002 are calculated to reflect deduction of blended annualized investment management fees of 1.15% and 1.05% in the periods in which those amounts were charged.
6 Gross portfolio performance is benchmarked against the NFI-ODCE Equal Weight.
7 Property returns are unlevered, before fees and calculated in accordance with NCREIF property return methodology.
8 Property level performance is benchmarked against the Open-end Fund Component of the NCREIF Property Index.

Portfolio Diversification*

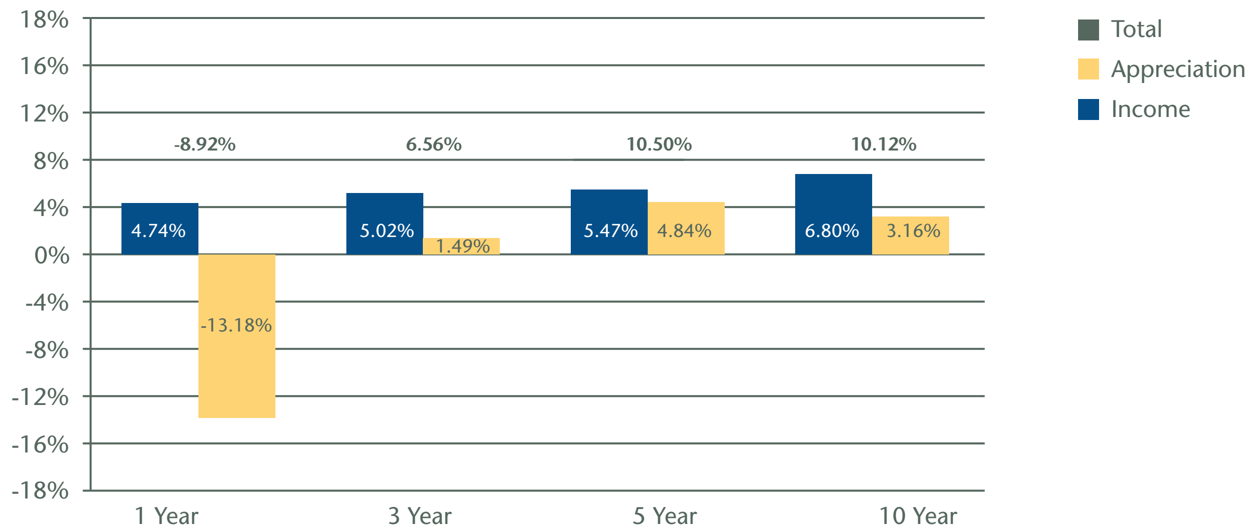
SECTOR WEIGHTING | GEOGRAPHIC WEIGHTING | PROPERTY SIZE



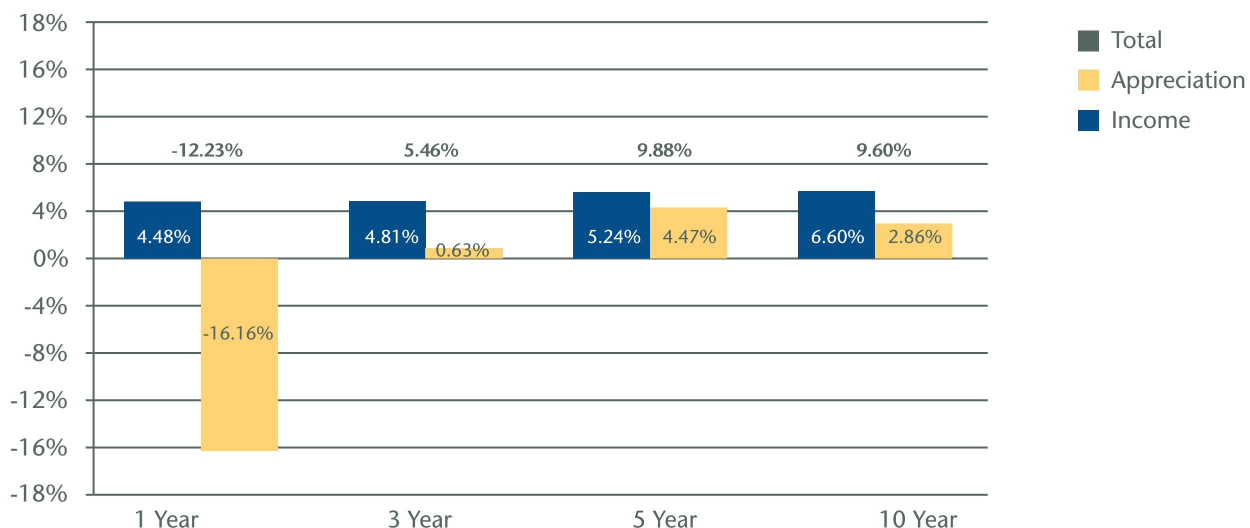
*Diversification is based upon the Separate Account's gross market value of real estate assets and mortgage loan receivable.
**Comprised of hotel and land investments.

Portfolio Highlights

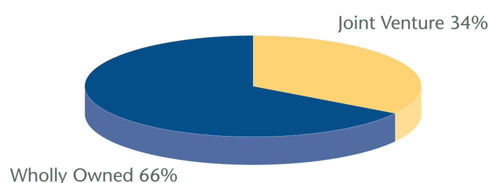
PROPERTY LEVEL RETURNS[1]



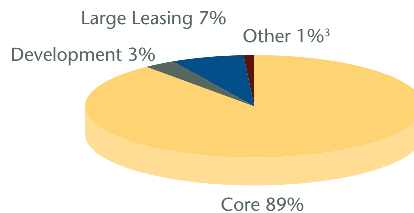
PORTFOLIO LEVEL RETURNS[2]



PROPERTY OWNERSHIP STRUCTURE

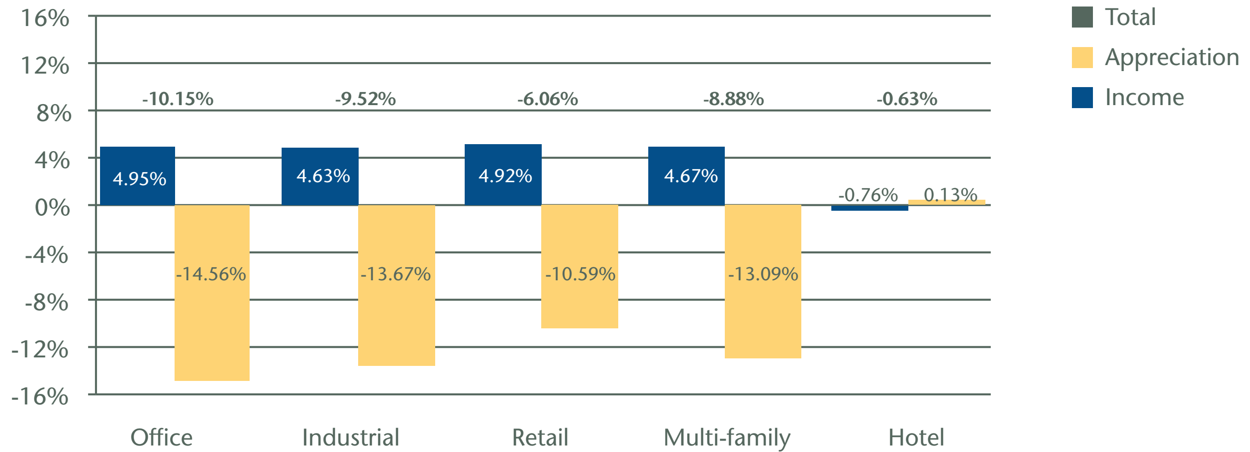


LIFE CYCLE

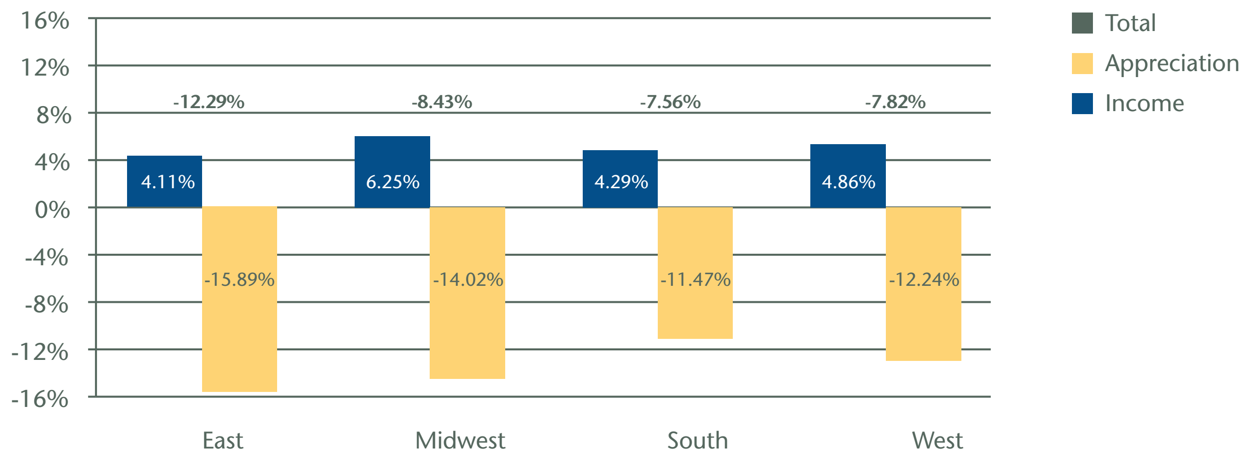


1 Property level returns are unlevered, before fees and calculated in accordance with NCREIF property return methodology.
2 Portfolio level returns are levered and pre-fee.
3 Includes the sale of individual condominium units.

ONE YEAR PERFORMANCE BY PROPERTY SECTOR[1]



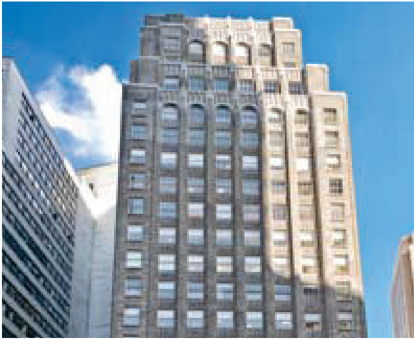
ONE YEAR PERFORMANCE BY GEOGRAPHIC REGION[1]



Ten Largest Investments

INVESTMENT NAME	MSA	SECTOR	OCCUPANCY	% OF GROSS REAL ESTATE ASSETS
333 Market Street	San Francisco, CA	Office	100.0%	5.5%
1370 Avenue of the Americas	New York, NY	Office	99.9%	4.4%
112th at 12th Street	Seattle, WA	Office	95.5%	3.3%
Burbank Empire Center	Los Angeles, CA	Retail	90.4%	2.5%
1412 Broadway	New York, NY	Office	78.2%	2.5%
Portales Corporate Center	Phoenix, AZ	Office	92.1%	2.3%
Watermark	Cambridge, MA	Multi-family/Retail	78.3%	2.1%
Shorewood Heights	Seattle, WA	Multi-family	91.5%	2.0%
Charles Park	Cambridge, MA	Office	82.6%	1.9%
Hazard Center	San Diego, CA	Office/Retail	93.5%	1.9%

1 Property returns are unlevered, before fees and calculated in accordance with NCREIF property return methodology.



Portfolio Manager Commentary

The performance of private real estate equity portfolios relies primarily on two factors – the space markets (the supply and demand for physical space) and the capital markets (investor demand for real estate investments and the supply of capital). Both factors experienced material unfavorable changes in 2008, adversely impacting the performance of real estate portfolios, including the Principal U.S. Property Separate Account. The total return for the separate account in 2008 was -12.2%, the lowest nominal calendar year performance in the history of the separate account. Relative performance in 2008 trailed the NFI-ODCE Equal Weight index return of –10.3%.

The U.S. is enmeshed in a deep recession that began in late 2007, entailing large job losses and tenant credit problems that have contributed to deteriorating space market fundamentals. In particular, tenant demand for space decreased materially as white collar job losses weighed on the office sector, a slowdown in global trade negatively impacted user demand for industrial space, sharply retrenching consumer spending hurt retailers and hotels struggled with a slowdown in both business and leisure travel. Only partially offsetting these adverse developments were an uptick in demand for apartments due to increased home foreclosures and the inability of many renters to finance home purchases and the reasonable overall supply of new commercial property across most property types, particularly when compared to the dramatic overbuilding of the early 1990s. Nevertheless, overall space market fundamentals deteriorated materially in 2008, as reasonably well disciplined supply was more than offset by weakness in demand associated with what will likely be the most severe recession since at least 1982.

Real estate was not immune from the global financial crisis that accelerated in the fourth quarter of 2008. The flight to lower risk assets evidenced by money pouring into Treasury bills and bonds and commensurate low yields was accompanied by a simultaneous move away from assets perceived to have any material downside risk, including real estate. The transition from risk complacency to risk aversion, combined with the negative ramifications of the denominator effect of falling stock prices on real estate allocation metrics, has resulted in decreased demand for property ownership by most investors. This imbalance, as well as a sudden shift in debt markets to much less available and more highly priced capital, is manifesting itself in higher required rates of return by investors for commercial real estate across virtually all property types and geographies. The core nature of the separate account mitigates some of the fallout related to the change in investor sentiment, as most properties in the portfolio are well-leased and at the lower end of the risk spectrum for private real estate investments. Therefore, the separate account has been less impacted by risk aversion relative to strategies focused primarily on value-added or opportunistic investing, because of both the separate account's lower asset risk profile and its lower overall financial leverage.

Several factors, but primarily driven by an elevated level of client redemption requests, led to the first-ever implementation of a client withdrawal queue (the Queue) for the separate account on September 26, 2008. The Queue was implemented for the benefit and protection of all investors in the separate account and is intended to allow for the continued execution of separate account strategy and the orderly generation of cash through separate account activities, including property sales, to redeem investor interests in the Queue, manage debt and meet other separate account obligations. At year-end, the outstanding amount in the Queue was $837.8 million. Investor withdrawal queues have become common in the current market environment, with most U.S. core open-end private equity real estate funds experiencing a client redemption queue at the end of 2008.

Managing both the assets and the liabilities of the separate account with a dual focus on return generation and risk management will remain the primary objective in 2009. Active asset management will be a key to investment performance, with tenant retention, new leasing and expense management comprising areas of significant focus. These are the “blocking and tackling” basics of asset management and Principal Real Estate Investors will continue to concentrate on these fundamentals. In addition, we are committed to navigating the challenging economic, employment and capital market landscape to operate the portfolio in the best interest of all investors and within the separate account’s investment guidelines and debt covenants.

The resources of Principal Real Estate Investors are fully committed to overcoming the challenges of the nearly unprecedented current market conditions. Despite the present environment, core real estate can serve as an important component of a multi-asset class investment portfolio and offers investors diversification and other benefits, given its unique income and appreciation components. While 2008 was clearly a very difficult year for commercial real estate and 2009 will bring additional challenges, the separate account will strive to offer the same long-term benefits it has over the past 27 years. Since its inception in January 1982, the separate account has weathered multiple real estate and economic cycles while generating an annualized total return of 8.2%.

Thank you for your continued support and consideration of the Principal U.S. Property Separate Account.
We look forward to working with you in the future.

John T. Berg
Portfolio Manager

Market Aftershocks and the Road to Recovery

More than a year into the credit crisis, the market has continued to experience multiple and increasingly severe aftershocks. The past year has been characterized by significant levels of government intervention in the capital markets and the economy in an attempt to restore market stability and investor confidence. These initiatives include a return to highly-accommodative monetary policy; plans for a second, much more comprehensive fiscal stimulus package; direct equity infusions into various financial institutions to shore up their capital base and restore lending capacity; and direct intervention in various credit markets to restore confidence and market functionality.

The road to economic recovery will be very challenging, especially given simultaneous weakness in the consumer and business sectors, coupled with the economy's dependency on credit availability as a result of low savings rates. Export activity is expected to continue to support economic growth, but exports are coming under pressure due to the recessionary global economic outlook. As a result, the proposed government fiscal stimulus plan is becoming increasingly critical to reducing the severity and duration of the U.S. recession and providing a catalyst to economic recovery.

Despite the many challenges facing the U.S. and global economy and financial systems, there are reasons for long-term optimism. The U.S. economy remains resilient and will be supported by what is shaping up to be a large, multi-year fiscal stimulus plan. Regulatory infrastructure will have the opportunity to catch up with financial innovation, and thus will be a positive for enhanced stability going forward – so long as the regulatory environment doesn't become overly burdensome or counterproductive. The deleveraging of the financial markets, while extremely disruptive over the near to intermediate term, should be a long-term positive for the resumption of economic growth. While painful, the credit crisis and global economic downturn also has led to the unwinding of several major global imbalances, including the housing price bubble and the commodity bull market, causing a major correction in energy prices and reducing inflationary pressures within the system.

Commentary on pages 8-12 includes excerpts from *Expectations & Market Realities in Real Estate: 2009*, published by Principal Real Estate Investors, CBRE/Torto Wheaton Research and Real Estate Research Corporation and includes updated information through year-end 2008. The full report is available to investors on the Separate account's website or upon request. Opinions and predictions are subject to change and are not intended as a forecast or guarantee of future events, or as a predictor of performance.

U.S. Economic Outlook

The U.S. economy has been confronted with an increasingly weak job market, a stock market crash, a continuing decline in home prices, consumer confidence at an all-time low, extremely volatile energy and food prices, and a credit freeze that has largely brought consumer and business activity to a standstill. Despite the resiliency of the economy, the severity and persistence of the credit crisis and associated market aftershocks have pushed the U.S. into its third, and what will likely be its most severe, recession since 1982.

Despite the severity of the housing market downturn and the financial crisis, U.S. economic growth was supported throughout the first half of 2008 by the business, export and government sectors. Beginning in third quarter, however, the economy began to contract with initial reports of 2008 full year GDP of 1.3%. The drag from housing will likely begin to abate in 2009, if only because new home construction has been driven to such low levels that there is little room for further decline. However, it will take some time before housing makes a material positive contribution to economic growth, given that unsold inventories remain very high. In 2009, the overall economy is expected to continue contracting during the first half of the year before beginning to expand again in the second half, aided by a sizable fiscal stimulus package, resulting in 2009 GDP growth of -1.5% to -2.0%.

The U.S. economy has generated negative payroll employment growth for 12 consecutive months amidst cumulative payroll employment losses of nearly 2.6 million and unemployment rates that have climbed to 7.2%, a 15 year high. The average rate of job losses has already exceeded that of the past two recessions and is still accelerating as weakness spreads across more employment sectors. Declines in payroll employment will likely continue through at least mid-2009 as businesses are under increasing pressure to cut expenses.

Consumer spending turned negative in third quarter 2008 for the first time since 1991 and fourth quarter holiday sales were extremely weak (down 3.5%). The consumer sector will likely continue to be a significant drag on economic growth through 2009, and it is conceivable that real personal consumption will experience its steepest decline in several decades.

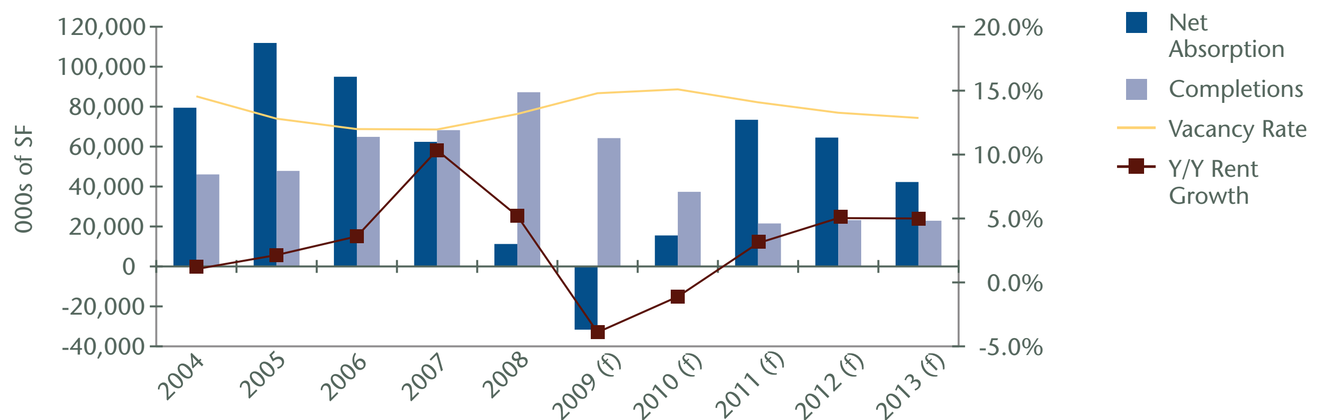
U.S. ECONOMIC ACTIVITY

Space Market Fundamentals

Despite reasonably well-controlled new supply in recent years, space market fundamentals are weakening across all property types, primarily as a result of declining demand as consumers and businesses retrench in the face of tremendous economic uncertainty and restrictive capital markets. Rent levels across many property types are expected to decline in the face of diminishing net absorption and the return of rent concessions to the real estate markets.

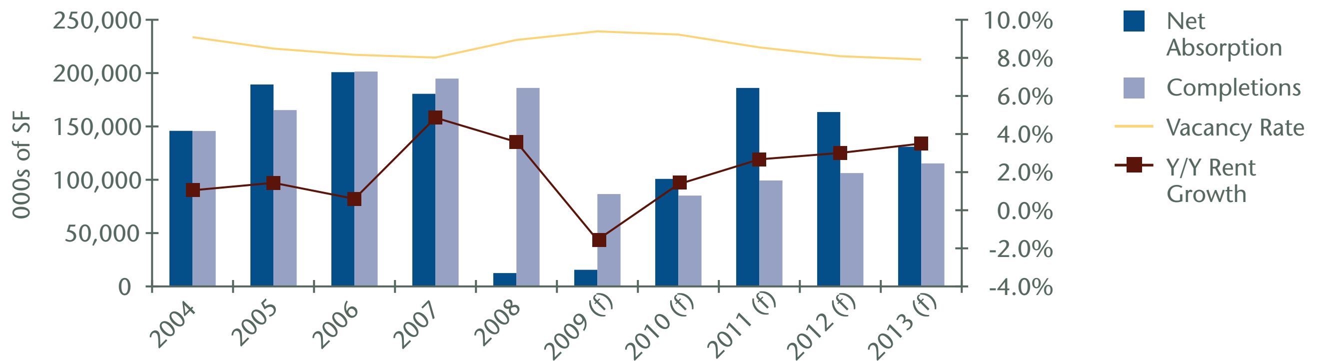
Office properties are likely to see vacancy rates climb into the high teens over the next few years, primarily as a result of the dramatic decline in office-using employment. While these levels represent a marked increase over 2008, vacancy rates are not expected to top the peak level of 19% recorded during the down cycle in the early 1990s. The impact of disproportionate job losses in office-using employment will only be compounded by a moderate supply pipeline anticipated to deliver in the next 18 months. Despite a forecasted return to positive economic growth in the latter half of 2009, the office sector will likely face continued declines in rental rates and negative net absorption throughout 2009 and into 2010, as job growth generally lags economic growth.

OFFICE SPACE MARKET FUNDAMENTALS



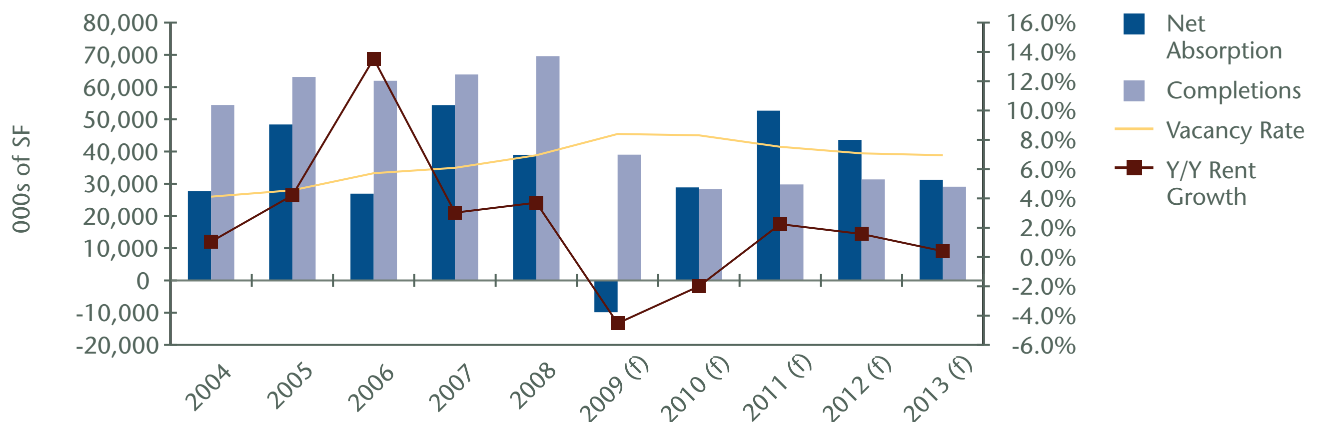
The global recession is expected to have an adverse impact on both global and domestic trade volumes, which combined with sharply-reduced U.S. consumer spending, will cause industrial vacancy rates to also increase materially. The sector began to show signs of weakening during 2008, posting negative net absorption and declines in rent growth beginning during the first half of the year. Job losses in the manufacturing sector were widespread throughout the year and also contributed to the sharp drop in tenant demand. While the long-term outlook for industrial remains favorable due to global trade that will resume post-recession, the near-term outlook may also be stronger than other sectors. The sector is well-positioned relative to other sectors due to a relatively low-leveraged tenant base, inexpensive cost of re-tenanting and its position as a more defensive, less-volatile property type.

INDUSTRIAL SPACE MARKET FUNDAMENTALS



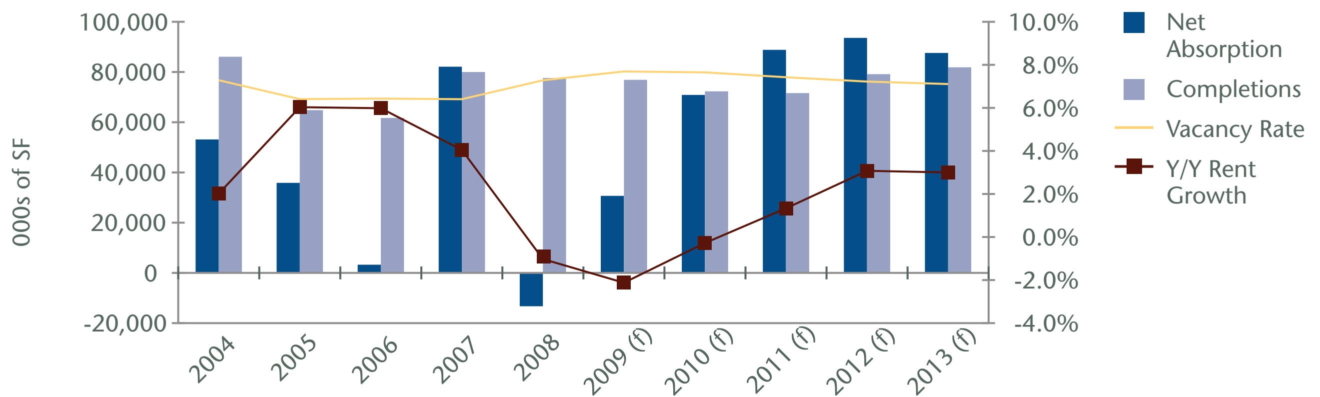
As a collective result of an expected continued contraction in real consumer spending over the next few quarters, an increase in retailer credit defaults and bankruptcies, and the delivery of remaining new supply in the construction pipeline, the retail sector is expected to weaken significantly in the near term. Retail performance was buoyed in recent years by increasing home prices, historically low unemployment rates and unparalleled access to inexpensive debt. Today, those factors which drove consumer spending and as such, retail performance, are the same factors that will result in decreasing rental rates and increasing vacancy rates. The sector is especially vulnerable to tenant credit issues as retailers are forced to close stores and halt expansion plans. The impact of these factors varies widely by region and retail format, although properties located in markets severely impacted by depressed housing prices will likely struggle the most.

RETAIL SPACE MARKET FUNDAMENTALS



Multi-family is the only property type likely to see a potential increase in their tenant universe, as home ownership rates continue to fall amidst tighter credit standards and increasing foreclosures. Even so, the sector is expected to experience a near-term increase in vacancy due to increasing unemployment rates, a near-term moderation in immigration, and renters doubling up or living at home while waiting out the recession. Further, in some markets, the sector will experience increased competition from single-family homes and condominiums for rent. Despite added volatility due to what amounts to the nationalization of the home lending market and continued government intervention, the sector will likely benefit from declining home ownership rates as credit requirements and larger down payments will force some people to rent by necessity.

MULTI-FAMILY SPACE MARKET FUNDAMENTALS



Hotel properties are also expected to encounter significant pressure, with negative RevPar (revenue per available room) growth from 2008 continuing in 2009 amidst falling occupancy rates as businesses aggressively reduce travel expenses and negative consumer spending persists. The sector is not unlike other commercial property types facing mostly demand related challenges: weak business and consumer spending; decreasing levels of tourism as a result of a global recession; and declines in airline capacity have all placed significant negative pressure on the sector. While price corrections and volatility in rates and occupancy will continue throughout 2009, it is likely that barring a prolonged recession, the sector will not experience a downturn of the same magnitude experienced after the terrorist attacks in 2001.

U.S. Property Separate Account Performance

2008 was an increasingly challenging year for commercial real estate, and the U.S. Property Separate Account was not immune from decreasing asset values as the market endured an accelerating credit freeze and deteriorating national economic condition. Negative appreciation in all four quarters drove a total separate account return of -12.2% in 2008. The return was comprised of 4.5% income and -16.2% appreciation. The negative appreciation includes the impact of negative leverage, which is the result of borrowing rates that were higher than property returns. The 2008 results mark the first calendar year of a negative total return since 1991, the last major period of widespread value declines within the market and the separate account.

Property performance of the U.S. Property Separate Account exceeds its property-level benchmark, the Open-end Fund Component of the National Council of Real Estate Investment Fiduciaries (NCREIF) Index, by 48 basis points over the ten-year time period. Over the one and three-year time periods, the separate account trails the benchmark by 92 and 35 basis points, respectively, while performance is equal to the benchmark over five years. The separate account lags its fund-level benchmark, the Equal Weight NCREIF Fund Index – Open-end Diversified Core Equity (NFI-ODCE) over all time periods primarily due to property performance in the short-term and historically lower leverage than the peer group when property level returns exceeded borrowing rates over longer time periods.

The decline in asset values was widespread throughout all sectors of the separate account. Office assets recorded the largest value decreases led by two properties in the East Bay and a property in New York, all of which have a significant amount of building vacancy. Industrial assets followed with the second largest declines within the Portfolio. Industrial assets that posted the largest declines include two vacant buildings in northern New Jersey and several smaller assets with additional leasing to be completed. Value decreases extended to the separate account's multi-family sector with declines in suburban properties driving negative returns. Assets in Fort Myers and Washington, D.C. posted the largest value decreases within the retail sector.

Principal Real Estate Investors believes that assets within the U.S. Property Separate Account are well-positioned to withstand the continued recession through on-going operational efforts both at the property and portfolio level. Despite dramatic decreases in tenant demand, core assets in the separate account are well-leased finishing the year with 90% occupancy. The decrease in occupancy was due to negative net absorption of 368,191 square feet during 2008, although this was entirely the result of two known tenant moveouts at industrial assets in Riverside, California and Edison, New Jersey totaling over 555,000 square feet. Going forward, only 10% of commercial space within the Separate Account has lease expirations during the next 12 months.

Lease Expiration Schedule
(for the years ending)

	12/31/09	12/31/10	12/31/11	12/31/12	12/31/13
Office	9%	15%	17%	10%	13%
Retail	5%	6%	7%	11%	7%
Industrial	13%	13%	13%	9%	7%
Multi-family	N/A	N/A	N/A	N/A	N/A
Total	**10%**	**13%**	**13%**	**9%**	**9%**

U.S. Property Separate Account Performance

Portfolio Occupancy

PROPERTY TYPE	OCCUPANCY	OCCUPANCY EXCLUDING VALUE-ADDED PROPERTIES[1]	NET ABSORPTION[2] (square feet)
Office	90%	92%	(151,611)
Retail	85%	89%	204,983
Industrial	74%	89%	(683,038)
Multi-family	89%	89%	261,475
Total	**82%**	**90%**	**(368,191)**

1Value-added assets include those that are acquired at less than 85% occupancy, are under development or include the sale of individual condominium units.
2Net absorption reflects change in occupied square feet since the end of the previous year.

Leverage increased throughout the year from 16.5% to 26.1%, which is slightly below the average loan to value of the NFI-ODCE. The increased borrowing is at attractive rates relative to market with the weighted average annual interest rate of all debt at 5.0%. Maturities in 2009, excluding the Separate Account's lines of credit, are minimal at 11% of outstanding debt.

Leverage Information

	INTEREST RATE	% OF TOTAL DEBT
Fixed Interest Rate Obligations	5.52%	69.1%
Floating Interest Rate Obligations	3.68%	30.9%
Total Obligations	**4.95%**	**100.0%**
Secured Obligations	5.40%	80.5%
Unsecured Obligations	3.11%	19.5%
Total Obligations	**4.95%**	**100.0%**

Impact of Marking Debt to Market

1 Year	1.08%
3 Year	0.32%
5 Year	0.24%

Debt Maturity Schedule[1]

YEAR	% OF DEBT MATURING
2009	11.1%
2010	23.8%
2011	15.5%
2012	19.4%
2013	3.7%
2014 and later	26.5%

1 Debt maturity schedule is calculated using the total book value of all outstanding notes and excludes lines of credit.

The change in capital markets was the greatest driver of asset value declines throughout the Separate Account in 2008; however, evidence of space market deterioration also contributed to value decreases. Over 80% of the Separate Account's 149 assets were written down over the course of the year, including material write downs in the fourth quarter during which deterioration of both fundamentals in the space markets and capital markets accelerated. Below is a chart which includes the weighted average capitalization and discount rates at the end of 2008 and the change in each metric during 2008. Both metrics of valuation recorded substantial upward adjustments during the year signaling investor re-pricing of risk associated with commercial real estate investments.

Valuation Metrics[1]

VALUATION	INITIAL CAP RATE	2007-2008 CHANGE (basis points)	DISCOUNT RATE (IRR)	2007-2008 CHANGE (basis points)
Office	5.6%	46 bp	8.1%	74 bp
Retail	6.5%	63 bp	8.5%	89 bp
Industrial	5.8%	2 bp	8.0%	30 bp
Multi-Family	5.5%	50 bp	8.0%	63 bp
Weighted Average	**5.8%**	**45 bp**	**8.1%**	**67 bp**

1Excludes value-added properties

Assets in the Separate Account posted marginal, but positive growth in same-property net operating income (NOI) during 2008. Year-over-year NOI growth for all assets held in the Separate account at December 31, 2007 and December 31, 2008 was 1.7%. Assets that include a value-added component (such as properties with large vacancies at acquisition or properties under development) posted much stronger year-over-year NOI growth of 8.5%.

Same-Property Net Operating Income (in $ millions)

Actual ending 12/31/2007	$291.0
Actual ending 12/31/2008	$295.9
NOI Growth	1.7%

Forward Commitments[1]

YEAR	AGGREGATE DOLLAR AMOUNT
2009	$117.3
2010	$95.3
2011	$309.3
Land and predevelopment	$242.0

1Based on projected acquisition date and current approved dollar amounts

Capital Markets[1]

The prolonged credit crisis and outlook for a major recession portend a dual adverse impact on the commercial real estate markets. First, like the broader financial system, the commercial real estate asset class is under pressure to deleverage, and as such, is forced to compete for increasingly expensive equity capital within a broader global system that is simultaneously deleveraging. The result has been a sharp increase in commercial real estate's cost of capital and continued upward pressure on capitalization (cap) rates and discount rates. Second, despite reasonably well-constrained new supply, the reality of a major recession has dramatically reduced the user demand outlook, resulting in a marked deterioration of space market fundamentals relative to what previously had been priced into commercial real estate.

The commercial real estate markets have experienced a major reversal in the cost and availability of debt capital. The commercial mortgage-backed securities (CMBS) issuance market has become virtually non-existent amidst extreme spread widening. Portfolio lenders have become highly risk averse and much less active, with spreads on senior mortgages having tripled throughout 2008. Given the major correction that has occurred in risk pricing in the debt capital markets, there has been a notable sector rotation of capital originally targeted for real estate equity strategies into real estate debt strategies instead.

Private commercial real estate equity has been impacted not only by this change in assumptions regarding the cost and availability of debt capital, but also by virtually all previous investor assumptions. Cash flow assumptions regarding net absorption, tenant retention, rent growth, credit losses and cap rates that were impounded into peak property valuations have undergone an unfavorable revision as a result of the intensification of the credit crisis, uncertainty regarding the severity of the U.S. recession, and growing fears of a major global recession. As a result, the private commercial real estate equity market has entered the early stages of what will likely be a major price correction that, based upon pricing signals from the property derivatives marketplace, could be comparable to the peak-to-trough price declines experienced in the 1990s, depending upon the severity and duration of the recession. Equity sales transaction volumes in 2008 have declined by approximately 73% percent from prior year levels per data from Real Capital Analytics.

The publicly-traded real estate investment trust (REIT) marketplace has suffered through its second consecutive year of major price declines, amidst an outlook for continued deterioration of space markets, worries about dividend cuts, and concerns about the ability to refinance maturing debt. Merger and acquisition activity – a dominant theme of the public REIT markets in 2006 and 2007 – was a non-factor in 2008.

With market turmoil often comes opportunity. Not only is commercial real estate no longer priced for perfection, but certain sectors of the commercial real estate investment market appear to be priced for a depression as opposed to a recession. This possible overcorrection may signal a potential opportunity for investors, especially those with a long-term investment horizon. While the credit crisis and recession clearly represent a major turning point for commercial real estate pricing and return performance, there has thus far been little evidence of a material reduction in institutional investors' strategic commitment to the real estate asset class. Unlike the early 1990s when many investors completely withdrew from the market, today many institutional investors are examining the real estate market from the perspective of how to reposition or rebalance real estate portfolios to take advantage of opportunities created by the market turmoil rather than how to exit the asset class. This strategic commitment in the face of market corrections is another sign of commercial real estate's coming of age as an asset class and likely will ultimately represent an important force of stabilization in the real estate capital markets.

1 Commentary above includes excerpts from *Expectations & Market Realities in Real Estate: 2009*, published by Principal Real Estate Investors, CBRE/Torto Wheaton Research and Real Estate Research Corporation and includes updated information through year-end 2008. The full report is available to investors on the Separate Account's website or upon request. Opinions and predictions are subject to change and are not intended as a forecast or guarantee of future events, or as a predictor of performance.

2008 Transaction Activity

2008 Transactions

Transaction activity within the U.S. Property Separate Account was lower in 2008 than in recent years. The Separate Account purchased two assets throughout the course of the year, in addition to one mortgage loan on a property. Both asset acquisitions were closed during the first half of the year, with the loan closing in December commensurate with the original loan maturity. Looking to 2009, anticipated acquisition activity will be primarily driven by forward commitments. All of the assets in the pipeline are well-aligned with Separate Account strategy and located in markets with strong prospects for long-term growth. Strategic direction for new transactions is based upon the following sector-specific strategies:

- Office: The Separate Account will look to reduce its weighting to the office sector over the next several quarters. Further, any new acquisitions will be concentrated in major markets with investment in secondary markets only when the discount to reproduction costs represents significant relative value.
- Retail: The prevailing strategic theme for the retail sector includes maintaining the Separate Account's underweight position relative to the NCREIF Index. Additionally, new portfolio positioning will focus on owning necessity-based formats.
- Multi-family: The Separate Account achieved an underweighting to the multi-family sector during the course of 2008 and will likely maintain that position throughout 2009. Strategic themes looking forward include continued focus on non-commodity properties in infill locations.
- Industrial: During 2007 and 2008, the Separate Account diligently pursued an overweighting to the industrial sector and will focus efforts to preserve this relationship relative to the Index. Further, new activity will be based primarily in the warehouse sub-sector in major transportation hubs.

Disposition activity during the year was relatively strong given market volatility and the lack of available financing for potential buyers. In stark contrast to recent years, sales activity included a high degree of uncertainty as lenders exited the market and buyers were required to invest significantly more equity in acquisitions. In all, disposition activity totaled $391.3 million including 14 dispositions and 4 partial sales, all of which were aligned with Separate Account strategy of continuing to urbanize and enhance the quality of assets within the Separate Account. The Separate Account will pursue additional disposition activity in 2009 following the strategic initiatives outlined below:

- Utilize the sales process to strategically reduce exposure to selected sectors and markets.
- Continue the urbanization of the Separate Account.
- Upgrade overall asset quality by selling B quality assets.

2008 Acquisitions

The Separate Account closed two acquisitions during the year in addition to a mortgage loan for total activity of $231.9 million. Additional details regarding each transaction are included below:

- Portales Corporate Center is a 452,349 square foot Class-A office building located on North Scottsdale Road in Phoenix, Arizona. The asset, which includes two trophy buildings, was acquired in March and as of December 31, 2008, is 92% leased.
- Lyons Technology Center is located in Fort Lauderdale, Florida and primarily includes industrial warehouse properties (81% of space) in addition to two office buildings (19% of space). The project totals 310,779 square feet throughout nine buildings on 26 acres.
- Henderson Lofts is a 16.25 acre land parcel located in Henderson, a major suburb of Las Vegas, Nevada. The Separate Account purchased the outstanding mortgage note on the property in December.

Acquisitions

PROPERTY	SECTOR	MSA	PRICE ($MILLION)	STRUCTURE
Portales Corporate Center	Office	Phoenix, AZ	$172.8	Wholly Owned
Lyons Technology Center	Industrial/Office	Ft. Lauderdale, FL	$45.9	Wholly Owned
Henderson Lofts	Land	Las Vegas, NV	$13.2	Mortgage Loan
2008 Acquisitions			**$231.9**	

2008 Dispositions

The Separate Account sold 14 assets during the year for total activity of $391.3 million. Additional details regarding each transaction are included below:

Office

- Windward Oaks, located in suburban Atlanta, Georgia, was sold to execute the Separate Account's strategy of upgrading portfolio quality and exiting a non-strategic office location.
- The Minneapolis Portfolio, a collection of five assets including two office properties, was sold during the second quarter. The sale continued the strategic theme of the Separate Account to upgrade overall portfolio quality and allowed for a reduction in the Separate Account's overweighting to the Minneapolis market.
- Lakeview I and II, assets located in Columbia, Maryland, were sold during the third quarter. The assets, totaling over 215,000 square feet, were sold to execute the Separate Account strategy of reducing its office weighting and upgrading the quality of the overall portfolio.
- 1875 Lawrence Street is a 186,000 square foot asset located in Denver, Colorado. The B quality property was sold to narrow the Separate Account overweighting to Denver and mitigate rollover risk as nearly 80% of the existing tenant base expires in the next three years.
- Music Row, a Nashville, Tennessee asset totaling approximately 41,000 square feet was sold to a private owner-user during the fourth quarter. The sale was advantageous for the Separate Account as approximately 93% of the building was scheduled to become vacant upon a planned tenant move out.

2008 Transaction Activity

Retail

- Alban Shopping Center, located in Washington, D.C. was sold at above-market pricing in order to accommodate a buyer's investment need. Further, the sale reduces Separate Account exposure to unanchored retail centers.
- Partial sale activity in the sector included the sale of 38,000 square feet of space that was sold to a grocery operator at Lantana Square, a center in West Palm Beach, Florida.

Multi-family

- Gleneagles I and II, assets in suburban Denver, Colorado, were sold in order to exit suburban, commodity-type multi-family product.
- Canyon Ridge, located in Nashville, Tennessee, was sold to execute the Separate Account's original business plan of stabilization and disposition.
- Club at North Hills, located in Pittsburgh, Pennsylvania, was sold to execute the original business plan which identified a short holding period.
- Shadow Hills, located in Minneapolis, Minnesota, was sold to reduce the Separate Account's exposure to the Minneapolis market and decrease suburban multi-family holdings.
- Presidio, located in Austin, Texas, was sold during the fourth quarter due to limited additional growth potential at the asset and to reduce Separate Account exposure to the Austin apartment market.
- Partial sale activity included the sale of individual condominium units at 170 Off Third in San Francisco, California. The asset was developed by the Separate Account and is located at 170 King Street, directly across from the baseball stadium, AT&T Ballpark.

Industrial

- Trade Center III and 145 Plymouth Street, industrial warehouse assets located in St. Louis, Missouri and suburban Boston, Massachusetts, were sold in order to exit non-strategic industrial markets for the Separate Account.
- The Minneapolis Portfolio, a collection of five assets including three industrial properties was sold during the second quarter. The sale continued the strategic theme of the Separate Account to upgrade overall portfolio quality and allowed for a reduction in the Separate Account's overweighting to the Minneapolis market.
- Westbrooke Corporate Park is an asset located in suburban Portland, Oregon that was sold during the fourth quarter. The asset, a 170,000 square foot flex property, was sold to reduce Separate Account exposure to the Portland flex market and a building with historical leasing challenges.
- Partial sale activity included the disposition of a 55,000 square foot warehouse at Enterprise Distribution Center located in Riverside, California to an owner-user.

Land

- One partial sale was completed during 2008 within the land sector. A 0.54 acre parcel at Fountainhead Corporate Center was sold to mitigate exposure to potential future condemnation.

Dispositions

PROPERTY	SECTOR	MSA	PRICE ($ MILLION)
Windward Oaks	Office	Altanta, GA	$16.6
Lakeview I	Office	Baltimore, MD	$21.1
Lakeview II	Office	Baltimore, MD	$11.1
1875 Lawrence	Office	Denver, CO	$34.0
Music Row	Office	Nashville, TN	$4.7
Minneapolis Portfolio	Office	Minneapolis, MN	$11.3
Total Office			**$98.8**
Gleneagles I	Multi-family	Denver, CO	$28.9
Gleneagles II	Multi-family	Denver, CO	$31.4
Canyon Ridge	Multi-family	Nashville, TN	$35.8
Club at North Hills	Multi-family	Pittsburgh, PA	$29.1
Shadow Hills	Multi-family	Minneapolis, MN	$32.1
Presidio	Multi-family	Austin, TX	$18.5
170 King	Multi-family*	San Francisco, CA	$24.9
Total Multi-family			**$200.7**
Alban Shopping Center	Retail	Washington, D.C.	$7.1
Lantana Square	Retail*	Palm Beach, FL	$5.6
Total Retail			**$12.7**
Westbrooke	Ind/R&D	Portland, OR	$18.7
Enterprise	Ind/WH*	Riverside, CA	$3.7
Trade Center III	Industrial	St. Louis, MO	$13.9
145 Plymouth Street	Industrial	Providence, RI	$14.8
Minneapolis Portfolio	Industrial	Minneapolis, MN	$27.6
Total Industrial			**$78.7**
Fountainhead	Land*	Phoenix, AZ	$0.4
Total Land			**$0.4**
2008 Dispositions			**$391.3**

*Denotes partial sale.

Independent Auditors' Report

TO THE ACCOUNT MANAGEMENT AND CONTRACTHOLDERS
PRINCIPAL LIFE INSURANCE COMPANY U.S. PROPERTY SEPARATE ACCOUNT
DES MOINES, IOWA

We have audited the accompanying consolidated statements of assets and liabilities of Principal Life Insurance Company U.S. Property Separate Account ("USPSA"), including the consolidated schedules of investments, as of December 31, 2008 and 2007, and the related consolidated statements of operations, changes in net assets, cash flows, and the financial highlights for the years then ended. These financial statements and financial highlights are the responsibility of USPSA's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of USPSA's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the separate accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of USPSA as of December 31, 2008 and 2007, the results of its operations, changes in its net assets, its cash flows, and financial highlights for the years then ended, in conformity with separate accounting principles generally accepted in the United States of America.

As discussed in Note 3 to the consolidated financial statements, the fair value of substantially all assets and liabilities of USPSA have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on independent appraisals or cash flow projections.

Deloitte & Touche LLP

Des Moines, Iowa
January 26, 2009

Audited Financial Statements

PRINCIPAL LIFE INSURANCE COMPANY
U.S. PROPERTY SEPARATE ACCOUNT
CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES
DECEMBER 31, 2008 AND 2007

ASSETS	2008	2007
INVESTMENTS AT FAIR VALUE:		
Real estate (cost: 2008 - $6,313,675,968; 2007 - $6,243,606,944)	$6,758,425,000	$7,709,754,500
Real estate joint venture (cost: 2008 - $16,325,952; 2007 - $8,585,893)	15,733,715	8,862,862
Mortgage loan receivable (cost: 2008 - $13,220,131; 2007 - $0)	11,658,331	-
Short-term investments (cost: 2008 - $39,722,779; 2007 - $94,970,033)	39,722,779	94,970,033
Total investments (cost: 2008 - $6,382,944,830; 2007 - $6,347,162,870)	6,825,539,825	7,813,587,395
CASH	33,555,298	31,157,295
ACCRUED INVESTMENT INCOME AND OTHER ASSETS	77,674,853	90,925,204
TOTAL ASSETS	6,936,769,976	7,935,669,894
LIABILITIES		
Lines of credit	370,625,000	-
Debt	1,441,225,688	1,305,837,921
Accounts payable and accrued expenses	80,129,663	60,469,028
Accrued property taxes	30,345,372	27,114,837
Security deposits	17,088,658	18,219,605
	1,939,414,381	1,411,641,391
Minority interest	119,677,058	176,469,973
TOTAL LIABILITIES	2,059,091,439	1,588,111,364
NET ASSETS	$4,877,678,537	$6,347,558,530

See notes to consolidated financial statements.

Audited Financial Statements

PRINCIPAL LIFE INSURANCE COMPANY
U.S. PROPERTY SEPARATE ACCOUNT
CONSOLIDATED SCHEDULE OF INVESTMENTS
DECEMBER 31, 2008

	FAIR VALUE
REAL ESTATE - 99.0%	
United States:	
Total office - 40.9% (cost $2,695,289,241)	
1370 Avenue of the Americas, New York, NY	$299,300,000
333 Market Street, San Francisco, CA	376,400,000
Other office	2,114,775,000
	2,790,475,000
Total land - 0.9% (cost $47,804,175)	59,690,000
Total retail - 19.6% (cost $1,223,578,938)	1,341,050,000
Total industrial - 16.2% (cost $966,213,487)	1,104,400,000
Total multi-family - 21.4% (cost $1,380,790,127)	1,462,810,000
Total real estate (cost $6,313,675,968)	6,758,425,000
REAL ESTATE JOINT VENTURE - 0.2%	
United States:	
Total hotel - 0.2% (cost $16,325,952)	15,733,715
MORTGAGE LOAN RECEIVABLE - 0.2%	
United States:	
Total land - 0.2% (cost $13,220,131)	11,658,331
SHORT-TERM INVESTMENTS - 0.6%	
United States:	
Merrill Lynch Government Fund - 0.4% (cost $25,650,000)	25,650,000
Money market separate account - 0.2% (cost $14,072,779)	14,072,779
Total short-term investments (cost $39,722,779)	39,722,779
TOTAL INVESTMENTS (cost $6,382,944,830)	$6,825,539,825

See notes to consolidated financial statements.

Audited Financial Statements

PRINCIPAL LIFE INSURANCE COMPANY
U.S. PROPERTY SEPARATE ACCOUNT
CONSOLIDATED SCHEDULE OF INVESTMENTS
DECEMBER 31, 2007

	FAIR VALUE
REAL ESTATE - 98.7%	
United States:	
Total office - 40.0% (cost $2,549,808,959)	
1370 Avenue of the Americas, New York, NY	$345,100,000
333 Market Street, San Francisco, CA	397,000,000
Other office	2,379,592,000
	3,121,692,000
Total land - 0.8% (cost $45,582,407)	62,784,000
Total retail - 17.6% (cost $1,125,748,307)	1,373,790,000
Total industrial - 16.6% (cost $989,594,142)	1,301,431,000
Total multi-family - 23.7% (cost $1,532,873,129)	1,850,057,500
Total real estate (cost $6,243,606,944)	7,709,754,500
REAL ESTATE JOINT VENTURE - 0.1%	
United States:	
Total hotel - 0.1% (cost $8,585,893)	8,862,862
SHORT-TERM INVESTMENTS - 1.2%	
United States:	
Blackrock TempFund - 0.5% (cost $38,317,000)	38,317,000
Money market separate account - 0.7% (cost $56,653,033)	56,653,033
Total short-term investments (cost $94,970,033)	94,970,033
TOTAL INVESTMENTS (cost $6,347,162,870)	$7,813,587,395

See notes to consolidated financial statements.

Audited Financial Statements

PRINCIPAL LIFE INSURANCE COMPANY
U.S. PROPERTY SEPARATE ACCOUNT
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
INVESTMENT INCOME:		
Rental and other income	$614,571,219	$557,921,229
Real estate taxes	(85,136,211)	(70,472,851)
Other operating expenses	(168,285,244)	(152,419,185)
Net operating income from real estate investments	361,149,764	335,029,193
Net operating loss from real estate joint venture	(647,988)	(289,390)
Interest income on short-term investments	4,379,289	18,661,885
Total investment income	364,881,065	353,401,688
EXPENSES:		
Interest expense	91,325,932	64,258,683
Investment management fees	65,200,822	65,474,671
Professional and other fees	7,660,728	4,907,240
Total expenses	164,187,482	134,640,594
MINORITY INTEREST IN NET INVESTMENT INCOME	2,496,730	2,633,039
NET INVESTMENT INCOME	198,196,853	216,128,055
REALIZED AND UNREALIZED GAIN (LOSS):		
Proceeds from real estate investment sales	391,296,252	691,508,943
Cost of real estate investments sold	(370,569,357)	(530,244,853)
Realization of prior period unrealized gain on real estate investments sold	(44,831,098)	(85,346,318)
Net gain (loss) recognized from real estate investment sales	(24,104,203)	75,917,772
Unrealized gain (loss) on investments and debt	(946,168,470)	492,736,161
NET REALIZED AND UNREALIZED GAIN (LOSS)	(970,272,673)	568,653,933
MINORITY INTEREST IN NET REALIZED AND UNREALIZED GAIN (LOSS)	(32,288,821)	47,641,988
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	$(739,786,999)	$737,140,000

See notes to consolidated financial statements.

Audited Financial Statements

PRINCIPAL LIFE INSURANCE COMPANY
U.S. PROPERTY SEPARATE ACCOUNT
CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS:		
Net investment income	$198,196,853	$216,128,055
Net gain (loss) recognized from real estate investment sales	(24,104,203)	75,917,772
Unrealized gain (loss) on investments and debt	(946,168,470)	492,736,161
Minority interest in net realized and unrealized gain (loss)	32,288,821	(47,641,988)
Net increase (decrease) in net assets resulting from operations	(739,786,999)	737,140,000
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM NET CONTRACTHOLDER CONTRIBUTIONS (DISTRIBUTIONS)	(730,092,994)	241,952,157
INCREASE (DECREASE) IN NET ASSETS	(1,469,879,993)	979,092,157
NET ASSETS AT BEGINNING OF YEAR	6,347,558,530	5,368,466,373
NET ASSETS AT END OF YEAR	$4,877,678,537	$6,347,558,530

See notes to consolidated financial statements.

Audited Financial Statements

PRINCIPAL LIFE INSURANCE COMPANY
U.S. PROPERTY SEPARATE ACCOUNT
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net increase (decrease) in net assets resulting from operations	$(739,786,999)	$737,140,000
Adjustment to reconcile net increase (decrease) in net assets resulting from operations to net cash provided by operating activities:		
Net realized and unrealized loss (gain)	970,272,673	(568,653,933)
Minority interest	(29,792,091)	50,275,027
Net operating loss from real estate joint venture	647,988	289,390
Changes in:		
Accrued investment income and other assets	11,794,729	(4,349,628)
Separate accounts payable and accrued expenses	(929,443)	12,478,642
Accrued property taxes	3,230,535	$850,549
Security deposits	(1,130,947)	4,683,451
Total adjustments	954,093,444	(504,426,502)
Net cash provided by operating activities	214,306,445	232,713,498
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from real estate investment sales	391,296,252	691,508,943
Purchases of real estate investments and improvements	(414,643,444)	(1,502,563,469)
Investment in real estate joint venture	(7,740,058)	(8,585,893)
Distribution from real estate joint venture	567,461	-
Net change in short-term investments	55,247,254	48,240,585
Net change in escrows and other restricted assets	3,200,331	(6,913,406)
Cash advanced for mortgage receivable	(13,220,131)	-
Net cash provided by (used in) investing activities	14,707,665	(778,313,240)

	2008	2007
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payment of financing costs	(3,662,509)	-
Net borrowings on lines of credit	370,625,000	-
Repayments of debt	(169,645,953)	(99,504,033)
Issuance of debt	333,161,173	427,798,523
Net contractholder contributions (distributions)	(730,092,994)	241,952,157
Contributions from minority interest partners	3,510,322	23,162,787
Distributions to minority interest partners	(30,511,146)	(35,467,756)
Net cash provided by (used in) financing activities	(226,616,107)	557,941,678
NET CHANGE IN CASH	2,398,003	12,341,936
CASH AT BEGINNING OF YEAR	31,157,295	18,815,359
CASH AT END OF YEAR	$33,555,298	$31,157,295
SUPPLEMENTAL DISCLOSURE OF CASH PAID FOR INTEREST	$91,577,462	$62,870,568

SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES:

USPSA had noncash purchases of real estate investments and improvements of $45,905,456 and $25,315,378 in 2008 and 2007, respectively.

USPSA assumed mortgages payable of $24,613,064 and $71,077,495 in 2008 and 2007, respectively, in connection with the purchase of real estate investments.

See notes to consolidated financial statements.

Audited Financial Statements

PRINCIPAL LIFE INSURANCE COMPANY
U.S. PROPERTY SEPARATE ACCOUNT
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

1. ORGANIZATION

Principal Life Insurance Company U.S. Property Separate Account ("USPSA") is an open-end, commingled real estate separate account and a separate account of Principal Life Insurance Company ("Principal Life") established in 1982 in accordance with the provisions of the State of Iowa insurance laws. Pursuant to such laws, the net assets of USPSA are not chargeable with liabilities arising out of any business of Principal Life. Participation in USPSA is available through the purchase of certain group contracts and policies issued by Principal Life. The investment advisor is Principal Real Estate Investors, LLC ("Principal Real Estate"), a wholly-owned subsidiary of Principal Life.

On September 26, 2008, Principal Life applied a limitation which delays the payment of withdrawal requests and provides for payment of such requests on a pro rata basis (a "Queue") as cash becomes available for distribution, as determined by Principal Life. On December 31, 2008, the outstanding balance in the Queue was $837.8 million.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

NEW ACCOUNTING PRONOUNCEMENTS - In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 157, *Fair Value Measurements* ("SFAS 157"). SFAS defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. SFAS 157 includes provisions that require expanded disclosure of the effect on earnings for items measured using unobservable data. USPSA adopted SFAS 157 effective January 1, 2008.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* ("SFAS 159"), which permits entities to choose to measure many financial instruments and certain other items at fair value ("Fair Value Option"). Election of the Fair Value Option is made on an instrument-by-instrument basis and is irrevocable. Effective January 1, 2008, USPSA elected to record its fund-level debt at fair value because it believes it is a better representation of the net asset value. USPSA will report unrealized gains and losses due to changes in fair value in earnings at each subsequent reporting date. The election did not have a material impact on the net assets or changes in net assets of USPSA.

In December 2007, the FASB issued SFAS No. 160, *Non-controlling Interests in Consolidated Financial Statements* ("SFAS 160"), an amendment of ARB No. 51. SFAS 160 establishes new accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 clarifies that changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation are equity transactions if the parent retains its controlling financial interest. In addition, this statement requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the non-controlling equity investment on the deconsolidation date. SFAS 160 also includes expanded disclosure requirements regarding the interest of the parent and its non-controlling interest. SFAS 160 is effective for fiscal years beginning on or after December 15, 2008. Early adoption is prohibited. USPSA is currently evaluating the potential impact of SFAS 160 on its financial position, results of operations and cash flows.

BASIS OF PRESENTATION - The accompanying consolidated financial statements of USPSA have been presented in conformity with accounting principles generally accepted in the United States of America. The consolidated financial statements of USPSA include the separate accounts of its wholly-owned and controlled real estate investments. All intercompany transactions are eliminated in the consolidation.

USPSA follows the provisions contained in the American Institute of Certified Public Separate Accountants ("AICPA") Audit and Accounting Guide "Investment Companies" ("Investment Company Guide"). Under the Investment Company Guide, assets and property-level debt are presented at fair value. Through December 31, 2007, debt which was not collateralized by a specific real estate investment was presented at amounts payable, net of any unamortized premium or discount. Effective January 1, 2008, with the adoption of SFAS No. 159, and at the election of USPSA management, debt which is not collateralized by a specific real estate investment is carried at fair value.

USE OF ESTIMATES - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

The real estate and capital markets are cyclical in nature. Property and investment values are affected by, among other things, the availability of capital, occupancy rates, rental rates and interest and inflation rates. As a result, determining real estate and investment values involves many assumptions. Amounts ultimately realized from each investment may vary significantly from the fair values presented.

RISKS AND UNCERTAINTIES - USPSA invests in commercial real estate properties located throughout the United States. The markets for commercial real estate in the United States have experienced significant challenges during 2008. Market conditions have had a negative impact on the estimated fair value of USPSA's investments, which are reflected as unrealized losses in the 2008 financial statements. Severe restrictions on the availability of real estate financing, as well as the economic uncertainties in the current environment, have resulted in a low volume of purchase and sale transactions, limiting the amount of observable inputs available to USPSA management in making their estimates of fair value. As discussed above, USPSA's estimates of fair value are based on the best information available to management as of the date of the valuation. Should market conditions continue to deteriorate, or should management's assumptions change, the USPSA may record additional unrealized losses in future periods.

REAL ESTATE - Real estate investments are carried at fair value. Properties owned are initially recorded at the purchase price plus closing costs. Development costs and major renovations are capitalized as a component of cost, and routine maintenance and repairs are charged to expense as incurred. Real estate costs include the cost of acquired property, including all tangible and intangible assets. Tangible assets include the value of all land, building and tenant improvements at the time of acquisition. Intangible assets include the value of any above and below market leases, in-place leases, and tenant relationships at the time of acquisition. Real estate costs also include leasing costs paid to third parties to obtain tenants. The cost of real estate investments presented in the accompanying consolidated statements of assets and liabilities includes approximately $80,600,000 and $75,000,000 of such deferred costs as of December 31, 2008 and 2007, respectively. USPSA does not record depreciation or amortization on real estate costs.

Real estate values are based upon independent appraisals. The fair value of real estate investments does not reflect transaction sale costs, which may be incurred upon disposition of the real estate investments. These values may vary significantly from the prices at which the real estate investments would sell, since market prices of real estate investments can only be determined by negotiation between a willing buyer and seller. Although the estimated fair values represent subjective estimates, management believes these estimated fair values are reasonable approximations of market prices and the aggregate estimated value of investments in real estate is fairly presented at December 31, 2008 and 2007.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Sale transactions are accounted for using the full accrual method in accordance with Statement of Financial Accounting Standards No. 66, "Accounting for Sales of Real Estate." All costs incurred to complete the sales of the properties are included in the computations of the gain or loss on sale.

REAL ESTATE JOINT VENTURE - Investment in real estate joint venture is comprised of a joint venture which USPSA does not control, but over which it has significant influence. The investment is included in the consolidated statements of assets and liabilities at USPSA's ratable share of the fair value of the underlying net assets of the joint venture, adjusted for the terms of the joint venture agreement. Net operating income (loss) from real estate joint venture represents USPSA's share of the current year's joint venture income (loss) as provided for under the terms of the joint venture agreement. Joint venture income (loss) is not reduced by depreciation or amortization expense. USPSA's ratable share of the change in the fair value of the joint venture is reported in net realized and unrealized gain (loss) in the accompanying consolidated statements of operations. Distributions from the joint venture is recorded on the ex-dividend date.

MORTGAGE LOAN RECEIVABLE - Investment in mortgage loan receivable is carried at fair value, equivalent to the lesser of the fair value of the underlying real estate asset or contractual cash flows discounted using current interest rates at which similar advances would be made with similar terms.

SHORT-TERM INVESTMENTS - Short-term investments are comprised of money market funds and are carried at fair value based on quoted market prices of the fund or underlying assets, which represent the net asset value of shares held by USPSA.

CASH - Cash includes cash on hand and demand deposit separate accounts.

FAIR VALUE OF DEBT - The fair value of debt is based on the present value of estimated cash flows using interest rates and anticipated returns a market participant would incur with similar risk and terms. The debt fair value adjustment was ($42,045,753) and $10,694,764 as of December 31, 2008 and 2007, respectively.

MINORITY INTEREST - USPSA has entered into joint development relationships with other investors to acquire and develop real estate properties. USPSA is the majority owner in such projects and has control over decision-making. Accordingly, the underlying assets and liabilities of the projects are consolidated into USPSA's financial statements, with the external investors' net share reflected as minority interest. Certain external investors earn additional equity if the estimated rate of return of the real estate property that they are invested in exceeds a contractually determined rate. This additional equity allocation is accrued at the same time that the underlying real estate property appreciates and is recorded in minority interest in net realized and unrealized gain (loss) in the accompanying consolidated statements of operations. The additional equity accrual included in minority interest in the consolidated statements of assets and liabilities was approximately $20,290,000 and $64,820,000 as of December 31, 2008 and 2007, respectively.

REVENUE RECOGNITION - Rental income is recognized as income when earned in accordance with the terms of the respective leases. Reimbursements from tenants for common area costs are recognized monthly based on an estimate of annual costs, subject to periodic adjustments to reflect actual costs.

INCOME TAXES - According to current provisions of the Internal Revenue Code pertaining to tax qualified separate accounts, no income taxes are attributable to the activities of USPSA. As a result, income taxes are not reflected in the accompanying consolidated financial statements.

3. FAIR VALUE MEASUREMENTS

In determining fair value, USPSA uses various valuation approaches. SFAS 157 establishes a fair value measurement framework, provides a single definition of fair value, and requires expanded disclosure summarizing fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing an asset or liability.

The statement establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable input be used when available. Observable inputs are inputs that the market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of USPSA. Unobservable inputs are inputs that reflect USPSA's assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The hierarchy is measured in three levels based on the reliability of inputs:

- Level 1 – Valuations based on quoted prices in active markets for identical assets or liabilities that USPSA has the ability to access. Valuation adjustments and block discounts are not applied to Level 1 instruments.
- Level 2 – Valuations based on quoted prices in less active, dealer or broker markets. Fair values are primarily obtained from third party pricing services for identical or comparable assets or liabilities.
- Level 3 – Valuations derived from other valuation methodologies, including pricing models, discounted cash flow models and similar techniques, and not based on market, exchange, dealer, or broker-traded transactions. Level 3 valuations incorporate certain assumptions and projections that are not observable in the market and significant professional judgment in determining the fair value assigned to such assets or liabilities.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

The following is a description of the valuation techniques used for investments measured at fair value:

REAL ESTATE - An independent consultant (the "Valuation Consultant") selected by Principal Real Estate oversees and administers the appraisal process for USPSA. Real estate investments are stated at fair value as determined by the Valuation Consultant and approved by USPSA management. Appraisals are performed for each investment annually by independent third party MAI certified appraisers with all appraisals being performed in accordance with the Uniform Standard of Professional Appraisal Practice. Thereafter, values are updated daily by the Valuation Consultant based on changes in factors such as occupancy levels, lease rates, overall market conditions and capital improvements. Determination of estimated fair value involves subjective judgment because the actual fair value of real estate can be determined only by negotiation between the parties in a sales transaction.

The values of real estate investments have been prepared giving consideration to the income, cost and sales comparison approaches of estimating property value. The income approach estimates an income stream for a property (typically 10 years) and discounts this income plus a reversion (presumed sale) into a present value at a risk adjusted rate. Yield rates and growth assumptions utilized in this approach are derived from market transactions as well as other financial and industry data. The cost approach estimates the replacement cost of the building less physical depreciation plus the land value. Generally, this approach provides a check on the value derived using the income approach. The sales comparison approach compares recent transactions to the appraised property. Adjustments are made for dissimilarities which typically provide a range of value. Generally, the income approach carries the most weight in the value reconciliation.

3. FAIR VALUE MEASUREMENTS (continued)

Since appraisals take into consideration the estimated effect of physical depreciation, historical cost depreciation and amortization on real estate related assets has been excluded from net investment income.

The values of real estate properties undergoing development have been prepared giving consideration to costs incurred to date and to key development risk factors, including entitlement risk, construction risk, leasing/sales risk, operation expense risk, credit risk, capital market risk, pricing risk, event risk and valuation risk. The fair value of properties undergoing development includes the timely recognition of estimated entrepreneurial profit after such consideration.

USPSA's real estate investments are generally classified within level 3 of the valuation hierarchy.

REAL ESTATE JOINT VENTURE - Real estate joint venture is stated at the fair value of USPSA's ownership interests of the underlying entity. USPSA's ownership interests are valued based on the fair value of the underlying assets and liabilities including the underlying real estate and any related debt, which are both valued consistently with USPSA's wholly-owned real estate investments, and other factors, such as ownership percentage, ownership rights and distribution provisions. Upon the disposition of all real estate investments by an investee entity, USPSA will continue to state its equity in the remaining net assets of the investee entity during the wind down period, if any that occurs prior to the dissolution of the investee entity. USPSA's real estate joint venture is generally classified within level 3 of the valuation hierarchy.

MORTGAGE LOAN RECEIVABLE - The fair value of the mortgage loan receivable held by USPSA has been determined by one or more of the following criteria as appropriate: (i) on the basis of estimated market interest rates for loans of comparable quality and maturity, and (ii) giving consideration to the value of the underlying collateral. USPSA's mortgage receivable is classified within level 3 of the valuation hierarchy.

SHORT-TERM INVESTMENTS - Short term investments are comprised of money market funds and are carried at fair value based on quoted market prices of the fund or its underlying assets. Short term investments are generally classified within level 2 of the valuation hierarchy.

LINES OF CREDIT AND DEBT - The fair value of the lines of credit and debt instruments are determined by discounting the future contractual cash flows to the present value using interest rates and anticipated returns a market participant would incur with similar risk and terms. The market rate is determined by giving consideration to one or more of the following criteria as appropriate: (i) interest rates for loans of comparable quality and maturity, (ii) the anticipated equity return to the market participant and (iii) the value of the underlying collateral. USPSA's lines of credit and debt are generally classified within level 3 of the valuation hierarchy.

The following are the major categories of assets and liabilities measured at fair value on a recurring basis during the year ended December 31, 2008, using unadjusted quoted prices in active markets for identical assets (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3):

DESCRIPTION	LEVEL 1: QUOTED PRICES IN ACTIVE MARKETS FOR IDENTICAL ASSETS	LEVEL 2: SIGNIFICANT OTHER OBSERVABLE INPUTS	LEVEL 3: SIGNIFICANT UNOBSERVABLE INPUTS	TOTAL AT DECEMBER 31, 2008
Real estate	$ -	$ -	$6,758,425,000	$6,758,425,000
Real estate joint venture	-	-	15,733,715	15,733,715
Mortgage loan receivable	-	-	11,658,331	11,658,331
Short-term investments	-	39,722,779	-	39,722,779
Total assets	$ -	$39,722,779	$6,785,817,046	$6,825,539,825
Lines of credit and debt	$ -	$ -	$1,811,850,688	$1,811,850,688

The following is a reconciliation of the beginning and ending balances for assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the year ended December 31, 2008:

	REAL ESTATE	REAL ESTATE JOINT VENTURE	MORTGAGE LOAN RECEIVABLE	TOTAL LEVEL3 INVESTMENTS	LINES OF CREDIT AND DEBT
Beginning balance - January 1, 2008	$7,709,754,500	$8,862,862	$ -	$7,718,617,362	$(1,305,837,921)
Total realized and unrealized gains (losses) included in changes in net assets	(1,021,149,646)	(301,744)	(1,561,800)	(1,023,013,190)	52,740,517
Purchases, issuances, settlements, and sales	69,820,146	7,172,597	13,220,131	90,212,874	(558,753,284)
Ending balance - December 31, 2008	$6,758,425,000	$15,733,715	$11,658,331	$6,785,817,046	$(1,811,850,688)

4. INVESTMENT MANAGEMENT FEES

Principal Life charges USPSA annual management fees based upon its net assets, with such fees deducted daily. These fees totaled $65,200,822 and $65,474,671 in 2008 and 2007, respectively. USPSA owed Principal Life management fees of $6,209,576 and $0 as of December 31, 2008 and 2007, respectively.

5. INVESTMENT COMMITMENTS

As of December 31, 2008, USPSA had outstanding commitments to purchase 13 properties for approximately $763,868,000. Certain properties are or will be under construction with USPSA agreeing to purchase the completed development subject to attaining certain development and leasing thresholds. It is anticipated that USPSA will acquire these properties between 2009 and 2013.

As of December 31, 2008, USPSA had outstanding commitments to sell 3 properties for approximately $58,957,000. It is anticipated that USPSA will sell these properties in 2009.

6. LINES OF CREDIT

USPSA maintains two unsecured lines of credit. Maximum availability under the lines of credit was $660,000,000 ($360,000,000 and $300,000,000 with maturity dates of July 2, 2009 and October 10, 2009, respectively) and $300,000,000 as of December 31, 2008 and 2007, respectively (reduced to $655,625,000 and $295,075,000, respectively, by the letters of credit described below). There were borrowings outstanding on the lines of credit of $370,625,000 and $0 at December 31, 2008 and 2007, respectively. Interest on outstanding borrowings accrues at LIBOR plus the applicable margins, as defined (1.09% and 1.94% at December 31, 2008 and 5.395% at December 31, 2007). Additionally, USPSA pays a quarterly commitment fee ranging from .15% to .20% per year, based on the total amounts of the lines of credit. The $300,000,000 line of credit has a one year extension option, subject to the terms of the credit agreement, including USPSA providing sufficient notice of extension and having no instances of default on the date of notice and extension.

One line of credit includes a $100,000,000 letter of credit sub facility at December 31, 2008 and 2007. At December 31, 2008 and 2007, there were letters of credit issued with a maximum availability of $4,375,000 and $4,925,000, respectively, of which $0 was outstanding. Interest on outstanding borrowings accrues at LIBOR plus the applicable margin, as defined (1.09% and 5.395% at December 31, 2008 and 2007, respectively). Additionally, USPSA pays a commitment fee of .125% plus the applicable margin per year, as defined, based on the unused amount of the letters of credit issued. The letters of credit expire in October 2009.

The line of credit agreements contain financial and non-financial covenants, including requirements regarding net assets, leverage ratio, debt service coverage ratio and unencumbered assets. USPSA was in compliance with all covenants as of December 31, 2008.

7. DEBT

MORTGAGE NOTES PAYABLE - Mortgage notes payable totaled $1,201,349,089 and $1,034,276,664 as of December 31, 2008 and 2007, respectively. These notes mature between 2009 and 2034 with fixed and variable interest rates ranging from 2.00% to 7.97% at December 31, 2008 and 2007. The notes are collateralized by mortgages on real property and all rents and profits of the underlying properties.

CONSTRUCTION NOTES PAYABLE - Construction notes payable totaled $208,369,812 and $122,009,000 as of December 31, 2008 and 2007, respectively. These notes mature between 2009 and 2010. Variable interest payments are due monthly ranging from 2.54% to 4.26% at December 31, 2008 and from 6.50% to 7.25% at December 31, 2007. The notes are collateralized by the underlying properties.

NOTE PAYABLE - Note payable totaled $0 and $65,000,000 as of December 31, 2008 and 2007, respectively. The note was paid off in 2008.

ASSESSMENTS - Assessments consist of amounts owed to the City of Pleasanton, California, and the City of New York, New York. The assessments totaled $73,552,540 and $73,857,493 as of December 31, 2008 and 2007, respectively. These assessments mature between 2015 and 2032 with fixed and variable interest rates ranging from .70% to 2.32% as of December 31, 2008 and from 1.28% to 3.48% as of December 31, 2007. The assessments are recorded as liens on real property.

As of December 31, 2008, aggregate contractual maturities of debt were as follows:

YEAR ENDING DECEMBER 31,	
2009	$172,796,597
2010	367,963,993
2011	243,131,451
2012	252,951,529
2013	61,682,263
Thereafter	384,745,608
	1,483,271,441
Debt fair value adjustment	(42,045,753)
	$1,441,225,688

8. TENANT LEASES

USPSA leases space to tenants under operating lease agreements. These agreements include renewal options and expire at various dates. At December 31, 2008, future minimum base rentals under non-cancelable leases having an original term of more than one year are as follows:

YEAR ENDING DECEMBER 31,	
2009	$354,302,801
2010	326,810,211
2011	272,196,106
2012	226,603,977
2013	180,676,351
Thereafter	773,102,933
	$2,133,692,379

The above future minimum base rental payments exclude residential lease agreements that separate accounted for approximately 22.7% of USPSA's annual rental income for the year ended December 31, 2008. Rental income for the year ended December 31, 2008 and 2007 included approximately $91,295,000 and $87,367,000, respectively, for expenses recovered from tenants for common area and other reimbursable costs.

9. REAL ESTATE JOINT VENTURE

The following is a summary of the financial position and operating results of USPSA's 33%-owned joint venture investment as of December 31, 2008 and 2007 and for the years then ended. The joint venture records its assets and liabilities at fair value.

9. REAL ESTATE JOINT VENTURE (continued)

	2008	2007
STATEMENTS OF ASSETS AND LIABILITIES:		
Real estate	$246,800,000	$62,900,000
Other assets	2,671,176	13,434,901
Debt	(131,267,433)	(23,075,046)
Other liabilities	(70,526,425)	(26,893,209)
Net assets	$47,677,318	$26,366,646
USPSA's share of net assets	$15,733,715	$8,862,962
STATEMENTS OF OPERATIONS:		
Revenues and other income	$440,380	$161,557
Expenses	(2,560,532)	(1,043,356)
Unrealized gain on investment and debt	1,423,705	114,635
Net loss	$(696,447)	$(767,164)
USPSA's share of net loss	$(301,744)	$(160,484)

10. FINANCIAL HIGHLIGHTS

	R6		PGI>$25 MILLION		PROVIDER		SIP <$25 MIL, NO COMM.	
	2008	2007	2008	2007	2008	2007	2008	2007
PER SHARE OPERATING PERFORMANCE								
Net asset value, beginning of year	$722.49	$636.99	$33.16	$29.17	$371.60	$332.08	$32.54	$28.73
Original issuance of shares in class	-	-	-	-	-	-	-	-
Income from investment operations:								
Net investment income	23.70	24.75	1.15	1.20	7.33	7.98	1.02	1.07
Net realized and unrealized gain (loss)	(119.32)	60.75	(5.48)	2.79	(60.83)	31.54	(5.37)	2.74
Total from investment operations	(95.62)	85.50	(4.33)	3.99	(53.50)	39.52	(4.35)	3.81
Net asset value, end of year	$626.87	$722.49	$28.83	$33.16	$318.10	$371.60	$28.19	$32.54
Total Return **	(13.23)%	13.42 %	(13.06)%	13.65 %	(14.40)%	11.90 %	(13.36)%	13.25 %

(continued)

	CLASSIC		R2		RETIREMENT ACCUM. CONTRACT		SIGNATURE	
	2008	2007	2008	2007	2008	2007	2008	2007
PER SHARE OPERATING PERFORMANCE								
Net asset value, beginning of year	$739.42	$649.97	$624.42	$553.79	$32.44	$28.65	$668.57	$591.23
Original issuance of shares in class	-	-	-	-	-	-	-	-
Income from investment operations:								
Net investment income	26.43	27.40	16.92	17.91	1.02	1.06	19.98	21.00
Net realized and unrealized gain (loss)	(122.36)	62.05	(102.74)	52.72	(5.35)	2.73	(110.20)	56.34
Total from investment operations	(95.93)	89.45	(85.82)	70.63	(4.33)	3.79	(90.22)	77.34
Net asset value, end of year	$643.49	$739.42	$538.60	$624.42	$28.11	$32.44	$578.35	$668.57
Total Return **	(12.97)%	13.76 %	(13.74)%	12.75 %	(13.36)%	13.25 %	(13.49)%	13.08 %

(continued)

	R4		R5		R1		R3	
	2008	2007	2008	2007	2008	2007	2008	2007
PER SHARE OPERATING PERFORMANCE								
Net asset value, beginning of year	$693.18	$612.50	$704.05	$621.36	$599.95	$532.78	$644.50	$570.57
Original issuance of shares in class	-	-	-	-	-	-	-	-
Income from investment operations:								
Net investment income	21.26	22.30	22.42	23.44	15.49	16.48	18.55	19.59
Net realized and unrealized gain (loss)	(114.32)	58.38	(116.21)	59.25	(98.62)	50.69	(106.13)	54.34
Total from investment operations	(93.06)	80.68	(93.79)	82.69	(83.13)	67.17	(87.58)	73.93
Net asset value, end of year	$600.12	$693.18	$610.26	$704.05	$516.82	$599.95	$556.92	$644.50
Total Return **	(13.42)%	13.17 %	(13.32)%	13.31 %	(13.86)%	12.61 %	(13.59)%	12.96 %

(continued)

	PGI>$10<=$25 Million		PGI<=$10 Million		Pre 2002 Nonpro		Rate Level 52	
	2008	2007	2008	2007	2008	2007	2008	2007
PER SHARE OPERATING PERFORMANCE								
Net asset value, beginning of year	$33.07	$29.11	$32.88	$28.98	$726.20	$639.63	$33.03	$29.08
Original issuance of shares in class	-	-	-	-	-	-	-	-
Income from investment operations:								
Net investment income	1.13	1.18	1.10	1.14	27.65	25.56	1.13	1.17
Net realized and unrealized gain (loss)	(5.47)	2.78	(5.43)	2.76	(120.17)	61.01	(5.46)	2.78
Total from investment operations	(4.34)	3.96	(4.33)	3.90	(92.52)	86.57	(4.33)	3.95
Net asset value, end of year	$28.73	$33.07	$28.55	$32.88	$633.68	$726.20	$28.70	$33.03
Total Return **	(13.10)%	13.59 %	(13.19)%	13.48 %	(12.74)%	13.53 %	(13.10)%	13.59 %

(continued)

	I3*		I4*		I5*		RIS INVESTMENT ONLY 1*	
	2008	2007	2008	2007	2008	2007	2008	2007
PER SHARE OPERATING PERFORMANCE								
Net asset value, beginning of year	$741.39	$ -	$753.04	$ -	$784.88	$ -	$ -	$ -
Original issuance of shares in class	-	741.26	-	711.36	-	739.00	9.95	-
Income from investment operations:								
Net investment income	25.03	0.09	25.79	11.06	28.06	14.08	0.34	-
Net realized and unrealized gain (loss)	(122.50)	0.04	(124.47)	30.62	(129.88)	31.80	(1.65)	-
Total from investment operations	(97.47)	0.13	(98.68)	41.68	(101.82)	45.88	(1.31)	-
Net asset value, end of year	$643.92	$741.39	$654.36	$753.04	$683.06	$784.88	$8.64	$ -
Total Return **	(13.15)%	0.20 %	(13.10)%	5.86 %	(12.97)%	6.21 %	(13.15)%	0.00%

(concluded)

FUND LEVEL SUPPLEMENTAL DATA	2008	2007
Net assets, end of year	$4,877,678,537	$6,347,558,530
RATIO TO AVERAGE NET ASSETS:		
Fund level expenses	1.14 %	1.01 %
Net investment income	3.32 %	3.73 %

* Share classes I3, I4, I5and RIS Investment Only 1 had inception dates of December 29, 2007, July 17, 2007, July 6, 2007, and January 3, 2008, respectively.

** Total return for newly issued share classes is from inception date.

Principal U.S. Property Separate Account Background

The Principal U.S. Property Separate Account is a commingled Separate Account managed by Principal Real Estate Investors, LLC, and maintained by Principal Life Insurance Company. It is available, through group annuity contracts issued by Principal Life Insurance Company, to plans meeting the requirements for qualification under Section 401(a) of the Internal Revenue Code of 1986 ("Code"), as amended, and governmental plans meeting the requirements of Section 457 of the Code, as amended. Since inception on January 1, 1982, the Principal U.S. Property Separate Account (the Separate Account) has been offered to clients as an open-end, commingled real estate portfolio sponsored by Principal Life Insurance Company and managed by Principal Real Estate Investors. The Separate Account is a diversified real estate equity portfolio consisting primarily of high quality, well-leased real estate properties in the multi-family, industrial, office, retail and hotel sectors. The Principal U.S. Property Separate Account is available to ERISA qualified retirement plans.

The information in this document has been derived from sources believed to be accurate. It contains general information only on investment matters and should not be considered as a comprehensive statement on any matter and should not be relied upon as such. The information it contains does not take account of any investor's investment objectives, particular needs or financial situation. You should consider whether an investment fits your investment objectives, particular needs and financial situation before making any investment decision.

*As of December 31, 2008 Principal Global Investors is the asset management arm of the Principal Financial Group ® (The Principal ®)'and includes the asset management operations of the following subsidiaries of The Principal: Principal Global Investors, LLC; Principal Real Estate Investors, LLC; Spectrum Asset Management, Inc.; Post Advisory Group, LLC; Columbus Circle Investors; Edge Asset Management, Inc.; Morley Financial Services Inc.; Principal Global Investors (Europe) Limited; Principal Global Investors (Singapore) Ltd.; Principal Global Investors (Australia) Ltd.; Principal Global Investors (Japan) Ltd.; Principal Global Investors (Hong Kong) Ltd.; and the majority owned affiliates of Principal International, Inc.

Insurance products and plan administrative services are provided by Principal Life Insurance Company a member of the Principal Financial Group, Des Moines, IA, 50392. This investment option is subject to investment and liquidity risk and other risks inherent in real estate such as those associated with general and local economic conditions. Payment of principal and earnings may be delayed.

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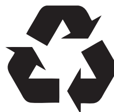

Principal Real Estate Investors is committed to operating practices that are environmentally sustainable

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