Sub-advised by:

Columbus Circle Investors

4Q - 2008
Commentary

as of 12/31/2008

SmallCap Growth III Separate Account-R6

MARKET CONDITIONS

Few could have predicted the capital market turmoil and transformation that occurred during 2008, when what began as a seemingly isolated U.S. subprime mortgage problem ballooned into an all-encompassing crisis affecting nearly all economies and every asset class worldwide.

In terms of 2008 fourth-quarter performance, many had hoped that after a tumultuous September, the worst was behind us. But the fourth quarter picked up where the third had left off. Volatility in domestic equity markets soared, with the Chicago Board Options Exchange Volatility Index reaching an all-time high in November. Uncertainty about the economy and a general lack of confidence in the capital markets worsened.

To combat the turmoil, the Federal Reserve Board used both conventional and innovative measures to provide monetary stimulus. They lowered the fed funds target rate to the lowest point possible, reducing it to a range of 0.0% to 0.25% (from its former 2.0%) and lowered the discount rate to 0.50%, from its former 2.25%. The Fed also initiated a number of other programs - representing hundreds of billions of dollars - and provided critical assistance to stave off possible failure at Citigroup, Chrysler, GM and GMAC, among others. In October Congress took action as well, passing a controversial $700 billion credit facility in an effort to slow or halt the escalating cycle of deleveraging by investing directly in troubled financial institutions.

Despite these efforts, the economy continued to falter. Faced with job losses, investment losses and tighter credit, consumers sharply cut back on purchases, and businesses followed suit, rapidly adjusting for deteriorating demand by slashing jobs and spending. Official confirmation of a recession came in November 2008, when the National Bureau of Economic Research determined that a peak in economic activity occurred in the U.S. economy in December 2007, marking the beginning of a recession.

In this environment the S&P 500 fell 21.94% for the quarter, one of its worst quarterly returns since its inception. Broad value stocks outpaced growth stocks, while large-cap stocks had a modest advantage over their smaller peers (although returns were decidedly negative for all market segments, as measured by the Russell Indexes). U.S. real estate investment trusts experienced heavy losses, even greater than the major U.S. equity indexes (as measured by the MSCI US REIT Index).

With risk aversion at record levels and increasingly gloomy signals for the health of the global economy, non-U.S. equity markets posted severe losses during the quarter. Negative returns were particularly significant in the emerging markets sector.

As credit risk climbed during the period, investors continued their months-long stampede to the relative safety of U.S. Treasuries. As a result, the broad U.S. fixed-income market significantly lagged Treasuries. Within the investment-grade fixed-income segment, commercial mortgage-backed securities suffered the worst, lagging Treasuries by 20%. Asset-backed securities - which are primarily collateralized by consumer debt - were down 12% relative to Treasuries. Investment-grade corporate bonds (as measured by the Barclay's Aggregate Bond Index) trailed like-duration Treasuries by 6%. High-yield corporate bonds fared even worse, trailing like-duration Treasuries by 25%.

PERFORMANCE

Investment results shown represent historical performance and do not guarantee future results. Investment returns and principal values fluctuate with changes in interest rates and other market conditions so the value, when redeemed may be worth more or less than original costs. Current performance may be lower or higher than the performance data shown. For more performance information, including most recent month-end performance, visit the Principal Sponsor Service Center℠ at www.principal.com, contact your representative of the Principal Financial Group®, or call our Client Contact Center at 1-800-547-7754.

The Gross Total Investment Expense (TIE Gross) figure does not reflect any waivers or caps on the mutual fund or underlying mutual fund in which a Separate Account invests. Returns displayed are always based on net total investment expense.

	QTD	YTD	1 YEAR	3 YEAR	5 YEAR	10 YEAR	SINCE INC.	T.I.E Gross	INC. DATE
SmallCap Growth III Separate Account-R6 [1, 2, 3]	-27.01	-46.43	-46.43	-14.64	-	-	-5.85	1.27	06/01/2004
Russell 2500 Growth Index	-27.77	-41.50	-41.50	-10.36	-2.24	0.75	-	-	-
Morningstar Small Growth Category Average	-26.65	-41.55	-41.55	-11.35	-3.52	1.51	-	-	-
Morningstar Small Growth Peer Ranking	-	-	86	84	-	-	-	-	-
Total Funds In Category	868	834	834	704	574	291	-	-	-

Please see important disclosures at the end of this document.

PERFORMANCE ANALYSIS

Primary Contributors and Detractors to Fund Performance during the last quarter:

Industry selection boosted results, as underweights to the poor-performing energy sector and real estate investment trusts, and an overweight to telecomm services, which performed well, were rewarded. On an individual-stock basis, the top-three positive contributors were an overweight to Cubist Pharmaceutical, lack of exposure to laggard Alpha Natural Resources and an underweight to another laggard, Covance Inc. On the negative side: Fundamental factors - including a higher price/earnings profile and a lower price/book profile relative to the index - were not beneficial. Also, security selection was modestly negative as weakness in consumer discretionary and telecomm were partially offset by strong results in health care and financials. Stocks detracting the most were an overweight to poor performer Polycom and out-of-index positions in Blackstone Group and Sunpower Corp.

Primary Contributors and Detractors to Fund Performance during the last 12 months:

Although security selection was generally a detractor, selection in health care and industrials was modestly positive. The top individual contributors were an overweight in (and timely exit from) Alpha Natural Resources, an underweight to poor-performing Whiting Pete Corp. and a lack of exposure to Sirius Xm Radio. On the negative side: Fundamental factor-positioning was not favorable due to an overweight to the most volatile stocks in the index as well as a higher price/earnings profile and lower price/book profile relative to the index. Security selection also hampered results, due primarily to weakness in information technology and consumer discretionary. Within information technology, overweights to Polycom and Rf Microdevices - as well as an out-of-index exposure to Flextronics International - hurt results. Within consumer discretionary, an out-of-index position in Crocs was the primary detractor.

EFFECT OF INVESTMENT STRATEGIES AND TECHNIQUES ON PORTFOLIO PERFORMANCE

Effective January 2009, Columbus Circle Investors (CCI) is responsible for 100% of the portfolio assets. The firm's investment strategies are based on the premise that companies doing better-than-expected will have rising securities prices, while companies producing less-than-expected results will not. This discipline is referred to as positive momentum and positive surprise. Through in-depth analysis of company fundamentals in the context of the prevailing economic environment, the portfolio management team selects companies that meet the criteria of positive momentum and positive surprise.

CHANGES TO THE INVESTMENT OPTION'S STRUCTURE OR PORTFOLIO

In January 2009 Mazama was terminated as a sub-advisor for this portfolio due to poor performance. CCI took over the assets previously managed by Mazama and now manages 100% of the portfolio. In May 2009, this portfolio is expected to merge (pending approval) into the Principal SmallCap Growth I portfolio, currently sub-advised by AllianceBernstein. Following the merger, the SmallCap Growth I portfolio will be co-sub-advised by AllianceBernstein and CCI.

TOP TEN HOLDINGS

Top 10 Holdings (% of Assets) as of 11/30/2008			
Polycom, Inc.	2.67	Riverbed Technology, Inc.	1.81
Cubist Pharmaceuticals, Inc.	2.45	Strayer Education, Inc.	1.50
Medarex, Inc.	2.29	SBA Communications Corporation	1.28
Red Hat, Inc.	1.84	SunPower Corporation	1.27
NASDAQ OMX Group, Inc.	1.84	Illumina, Inc.	1.26

DISCLOSURES

Separate Accounts are available through a group annuity contract with the Principal Life Insurance Company. Insurance products and plan administrative services are provided by Principal Life Insurance Company a member of the Principal Financial Group, Des Moines, IA 50392. See the group annuity contract for the full name of the Separate Account. Certain investment options may not be available in all states or U.S. commonwealths.

Since inception returns are only shown for funds/accounts in existence for less than 10 years. Returns shown for periods of less than one year are not annualized. All returns displayed here are after Total Investment Expense of the investment option.

Performance of indexes reflects the unmanaged result for the market segment the selected index represents. The index is not available for direct investments.

Percentile rankings are based on total returns.

Portfolio holdings are subject to change and companies referenced in this report may not currently be held. Information is current as of the creation of this piece. Keep in mind that portfolio holdings are subject to risk. For a complete list of the most recent publicly available holdings visit www.principal.com.

1. Small-cap and mid-cap investment options are subject to more fluctuation in value and may have additional risks than other investment options with stocks of larger, more stable companies.

2. This Separate Account invests solely in the Institutional class shares of the Principal Funds. All voting rights associated with ownership of shares in the mutual fund are the rights of the Separate Account, not of contract holders investing in the Separate Account. For further information on the underlying mutual fund, see the prospectus of the fund.

3. Effective January 21, 2009, this portfolio is sub-advised by Columbus Circle Investors. Prior to January 21, 2009, the portfolio was sub-advised by Mazama Capital Management and Columbus Circle Investors. The portfolio has had various sub-advisors since its inception. Performance results displayed reflect all sub-advisors managing this portfolio during the time periods displayed.

Benchmark Description

Russell 2500 Growth Index tracks the 2,500 smallest companies in the Russell 3000 Index having higher price-to-book ratio and higher forecasted growth values.