PROLOGIS
Form 10-K
March 02, 2009

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2008

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission File Number 1-12846

(Exact name of registrant as specified in its charter)

Maryland	**74-2604728**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)

4545 Airport Way
Denver, CO 80239
(Address of principal executive offices and zip code)

(303) 567-5000
(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	**Name of each exchange on which registered**
Common Shares of Beneficial Interest, par value $0.01 per share	New York Stock Exchange
Series F Cumulative Redeemable Preferred Shares of Beneficial Interest, par value $0.01 per share	New York Stock Exchange
Series G Cumulative Redeemable Preferred Shares of Beneficial Interest par value $0.01 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **NONE**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes þ No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes o No þ

Based on the closing price of the registrant s shares on June 30, 2008, the aggregate market value of the voting common equity held by non-affiliates of the registrant was $14,228,109,100.

At February 20, 2009, there were outstanding approximately 267,604,300 common shares of beneficial interest of the registrant.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s definitive proxy statement for the 2009 annual meeting of its shareholders are incorporated by reference in Part III of this report.

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Certain statements contained in this discussion or elsewhere in this report may be deemed forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Words and phrases such as expects , anticipates , intends , plans , believes , seeks , estimates , designed to achieve , variations of such words and similar expressio intended to identify such forward-looking statements, which generally are not historical in nature. All statements that address operating performance, events or developments that we expect or anticipate will occur in the future including statements relating to rent and occupancy growth, development activity and changes in sales or contribution volume or profitability of developed properties, economic and market conditions in the geographic areas where we operate and the availability of capital in existing or new property funds are forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Although we believe the expectations reflected in any forward-looking statements are based on reasonable assumptions, we can give no assurance that our expectations will be attained and therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. Many of the factors that may affect outcomes and results are beyond our ability to control. For further discussion of these factors see Item 1A. Risk Factors in this annual report on Form 10-K. All references to we , us and our refer to ProLogis an our consolidated subsidiaries.

PART I

ITEM 1. Business

ProLogis is a leading global provider of industrial distribution facilities. We are a Maryland real estate investment trust (REIT) and have elected to be taxed as such under the Internal Revenue Code of 1986, as amended (the Code). Our world headquarters is located in Denver, Colorado. Our European headquarters is located in the Grand Duchy of Luxembourg with our European customer service headquarters located in Amsterdam, the Netherlands. Our primary office in Asia is located in Tokyo, Japan.

Our Internet website address is www.prologis.com. All reports required to be filed with the Securities and Exchange Commission (the SEC) are available or may be accessed free of charge through the Investor Relations section of our Internet website as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Our Internet website and the information contained therein or connected thereto are not intended to be incorporated into this Annual Report on Form 10-K. Our common shares trade under the ticker symbol PLD on the New York Stock Exchange.

We were formed in 1991, primarily as a long-term owner of industrial distribution space operating in the United States. Over time, our business strategy evolved to include the development of properties for contribution to property funds in which we maintain an ownership interest and the management of those property funds and the properties they own. Originally, we sought to differentiate ourselves from our competition by focusing on our corporate customers distribution space requirements on a national, regional and local basis and providing customers with consistent levels of service throughout the United States. However, as our customers needs expanded to markets outside the United States, so did our portfolio and our management team. Today we are an international real estate company with operations in North America, Europe and Asia. Our business strategy is to integrate international scope and expertise with a strong local presence in our markets, thereby becoming an attractive choice for our targeted customer base, the largest global users of distribution space, while achieving long-term sustainable growth in cash flow.

Industrial distribution facilities are a crucial link in the modern supply chain, and they serve three primary purposes for supply-chain participants: (i) ensure accurate and seamless flow of goods to their appointed destinations; (ii) function as processing centers for goods; and (iii) enable companies to store enough inventory to meet surges in demand and to cushion themselves from the impact of a break in the supply chain.

At December 31, 2008, our total portfolio of properties owned, managed and under development, including direct-owned properties and properties owned by property funds and joint ventures that we manage, and

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excluding properties held for sale, consisted of the following properties in North America, Europe and Asia, broken down as follows:

	Number of Properties	Square Feet (in thousands)
Square feet owned, managed and under development:		
Direct owned:		
Industrial properties:		
Operating properties	1,297	195,710
Properties under development	65	19,837
Retail and mixed use properties	34	1,404
Total direct owned	1,396	216,951
Investment management-industrial properties	1,339	297,665
Total properties owned and under management	2,735	514,616

Business Strategy

Recently, the global financial markets have been undergoing pervasive and fundamental disruptions, which began to impact us late in the third quarter of 2008. As the global credit crisis worsened in the fourth quarter, it was necessary for us to modify our business strategy. As such, we discontinued most of our new development and acquisition activities in order to focus on our core business of owning and managing industrial properties. Narrowing our focus has allowed us to take the necessary steps toward reducing our debt and maximizing liquidity and cash flow. We believe our current business strategy, coupled with the following objectives for both the near and long-term, will position us to take advantage of business opportunities upon the stabilization of the global financial markets.

Near-term objectives:

- Simplify our business model and focus on our core business;
- Complete the development and leasing of properties currently in our development portfolio;
- Manage our core portfolio of industrial distribution properties to maintain and improve our net operating income stream from these assets;
- Provide exceptional customer service to our current and future customers;
- Generate liquidity through contributions of properties to our property funds and through sales to third parties;
- Reduce our debt at December 31, 2009 by $2 billion from our debt levels at September 30, 2008, through debt retirements; utilizing proceeds from property contributions and dispositions and other possible means, such as buying back outstanding debt and issuing additional equity;
- Recast our global line of credit; and

- Reduce our general and administrative expenses through various cost savings initiatives, including reductions in workforce.

Longer-term objectives:

- Employ a conservative growth expansion model;
- Develop industrial properties utilizing a portion of our existing land parcels, which we will hold for long-term direct investment, or otherwise monetize our land holdings through dispositions; and
- Grow the property funds by utilizing the property fund structure for the development of properties and the opportunistic acquisition of properties from third parties.

During the fourth quarter of 2008, we took the following steps that we believe will position us to accomplish the objectives identified above:

Appointed a new Chief Executive Officer;

Reduced our expected annual distribution rate from $2.07 to $1.00 per common share;

Halted the start of substantially all new development activity, other than those we were contractually committed to complete;

Entered into a binding contract to sell our China operations and our 20% equity interest in the Japan property funds for $1.3 billion of cash. This transaction closed in February 2009 with the receipt of $500 million that was used to pay down debt. The remaining proceeds will be funded upon satisfactory completion of year-end financial statement audits of certain entities. In the event that the audits reflect a material disparity from the unaudited information previously furnished, the buyer will have the option to unwind the transaction. (See Note 21 to our Consolidated Financial Statements in Item 8);

Purchased $310 million aggregate principal of our senior notes for $217 million in cash;

Received proceeds of $1.3 billion from the contribution or sale of properties to unconsolidated property funds or third parties; and

Implemented a reduction in workforce (RIF) plan that, along with other initiatives, will reduce our gross general and administrative expenses on a prospective basis by approximately $100 million in 2009.

Our Operating Segments

The following discussion of our business segments should be read in conjunction with Item 1A. Risk Factors , our property information presented in Item 2. Properties , Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations and Note 19 to our Consolidated Financial Statements in Item 8.

Our business was previously organized into three reportable business segments: (i) direct owned (previously called property operations); (ii) investment management; and (iii) development or CDFS business. Due to recent economic conditions, we have modified our business strategy and, as a result, we will no longer perform the investment and development activities within our CDFS business segment. As a result, we transferred all of our real estate and other assets that were in our development pipeline to our direct owned segment and we transferred our investments in industrial and retail joint ventures to our investment management segment. The discussion that follows discusses the segments as they were through 2008, as well as what we expect them to be on a prospective basis. Our China operations, which were sold in February 2009, are presented as held for sale at December 31, 2008 and not included in the discussion that follows.

Operating Segments Direct Owned

Our direct owned segment represents the long-term ownership of industrial properties. Our investment strategy in this segment focuses primarily on the ownership and leasing of industrial and retail properties in key distribution markets. We consider these properties to be our Core Properties. Also included in this segment are real estate properties that were previously acquired or developed within our CDFS business segment and that, because changes in our business strategy, were transferred to this segment due to our current intent to hold and operate these assets on a long-term

basis. These include operating properties that we previously developed with the intent to contribute to an unconsolidated property fund. We now refer to these properties as Completed Development Properties. We also have industrial properties that are currently under development and land available for development that are part of this segment, the majority of which we plan to hold and use in this segment.

Investments

At December 31, 2008, the following properties are in the direct owned segment (square feet and investment in thousands):

	Number of Properties	Square Feet/Acres		Investment (before depreciation) at December 31, 2008	Leased Percentage
Core Properties	1,191	156,351 square feet	$	8,284,011	92.2%
Completed Development Properties	140	40,763 square feet	$	3,031,449	43.5%
Properties under development	65	19,837 square feet	$	1,163,610	37.2%
Land held for development		10,134 acres	$	2,481,216	n/a

These properties are located in North America, Europe and Asia.

In the near term, we may occasionally acquire a property for this segment, generally to satisfy certain tax requirements that may arise due to the previous sale of a property.

Results of Operations

We earn rent from our customers, including reimbursement of certain operating costs, under long-term operating leases (with an average lease term of six to seven years at December 31, 2008). The revenue in this segment decreased in 2008 primarily due to the contribution of properties to property funds, offset partially by increases in occupancy levels within our development properties. However, due to current market challenges, leasing activity has slowed and rental revenues generated by the lease-up of newly developed properties have not been adequate to completely offset the loss of rental revenues from property contributions. We expect our total revenues from this segment will decrease in 2009 due to the contributions and dispositions of properties we made in 2008 and may make in 2009. We intend to grow our revenue in the remaining properties primarily through increases in occupied square feet in our Completed Development Properties and properties currently under development. The costs of our property management function for both our direct-owned portfolio and the properties owned by the property funds and managed by us are reported in rental expenses in the direct owned segment. As the portfolio of properties we manage has continued to grow, the related property management expenses have increased causing a decrease in margins and profitability in this segment (offset by increases in the investment management segment).

Market Presence

At December 31, 2008, our 1,331 operating properties in this segment aggregating 197.1 million square feet were located in 40 markets in North America (33 markets in the United States, 6 markets in Mexico and 1 market in Canada), 29 markets in Europe (Belgium, the Czech Republic, France, Germany, Hungary, Italy, the Netherlands, Poland, Romania, Slovakia, Spain, Sweden and the United Kingdom) and 6 markets in Asia (Japan and South Korea). Our largest markets for this segment in North America (based on our investment in the properties) are Atlanta, Chicago, Dallas/Fort Worth, Inland Empire, Los Angeles, New Jersey and San Francisco (East Bay). Our largest investment in Europe is in the United Kingdom and our largest investment in Asia is in Japan. Our 65 properties under development at December 31, 2008 aggregated 19.8 million square feet and were located in 8 markets in North

America, 23 markets in Europe and 3 markets in Asia. At December 31, 2008, we owned 10,134 acres of land with an investment of $2.5 billion and located in North America (6,400 acres, $1.1 billion investment), Europe (3,614 acres, $1.1 billion investment) and Asia (120 acres, $0.3 billion investment). See further detail in Item 2. Properties .

Competition

The existence of competitively priced distribution space available in any market could have a material impact on our ability to rent space and on the rents that we can charge. To the extent we wish to acquire land for future development of properties in our direct owned segment, we may compete with local, regional, and

national developers. We also face competition from other investment managers in attracting capital for our property funds to be utilized to acquire properties from us or third parties.

We believe we have competitive advantages due to (i) our ability to quickly respond to customer s needs for high-quality distribution space in key global distribution markets; (ii) our established relationships with key customers serviced by our local personnel; (iii) our ability to leverage our organizational structure to provide a single point of contact for our global customers; (iv) our property management and leasing expertise; (v) our relationships and proven track record with current and prospective investors in the property funds; (vi) our global experience in the development and management of industrial properties; (vii) the strategic locations of our land positions; and (viii) our personnel who are experienced in the land acquisition and entitlement process.

Property Management

Our business strategy includes a customer service focus that enables us to provide responsive, professional and effective property management services at the local level. To enhance our management services, we have developed and implemented proprietary operating and training systems to achieve consistent levels of performance and professionalism and to enable our property management team to give the proper level of attention to our customers. We manage substantially all of our operating properties.

Customers

We have developed a customer base that is diverse in terms of industry concentration and represents a broad spectrum of international, national, regional and local distribution space users. At December 31, 2008, in our direct owned segment, we had 2,815 customers occupying 157.3 million square feet of industrial and retail space. Our largest customer and 25 largest customers accounted for 1.9% and 11.8%, respectively, of our annualized collected base rents at December 31, 2008.

Employees

We employ 1,480 persons in our entire business. Our employees work in three countries in North America (840 persons), in 13 countries in Europe (490 persons) and in 2 countries in Asia (150 persons). Of the total, we have assigned 890 employees to our direct owned segment and 80 employees to our investment management segment. We have 510 employees who work in corporate positions who are not assigned to a segment who may assist with segment activities. We believe our relationships with our employees are good. Our employees are not organized under collective bargaining agreements, although some of our employees in Europe are represented by statutory Works Councils and benefit from applicable labor agreements. Our China operations are held for sale as of December 31, 2008 and the 240 employees in China are not included in the information above.

Future Plans

Our current business plan allows for the limited expansion of operating properties as necessary to: (i) address the specific expansion needs of customers; (ii) enhance our market presence in a specific country, market or submarket; (iii) take advantage of opportunities where we believe we have the ability to achieve favorable returns; and (iv) monetize our existing land positions through pre-committed development of industrial properties to hold and use in this segment. In addition, we expect to complete the development and leasing of our properties under development. As of December 31, 2008, we had 65 properties under development with a current investment of $1.2 billion and a total expected investment, when completed and leased, of $1.9 billion. These properties were 37.2% leased at December 31, 2008.

In 2009, we intend to fund our investment activities in the direct owned segment, depending on market conditions and other factors, primarily with operating cash flow from this segment, borrowings under existing credit facilities, equity issuances and proceeds from contributions and dispositions of properties. In the future, depending on market conditions and the capital available from our fund partners, we may contribute Core Properties and/or Completed Development Properties to the property funds or sell to a third party.

Operating Segments Investment Management

The investment management segment represents the investment management of unconsolidated property funds and certain joint ventures and the properties they own. We utilize our investment management expertise to manage the property funds and certain joint ventures and we utilize our leasing and property management expertise to manage the properties owned by these entities. We report the property management costs, for both our direct owned segment and the properties owned by the property funds, in rental expenses in the direct owned segment and we include the fund management costs in general and administrative expenses.

Our property fund strategy:

- allows us, as the manager of the property funds, to maintain and expand our market presence and customer relationships;
- allows us to maintain a long-term ownership position in the properties;
- allows us to earn fees for providing services to the property funds; and
- provides us an opportunity to earn incentive performance participation income based on the investors returns over a specified period.

Historically, our property fund strategy has also:

- allowed us to realize a portion of the profits from our development activities by contributing our stabilized development properties to property funds (profits are recognized to the extent of third party ownership in the property fund); and
- provided diversified sources of capital.

Although we may continue to make contributions of properties to the property funds, due to the current market conditions, including increasing capitalization rates, we do not expect to recognize gains at the level we have in the past. See further discussion in Operating Segments CDFS Business below.

Investments

As of December 31, 2008, we had investments in and advances to 17 property funds totaling $2.0 billion with ownership interests ranging from 20% to 50%. These investments are in North America 12 aggregating $941.7 million; Europe 2 aggregating $634.6 million; and Asia 3 aggregating $381.7 million. These property funds own, on a combined basis, 1,336 distribution properties aggregating 296.9 million square feet with a total entity investment (not our proportionate share) in operating properties of $24.7 billion. Also included in this segment are certain industrial and retail joint ventures, which we manage and that own 3 operating properties with 0.7 million square feet located in North America and Europe.

In December, we entered into a binding agreement to sell our 20% equity investments in our property funds in Japan to our fund partner. Our investments in the Japan property funds aggregated $359.8 million. These property funds owned 70 properties totaling 27.0 million square feet. In this same agreement, we agreed to sell our China operations, which include our investments in a property fund and joint ventures, which are classified as held for sale as of December 31, 2008 and are not included above.

Results of Operations

We recognize our proportionate share of the earnings or losses from our investments in unconsolidated property funds and certain joint ventures. In addition to the income recognized under the equity method, we recognize fees and incentives earned for services performed on behalf of these entities and interest earned on advances to these entities, if any. We provide services to these entities, such as property management, asset management, acquisition, financing and development. We may also earn incentives from our property funds depending on the return provided to the fund partners over a specified period. We expect any future growth in income recognized to result from growth in existing property funds, primarily from properties the funds

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acquired from us in 2008 and may acquire, from us or third parties, in the future, as well as the formation of future funds.

Market Presence

At December 31, 2008, the property funds on a combined basis owned 1,336 properties aggregating 296.9 million square feet located in 44 markets in North America (Canada, Mexico and the United States), 35 markets in Europe (Belgium, the Czech Republic, France, Germany, Hungary, Italy, the Netherlands, Poland, Slovakia, Spain, Sweden, and the United Kingdom) and 10 markets in Asia (Japan and South Korea). The industrial and retail joint ventures included in this segment are located in the United States and the United Kingdom and operate 3 industrial properties with 0.7 million square feet.

Competition

As the manager of the property funds, we compete with other fund managers for institutional capital. As the manager of the properties owned by the property funds, we compete with other industrial properties located in close proximity to the properties owned by the property funds. The amount of rentable distribution space available and its current occupancy in any market could have a material effect on the ability to rent space and on the rents that can be charged by the fund properties. We believe we have competitive advantages as discussed above in Operating Segments Direct Owned .

Property Management

We manage the properties owned by unconsolidated investees utilizing our leasing and property management experience from the employees who are in our direct owned segment. Our business strategy includes a customer service focus that enables us to provide responsive, professional and effective property management services at the local level. To enhance our management services, we have developed and implemented proprietary operating and training systems to achieve consistent levels of performance and professionalism and to enable our property management team to give the proper level of attention to our customers.

Customers

As in our direct owned segment, we have developed a customer base in the property funds and joint ventures that is diverse in terms of industry concentration and represents a broad spectrum of international, national, regional and local distribution space users. At December 31, 2008, our unconsolidated investees, on a combined basis, had 2,052 customers occupying 284.6 million square feet of distribution space. The largest customer and 25 largest customers of our unconsolidated investees, on a combined basis, accounted for 3.8% and 29.3%, respectively, of the total combined annualized collected base rents at December 31, 2008. In addition, in this segment we consider our fund partners to also be our customers. As of December 31, 2008, we partnered with 41 institutional investors, several of which invest in multiple funds.

Employees

The property funds generally have no employees of their own. Employees in our direct owned segment are responsible for the management of the properties owned by the property funds. We have assigned 80 additional employees directly to the management of the property funds in our investment management segment. We have 510 employees who work in corporate positions and are not assigned to a segment who may assist with these activities as well.

Future Plans

We expect to continue to increase our investments in property funds, although at a slower pace than in the past. We expect to achieve these increases through the existing property funds acquisition of properties from us, as well as from third parties. We expect the fee income we earn from the property funds and our proportionate share of net earnings of the property funds will increase as the size and value of the portfolios

owned by the property funds grows and as more equity is deployed in the funds. We will continue to explore our options related to both new and existing property funds.

Operating Segments   CDFS Business

Given the challenges that we are facing in this current economic environment and the corresponding changes we have made to our business strategy, we do not expect to have a CDFS business segment in 2009. As of December 31, 2008, all of the assets and liabilities that were in this segment have been transferred to our two remaining segments. We transferred all of our real estate and other assets that were in our development pipeline to our direct owned segment. Our investments in certain joint ventures were transferred to our investment management segment. As noted above, we may contribute Completed Development Properties and/or Core Properties to the property funds or sell to third parties, although these will no longer be reported in our CDFS business segment. Through the end of 2008, this segment primarily included the contribution of industrial properties we had developed or acquired with the intent to contribute to a property fund in which we had an ownership interest and acted as manager. At December 31, 2008, we had no investments remaining in this segment.

Other

We have other segments that do not meet the threshold criteria to disclose as a reportable segment. At December 31, 2008, these operations include primarily the management of land subject to ground leases.

Our Management

Our executive management team consists of:

Walter C. Rakowich, Chief Executive Officer

Ted R. Antenucci, Chief Investment Officer

Edward S. Nekritz, General Counsel and Secretary

William E. Sullivan, Chief Financial Officer

Mr. Rakowich also serves as a member of our Board of Trustees (the   Board).

In addition to the leadership and oversight provided by our executive management team, our investments and operations are overseen by Charles E. Sullivan, Head of Global Operations, John R. Rizzo, Managing Director of Global Development, Larry Harmsen, Managing Director for North America Capital Deployment, Ralf Wessel, Managing Director Global Investment Management, Silvano Solis, Regional Director   Mexico, Gary E. Anderson, Europe President, Philip Dunne, Europe Chief Operating Officer and Chief Financial Officer and Mike Yamada, Japan Co-President. Further, in the United States, two individuals lead each of our five regions (Central, Midwest, Northeast/Canada, Pacific and Southeast), one of whom is responsible for operations and one of whom is responsible for capital deployment. In Europe, each of the four regions (Northern Europe, Central Europe, Southern Europe and the United Kingdom) are led by either one or two individuals responsible for operations and capital deployment. John P. Morland is Managing Director of Global Human Resources.

Throughout 2008, Masato Miki served as our Japan Co-President. With the sale of our property fund investments in Japan, Mr. Miki is expected to become an employee of the buyer.

We maintain a Code of Ethics and Business Conduct applicable to our Board and all of our officers and employees, including the principal executive officer, the principal financial officer and the principal accounting officer, or persons performing similar functions. A copy of our Code of Ethics and Business Conduct is available on our website, www.prologis.com. In addition to being accessible through our website, copies of our Code of Ethics and Business Conduct can be obtained, free of charge, upon written request to Investor Relations, 4545 Airport Way, Denver, Colorado 80239. Any amendments to or waivers of our Code of Ethics and Business Conduct that apply to the principal executive officer, the principal financial officer, or the

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principal accounting officer, or persons performing similar functions, and that relate to any matter enumerated in Item 406(b) of Regulation S-K, will be disclosed on our website.

Capital Management and Capital Deployment

We have a team of professionals responsible for managing and leasing our properties and those owned by the property funds that we manage. We have market officers who are primarily responsible for understanding and meeting the needs of existing and prospective customers in their respective markets. In addition, the market officers, along with their team of property management and leasing professionals, use their knowledge of local market conditions to assist the Global Solutions Group in identifying and accommodating those customers with multiple market requirements and assisting in the marketing efforts directed at those customers. Access to our national and international resources enhance the market officers ability to serve customers in the local market. The focus of the market officers is on: (i) creating and maintaining relationships with customers, potential customers and industrial brokers; (ii) managing the capital invested in their markets; (iii) leasing our properties; and (iv) identifying potential acquisition and development opportunities in their markets.

Capital deployment is the responsibility of a team of professionals who ensure that our capital resources are deployed in an efficient and productive manner that will best serve our long-term objective of increasing shareholder value. The team members responsible for capital deployment evaluate acquisition, disposition and development opportunities in light of market conditions in their respective regions and our overall goals and objectives. Capital deployment officers work closely with the Global Development Group to, among other things, create master-planned distribution parks utilizing the extensive experience of the Global Development Group team members. The Global Development Group incorporates the latest technology with respect to building design and systems and has developed standards and procedures that we strictly adhere to in the development of all properties to ensure that properties we develop are of a consistent quality.

We strive to minimize the ecological footprint of our developments worldwide by meeting or exceeding relevant local or regional green building design standards. All of our future developments in the United States will comply with the U.S.Green Building Council s standards for Leadership in Energy and Environmental Design (LEED®). In the United Kingdom, we are committed to developing any new properties to achieve at least a Very Good rating in accordance with the Building Research Establishment s Environmental Assessment Method (BREEAM). In Japan, many of our facilities comply with the Comprehensive Assessment System for Building Environmental Efficiency (CASBEE). In countries where no green building rating system exists, we utilize a global standards checklist based on these three leading regional rating systems. In total, counting all three rating systems, ProLogis has 20 million square feet (1.8 million square meters) of development registered or certified as green buildings.

Customer Service

The Global Solutions Group s primary focus is to position us as the preferred provider of distribution space to large users of industrial distribution space. The professionals in the Global Solutions Group also seek to build long-term relationships with our existing customers by addressing their distribution and logistics needs. The Global Solutions Group provides our customers with outsourcing options for network optimization tools, strategic site selection assistance, business location services, material handling equipment and design consulting services.

Executive and Senior Management

*Walter C. Rakowich** 51 Chief Executive Officer of ProLogis since November 2008. Mr. Rakowich was ProLogis President and Chief Operating Officer from January 2005 to November 2008 and ProLogis Chief Financial Officer from December 1998 to September 2005. Mr. Rakowich has been with ProLogis in various capacities since July 1994.

Prior to joining ProLogis, Mr. Rakowich was a consultant to ProLogis in the area of due diligence and acquisitions and he was a principal with Trammell Crow Company, a diversified commercial real estate company in North America. Mr. Rakowich served on the Board from August 2004 to May 2008 and was reappointed to the Board in November 2008.

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*Ted R. Antenucci** 44 Chief Investment Officer since May 2007. Mr. Antenucci was ProLogis President of Global Development from September 2005 to May 2007. From September 2001 to September 2005, Mr. Antenucci was president of Catellus Commercial Development Corporation, an industrial and retail real estate company that was merged with ProLogis in September 2005. Mr. Antenucci was with affiliates of Catellus Commercial Development Corporation in various capacities from April 1999 to September 2001.

*Edward S. Nekritz** 43 General Counsel of ProLogis since December 1998 and Secretary of ProLogis since March 1999. Mr. Nekritz oversees legal services, due diligence and risk management for ProLogis. Mr. Nekritz has been with ProLogis in various capacities since September 1995. Prior to joining ProLogis, Mr. Nekritz was an attorney with Mayer, Brown & Platt (now Mayer Brown LLP).

*William E. Sullivan** 54 Chief Financial Officer since April 2007. Prior to joining ProLogis, Mr. Sullivan was the founder and president of Greenwood Advisors, Inc., a financial consulting and advisory firm focused on providing strategic planning and implementation services to small and mid-cap companies since 2005. From 2001 to 2005, Mr. Sullivan was chairman and chief executive officer of SiteStuff, an online procurement company serving the real estate industry and he continued as their chairman through June 2007.

Gary E. Anderson 43 Europe President since November 2008 and President and Chief Operating Officer since November 2006 where he is responsible for investment, development, leasing and operations in the European countries in which ProLogis operates. Mr. Anderson was the Managing Director responsible for investments and development in ProLogis Central and Mexico Regions from May 2003 to November 2006 and has been with ProLogis in various capacities since August 1994. Prior to joining ProLogis, Mr. Anderson was in the management development program of Security Capital Group, a real estate holding company.

John P. Morland 50 Managing Director of Global Human Resources since October 2006, where he is responsible for strategic human resources initiatives to align ProLogis human capital strategy with overall business activities. Prior to joining ProLogis, Mr. Morland was the Global Head of Compensation at Barclays Global Investors at its San Francisco headquarters from April 2000 to March 2005.

*Charles E. Sullivan ** 51 Head of Global Operations since February 2009 where he has overall responsibility for global operations, including property management, leasing, information technology, marketing and global customer relationships. Mr. Sullivan was Managing Director of ProLogis with overall responsibility for operations in North America from October 2006 to February 2009 and has been with ProLogis in various capacities since October 1994. Prior to joining ProLogis, Mr. Sullivan was an industrial broker with Cushman & Wakefield of Florida, a real estate brokerage and services company.

Mike Yamada 55 Japan Co-President since March 2006, where he is responsible for development and leasing activities in Japan. Mr. Yamada was a Managing Director with ProLogis from December 2004 to March 2006 with similar responsibilities in Japan. He has been with ProLogis in various capacities since April 2002. Prior to joining ProLogis, Mr. Yamada was a senior officer of Fujita Corporation, a construction company in Japan.

* These individuals are our Executive Officers under Item 401 of Regulation S-K.

Environmental Matters

We are exposed to various environmental risks that may result in unanticipated losses that could affect our operating results and financial condition. A majority of the properties we have acquired were subjected to environmental reviews by either us or the previous owners. While some of these assessments have led to further investigation and sampling, none of the environmental assessments has revealed an environmental liability that we believe would have a

material adverse effect on our business, financial condition or results of operations. See Note 18 to our Consolidated Financial Statements in Item 8 and Item 1A. Risk Factors.

Insurance Coverage

We carry insurance coverage on our properties. We determine the type of coverage and the policy specifications and limits based on what we deem to be the risks associated with our ownership of properties and other

of our business operations in specific markets. Such coverage includes property, liability, fire, named windstorm, flood, earthquake, environmental, terrorism, extended coverage and rental loss. We believe that our insurance coverage contains policy specifications and insured limits that are customary for similar properties, business activities and markets and we believe our properties are adequately insured. However, an uninsured loss could result in loss of capital investment and anticipated profits.

ITEM 1A. Risk Factors

Our operations and structure involve various risks that could adversely affect our financial condition, results of operations, distributable cash flow and the value of our common shares. These risks include, among others:

Current Events

The recent market disruptions may adversely affect our operating results and financial condition.

The global financial markets have been undergoing pervasive and fundamental disruptions. The continuation or intensification of such volatility may lead to additional adverse impact on the general availability of credit to businesses and could lead to a further weakening of the U.S. and global economies. To the extent that turmoil in the financial markets continues and/or intensifies, it has the potential to materially affect the value of our properties and our investments in our unconsolidated investees, the availability or the terms of financing that we and our unconsolidated investees have or may anticipate utilizing, our ability and that of our unconsolidated investees to make principal and interest payments on, or refinance, any outstanding debt when due and/or may impact the ability of our customers to enter into new leasing transactions or satisfy rental payments under existing leases. The current market disruption could also affect our operating results and financial condition as follows:

Debt and Equity Markets Our results of operations and share price are sensitive to the volatility of the credit markets. The commercial real estate debt markets are currently experiencing volatility as a result of certain factors, including the tightening of underwriting standards by lenders and credit rating agencies and the significant inventory of unsold collateralized mortgage backed securities in the market. Credit spreads for major sources of capital have widened significantly as investors have demanded a higher risk premium, resulting in lenders increasing the cost for debt financing. Should the overall cost of borrowings increase, either by increases in the index rates or by increases in lender spreads, we will need to factor such increases into the economics of our acquisitions, developments and property contributions and dispositions. This may result in lower overall economic returns and a reduced level of cash flow, which could potentially impact our ability to make distributions to our shareholders and to comply with certain debt covenants. In addition, the recent dislocations in the debt markets have reduced the amount of capital that is available to finance real estate, which, in turn: (i) limits the ability of real estate investors to benefit from lower real estate values; (ii) has slowed real estate transaction activity; and (iii) may result in an inability to refinance debt as it becomes due, all of which may reasonably be expected to have a material adverse impact on revenues, income and/or cash flow from the acquisition and operations of real properties and mortgage loans. In addition, the state of the debt markets could have an impact on the overall amount of capital being invested in real estate, which may result in price or value decreases of real estate assets and impact the ability to raise equity capital for us and within our unconsolidated investees.

Valuations The recent market volatility will likely make the valuation of our properties and those of our unconsolidated investees more difficult. There may be significant uncertainty in the valuation, or in the stability of the value, of our properties and those of our unconsolidated investees, that could result in a substantial decrease in the value of our properties and those of our unconsolidated investees. As a result, we may not be able to recover the current carrying amount of our properties, our investments in our unconsolidated investees and/or goodwill, which may require us to recognize an impairment charge in earnings in addition to the charges we recognized in

the fourth quarter of 2008. Additionally, certain of the fees we generate from our unconsolidated investees are dependent upon the value of the properties held by the investees or the level of contributions we make to the investees. Therefore, if property values decrease or our level of contributions decrease, certain fees paid to us by our unconsolidated investees may also decrease.

Government Intervention The pervasive and fundamental disruptions that the global financial markets are currently undergoing have led to extensive and unprecedented governmental intervention. Such intervention has in certain cases been implemented on an emergency basis, suddenly and substantially eliminating market participants ability to continue to implement certain strategies or manage the risk of their outstanding positions. It is impossible to predict what, if any, additional interim or permanent governmental restrictions may be imposed on the markets and/or the effect of such restrictions on us and our results of operations. There is a high likelihood of significantly increased regulation of the financial markets that could have a material impact on our operating results and financial condition.

General Real Estate Risks

General economic conditions and other events or occurrences that affect areas in which our properties are geographically concentrated, may impact financial results.

We are exposed to the general economic conditions, the local, regional, national and international economic conditions and other events and occurrences that affect the markets in which we own properties. Our operating performance is further impacted by the economic conditions of the specific markets in which we have concentrations of properties. Approximately 24.3% of our direct owned operating properties (based on our investment before depreciation) are located in California. Properties in California may be more susceptible to certain types of natural disasters, such as earthquakes, brush fires, flooding and mudslides, than properties located in other markets and a major natural disaster in California could have a material adverse effect on our operating results. We also have significant holdings (defined as more than 3.0% of our total investment before depreciation in direct owned operating properties), in certain markets located in Atlanta, Chicago, Dallas/Fort Worth, New Jersey, Japan and the United Kingdom. Our operating performance could be adversely affected if conditions become less favorable in any of the markets in which we have a concentration of properties. Conditions such as an oversupply of distribution space or a reduction in demand for distribution space, among other factors, may impact operating conditions. Any material oversupply of distribution space or material reduction in demand for distribution space could adversely affect our results of operations, distributable cash flow and the value of our securities. In addition, the property funds and joint ventures in which we have an ownership interest have concentrations of properties in the same markets mentioned above, as well as Pennsylvania, Reno, France and Poland and are subject to the economic conditions in those markets.

Real property investments are subject to risks that could adversely affect our business.

Real property investments are subject to varying degrees of risk. While we seek to minimize these risks through geographic diversification of our portfolio, market research and our property management capabilities, these risks cannot be eliminated. Some of the factors that may affect real estate values include:

local conditions, such as an oversupply of distribution space or a reduction in demand for distribution space in an area;

the attractiveness of our properties to potential customers;

competition from other available properties;

our ability to provide adequate maintenance of, and insurance on, our properties;

our ability to control rents and variable operating costs;

governmental regulations, including zoning, usage and tax laws and changes in these laws; and

potential liability under, and changes in, environmental, zoning and other laws.

Our investments are concentrated in the industrial distribution sector and our business would be adversely affected by an economic downturn in that sector or an unanticipated change in the supply chain dynamics.

Our investments in real estate assets are primarily concentrated in the industrial distribution sector. This concentration may expose us to the risk of economic downturns in this sector to a greater extent than if our business activities were more diversified.

Our real estate development strategies may not be successful.

We have developed a significant number of industrial properties since our inception. In late 2008, we scaled back our development activities in response to current economic conditions. Although, we do expect to pursue development activities in the future, our near- term strategy is to complete and lease the buildings currently in development and lease the properties we have recently completed. As of December 31, 2008, we had 140 Completed Development Properties that were 43.5% leased (23.0 million square feet of unleased space) and we had 65 industrial properties that were under development that were 37.2% leased (12.5 million square feet of unleased space). As of December 31, 2008, we had approximately $885.4 million of costs remaining to be spent related to our development portfolio to complete the development and lease the space in these properties.

Additionally as of December 31, 2008, we had 10,134 acres of land with a current investment of $2.5 billion for potential future development of industrial properties or other commercial real estate projects or for sale to third parties. Within our land positions, we have concentrations in many of the same markets as our operating properties. Approximately 16.8% of our land (based on the current investment balance) is in the United Kingdom. During 2008, we recorded impairment charges of $194.2 million, predominantly in the United Kingdom, due to the decrease in current estimated fair value of the land and increased probability that we will dispose of certain land parcels rather than develop as previously planned. We will look to monetize the land in the future through sale to third parties, development of industrial properties to own and use or sale to an unconsolidated investee for development, depending on market conditions and other factors.

We will be subject to risks associated with such development and disposition activities, all of which may adversely affect our results of operations and available cash flow, including, but not limited to:

- the risk that we may not be able to lease the available space in our properties under development or recently completed developments at rents that are sufficient to be profitable;

- the risk that we will decide to sell certain land parcels and we will not be able to find a third party to acquire such land or that the sales price will not allow us to recover our investment, resulting in additional impairment charges;

- the risk that development opportunities explored by us may be abandoned and the related investment will be impaired;

- the risk that we may not be able to obtain, or may experience delays in obtaining, all necessary zoning, building, occupancy and other governmental permits and authorizations;

- the risk that due to the increased cost of land our activities may not be as profitable, especially in certain land constrained areas;

- the risk that construction costs of a property may exceed the original estimates, or that construction may not be concluded on schedule, making the project less profitable than originally estimated or not profitable at all;

including the possibility of contract default, the effects of local weather conditions, the possibility of local or national strikes and the possibility of shortages in materials, building supplies or energy and fuel for equipment; and

the risk that occupancy levels and the rents that can be earned for a completed project will not be sufficient to recover our investment.

Our business strategy to provide liquidity to reduce debt by contributing properties to property funds or disposing of properties to third parties may not be successful.

Our ability to contribute or sell properties on advantageous terms is affected by competition from other owners of properties that are trying to dispose of their properties, current market conditions, including the capitalization rates applicable to our properties, and other factors beyond our control. The property funds or third parties who might acquire our properties may need to have access to debt and equity capital, in the private and public markets, in order to acquire properties from us. Should the property funds or third parties have limited or no access to capital on favorable terms, then contributions and distributions could be delayed resulting in adverse effects on our liquidity, results of operations, distributable cash flow, debt covenant ratios and on the value of our securities.

We may acquire properties, which involves risks that could adversely affect our operating results and the value of our securities.

We may acquire industrial properties in our direct owned segment. The acquisition of properties involves risks, including the risk that the acquired property will not perform as anticipated and that any actual costs for rehabilitation, repositioning, renovation and improvements identified in the pre-acquisition due diligence process will exceed estimates. There is, and it is expected there will continue to be, significant competition for properties that meet our investment criteria as well as risks associated with obtaining financing for acquisition activities.

Our operating results and distributable cash flow will depend on the continued generation of lease revenues from customers.

Our operating results and distributable cash flow would be adversely affected if a significant number of our customers were unable to meet their lease obligations. We are also subject to the risk that, upon the expiration of leases for space located in our properties, leases may not be renewed by existing customers, the space may not be re-leased to new customers or the terms of renewal or re-leasing (including the cost of required renovations or concessions to customers) may be less favorable to us than current lease terms. In the event of default by a significant number of customers, we may experience delays and incur substantial costs in enforcing our rights as landlord. A customer may experience a downturn in its business, which may cause the loss of the customer or may weaken its financial condition, resulting in the customer s failure to make rental payments when due or requiring a restructuring that might reduce cash flow from the lease. In addition, a customer may seek the protection of bankruptcy, insolvency or similar laws, which could result in the rejection and termination of such customer s lease and thereby cause a reduction in our available cash flow.

Our ability to renew leases or re-lease space on favorable terms as leases expire significantly affects our business.

Our results of operations, distributable cash flow and the value of our securities would be adversely affected if we were unable to lease, on economically favorable terms, a significant amount of space in our operating properties. We have 30.2 million square feet of industrial and retail space (out of a total of 157.3 million occupied square feet representing 16.7% of total annual base rents) with leases that expire in 2009, including 3.9 million square feet of leases that are on a month-to-month basis. In addition, our unconsolidated investees have a combined 36.5 million square feet of industrial space (out of a total 284.6 million occupied square feet representing 10.1% of total annual base rent) with leases that expire in 2009, including 6.6 million square feet of leases that are on a month-to-month basis. The number of industrial and retail properties in a market or submarket could adversely affect both our ability to re-lease the space and the rental rates that can be obtained in new leases.

Real estate investments are not as liquid as other types of assets, which may reduce economic returns to investors.

Real estate investments are not as liquid as other types of investments and this lack of liquidity may limit our ability to react promptly to changes in economic or other conditions. In addition, significant expenditures associated with real estate investments, such as mortgage payments, real estate taxes and maintenance costs, are generally not reduced when circumstances cause a reduction in income from the investments. Like other companies qualifying as REITs under the Code, we are only able to hold property for sale in the ordinary course of business through taxable REIT subsidiaries in order to avoid punitive taxation on the gain from the sale of such property. While we are planning to dispose of certain properties that have been held for investment in order to generate liquidity, if we do not satisfy certain safe harbors or if we believe there is too much risk of incurring the punitive tax on the gain from the sale, we may not pursue such sales.

Our insurance coverage does not include all potential losses.

We and our unconsolidated investees currently carry insurance coverage including property, liability, fire, named windstorm, flood, earthquake, environmental, terrorism, extended coverage and rental loss as appropriate for the markets where each of our properties and business operations are located. The insurance coverage contains policy specifications and insured limits customarily carried for similar properties, business activities and markets. We believe our properties and the properties of our unconsolidated investees, including the property funds, are adequately insured. However, there are certain losses, including losses from floods, earthquakes, acts of war, acts of terrorism or riots, that are not generally insured against or that are not generally fully insured against because it is not deemed economically feasible or prudent to do so. If an uninsured loss or a loss in excess of insured limits occurs with respect to one or more of our properties, we could experience a significant loss of capital invested and potential revenues in these properties and could potentially remain obligated under any recourse debt associated with the property.

We are exposed to various environmental risks that may result in unanticipated losses that could affect our operating results and financial condition.

Under various federal, state and local laws, ordinances and regulations, a current or previous owner, developer or operator of real estate may be liable for the costs of removal or remediation of certain hazardous or toxic substances. The costs of removal or remediation of such substances could be substantial. Such laws often impose liability without regard to whether the owner or operator knew of, or was responsible for, the release or presence of such hazardous substances.

A majority of the properties we acquire are subjected to environmental reviews either by us or by the predecessor owners. In addition, we may incur environmental remediation costs associated with certain land parcels we acquire in connection with the development of the land. In connection with the merger in 2005 with Catellus Development Corporation (Catellus), we acquired certain properties in urban and industrial areas that may have been leased to, or previously owned by, commercial and industrial companies that discharged hazardous materials. We establish a liability at the time of acquisition to cover such costs. We adjust the liabilities as appropriate when additional information becomes available. We purchase various environmental insurance policies to mitigate our exposure to environmental liabilities. We are not aware of any environmental liability that we believe would have a material adverse effect on our business, financial condition or results of operations.

We cannot give any assurance that other such conditions do not exist or may not arise in the future. The presence of such substances on our real estate properties could adversely affect our ability to sell such properties or to borrow using such properties as collateral and may have an adverse effect on our distributable cash flow.

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Risks Related to Financing and Capital

Our operating results and financial condition could be adversely affected if we are unable to make required payments on our debt or are unable to refinance our debt.

We are subject to risks normally associated with debt financing, including the risk that our cash flow will be insufficient to meet required payments of principal and interest. There can be no assurance that we will be able to refinance any maturing indebtedness, that such refinancing would be on terms as favorable as the terms of the maturing indebtedness, or we will be able to otherwise obtain funds by selling assets or raising equity to make required payments on maturing indebtedness. If we are unable to refinance our indebtedness at maturity or meet our payment obligations, the amount of our distributable cash flow and our financial condition would be adversely affected and, if the maturing debt is secured, the lender may foreclose on the property securing such indebtedness. Our unsecured credit facilities and certain other unsecured debt bear interest at variable rates. Increases in interest rates would increase our interest expense under these agreements. In addition, our unconsolidated investees have short-term debt that was used to acquire properties from us or third parties and other maturing indebtedness. If these investees are unable to refinance their indebtedness or meet their payment obligations, it may impact our distributable cash flow and our financial condition.

Covenants in our credit agreements could limit our flexibility and breaches of these covenants could adversely affect our financial condition.

The terms of our various credit agreements, including our credit facilities and the indenture under which our senior and other notes are issued, require us to comply with a number of customary financial covenants, such as maintaining debt service coverage, leverage ratios, fixed charge ratios and other operating covenants including maintaining insurance coverage. These covenants may limit our flexibility in our operations, and breaches of these covenants could result in defaults under the instruments governing the applicable indebtedness. If we default under our covenant provisions and are unable to cure the default, refinance our indebtedness or meet our payment obligations, the amount of our distributable cash flow and our financial condition would be adversely affected.

Federal Income Tax Risks

Failure to qualify as a REIT could adversely affect our cash flows.

We have elected to be taxed as a REIT under the Code commencing with our taxable year ended December 31, 1993. In addition, we have a consolidated subsidiary that has elected to be taxed as a REIT and certain unconsolidated investees that are REITs and are subject to all the risks pertaining to the REIT structure, discussed herein. To maintain REIT status, we must meet a number of highly technical requirements on a continuing basis. Those requirements seek to ensure, among other things, that the gross income and investments of a REIT are largely real estate related, that a REIT distributes substantially all of its ordinary taxable income to shareholders on a current basis and that the REIT s equity ownership is not overly concentrated. Due to the complex nature of these rules, the available guidance concerning interpretation of the rules, the importance of ongoing factual determinations and the possibility of adverse changes in the law, administrative interpretations of the law and changes in our business, no assurance can be given that we, or our REIT subsidiaries, will qualify as a REIT for any particular period.

If we fail to qualify as a REIT, we will be taxed as a regular corporation, and distributions to shareholders will not be deductible in computing our taxable income. The resulting corporate income tax liabilities could materially reduce our cash flow and funds available for reinvestment. Moreover, we might not be able to elect to be treated as a REIT for the four taxable years after the year during which we ceased to qualify as a REIT. In addition, if we later requalified as a REIT, we might be required to pay a full corporate-level tax on any unrealized gains in our assets as of the date of

requalification, or upon subsequent disposition, and to make distributions to our shareholders equal to any earnings accumulated during the period of non-REIT status.

REIT distribution requirements could adversely affect our financial condition.

To maintain qualification as a REIT under the Code, generally a REIT must annually distribute to its shareholders at least 90% of its REIT taxable income, computed without regard to the dividends paid deduction and net capital gains. This requirement limits our ability to accumulate capital and, therefore, we may not have sufficient cash or other liquid assets to meet the distribution requirements. Difficulties in meeting the distribution requirements might arise due to competing demands for our funds or to timing differences between tax reporting and cash receipts and disbursements, because income may have to be reported before cash is received or because expenses may have to be paid before a deduction is allowed. In addition, the Internal Revenue Service (the IRS) may make a determination in connection with the settlement of an audit by the IRS that increases taxable income or disallows or limits deductions taken thereby increasing the distribution we are required to make. In those situations, we might be required to borrow funds or sell properties on adverse terms in order to meet the distribution requirements and interest and penalties could apply, which could adversely affect our financial condition. If we fail to make a required distribution, we would cease to qualify as a REIT.

Prohibited transaction income could result from certain property transfers.

We contribute properties to property funds and sell properties to third parties from the REIT and from taxable REIT subsidiaries (TRS). Under the Code, a disposition of a property from other than a TRS could be deemed a prohibited transaction. In such case, a 100% penalty tax on the resulting gain could be assessed. The determination that a transaction constitutes a prohibited transaction is based on the facts and circumstances surrounding each transaction. The IRS could contend that certain contributions or sales of properties by us are prohibited transactions. While we do not believe the IRS would prevail in such a dispute, if the IRS successfully argued the matter, the 100% penalty tax could be assessed against the gains from these transactions, which may be significant. Additionally, any gain from a prohibited transaction may adversely affect our ability to satisfy the income tests for qualification as a REIT.

Liabilities recorded for pre-existing tax audits may not be sufficient.

We are subject to pending audits by the IRS and the California Franchise Tax Board of the 1999 through 2005 income tax returns of Catellus, including certain of its subsidiaries and partnerships. We have recorded an accrual for the liabilities that may arise from these audits. During 2008, we agreed to enter into a closing agreement with the IRS for the settlement of the 1999-2002 audits and we increased the recorded liability by $85.4 million for all audits accordingly. See Note 14 to our Consolidated Financial Statements in Item 8. The finalization of the remaining audits may result in an adjustment in which the actual liabilities or settlement costs, including interest and potential penalties, if any, may prove to be more than the liability we have recorded.

Uncertainties relating to Catellus estimate of its earnings and profits attributable to C-corporation taxable years may have an adverse effect on our distributable cash flow.

In order to qualify as a REIT, a REIT cannot have at the end of any REIT taxable year any undistributed earnings and profits that are attributable to a C-corporation taxable year. A REIT has until the close of its first full taxable year as a REIT in which it has non-REIT earnings and profits to distribute these accumulated earnings and profits. Because Catellus first full taxable year as a REIT was 2004, Catellus was required to distribute these earnings and profits prior to the end of 2004. Failure to meet this requirement would result in Catellus disqualification as a REIT. Catellus distributed its accumulated non-REIT earnings and profits in December 2003, well in advance of the 2004 year-end deadline, and believed that this distribution was sufficient to distribute all of its non-REIT earnings and profits. However, the determination of non-REIT earnings and profits is complicated and depends upon facts with respect to which Catellus may have less than complete information or the application of the law governing earnings and profits, which is subject to differing interpretations, or both. Consequently, there are substantial uncertainties relating to the

estimate of Catellus non-REIT earnings and profits, and we cannot be assured that the earnings and profits distribution requirement has been met. These uncertainties include the possibility that the IRS could upon audit, as discussed above,

increase the taxable income of Catellus, which would increase the non-REIT earnings and profits of Catellus. There can be no assurances that we have satisfied the requirement that Catellus distribute all of its non-REIT earnings and profits by the close of its first taxable year as a REIT, and therefore, this may have an adverse effect on our distributable cash flow.

There are potential deferred and contingent tax liabilities that could affect our operating results or financial condition.

Palmtree Acquisition Corporation, our subsidiary that was the surviving corporation in the merger with Catellus in 2005, is subject to a federal corporate level tax at the highest regular corporate rate (currently 35%) and potential state taxes on any gain recognized within ten years of Catellus conversion to a REIT from a disposition of any assets that Catellus held at the effective time of its election to be a REIT, but only to the extent of the built-in-gain based on the fair market value of those assets on the effective date of the REIT election (which was January 1, 2004). Gain from a sale of an asset occurring more than 10 years after the REIT conversion will not be subject to this corporate-level tax. We do not currently expect to dispose of any asset of the surviving corporation in the merger if such disposition would result in the imposition of a material tax liability unless we can affect a tax-deferred exchange of the property. However, certain assets are subject to third party purchase options that may require us to sell such assets, and those assets may carry deferred tax liabilities that would be triggered on such sales. We have recorded deferred tax liabilities related to these built-in-gains. There can be no assurances that our plans in this regard will not change and, if such plans do change or if a purchase option is exercised, that we will be successful in structuring a tax-deferred exchange.

Other Risks

We are dependent on key personnel.

Our executive and other senior officers have a significant role in our success. Our ability to retain our management group or to attract suitable replacements should any members of the management group leave is dependent on the competitive nature of the employment market. The loss of services from key members of the management group or a limitation in their availability could adversely affect our financial condition and cash flow. Further, such a loss could be negatively perceived in the capital markets.

Share prices may be affected by market interest rates.

In response to current economic conditions, we reduced the expected annual distribution rate for 2009 to $1.00 per common share. The annual distribution rate on common shares as a percentage of our market price may influence the trading price of such common shares. An increase in market interest rates may lead investors to demand a higher annual distribution rate than we have set, which could adversely affect the value of our common shares.

As a global company, we are subject to social, political and economic risks of doing business in foreign countries.

We conduct a significant portion of our business and employ a substantial number of people outside of the United States. During 2008, we generated approximately 70% of our revenue from operations outside the United States, primarily due to proceeds from contributions of properties to property funds in Europe and Japan. Circumstances and developments related to international operations that could negatively affect our business, financial condition or results of operations include, but are not limited to, the following factors:

- difficulties and costs of staffing and managing international operations in certain regions;

- currency restrictions, which may prevent the transfer of capital and profits to the United States;

unexpected changes in regulatory requirements;

potentially adverse tax consequences;

- the responsibility of complying with multiple and potentially conflicting laws, e.g., with respect to corrupt practices, employment and licensing;
- the impact of regional or country-specific business cycles and economic instability;
- political instability, civil unrest, drug trafficking, political activism or the continuation or escalation of terrorist or gang activities (particularly with respect to our operations in Mexico); and
- foreign ownership restrictions with respect to operations in certain foreign countries.

Although we have committed substantial resources to expand our global development platform, if we are unable to successfully manage the risks associated with our global business or to adequately manage operational fluctuations, our business, financial condition and results of operations could be harmed.

In addition, our international operations and, specifically, the ability of our non-U.S. subsidiaries to dividend or otherwise transfer cash among our subsidiaries, including transfers of cash to pay interest and principal on our debt, may be affected by currency exchange control regulations, transfer pricing regulations and potentially adverse tax consequences, among other things.

The depreciation in the value of the foreign currency in countries where we have a significant investment may adversely affect our results of operations and financial position.

We have pursued, and intend to continue to pursue, growth opportunities in international markets where the U.S. dollar is not the national currency. At December 31, 2008, approximately 47% of our total assets, excluding our China operations, which were sold in February 2009 and presented as assets held for sale, are invested in a currency other than the U.S. dollar, primarily the euro, Japanese yen and British pound sterling. As a result, we are subject to foreign currency risk due to potential fluctuations in exchange rates between foreign currencies and the U.S. dollar. A significant change in the value of the foreign currency of one or more countries where we have a significant investment may have a material adverse effect on our results of operations and financial position. Although we attempt to mitigate adverse effects by borrowing under debt agreements denominated in foreign currencies and, on occasion and when deemed appropriate, through the use of derivative contracts, there can be no assurance that those attempts to mitigate foreign currency risk will be successful.

We are subject to governmental regulations and actions that affect operating results and financial condition.

Many laws and governmental regulations apply to us, our unconsolidated investees and our properties. Changes in these laws and governmental regulations, or their interpretation by agencies or the courts, could occur, which might affect our ability to conduct business.

ITEM 1B. Unresolved Staff Comments

None.

ITEM 2. Properties

We have directly invested in real estate assets that are primarily generic industrial properties. In Japan, our industrial properties are generally multi-level centers, which is common in Japan due to the high cost and limited availability of land. Our properties are typically used for storage, packaging, assembly, distribution and light manufacturing of

consumer and industrial products. Based on the square footage of our operating properties in the direct owned segment at December 31, 2008, our properties are 99.3% industrial properties, including 91.8% of properties used for bulk distribution, 6.6% used for light manufacturing and assembly and 0.9% for other purposes, primarily service centers, while the remaining 0.7% of our properties are retail.

At December 31, 2008, we owned 1,331 operating properties, including 1,297 industrial properties located in North America, Europe and Asia and 34 retail properties in North America. In North America, our properties are located in 33 markets in 20 states and the District of Columbia in the United States, 6 markets in Mexico and 1 market in Canada. Our properties are located in 29 markets in 13 countries in Europe and 6 markets in

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2 countries in Asia. This information excludes our China operations that are classified as held for sale at December 31, 2008.

Geographic Distribution

For this presentation, we define our markets based on the concentration of properties in a specific area. A market, as defined by us, can be a metropolitan area, a city, a subsection of a metropolitan area, a subsection of a city or a region of a state or country.

Properties

The information in the following tables is as of December 31, 2008 for the operating properties, properties under development and land we own, including 80 buildings owned by entities we consolidate but of which we own less than 100%. All of these assets are included in our direct owned segment. This includes our development portfolio of operating properties we recently developed or are currently developing. No individual property or group of properties operating as a single business unit amounted to 10% or more of our consolidated total assets at December 31, 2008 or generated income equal to 10% or more of our consolidated gross revenues for the year ended December 31, 2008. The table does not include properties that are owned by property funds or other unconsolidated investees which are discussed under Unconsolidated Investees .

	No. of Bldgs.	Percentage Leased (1)	Rentable Square Footage	Investment Before Depreciation	Encumbrances (2)
Operating properties owned in the direct owned segment at December 31, 2008 (dollars and rentable square footage in thousands):					
Industrial properties:					
North America by Country (40 markets) (3):					
United States:					
Atlanta, Georgia	81	91.80%	12,630	$ 447,178	$ 30,260
Austin, Texas	16	89.95%	1,095	44,596	
Central Valley, California	13	84.54%	3,486	172,142	24,611
Charlotte, North Carolina	31	96.79%	3,623	117,300	35,673
Chicago, Illinois	86	89.62%	18,660	985,289	158,299
Cincinnati, Ohio	21	87.41%	3,603	106,996	22,504
Columbus, Ohio	30	87.02%	5,873	221,767	27,353
Dallas/Fort Worth, Texas	106	86.10%	16,128	644,492	42,919
Denver, Colorado	30	93.56%	4,700	234,834	49,717
El Paso, Texas	16	94.87%	2,051	63,578	
Houston, Texas	77	98.12%	7,227	251,459	
I-81 Corridor, Pennsylvania	10	71.69%	3,736	192,452	
Indianapolis, Indiana	30	95.37%	3,155	113,481	
Inland Empire, California	38	83.79%	15,775	1,204,255	173,979
Las Vegas, Nevada	17	92.12%	2,061	96,622	10,173
Los Angeles, California	65	98.30%	5,465	596,057	87,870
Louisville, Kentucky	12	81.80%	3,259	109,773	11,530
Memphis, Tennessee	22	88.49%	4,905	137,976	
Nashville, Tennessee	29	97.19%	2,983	84,678	
New Jersey	36	88.51%	6,890	424,645	33,437
Orlando, Florida	21	67.97%	2,365	114,616	
Phoenix, Arizona	33	94.40%	2,700	127,811	
Portland, Oregon	26	86.75%	2,371	133,305	29,306
Reno, Nevada	18	87.06%	3,211	133,881	5,200
Salt Lake City, Utah	4	100.00%	661	24,389	
San Antonio, Texas	42	87.49%	3,826	136,886	3,437
San Francisco (East Bay), California	57	98.12%	4,901	312,710	58,011
San Francisco (South Bay), California	84	94.09%	5,516	465,083	36,591
Seattle, Washington	11	83.65%	1,281	72,663	264
South Florida	17	59.04%	1,533	106,048	6,215
St. Louis, Missouri	6	77.87%	685	23,026	
Tampa, Florida	52	90.50%	3,562	146,773	8,931
Washington D.C./Baltimore, Maryland	39	96.72%	5,232	266,231	36,305
Other	2	100.00%	367	19,263	

Subtotal United States	1,178	89.23%	165,516	8,332,255	892,585
Mexico:					
Guadalajara	2	14.32%	269	10,632	
Juarez	5	0.00%	489	19,146	
Mexico City	7	59.70%	1,507	83,962	
Monterrey	6	20.35%	909	34,990	
Reynosa	3	58.35%	305	12,498	
Tijuana	3	46.12%	691	37,622	
Subtotal Mexico	26	35.10%	4,170	198,850	
Canada Toronto	1	100.00%	110	7,832	
Subtotal North America	1,205	88.00%	169,796	8,538,937	892,585
Europe by Country (29 markets) (4):					
Belgium	1	0.00%	187	14,136	
Czech Republic	6	27.38%	1,702	142,903	
France	6	74.14%	2,024	136,812	2,900
Germany	10	44.70%	1,569	122,536	
Hungary	5	34.69%	1,279	75,007	
Italy	5	28.62%	1,562	103,730	
Netherlands	1	0.00%	280	14,879	
Poland	17	58.58%	3,700	208,471	
Romania	4	89.63%	1,170	72,085	
Slovakia	7	83.65%	1,895	129,931	
Spain	1	0.00%	470	22,465	
Sweden	1	78.68%	84	6,051	
United Kingdom	18	4.68%	4,010	390,982	
Subtotal Europe	82	43.21%	19,932	1,439,988	2,900
Asia by Country (6 markets) (5):					
Japan	7	39.17%	5,725	951,857	
Korea	3	100.00%	257	25,686	4,540
Subtotal Asia	10	41.79%	5,982	977,543	4,540
Total industrial properties	**1,297**	**82.02%**	**195,710**	**10,956,468**	**900,025**
Retail properties:					
North America by Country (5 markets):					
United States	34	94.48%	1,404	358,992	4,447
Total retail properties	**34**	**94.48%**	**1,404**	**358,992**	**4,447**
Total operating properties owned in the direct owned segment at	**1,331**	**82.11%**	**197,114**	**$ 11,315,460**	**$ 904,472**

December 31, 2008

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	Land Held for Development			Properties Under Development			
	Acreage	Investment	No. of Bldgs.	Percentage Leased (1)	Rentable Square Footage	Current Investment	Total Expected Cost (6)
Land held for development and properties under development at December 31, 2008 (dollars and rentable square footage in thousands):							
North America by Market (37 total markets):							
United States:							
Atlanta, Georgia	467	$ 37,460				$	$
Austin, Texas	6	2,869					
Central Valley, California	845	27,505	2	100.00%	1,226	68,979	80,286
Charlotte, North Carolina	29	4,929					
Chicago, Illinois	753	93,295	1	0.00%	257	22,559	30,345
Cincinnati, Ohio	85	8,594					
Columbus, Ohio	233	13,775					
Dallas, Texas	501	42,657					
Denver, Colorado	94	10,664					
East Bay, California	2	7,849					
El Paso, Texas	70	4,048					
Houston, Texas	120	9,774					
Indianapolis, Indiana	93	5,235					
Inland Empire, California	463	137,411	1	100.00%	658	69,572	78,460
Jacksonville, Florida	103	16,806					
Las Vegas, Nevada	68	34,634					
Los Angeles, California	30	46,373					
Louisville, Kentucky	13	995					
Memphis, Tennessee	159	11,643					
Nashville, Tennessee	24	3,002					
New Jersey	301	177,339					
Norfolk, Virginia	83	9,165					
Pennsylvania	307	43,756					

Phoenix, Arizona	148	23,102					
Portland, Oregon	23	5,204					
Reno, Nevada	178	22,828					
San Antonio, Texas	55	5,958					
South Florida	81	53,562	2	0.00%	200	20,558	23,366
Tampa, Florida	45	6,319					
Washington D.C./Baltimore, Maryland	138	23,973					
Mexico:							
Guadalajara	48	17,296					
Juarez	146	17,181	3	0.00%	458	21,123	27,296
Matamoros	122	15,956					
Mexico City	121	41,838	2	0.00%	793	33,454	40,874
Monterrey	159	30,163					
Reynosa	108	11,689	1	0.00%	302	10,754	15,290
Canada Toronto	179	84,796	1	0.00%	416	19,905	28,931
Subtotal North America	6,400	1,109,643	13	43.69%	4,310	266,904	324,848
Europe by Country (35 total markets):							
Austria	33	29,518					
Belgium	30	13,622	1	100.00%	247	9,228	17,686
Czech Republic	307	85,953	3	24.02%	694	64,168	65,954
France	316	74,462	9	10.92%	2,241	68,156	175,886
Germany	251	96,231	14	56.64%	3,020	164,365	257,326
Hungary	162	34,700					
Italy	74	28,623	1	0.00%	130	107	10,560
Netherlands	58	41,910	1	100.00%	306	7,065	26,314
Poland	839	154,697	13	27.89%	3,695	180,539	288,912
Romania	90	21,136					
Slovakia	86	27,568	1	50.12%	285	17,182	19,825
Spain	98	67,752	3	76.26%	1,301	30,041	99,273
Sweden	6	1,881	1	27.35%	921	55,238	70,124
United Kingdom	1,264	416,771	1	100.00%	47	2,719	5,744
Subtotal Europe	3,614	1,094,824	48	39.88%	12,887	598,808	1,037,604
Asia by Country (6 total markets):							
Japan	100	267,691	3	7.68%	2,470	288,784	489,335
Korea	20	9,058	1	100.00%	170	9,114	13,258
Subtotal Asia	120	276,749	4	13.59%	2,640	297,898	502,593
Total land held for development and properties under development in the	**10,134**	**$ 2,481,216**	**65**	**37.21%**	**19,837**	**$ 1,163,610**	**$ 1,865,045**

direct owned segment at December 31, 2008

The following is a summary of our direct-owned investments in real estate assets at December 31, 2008:

	Investment Before Depreciation (in thousands)	
Operating properties	$	11,315,460
Land subject to ground leases and other (7)		424,489
Properties under development		1,163,610
Land held for development		2,481,216
Other investments (8)		321,397
Total	**$**	**15,706,172**

(1) Represents the percentage leased at December 31, 2008. Operating properties at December 31, 2008 include recently completed development properties and recently acquired properties that may be in the initial lease-up phase, which reduces the overall leased percentage (see notes 3, 4 and 5 below for information regarding developed properties).

(2) Certain properties are pledged as security under our secured debt and assessment bonds at December 31, 2008. For purposes of this table, the total principal balance of a debt issuance that is secured by a pool of properties is allocated among the properties in the pool based on each property s investment balance. In addition to the amounts reflected here, we also have $3.1 million of encumbrances related to other real estate assets not included in the direct owned segment. See Schedule III Real Estate and Accumulated Depreciation to our Consolidated Financial Statements in Item 8 for additional identification of the properties pledged.

(3) In North America, includes 55 recently Completed Development Properties aggregating 16.8 million square feet at a total investment of $772.2 million that are 47.5% leased and in our development portfolio.

(4) In Europe, includes 77 recently Completed Development Properties aggregating 18.1 million square feet at a total investment of $1.3 billion that are 41.0% leased and in our development portfolio.

(5) In Asia, includes 8 recently Completed Development Properties aggregating 5.8 million square feet at a total investment of $955.0 million that are 39.7% leased and in our development portfolio.

(6) Represents the total expected cost to complete a property under development and may include the cost of land, fees, permits, payments to contractors, architectural and engineering fees, interest, project management costs and other appropriate costs to be capitalized during construction and also leasing costs, rather than the total actual costs incurred to date.

(7) Amounts represent investments of $389.2 million in land subject to ground leases and an investment of $35.3 million in railway depots.

(8) Other investments include: (i) restricted funds that are held in escrow pending the completion of tax-deferred exchange transactions involving operating properties; (ii) earnest money deposits associated with potential acquisitions; (iii) costs incurred during the pre-acquisition due diligence process; (iv) costs incurred during the

pre-construction phase related to future development projects, including purchase options on land and certain infrastructure costs; and (v) costs related to our corporate office buildings.

Unconsolidated Investees

At December 31, 2008, our investments in and advances to unconsolidated investees totaled $2.3 billion. The property funds totaled $2.0 billion and the industrial and retail joint ventures totaled $207 million at December 31, 2008 and are all included in our investment management segment. The remaining unconsolidated investees totaled $105 million at December 31, 2008.

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Property Funds

At December 31, 2008, we had ownership interests ranging from 20% to 50% in 17 property funds and 3 joint ventures that are presented under the equity method. These entities primarily own industrial and retail operating properties. We act as manager of each property fund.

The information provided in the table below (dollars and square footage in thousands) is for our unconsolidated entities with investments in industrial properties and represents the total entity, not just our proportionate share. See Item 1. Business and Note 5 to our Consolidated Financial Statements in Item 8.

	No. of Bldgs.	No. of Markets	Rentable Square Footage	Percentage Leased	Entity s Investment (1)
North America:					
Property funds:					
ProLogis California	80	1	14,178	98.67%	$ 697,590
ProLogis North American Properties Fund I	36	16	9,406	95.57%	386,572
ProLogis North American Properties Fund VI	22	7	8,648	93.01%	516,675
ProLogis North American Properties Fund VII	29	8	6,205	90.13%	397,327
ProLogis North American Properties Fund VIII	24	9	3,064	97.31%	193,380
ProLogis North American Properties Fund IX	20	7	3,439	71.83%	197,066
ProLogis North American Properties Fund X	29	9	4,191	92.28%	223,441
ProLogis North American Properties Fund XI	13	2	4,112	95.21%	219,487
ProLogis North American Industrial Fund	258	31	49,656	96.31%	2,916,806
ProLogis North American Industrial Fund II	150	30	35,752	94.54%	2,161,805
ProLogis North American Industrial Fund III	120	7	24,709	94.39%	1,746,538
ProLogis Mexico Industrial Fund	73	11	9,494	94.23%	588,382
Property funds	854	44(2)	172,854	94.73%	10,245,069
Other unconsolidated investees	3	2	736	47.74%	31,762
Total North America	857	44(2)	173,590	94.53%	10,276,831
Europe property funds:					
ProLogis European Properties	246	28	56,273	97.42%	4,819,603
ProLogis European Properties Fund II	153	26	38,853	97.89%	3,918,541
Total Europe	399	35(2)	95,126	97.62%	8,738,144

Asia property funds:					
ProLogis Japan property funds (3)	70	8	27,034	99.56%	5,595,985
ProLogis Korea Fund	13	2	1,915	100.00%	142,896
Total Asia	83	10 (2)	28,949	99.59%	5,738,881
Total unconsolidated investees	1,339	89	297,665	96.01%	$ 24,753,856

(1) Investment represents 100% of the carrying value of the properties, before depreciation, of each entity at December 31, 2008.

(2) Represents the total number of markets in each continent on a combined basis.

(3) We entered into a binding agreement in December 2008 to sell these investments, along with the ProLogis China Acquisition fund, which was formed in 2008 and is classified as held for sale. See Note 21 to our Consolidated Financial Statements in Item 8 for more information.

ITEM 3. Legal Proceedings

From time to time, we and our unconsolidated investees are parties to a variety of legal proceedings arising in the ordinary course of business. We believe that, with respect to any such matters that we are currently a party to, the ultimate disposition of any such matter will not result in a material adverse effect on our business, financial position or results of operations.

ITEM 4. Submission of Matters to a Vote of Security Holders

Not applicable.

PART II

ITEM 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information and Holders

Our common shares are listed on the NYSE under the symbol PLD . The following table sets forth the high and low sale prices, as reported in the NYSE Composite Tape, and distributions per common share, for the periods indicated.

	High Sale Price	Low Sale Price	Per Common Share Cash Distribution
2007:			
First Quarter	$ 72.08	$ 58.00	$ 0.46
Second Quarter	67.99	55.76	0.46
Third Quarter	66.86	51.65	0.46
Fourth Quarter	73.34	59.37	0.46
2008:			
First Quarter	$ 64.00	$ 51.04	$ 0.5175
Second Quarter	66.51	53.42	0.5175
Third Quarter	54.89	34.61	0.5175
Fourth Quarter	39.85	2.20	0.5175
2009:			
First Quarter (through February 20)	$ 16.68	$ 5.90	$ 0.25 (1)

(1) Declared on February 9, 2009 and payable on February 27, 2009 to holders of record on February 19, 2009.

On February 20, 2009, we had approximately 267,604,300 common shares outstanding, which were held of record by approximately 8,900 shareholders.

Distributions and Dividends

In order to comply with the REIT requirements of the Code, we are generally required to make common share distributions and preferred share dividends (other than capital gain distributions) to our shareholders in amounts that together at least equal (i) the sum of (a) 90% of our REIT taxable income computed without regard to the dividends paid deduction and net capital gains and (b) 90% of the net income (after tax), if any, from foreclosure property, minus (ii) certain excess non-cash income. Our common share distribution policy is to distribute a percentage of our cash flow that ensures that we will meet the distribution requirements of the

Code and that allows us to maximize the cash retained to meet other cash needs, such as capital improvements and other investment activities.

The annual distribution rate for 2008 was $2.07 per common share. In November 2008, the Board set the expected annual distribution rate for 2009 at $1.00 per common share, subject to market conditions and REIT distribution requirements. The payment of common share distributions, as well as whether the distribution will be payable in cash or shares of beneficial interest, or some combination, is dependent upon our financial condition and operating results and may be adjusted at the discretion of the Board during the year.

In addition to common shares, we have issued cumulative redeemable preferred shares of beneficial interest. At December 31, 2008, we had three series of preferred shares outstanding (Series C Preferred Shares , Series F Preferred Shares and Series G Preferred Shares). Holders of each series of preferred shares outstanding have limited voting rights, subject to certain conditions, and are entitled to receive cumulative preferential dividends based upon each series respective liquidation preference. Such dividends are payable quarterly in arrears on the last day of March, June, September and December. Dividends on preferred shares are payable when, and if, they have been declared by the Board, out of funds legally available for payment of dividends. After the respective redemption dates, each series of preferred shares can be redeemed at our option. The cash redemption price (other than the portion consisting of accrued and unpaid dividends) with respect to Series C Preferred Shares is payable solely out of the cumulative sales proceeds of other capital shares of ours, which may include shares of other series of preferred shares. With respect to the payment of dividends, each series of preferred shares ranks on parity with our other series of preferred shares. Annual per share dividends paid on each series of preferred shares were as follows for the periods indicated:

	Years Ended December 31,	
	2008	**2007**
Series C Preferred Shares	$ 4.27	$ 4.27
Series F Preferred Shares	$ 1.69	$ 1.69
Series G Preferred Shares	$ 1.69	$ 1.69

Pursuant to the terms of our preferred shares, we are restricted from declaring or paying any distribution with respect to our common shares unless and until all cumulative dividends with respect to the preferred shares have been paid and sufficient funds have been set aside for dividends that have been declared for the then-current dividend period with respect to the preferred shares.

For more information regarding our distributions and dividends, see Note 10 to our Consolidated Financial Statements in Item 8.

Securities Authorized for Issuance Under Equity Compensation Plans

For information regarding securities authorized for issuance under our equity compensation plans see Notes 10 and 11 to our Consolidated Financial Statements in Item 8.

Other Shareholder Matters

Other Issuances of Common Shares

In 2008, we issued 3,911,923 common shares, upon exchange of limited partnership units in our majority-owned and consolidated real estate partnerships. These common shares were issued in transactions exempt from registration under Section 4(2) of the Securities Act of 1933.

Common Share Plans

We have approximately $84.1 million remaining on our Board authorization to repurchase common shares that began in 2001. We have not repurchased our common shares since 2003.

See our 2009 Proxy Statement for further information relative to our equity compensation plans.

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ITEM 6. Selected Financial Data

The following table sets forth selected financial data relating to our historical financial condition and results of operations for 2008 and the four preceding years. Certain amounts for the years prior to 2008 presented in the table below have been reclassified to conform to the 2008 financial statement presentation and to reflect discontinued operations. The amounts in the table below are in millions, except for per share amounts.

	Years Ended December 31,				
	2008	2007	2006	2005	2004
Operating Data:					
Total revenues	$ 5,655	$ 6,189	$ 2,438	$ 1,815	$ 1,837
Total expenses	$ 5,031	$ 5,047	$ 1,673	$ 1,388	$ 1,492
Operating income	$ 624	$ 1,142	$ 765	$ 427	$ 345
Interest expense	$ 341	$ 369	$ 296	$ 177	$ 153
Earnings (loss) from continuing operations (1)	$ (195)	$ 988	$ 714	$ 301	$ 216
Discontinued operations (2)	$ (212)	$ 86	$ 160	$ 95	$ 17
Net earnings (loss)	$ (407)	$ 1,074	$ 874	$ 396	$ 233
Net earnings (loss) attributable to common shares	$ (432)	$ 1,049	$ 849	$ 371	$ 203
Net earnings (loss) per share attributable to common shares Basic:					
Continuing operations	$ (0.85)	$ 3.74	$ 2.79	$ 1.35	$ 1.02
Discontinued operations	(0.80)	0.34	0.66	0.47	0.09
Net earnings (loss) per share attributable to common shares Basic	$ (1.65)	$ 4.08	$ 3.45	$ 1.82	$ 1.11
Net earnings (loss) per share attributable to common shares Diluted:					
Continuing operations	$ (0.85)	$ 3.62	$ 2.69	$ 1.31	$ 0.99
Discontinued operations	(0.80)	0.32	0.63	0.45	0.09
Net earnings (loss) per share attributable to common shares Diluted	$ (1.65)	$ 3.94	$ 3.32	$ 1.76	$ 1.08
Weighted average common shares outstanding:					
Basic	263	257	246	203	182
Diluted	263	267	257	214	192
Common Share Distributions:					
Common share cash distributions paid	$ 551	$ 473	$ 393	$ 297	$ 266
Common share distributions paid per share	$ 2.07	$ 1.84	$ 1.60	$ 1.48	$ 1.46
FFO (3):					
Reconciliation of net earnings to FFO:					
Net earnings (loss) attributable to common shares	$ (432)	$ 1,049	$ 849	$ 371	$ 203
Total NAREIT defined adjustments	449	150	149	161	196
Total our defined adjustments	164	28	(53)	(2)	1

FFO attributable to common shares as defined by ProLogis, including significant non-cash items	$	181	$	1,227	$	945	$	530	$	400
Add (deduct) significant non-cash items:										
Impairment of goodwill and other assets		321								
Impairment related to assets held for sale China operations		198								
Losses related to temperature-controlled distribution assets								25		37
Impairment of real estate properties		275								
Our share of the loss/impairment recorded by an unconsolidated investee		108								
Gain on early extinguishment of debt		(91)								
FFO attributable to common shares as defined by ProLogis, excluding significant non-cash items	$	992	$	1,227	$	945	$	555	$	437
Cash Flow Data:										
Net cash provided by operating activities	$	844	$	1,206	$	687	$	488	$	484
Net cash used in investing activities	$	(1,302)	$	(4,053)	$	(2,069)	$	(2,223)	$	(620)
Net cash provided by financing activities	$	358	$	2,742	$	1,645	$	1,713	$	37

	As of December 31,				
	2008	2007	2006	2005	2004
Financial Position:					
Real estate owned, excluding land held for development, before depreciation	$ 13,225	$ 14,426	$ 12,500	$ 10,830	$ 5,738
Land held for development	$ 2,481	$ 2,153	$ 1,397	$ 1,045	$ 596
Investments in and advances to unconsolidated investees	$ 2,270	$ 2,345	$ 1,300	$ 1,050	$ 909
Total assets	$ 19,252	$ 19,724	$ 15,904	$ 13,126	$ 7,098
Total debt	$ 11,008	$ 10,506	$ 8,387	$ 6,678	$ 3,414
Total liabilities	$ 12,808	$ 12,209	$ 9,453	$ 7,580	$ 3,929
Minority interest	$ 19	$ 79	$ 52	$ 58	$ 67
Total shareholders equity	$ 6,425	$ 7,436	$ 6,399	$ 5,488	$ 3,102
Number of common shares outstanding	267	258	251	244	186

(1) During 2008, we recognized impairment charges on certain of our real estate properties of $274.7 million and on goodwill and other assets of $320.6 million and our share of impairment charges recorded by an unconsolidated investee of $108.2 million. See our Consolidated Financial Statements in Item 8 for more information.

(2) Discontinued operations include income (loss) attributable to assets held for sale and disposed properties, net gains recognized on the disposition of properties to third parties and, in 2008, an impairment charge of $198.2 million as a result of our sale in February 2009 of our China operations. See Note 21 to our Consolidated Financial Statements in Item 8 for additional information. Amounts include impairment charges related to temperature controlled distribution assets of $25.2 million and $36.7 million in 2005 and 2004, respectively.

(3) Funds from operations (FFO) is a non-U.S. generally accepted accounting principle (GAAP) measure that is commonly used in the real estate industry. The most directly comparable GAAP measure to FFO is net earnings. Although the National Association of Real Estate Investment Trusts (NAREIT) has published a definition of FFO, modifications to the NAREIT calculation of FFO are common among REITs, as companies seek to provide financial measures that meaningfully reflect their business. FFO, as we define it, is presented as a supplemental financial measure. FFO is not used by us as, nor should it be considered to be, an alternative to net earnings computed under GAAP as an indicator of our operating performance or as an alternative to cash from operating activities computed under GAAP as an indicator of our ability to fund our cash needs.

FFO is not meant to represent a comprehensive system of financial reporting and does not present, nor do we intend it to present, a complete picture of our financial condition and operating performance. We believe net earnings computed under GAAP remains the primary measure of performance and that FFO is only meaningful when it is used in conjunction with net earnings computed under GAAP. Further, we believe that our consolidated financial statements, prepared in accordance with GAAP, provide the most meaningful picture of our financial condition and our operating performance.

At the same time that NAREIT created and defined its FFO concept for the REIT industry, it also recognized that management of each of its member companies has the responsibility and authority to publish financial information that it regards as useful to the financial community. We believe that financial analysts, potential investors and shareholders who review our operating results are best served by a defined FFO measure that includes other adjustments to net earnings computed under GAAP in addition to those included in the NAREIT

defined measure of FFO. Our FFO measure is discussed in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Funds From Operations .

ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

You should read the following discussion in conjunction with our Consolidated Financial Statements included in Item 8 of this report and the matters described under Item 1A. Risk Factors .

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Management s Overview

We are a self-administered and self-managed REIT that owns, operates and develops real estate properties, primarily industrial properties, in North America, Europe and Asia (directly and through our unconsolidated investees). Our business is primarily driven by requirements for modern, well-located inventory space in key global distribution locations. Our focus on our customers needs has enabled us to become a leading global provider of industrial distribution properties.

Recently, the global financial markets have been undergoing pervasive and fundamental disruptions, which began to impact us late in the third quarter of 2008. As the global credit crisis worsened in the fourth quarter, it was necessary for us to modify our business strategy. As such, we discontinued most of our new development and acquisition activities in order to focus on our core business of owning and managing industrial properties. Narrowing our focus has allowed us to take the necessary steps toward reducing our debt and maximizing liquidity and cash flow. We believe our current business strategy, coupled with the following objectives for both the near and long-term, will position us to take advantage of business opportunities upon the stabilization of the global financial markets.

Near-term objectives:

- Simplify our business model and focus on our core business;
- Complete the development and leasing of properties currently in our development portfolio;
- Manage our core portfolio of industrial distribution properties to maintain and improve our net operating income stream from these assets;
- Provide exceptional customer service to our current and future customers;
- Generate liquidity through contributions of properties to our property funds and through sales to third parties;
- Reduce our debt at December 31, 2009 by $2.0 billion from our debt levels at September 30, 2008, through debt retirements; utilizing proceeds from property contributions and dispositions and other possible means, such as buying back outstanding debt and issuing additional equity;
- Recast our global line of credit; and
- Reduce our general and administrative expenses through various cost savings initiatives, including reductions in workforce.

Longer-term objectives:

- Employ a conservative growth expansion model;
- Develop industrial properties utilizing a portion of our existing land parcels, which we will hold for long-term direct investment, or otherwise monetize our land holdings through dispositions; and
- Grow the property funds by utilizing the property fund structure for the development of properties and the opportunistic acquisition of properties from third parties.

Due to recent economic conditions, we have changed our near-term business strategy, which will no longer focus on CDFS business activities. As a result, as of December 31, 2008, we have two operating segments: (i) direct owned and (ii) investment management. Our direct owned segment represents the direct long-term ownership of industrial and retail properties. Our investment management segment represents the long-term investment management of property funds and the properties they own. Our development or CDFS business segment, which had results through December 31, 2008, primarily encompassed our development or acquisition of real estate properties that were subsequently contributed to a property fund in which we have an ownership interest and act as manager, or sold to third parties. As of December 31, 2008, all of the assets and liabilities in this segment have been transferred into our two remaining segments.

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We generate and seek to increase revenues; earnings; FFO, as defined at the end of Item 7; and cash flows through our segments primarily as follows:

Direct Owned Segment We earn rent from our customers, including reimbursements of certain operating costs, under long-term operating leases for the industrial and retail properties that we own directly. The revenue in this segment decreased in 2008 primarily due to the contribution of properties to property funds, offset partially with increases in occupancy levels within our development portfolio. However, due to current market challenges, leasing activity has slowed and rental revenues generated by the lease-up of newly developed properties has not been adequate to completely offset the loss of rental revenues from property contributions. We expect our total revenues from this segment will decrease in 2009 due to the contributions and dispositions of properties we made in 2008. We intend to grow our revenue in the remaining properties primarily through increases in occupied square feet in our development portfolio. Our development portfolio, including Completed Development Properties and those currently under development, was 41.4% leased at December 31, 2008. Our current business plan allows for the limited expansion of operating properties as necessary to: (i) address the specific expansion needs of customers; (ii) initiate or enhance our market presence in a specific country, market or submarket; (iii) take advantage of opportunities where we believe we have the ability to achieve favorable returns; and (iv) expand the portfolio of properties we own through opportunistic acquisitions.

Investment Management Segment We recognize our proportionate share of the earnings or losses from our investments in unconsolidated property funds and certain joint ventures. In addition to the income recognized under the equity method, we recognize fees and incentives earned for services performed on behalf of these entities and interest earned on advances to these entities, if any. We provide services to these entities, such as property management, asset management, acquisition, financing and development. We may also earn incentives from our property funds depending on the return provided to the fund partners over a specified period. We expect future growth in income recognized to result from growth in existing property funds, primarily from properties the funds acquired from us in 2008 and may acquire, from us or third parties, in the future, as well as the formation of future funds.

CDFS Business Segment Through December 31, 2008, we recognized income primarily from the contributions of developed, rehabilitated and repositioned properties and acquired portfolios of properties to the property funds as well as from dispositions of land and properties to third parties. The income was generated due to the increased fair value of the properties at the time of contribution, based on third party appraisals, and income was recognized only to the extent of the third party ownership interest in the property fund acquiring the property. Given the challenges that we are facing in this current environment and the corresponding changes we have made to our business strategy, we do not expect to have a CDFS business segment in 2009. All of the assets and liabilities that were in this segment have been transferred to our two remaining segments. We transferred all of our real estate and other assets that were in our development pipeline to our direct owned segment. The investments we had in certain joint ventures have been transferred to our investment management segment. We may contribute Completed Development Properties and/or Core Properties to the property funds or sell to third parties, although these will no longer be reported in our CDFS business segment.

Key Items in 2008

In December 2008, we entered into a binding agreement to sell our China operations and our investments in the Japan property funds for $1.3 billion of cash. This resulted in an impairment charge of $198.2 million on the sale of our China operations, which is included in Discontinued Operations in our Consolidated Financial Statements in Item 8. In 2009, after the sale has closed and we have received all the proceeds, we will recognize a gain related to the sale of our interests in the Japan property funds. See Note 21 to our Consolidated Financial Statements in Item 8.

In 2008, we generated aggregate proceeds of $4.7 billion and recognized aggregate gains of $690.1 million from contributions and dispositions of properties, net of amounts deferred, as follows:

- We generated $4.2 billion of proceeds and $658.9 million of gains from the contributions of CDFS developed and repositioned properties and sales of land. This is net of the deferral of $209.5 million of gains related to our ongoing ownership in the property funds or other unconsolidated investees that acquired the properties and also includes $25.0 million of previously deferred gains. This also includes one property sold to a third party that was developed under a pre-sale agreement.

- We contributed, to certain property funds, acquired CDFS property portfolios at cost, generating $372.7 million of proceeds. We acquired these portfolios of properties in 2008, 2007 and 2006 with the intent to contribute them to a new or existing property fund at our cost. In addition, we contributed two non-CDFS properties to property funds generating $35.5 million of proceeds and $11.7 million of gains.

- We disposed of 15 properties and land subject to a ground lease to third parties, all of which are included in discontinued operations, generating proceeds of $127.4 million and $19.5 million of gains.

We increased our direct investment in PEPF II by 20% by acquiring units from PEPR for $61.1 million.

As a result of significant adverse changes in market conditions, we reviewed our assets for potential impairment under the appropriate accounting literature, considering current market conditions as well as our intent with regard to owning or disposing of the asset. In connection with that review, in the fourth quarter of 2008, we recorded impairment charges of $274.7 million on our real estate properties and $320.6 million on goodwill and other assets. See Note 13 to our Consolidated Financial Statements in Item 8.

In connection with cost savings initiatives we implemented to reduce our general and administrative expenses, we initiated a RIF plan with a total cost of $26.4 million, including $3.3 million related to our China operations and reflected in discontinued operations.

During the fourth quarter of 2008, we completed a tender offer related to our senior notes. We purchased $309.7 million aggregate principal amount of 5.25% notes due November 2010 for $216.8 million, resulting in a gain of $90.7 million, after transaction costs and expensing previously deferred debt issuance and discount costs of $2.2 million.

We raised $1.1 billion of proceeds through the issuance of $600 million of 6.625% senior notes and $550 million of 2.625% convertible senior notes.

We generated $196.4 million from the issuance of 3.4 million common shares under our Controlled Equity Offering Program.

Summary of 2008

Our direct owned portfolio decreased in 2008, on average, due to the contributions of properties to the property funds. Net operating income from our direct owned segment decreased to $641.7 million for the year ended December 31, 2008 from $739.6 million for the same period in 2007. The decrease was largely due to us owning a smaller operating portfolio, on average, during 2008 over the same period in 2007, an increase in property management expenses, insurance and other rental expenses not recoverable from our customers, offset partially by an increase in occupancy levels and rental rate increases. Rental expenses in this segment include the property management costs we incur to

manage our properties and the properties owned by the property funds for which we receive management fee income. The property management costs increased $10.5 million in 2008 compared with 2007, primarily due to the growth in the portfolios we manage on behalf of the property funds. Non-recoverable rental expenses increased due to a $6.0 million increase in insurance expense related to a tornado in the first quarter of 2008.

We had net operating income from the investment management segment of $66.4 million for the year ended December 31, 2008, compared to $196.0 million for 2007. In 2008, we recognized a loss of $108.2 million

representing our share of the loss recognized by ProLogis European Properties (PEPR) upon the sale and impairment of its ownership interests in ProLogis European Properties Fund II (PEPF II). We also recognized our share of realized and unrealized losses of $32.3 million related to interest rate derivative contracts held by certain property funds. In 2007, we recognized $38.2 million that represented our proportionate share of a gain recognized by PEPR from the sale of certain properties. Without these items in both 2008 and 2007, net operating income from this segment increased $49.1 million or 31% due to the increased size of the portfolios owned by the property funds.

Net operating income of the CDFS business segment decreased for the year ended December 31, 2008 to $657.9 million from $786.2 million for the same period in 2007 primarily due to decreased levels of contributions and lower profit margins. In 2007, we repositioned a property fund and recognized gains of $68.6 million in this segment.

Results of Operations

Information for the years ended December 31, regarding net earnings (loss) attributable to common shares was as follows:

	2008	2007	2006
Net earnings (loss) attributable to common shares (in millions)	$ (432.2)	$ 1,048.9	$ 849.0
Net earnings (loss) per share attributable to common shares Basic	$ (1.65)	$ 4.08	$ 3.45
Net earnings (loss) per share attributable to common shares Diluted	$ (1.65)	$ 3.94	$ 3.32

The decrease in net earnings in 2008 from 2007 is primarily due to impairment charges recognized in 2008 of $901.8 million, charges of $26.4 million related to our RIF plan, lower gains on dispositions of properties, lower rental income and higher rental expenses, offset by a $90.7 million gain on the extinguishment of debt. The impairment charges related to our real estate properties, goodwill, China operations, unconsolidated investees and other assets and are discussed in more detail in Notes 5, 7 and 13 to our Consolidated Financial Statements in Item 8. In 2007, we recognized gains on dispositions of both CDFS and non-CDFS properties of $991.9 million as compared with $690.1 million of gains in 2008. Net earnings in 2007 included; (i) the repositioning of a property fund resulting in total gains from CDFS contributions and foreign exchange contracts of $95.2 million; (ii) the disposition of 77 properties from our direct owned segment to two of the unconsolidated property funds, which generated gains of $146.7 million; and (iii) the recognition of our share of net gains of $38.2 million from the property funds due to the disposition of properties in 2007. These transactions have also resulted in less rental income in 2008 compared with 2007. The increase in net earnings attributable to common shares in 2007 over 2006 was due to increased gains on contributions of CDFS and non-CDFS properties to property funds (outlined above), higher gains on sales of land and improved property operating performance, partially offset by lower incentive fees from property funds and lower gains on sales of properties to third parties.

Direct Owned Segment

The net operating income of the direct owned segment consists of rental income and rental expenses from industrial and retail properties during the time we directly own it. The rental income and expenses of operating properties that were developed or acquired with the intent to contribute to a property fund are included in this segment prior to contribution. When a property is contributed to a property fund, we begin reporting our share of the earnings of the property under the equity method in the investment management segment. However, the overhead costs incurred by us to provide the management services to the property fund continue to be reported as part of rental expenses in this segment. The size and leased percentage of our direct owned operating portfolio fluctuates due to the timing of contributions and dispositions of properties and the acquisition and development of properties and impacts the net

operating income we recognize in this segment. See Note 19 to our Consolidated Financial Statements in Item 8 for a reconciliation of net operating income to earnings (loss)

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before minority interest. The net operating income from the direct owned segment, excluding amounts presented as discontinued operations in our Consolidated Financial Statements, was as follows (in thousands):

	Years Ended December 31,		
	2008	2007	2006
Rental income	$ 953,866	$ 1,009,173	$ 865,145
Rental expenses	312,121	269,602	221,780
Total net operating income direct owned segment	$ 641,745	$ 739,571	$ 643,365

We had a direct owned operating portfolio at December 31, 2008 and 2007, as follows (square feet in thousands):

	December 31, 2008			December 31, 2007		
	Number of Properties	Square Feet	Leased %	Number of Properties	Square Feet	Leased %
Industrial properties	1,157	154,947	92.2%	1,187	161,105	93.2%
Retail properties	34	1,404	94.5%	32	1,282	94.0%
Subtotal non-development properties	1,191	156,351	92.2%	1,219	162,387	93.2%
Completed development properties (1)	140	40,763	43.5%	141	38,634	56.4%
Total operating portfolio	1,331	197,114	82.1%	1,360	201,021	86.1%
Assets held for sale at December 31, 2008				50	7,559	67.0%
Total	1,331	197,114	82.1%	1,410	208,580	85.5%

(1) Included at December 31, 2008, are 93 properties with 23.7 million square feet on which development was completed in 2008. Included as of December 31, 2007, are 94 properties with 21.5 million square feet that were contributed to property funds during 2008 and therefore are no longer in our portfolio as of December 31, 2008. The leased percentage fluctuates based on the composition of properties.

The decrease in rental income in 2008 from 2007 is due primarily to the contributions of properties to the unconsolidated property funds, offset partially by increases in rental rates on turnovers, new leasing activity in our development properties and increases in rental recoveries. Under the terms of our lease agreements, we are able to recover the majority of our rental expenses from customers. Rental expense recoveries, included in both rental income and expenses, were $226.3 million, $209.4 million and $174.5 million for the years ended December 31, 2008, 2007 and 2006 respectively. The increases in rental expense recoveries were driven by increased property taxes and

common area maintenance expenses such as utilities and snow removal costs. In addition to the increased recoverable expenses, property management costs and certain non-recoverable costs have increased as well, offset somewhat by a decrease in expenses due to the contribution or disposition of the properties. The increase in property management costs in 2008 over 2007 of $10.5 million is due largely to the increase in the number of properties we manage on behalf of the property funds. The increase in non-recoverable costs included a $6.0 million insurance adjustment made during the first quarter of 2008 due to a tornado that struck certain properties owned by us and owned by the property funds and insured by us through our insurance company.

The increases in rental income and rental expenses, in 2007 over 2006, are due to us owning more properties in 2007 than 2006 as a result of the timing of contributions, as well as increases in the net operating income of the same store properties we own directly. During the third quarter of 2007, we acquired all of the units in MPR, an Australian listed property trust that had an 89% ownership interest in ProLogis North American Properties Fund V. This transaction resulted in us owning 100% of the assets for approximately two months, when the lender converted certain of the bridge debt into equity of a new property fund, ProLogis North American Industrial Fund II, in which we have a 36.9% equity interest (collectively the MPR Transaction). As we held these properties directly and consolidated their operating results for a short time in 2007, we had net operating income associated with these properties of approximately $17 million in 2007. During the

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remainder of 2007 and all of 2008, we recognized our proportionate share of the results of these properties through our Earnings (Loss) from Unconsolidated Property Funds.

Investment Management Segment

The net operating income of the investment management segment consists of: (i) earnings or losses recognized under the equity method from our investments in property funds and certain joint ventures (that develop or own industrial or retail properties); (ii) fees and incentives earned for services performed; and (iii) interest earned on advances. The net earnings or losses of the unconsolidated investees may include the following income and expense items of our unconsolidated investees, in addition to rental income and rental expenses: (i) interest income and interest expense; (ii) depreciation and amortization expenses; (iii) general and administrative expenses; (iv) income tax expense; (v) foreign currency exchange gains and losses; (vi) gains or losses on dispositions of properties or investments; and (vii) impairment charges. The fluctuations in income we recognize in any given period are generally the result of: (i) variances in the income and expense items of the unconsolidated investees; (ii) the size of the portfolio and occupancy levels in each period; (iii) changes in our ownership interest; and (iv) fluctuations in foreign currency exchange rates at which we translate our share of net earnings to U.S. dollars, if applicable. The costs of the property management function performed by us for the properties owned by the property funds and joint ventures are reported in the direct owned segment and the costs of the investment management function are included in our general and administrative expenses. See Notes 5 and 19 to our Consolidated Financial Statements in Item 8 for additional information on our unconsolidated investees and for a reconciliation of net operating income to earnings (loss) before minority interest.

The net operating income from the investment management segment was as follows for the periods indicated (in thousands):

	Years Ended December 31,		
	2008	**2007**	**2006**
Unconsolidated property funds:			
North America (1)	$ 65,024	$ 64,325	$ 117,532
Europe (2)	(42,460)	104,665	167,227
Asia (3)	39,331	30,182	20,225
Unconsolidated joint ventures (4)	4,546	(3,221)	41,996
Total net operating income investment management segment	$ 66,441	$ 195,951	$ 346,980

(1) Represents the income earned by us from our investments in property funds in North America. We had interests in 12, 12 and 10 property funds at December 31, 2008, 2007 and 2006, respectively that owned, on a combined basis, 854, 777 and 535 properties at December 31, 2008, 2007 and 2006, respectively. Our ownership interests ranged from 20% to 50% at December 31, 2008. Included in 2008 are net losses of $28.2 million, which represent our proportionate share of losses that were recognized by certain of the property funds, related to interest rate derivative contracts that no longer met the requirements for hedge accounting. Excluding these losses, the increase in net operating income we recognized in 2008 over 2007 is due principally to increased management fees and income from the larger portfolios in the property funds.

In January 2006, we purchased the 80% ownership interests held by our fund partner in three property funds and subsequently contributed substantially all of the assets and associated liabilities to the North American Industrial Fund in March 2006. In connection with this transaction, we earned an incentive return of $22.0 million and we recognized $37.1 million in income, representing our proportionate share of the net gain recognized by the property funds upon termination.

(2) In 2008 and 2007, amounts represent the income earned by us from our investments in two property funds in Europe, PEPR and PEPF II, and, prior to the formation of PEPF II in the third quarter of 2007, represents the income from our investment in PEPR. On a combined basis, these funds owned 399, 288 and

277 properties at December 31, 2008, 2007 and 2006, respectively. Our ownership interest in PEPR and PEPF II was 24.9% and 36.9%, respectively, at December 31, 2008 including both our direct and indirect investments. Our ownership interest in PEPF II includes our direct ownership interest of 34.3% and our indirect 2.6% interest through our ownership in PEPR, which owned a 10.4% interest in PEPF II.

Included in 2008, are $108.2 million of losses representing our share of losses recognized by PEPR on the sale of its 20% investment in PEPF II to us and an impairment charge related to its remaining 10% interest. In February 2009, PEPR sold its 10% interest to a third party, which decreased our ownership interest in PEPF II to 34.3%. In July 2007, PEPR disposed of 47 properties, which resulted in our recognition of additional earnings of $38.2 million, representing our proportionate share of the gain recognized by PEPR. In 2006, we recognized $109.2 million in incentive return fees in connection with PEPR s Initial Public Offering (IPO).

(3) Represents the income earned by us from our 20% ownership interest in two property funds in Japan and one property fund in South Korea. These property funds on a combined basis owned 83, 66 and 31 properties at December 31, 2008, 2007 and 2006. In 2009, we sold our investments in the Japan property funds to our fund partner. See Note 21 to our Consolidated Financial Statements in Item 8.

(4) All periods have been restated to include our proportionate share of the net earnings or losses related to our joint ventures that develop and operate principally industrial and retail properties. These amounts were previously included in the CDFS business segment but were transferred in connection with the changes in our business segments made in 2008. Included in the earnings for 2006 was $35.0 million, representing our share of the earnings of a joint venture, that redeveloped and sold land parcels. This entity substantially completed its operations at the end of 2006.

CDFS Business Segment

Net operating income from the CDFS business segment consists primarily of: (i) gains resulting from the contributions and dispositions of properties, generally developed by us or acquired with the intent to contribute to an existing or new property fund; (ii) gains from the dispositions of land parcels, including land subject to ground leases and properties to third parties; (iii) fees earned for development services provided to customers and third parties; and (iv) certain costs associated with the potential acquisition of CDFS business assets and land holding costs. We recognize a gain based on the increased fair value of the property at the time of contribution, as supported by third party appraisals, to the extent of third party ownership interest in the property fund or unconsolidated investee acquiring the property. See Note 19 to our Consolidated Financial Statements in Item 8 for a reconciliation of net operating income to earnings (loss) before minority interest.

For 2008, our net operating income in this segment, excluding amounts presented as discontinued operations in our Consolidated Financial Statements, was $657.9 million, as compared to $786.2 million in 2007, a decrease of $128.3 million. The decrease was due to a lower level of contributions in 2008, a decrease in our net profit margins on developed and repositioned properties and lower gains on sales of land. In 2008, 18.6% of the net operating income of this operating segment was generated in North America, 47.3% was generated in Europe and 34.1% was generated in Asia.

For 2007, our net operating income in this segment, excluding amounts presented as discontinued operations in our Consolidated Financial Statements, was $786.2 million, as compared to $334.5 million in 2006, an increase of $451.7 million or 135%. The increased net operating income in this segment in 2007 over 2006 was primarily due to increased levels of dispositions brought about by increased development activity, the creation of new property funds in Europe and North America, the MPR acquisition as discussed above and additional gains on the sales of land parcels. In 2007, 32.5% of the net operating income of this operating segment was generated in North America, 36.8%

was generated in Europe and 30.7% was generated in Asia. In 2006, 40.6% of the net operating income of this segment was generated in North America, 32.0% was generated in Europe and 27.4% was generated in Asia.

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The CDFS business segment s net operating income includes the following components for the periods indicated (in thousands):

	Years Ended December 31,		
	2008	2007	2006
CDFS transactions in continuing operations:			
Disposition proceeds, prior to deferral (1)	$ 4,679,900	$ 5,230,788	$ 1,337,278
Proceeds deferred and not recognized (2)	(209,484)	(243,411)	(65,542)
Recognition of previously deferred amounts (2)	25,049	18,035	15,105
Cost of dispositions (1)	(3,836,519)	(4,241,700)	(993,926)
Net gains	658,946	763,712	292,915
Development management and other income (3)	25,857	26,322	37,443
Other income (expense), net (4)	(26,924)	(3,853)	4,176
Total net operating income - CDFS business segment	$ 657,879	$ 786,181	$ 334,534

(1) During 2008, we contributed 163 developed and repositioned properties to the property funds (53 in North America, 99 in Europe and 11 in Japan) and we contributed 17 properties that were acquired property portfolios to the property funds, (6 in North America and 11 in Europe). This compares with 2007 when we contributed 87 developed and repositioned properties (41 in North America, 41 in Europe and 5 in Japan) and we contributed 175 properties that were part of acquired property portfolios to the property funds (162 in North America and 13 in Europe). In 2006 we contributed 55 developed and repositioned properties (30 in North America, 19 in Europe and 6 in Japan). We also recognized net gains of \$3.3 million, \$93.3 million and \$24.6 million from the disposition of land parcels to third parties during 2008, 2007 and 2006, respectively. In addition, we contributed non CDFS properties to the property funds. See discussion below in Gains Recognized on Dispositions of Certain Non-CDFS Business Assets .

The net profit margins we earn in this segment vary quarter to quarter depending on a number of factors, including the type of property contributed, the market in which the land parcel or property is located and other market conditions, including investment capitalization rates. Additionally, we experienced an increase in construction costs due to higher average concrete, oil and steel prices, increasing both our construction costs and the replacement cost of our portfolio during 2008. The net profit margins we earned on developed and repositioned properties contributed in 2008 were lower than 2007 due to a combination of these factors.

(2) When we contribute a property to an entity in which we have an ownership interest, we do not recognize a portion of the proceeds in our computation of the gain resulting from the contribution. The amount of the gain that we defer is based on our continuing ownership interest in the contributed property that arises due to our ownership interest in the entity acquiring the property. We defer this portion of the gain by recognizing a reduction to our investment in the applicable unconsolidated investee. If a loss results when a property is contributed, the entire loss is recognized when it is known.

When a property that we originally contributed to an unconsolidated investee is disposed of by the unconsolidated investee to a third party, we recognize a gain during the period that the disposition occurs related to the gains we had previously deferred, in addition to our proportionate share of the gain recognized by the

entity. Further, during periods when our ownership interest in a property fund decreases, we recognize gains to the extent that gains were previously deferred to coincide with our new ownership interest in the property fund.

(3) Amounts include fees we earned for the performance of development activities on behalf of our customers or other third parties. These amounts fluctuate based on the level of third party development activities.

(4) Includes land holding costs and charges for previously capitalized costs related to potential CDFS business segment projects when the acquisition is no longer probable, offset by interest income in notes receivable. Due to the changes in our development plans in the fourth quarter of 2008, we expensed certain costs that had been incurred related to potential development projects that we are no longer pursuing.

As discussed earlier, given the challenges that we are facing in this current environment and the corresponding changes we have made to our business strategy, we do not expect to have significant CDFS gains in 2009. Depending on market conditions and other factors, we may contribute either Completed Development Properties and/or Core Properties to the property funds or sell to third parties, although we will no longer report the sales as CDFS proceeds, but instead as gains on the disposition of properties.

Operational Outlook

During the year ended December 31, 2008, our property market fundamentals have held up reasonably well, notwithstanding the current credit markets, which have negatively affected the global economy and our business.

In our total operating portfolio, including properties owned by our unconsolidated investees and managed by us, we leased 121.5 million square feet of space during the year ended December 31, 2008 as compared with 108.6 million square feet in 2007, which included 3.5 million square feet in China. In our direct owned portfolio, we leased 76.8 million square feet, including 32.1 million square feet leased in our development portfolio (both completed properties and those under development). An important fundamental to our long-term growth is repeat business with our global customers. During 2008, 54% of the space leased in our newly developed properties was with repeat customers. We have begun to see customers deferring moving decisions while assessing the impact of current market conditions on their business, which has resulted in a decrease in leasing activity. However, for the leases that expired in 2008, existing customers renewed their leases 79% of the time. Although several of our markets have not been impacted, overall, we expect that leasing will continue to slow and that rents will likely decrease until economic conditions improve.

Due to the great degree of uncertainty in the global markets, we have significantly reduced new development starts. During the fourth quarter, we halted the development of early-stage projects that aggregated 4.0 million square feet with a total expected investment of $559 million. As of December 31, 2008, we had 140 completed development properties that were 43.5% leased with a current investment of approximately $3.0 billion and a total expected investment (including estimated remaining leasing costs) of $3.2 billion. We had 65 properties under development that were 37.2% leased with a current investment of $1.2 billion and a total expected investment of $1.9 billion when completed and leased. Our near-term focus will be to complete the development and leasing of these properties. Once these buildings are leased, we may continue to own them directly, thereby creating additional income in our direct owned segment or we may contribute them to a property fund or sell to a third party, generating cash to reduce our debt.

Other Components of Operating Income

General and Administrative (G&A) Expenses *and* Reduction in Workforce

G&A expenses were $204.3 million in 2008, $193.2 million in 2007 and $147.2 million in 2006. The increases in G&A expenses have been related to our investment in the infrastructure necessary to support our business growth and

expansion into new and existing international markets, the increase in our investment management business, our growing portfolio of properties through acquisitions and development and increased contribution activity. This increase in infrastructure included additional headcount and a higher level of performance-based

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compensation. Strengthening foreign currencies account for a portion of the increase when our international operations are translated into U.S. dollars at consolidation.

In response to the difficult economic climate, we initiated G&A expense reductions with a near-term target of a 20 to 25 percent reduction in G&A, prior to capitalization. In December, we implemented a RIF plan with a total cost of $26.4 million, including $3.3 million for China that is included as discontinued operations in our Consolidated Statements of Operations in Item 8. In addition, we have implemented various cost savings measures in an effort to reduce G&A. Of the total cost of the RIF plan, $20.2 million was unpaid and accrued at December 31, 2008, the majority of which will be paid by March 31, 2009. We may incur RIF charges in 2009 for additional employees identified due to our change in business strategy. Certain of our G&A costs are capitalized as a component of our properties under development. As our development activities have decreased, it is likely the amount we capitalize will decrease and G&A costs on a net basis will increase.

In each of 2007 and 2006, we recognized $5.0 million of expense related to a contribution to our charitable foundation.

Impairment of Real Estate Properties

During 2008 and 2007, we recognized impairment charges of $274.7 million and $12.6 million, respectively. During 2008, as a result of significant adverse changes in market conditions, we reviewed our assets for potential impairment under the appropriate accounting literature. We considered current market conditions, as well as our intent with regard to owning or disposing of the asset, and recognized impairments of certain operating buildings, land held for development or sale and predevelopment costs, all included in our direct owned segment. See Note 13 to our Consolidated Financial Statements in Item 8 for more information.

Depreciation and Amortization

Depreciation and amortization expenses were $339.5 million in 2008, $302.4 million in 2007 and $283.3 million in 2006. The increase in 2008 over 2007 is due primarily to an adjustment in depreciation expense and a higher level of amortization expense related to leasing commissions and other leasing costs. As of September 30, 2008, we had classified a group of properties that we had developed or acquired with the intent to contribute to a property fund or sell to a third party. Our policy is to not depreciate these properties during the period from completion until their contribution provided they meet certain criteria. With the changes in our business segments and the uncertainty as to when, or if, these properties will be contributed and our intent to hold and operate these properties, in the fourth quarter we recorded an adjustment of $30.9 million to depreciate these buildings through December 31, 2008 based on our policy. The increase in 2007 over 2006 is due to acquired real estate assets and intangible lease assets, improvements made to the properties in our direct owned segment and increased leasing activity.

Interest Expense

Interest expense includes the following components (in thousands):

	Year Ended December 31,		
	2008	**2007**	**2006**
Gross interest expense	$ 477,933	$ 487,410	$ 397,453
Net premium amortization	(702)	(7,797)	(13,861)
Amortization of deferred loan costs	12,759	10,555	7,673

Interest expense before capitalization	489,990	490,168	391,265
Capitalized amounts	(148,685)	(121,656)	(95,636)
Net interest expense	$ 341,305	$ 368,512	$ 295,629

Gross interest expense, before capitalization, decreased in 2008 as compared with the same period in 2007 primarily as a result of additional interest costs incurred in 2007 related to the MPR Transaction discussed earlier, offset with increased borrowing (a function of increased development activities, partially offset by contribution activity) at lower borrowing rates. The increase in our development activities also accounted for

the increased capitalized interest. See Note 2 to our Consolidated Financial Statements in Item 8 for a change in accounting that will be adopted in 2009 and will increase our non-cash interest expense between $73 million and $83 million per annum, prior to capitalization of interest. Our future interest expense, both gross and the portion capitalized, will vary depending on the level of our development activities and the interest rates available.

Impairment of Goodwill and Other Assets

In the fourth quarter of 2008, we recognized $320.6 million of impairment charges associated with goodwill and other assets. In connection with our review of the recoverability of goodwill, caused by adverse market conditions, we recognized an impairment charge of $175.4 million related to goodwill in our direct owned segment in Europe. Additionally, we recognized an impairment charge of $145.2 million related to investments in unconsolidated investees, notes receivable and other assets to record these assets at their fair value. See Note 13 to our Consolidated Financial Statements in Item 8 for further information on our goodwill impairment.

Gain on Early Extinguishment of Debt

We completed a tender offer in December 2008 by purchasing $309.7 million aggregate principal amount of 5.25% senior notes due November 15, 2010 for $216.8 million. We utilized cash on hand and borrowings under our global lines of credit to fund the tender offer. Our purchase represents approximately 62 percent of the principal amount of this series of notes outstanding prior to the tender offer. In connection with this transaction, we recognized a gain of $90.7 million that is reported as Gain on Early Extinguishment of Debt in our Consolidated Statements of Operations.

Gains Recognized on Dispositions of Certain Non-CDFS Business Assets

In 2008, 2007 and 2006, we recognized gains of $11.7 million, $146.7 million and $81.5 million on the disposition of 2 properties, 77 properties and 39 properties, respectively, from our direct owned segment to certain of the unconsolidated property funds. Due to our continuing involvement through our ownership in the property funds, these dispositions are not included in discontinued operations and the gains recognized represent the portion attributable to the third party ownership in the property funds that acquired the properties.

Foreign Currency Exchange Gains (Losses), Net

We and certain of our foreign consolidated subsidiaries have intercompany or third party debt that is not denominated in the entity s functional currency. When the debt is remeasured against the functional currency of the entity, a gain or loss may result. To mitigate our foreign currency exchange exposure, we borrow in the functional currency of the borrowing entity when appropriate. Certain of our intercompany debt is remeasured with the resulting adjustment recognized as a cumulative translation adjustment in Other Comprehensive Income (Loss). This treatment is applicable to intercompany debt that is deemed to be long-term in nature. If the intercompany debt is deemed short-term in nature, when the debt is remeasured, we recognize a gain or loss in earnings.

We recognized net foreign currency exchange losses of $148.3 million during 2008 and net foreign currency exchange gains of $8.1 million and $21.4 million during 2007 and 2006, respectively. Predominantly the gains or losses recognized in earnings relate to the intercompany loans between the U.S. parent and our consolidated subsidiaries in Japan and Europe due to the fluctuations in the exchange rates of U.S. dollars to the yen, euro and pound sterling. Included in our 2007 foreign currency exchange gains was $26.6 million from the settlement of several foreign currency forward contracts we purchased to manage the foreign currency fluctuations of the purchase price of MPR, which was denominated in Australian dollars and closed in 2007.

Additionally, we may utilize derivative financial instruments to manage certain foreign currency exchange risks. As of December 31, 2008, we have no outstanding contracts. See Note 17 to our Consolidated Financial Statements in Item 8 for more information on our derivative financial instruments.

Income Taxes

During, 2008, 2007 and 2006, our current income tax expense was $63.4 million, $66.3 million and $83.5 million, respectively. We recognize current income tax expense for income taxes incurred by our taxable REIT subsidiaries and in certain foreign jurisdictions, as well as certain state taxes. We also include in current income tax expense the interest associated with our unrecognized tax benefit liabilities. Our current income tax expense fluctuates from period to period based primarily on the timing of our taxable CDFS income and changes in tax and interest rates.

Certain 1999 through 2005 federal and state income tax returns of Catellus are currently under audit by the Internal Revenue Service (IRS) and various state taxing authorities. In November 2008, we agreed to enter into a closing agreement with the IRS for the settlement of the 1999 through 2002 audits. As a result, we increased our unrecognized tax liability by $85.4 million, including interest and penalties. As this liability was an income tax uncertainty related to an acquired company, we increased goodwill by $66.6 million related to the liability that existed at the acquisition date. The remaining amount is included in current income tax expense in 2008. The payment terms and the closing agreement related to the $230.0 million settlement are in the process of being finalized.

During 2008 and 2007, we recognized deferred tax expense of $4.6 million and $0.5 million, respectively, and a deferred tax benefit of $53.7 million in 2006. In 2008, we recognized indemnification liabilities partially offset by a deferred tax benefit related to the reversal of deferred tax liabilities as a result of impairment charges we recorded that reduced the carrying value of certain assets. In 2007, we recognized deferred tax expense relating primarily to tax indemnification agreements we entered into during the third quarter of 2007 in connection with the formation of PEPF II and the ProLogis Mexico Industrial Fund, net of the benefit recognized from the termination of the indemnification previously provided to ProLogis North American Properties Fund V.

The deferred tax benefit recognized in 2006 was primarily the result of the reversal of deferred tax liabilities recorded in connection with investments acquired through the Catellus Merger, as well as the reversal of a deferred tax obligation related to PEPR. We were previously obligated to the pre-IPO unitholders of PEPR under a tax indemnification agreement related to properties we contributed to PEPR prior to its IPO. Based on the average closing price of the ordinary units of PEPR during the 30-day post-IPO period, we were no longer obligated for indemnification with respect to those properties in the fourth quarter of 2006, and we recognized a deferred tax benefit of $36.8 million related to the reversal of this obligation.

Our income taxes and the current tax indemnification agreements are discussed in more detail in Note 14 to our Consolidated Financial Statements in Item 8.

Discontinued Operations

Discontinued operations represent a component of an entity that has either been disposed of or is classified as held for sale if both the operations and cash flows of the component have been or will be eliminated from ongoing operations of the entity as a result of the disposal transaction and the entity will not have any significant continuing involvement in the operations of the component after the disposal transaction. The results of operations of the component of the entity that has been classified as discontinued operations are reported separately in our consolidated financial statements.

In February 2009, we sold our operations in China to affiliates of GIC Real Estate (GIC RE), the real estate investment arm of the Government of Singapore Investment Corporation. Accordingly, we have classified our China operations as held for sale at December 31, 2008 and included the results in Discontinued Operations for all periods presented in our Consolidated Statements of Operations. Based on the carrying values of the assets and liabilities to be sold as compared with the estimated sales proceeds, less costs to sell, we recognized an impairment charge of

$198.2 million, which is included in Discontinued Operations. See additional information on the sale in Note 21 to our Consolidated Financial Statements in Item 8.

During 2008, 2007 and 2006, we disposed of 15, 80 and 89 properties, respectively, as well as land subject to ground leases, to third parties that met the requirements to be classified as discontinued operations. Therefore,

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the results of operations for these properties, as well as the gain recognized upon disposition, are included in discontinued operations. In addition to our China operations, as of December 31, 2008, 2007 and 2006, we had one, two and eight properties, respectively, classified as held for sale and therefore, the results of operations of these properties are also included in discontinued operations. See Note 7 to our Consolidated Financial Statements in Item 8 for further discussion of discontinued operations.

Other Comprehensive Income (Loss) Foreign Currency Translation Gains (Losses), Net

For our consolidated subsidiaries whose functional currency is not the U.S. dollar, we translate their financial statements into U.S. dollars at the time we consolidate those subsidiaries financial statements. Generally, assets and liabilities are translated at the exchange rate in effect as of the balance sheet date. The resulting translation adjustments, due to the fluctuations in exchange rates from the beginning of the period to the end of the period, are included in Accumulated Other Comprehensive Income (Loss).

During the year ended December 31, 2008, we recognized losses in Other Comprehensive Income (Loss) of $279.6 million related to foreign currency translations of our international business units into U.S. dollars upon consolidation. These losses are mainly the result of the strengthening of the U.S. dollar to the euro and pound sterling offset somewhat by the strengthening of the yen to the U.S. dollar from the beginning of the period to December 31, 2008. During the years ended December 31, 2007 and 2006, we recognized net gains of $90.0 million and $70.8 million, respectively, due primarily to the strengthening euro and pound sterling to the U.S. dollar from the beginning of the period to December 31, 2007 and December 31, 2006, respectively.

Weighted Average Shares Diluted

During the year ended December 31, 2008, approximately 32% of our potentially dilutive stock options and awards were anti-dilutive due to the decline in our average stock price, which caused a decrease in our weighted average common shares outstanding on a dilutive basis. The number of dilutive instruments included fluctuates each period based on our stock price for the period. This decrease in 2008 was partially offset by the larger number of basic common shares outstanding due to the issuance of shares during the respective periods.

Portfolio Information

Our total operating portfolio of properties includes industrial and retail properties owned by us and industrial properties owned by the property funds and joint ventures we manage. The operating portfolio does not include properties under development, properties held for sale or any other properties owned by unconsolidated investees, other than industrial properties, and was as follows (square feet in thousands):

	December 31,					
	2008		2007		2006	
Reportable Business Segment	**Number of Properties**	**Square Feet**	**Number of Properties**	**Square Feet**	**Number of Properties**	**Square Feet**
Direct Owned	1,331	197,114	1,409	208,530	1,473	204,674
Investment Management (1)	1,339	297,665	1,170	250,951	875	186,747
Totals	2,670	494,779	2,579	459,481	2,348	391,421

(1) Amounts for 2007 and 2006 include 39 and 32 industrial properties owned by joint ventures that were previously included in our CDFS segment, primarily China joint ventures that are classified as held for sale at December 31, 2008.

Same Store Analysis

We evaluate the operating performance of the operating properties we own and manage using a same store analysis because the population of properties in this analysis is consistent from period to period, thereby eliminating the effects of changes in the composition of the portfolio on performance measures. We include properties owned by us, and properties owned by the property funds and joint ventures that are managed by us

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(referred to as unconsolidated investees), in our same store analysis. We have defined the same store portfolio, for the year ended December 31, 2008, as those properties that were in operation at January 1, 2007 and have been in operation throughout the full periods in both 2008 and 2007. We have removed all properties that were disposed of to a third party and properties held for sale (including our China operations) from the population for both periods. We believe the factors that impact rental income, rental expenses and net operating income in the same store portfolio are generally the same as for the total portfolio. In order to derive an appropriate measure of period-to-period operating performance, we remove the effects of foreign currency exchange rate movements by using the current exchange rate to translate from local currency into U.S. dollars, for both periods, to derive the same store results. The same store portfolio, for the year ended December 31, 2008, aggregated 369.9 million square feet.

The following is a reconciliation of our consolidated rental income, rental expenses and net operating income, as included in our Consolidated Financial Statements in Item 8, to the respective amounts in our same store portfolio analysis.

	For the Years Ended December 31,		Percentage
	2008	**2007**	**Change**
Rental Income (1)(2)			
Consolidated:			
Rental income per our Consolidated Statements of Operations	$ 1,002,493	$ 1,052,219	
Adjustments to derive same store results:			
Rental income of properties not in the same store portfolio properties developed and acquired during the period	(158,016)	(95,381)	
Rental income of properties in our other segment, not included in the same store portfolio see Note 19 to our Consolidated Financial Statements	(48,627)	(43,046)	
Effect of changes in foreign currency exchange rates and other	(2,298)	(14,105)	
Unconsolidated investees :			
Rental income of properties managed by us and owned by our unconsolidated investees	1,428,908	1,245,748	
Same store portfolio rental income (2)(3)	$ 2,222,460	$ 2,145,435	3.59%
Rental Expenses (1)(4)			
Consolidated:			
Rental expenses per our Consolidated Statements of Operations	$ 325,049	$ 284,421	
Adjustments to derive same store results:			
Rental expenses of properties not in the same store portfolio properties developed and acquired during the period	(60,845)	(29,271)	
Rental expenses of properties in our other segment, not included in the same store portfolio see Note 19 to our Consolidated Financial Statements	(12,928)	(14,819)	
Effect of changes in foreign currency exchange rates and other	(25,360)	(9,483)	
Unconsolidated investees :			
Rental expenses of properties managed by us and owned by our unconsolidated investees	310,978	255,918	

Same store portfolio rental expenses (3)(4)	$ 536,894	$ 486,766	10.30%

	For the Years Ended December 31, 2008	2007	Percentage Change
Net Operating Income (1)			
Consolidated:			
Net operating income per our Consolidated Statements of Operations	$ 677,444	$ 767,798	
Adjustments to derive same store results:			
Net operating income of properties not in the same store portfolio properties developed and acquired during the period	(97,171)	(66,110)	
Net operating income of properties in our other segment, not included in the same store portfolio see Note 19 to our Consolidated Financial Statements	(35,699)	(28,227)	
Effect of changes in foreign currency exchange rates and other	23,062	(4,622)	
Unconsolidated investees :			
Net operating income of properties managed by us and owned by our unconsolidated investees	1,117,930	989,830	
Same store portfolio net operating income (3)	$ 1,685,566	$ 1,658,669	1.62%

(1) As discussed above, our same store portfolio aggregates properties from our consolidated portfolio and properties owned by the property funds and industrial joint ventures that are managed by us and in which we invest. During the periods presented, certain properties owned by us were contributed to an unconsolidated investee and are included in the same store portfolio on an aggregate basis. Neither our consolidated results nor that of the unconsolidated investees, when viewed individually, would be comparable on a same store basis due to the changes in composition of the respective portfolios from period to period (for example, the results of a contributed property would be included in our consolidated results through the contribution date and in the results of the unconsolidated investee subsequent to the contribution date).

(2) Rental income in the same store portfolio includes straight-line rents and rental recoveries, as well as base rent. We exclude the net termination and renegotiation fees from our same store rental income to allow us to evaluate the growth or decline in each property s rental income without regard to items that are not indicative of the property s recurring operating performance. Net termination and renegotiation fees represent the gross fee negotiated to allow a customer to terminate or renegotiate their lease, offset by the write-off of the asset recognized due to the adjustment to straight-line rents over the lease term. The adjustments to remove these items are included as effect of changes in foreign currency exchange rates and other in the tables above.

(3) These amounts include rental income, rental expenses and net operating income of both our consolidated properties and those properties owned by our unconsolidated investees and managed by us.

(4) Rental expenses in the same store portfolio include the direct operating expenses of the property such as property taxes, insurance, utilities, etc. In addition, we include an allocation of the property management expenses for our direct-owned properties based on the property management fee that is provided for in the individual management agreements under which our wholly owned management companies provides property management services to each property (generally, the fee is based on a percentage of revenues). On consolidation, the management fee

income earned by the management company and the management fee expense recognized by the properties are eliminated and the actual costs of providing property management services are recognized as part of our consolidated rental expenses. These include the costs to manage the properties we own directly and the properties owned by our unconsolidated investees. These expenses fluctuate based on the level of properties included in the same store portfolio and any adjustment is included as effect of changes in foreign currency exchange rates and other in the above table. In

addition, for the year ended December 31, 2008, we recognized a $6.0 million increase in insurance expense due to a tornado that struck certain properties owned by us and the property funds, which we insure through our insurance company. This amount is included as effect of changes in foreign currency exchange rates and other in the tables above.

Environmental Matters

For a discussion of environmental matters, see Note 18 to our Consolidated Financial Statements in Item 8 and also Item 1A. Risk Factors.

Liquidity and Capital Resources

Overview

We consider our ability to generate cash from operating activities, contributions and dispositions of properties and from available financing sources to be adequate to meet our anticipated future development, acquisition, operating, debt service and shareholder distribution requirements.

As discussed earlier, our current business strategy has a significant emphasis on liquidity. At the beginning of the fourth quarter, we set a goal to reduce leverage through the reduction of our total debt by $2 billion as of December 31, 2009. We intend to accomplish this goal through a number of actions, which have included or may include the following (depending on market conditions and other factors):

Generate cash through the contributions of properties to the unconsolidated property funds or sales of assets to third parties. In the fourth quarter, we generated $1.3 billion of proceeds from the contributions of properties to the unconsolidated property funds or sales to third parties. In February 2009, we sold our China operations and investments in the Japan property funds for $1.3 billion of cash, of which $500 million was received on closing and was used to pay down borrowings on our credit facilities and the remaining $800 million will be funded upon satisfactory completion of certain year-end audits. In the event that the audits reflect a material disparity from the unaudited information previously furnished, the buyer will have the option to unwind the transaction at our expense. If this happens, we will use available credit facilities to refund the $500 million to the buyer and pay expenses;

Repurchase our senior notes. In December, we bought $310 million aggregate principal of notes for $217 million using proceeds on our line of credit;

Issue equity;

Reduce cash needs. We halted early-stage development projects, initiated G&A cost savings initiatives and implemented a RIF plan; and

Lower our common share distribution. We reduced our expected annual distribution rate from $2.07 to $1.00 per common share beginning with the first quarter of 2009.

At December 31, 2008, our credit facilities provide aggregate borrowing capacity of $4.4 billion. This includes our global line of credit, where a syndicate of banks allows us to draw funds in U.S. dollar, euro, Japanese yen, British pound sterling, South Korean won and Canadian dollar (Global Line). This also includes a multi-currency credit facility that allows us to borrow in U.S. dollar, euro, Japanese yen, and British pound sterling (Credit Facility) and a 35 million British pound sterling facility (Sterling Facility). The total commitments under our credit facilities fluctuate

in U.S. dollars based on the underlying currencies. Based on our public debt ratings, interest on the borrowings under the Global Line and Credit Facility primarily accrues at a variable rate based upon the interbank offered rate in each respective jurisdiction in which the borrowings are outstanding (2.46% per annum at December 31, 2008 based on a weighted average using local currency rates).

The Global Line and Credit Facility mature in October 2009; however, we can exercise a 12-month extension at our option for all currencies, subject to certain customary conditions and the payment of an extension fee.

These customary conditions include: (i) we are not in default; (ii) we have appropriately approved such an extension; and (iii) we certify that certain representations and warranties, contained in the agreements, are true and correct in all material respects. We expect to exercise this option. The Credit Facility provides us the ability to re-borrow, within a specified period of time, any amounts repaid on the facility. The Sterling Facility matures December 31, 2009.

As of December 31, 2008, under these facilities, we had outstanding borrowings of $3.2 billion and letters of credit of $142.4 million, resulting in remaining borrowing capacity of approximately $1.1 billion. These amounts do not include borrowing capacity of $106.0 million with outstanding borrowings of $78.6 million related to our China operations, which are presented as held for sale at December 31, 2008. All outstanding amounts related to the China borrowings were refinanced subsequent to December 31, 2008 and assumed by the buyer in connection with the sale and we no longer have a renminbi tranche under the Global Line.

As of December 31, 2008, we had the following amounts outstanding under all our credit facilities (in millions):

	Total Commitment	Outstanding Debt Balance	Outstanding Letters of Credit	Remaining Capacity
Global Line	$ 3,783	$ 2,618	$ 109	$ 1,056
Credit Facility	600	600		
Sterling Facility	49		33	16
Total	$ 4,432	$ 3,218	$ 142	$ 1,072

In April 2008, we repaid $250.0 million of maturing senior notes with available cash. In May 2008, we closed on $600.0 million of senior notes maturing 2018 with a coupon rate of 6.625% and $550.0 million of 2.625% convertible senior notes. The proceeds were used to repay $346.6 million of secured debt that was scheduled to mature in November 2008, borrowings on our credit facilities and for general corporate purposes. See Note 8 to our Consolidated Financial Statements in Item 8 for further information on the convertible notes.

In addition to common share distributions and preferred share dividend requirements, we expect our primary short and long-term cash needs will consist of the following for 2009 and future years:

- completion of the development and leasing of the properties in our development portfolio. As of December 31, 2008, we had 65 properties under development with a current investment of $1.2 billion and a total expected investment of $1.9 billion when completed and leased;

- repayment of debt, including payments on our credit facilities or buy-back of senior unsecured notes in order to achieve our goal of reducing debt;

- scheduled principal payments. In 2009, we have scheduled principal payments of $339.3 million, which includes $250.0 million of floating rate senior notes that mature in August 2009;

- tax and interest payments of $230.0 million related to the completion of certain audits of Catellus tax returns;

capital expenditures and leasing costs on properties, including completed development properties that are not yet leased;

investments in current or future unconsolidated property funds, including our remaining capital commitments of $970.4 million. Generally, we fulfill our equity commitment with a portion of the proceeds from properties we contribute to the property fund. However, to the extent a property fund acquires properties from a third party or requires cash to pay-off debt or has other cash needs, we may be required to contribute our proportionate share of the equity component in cash to the property fund; and depending on market conditions, direct acquisitions or development of operating properties and/or portfolios of operating properties in key distribution markets for direct, long-term investment in the direct owned segment;

We expect to fund cash needs for 2009 and future years primarily with cash from the following sources, all subject to market conditions:

- proceeds of $1.3 billion expected to be received from the sale of our China operations and investments in the Japan property funds;
- available cash balances ($174.6 million at December 31, 2008);
- property operations;
- fees and incentives earned for services performed on behalf of the property funds and distributions received from the property funds;
- proceeds from the disposition of properties or land parcels to third parties;
- cash proceeds from the contributions of properties to property funds;
- borrowing capacity under existing credit facilities ($1.1 billion available as of December 31, 2008), or other future facilities;
- proceeds from the issuance of equity securities, including sales under various common share plans, all subject to market conditions. We have 11.6 million authorized shares available under our Controlled Equity Offering Program and our Board has authorized an increase to 40.0 million shares); and
- proceeds from the issuance of debt securities, including the issuance of secured debt.

We consider our ability to generate cash from operating activities, contributions and dispositions of properties and from available financing sources to be adequate to meet our anticipated development, acquisition, operating, debt service and shareholder distribution requirements for 2009.

We may seek to retire or purchase our outstanding debt or equity securities through cash purchases, in open market purchases, privately negotiated transactions or otherwise. Such repurchases or exchanges, if any, will depend on prevailing market conditions, our liquidity requirements, contractual restrictions and other factors. The amounts involved may be material. We have approximately $84.1 million remaining on authorization to repurchase common shares that was approved by our Board in 2001. We have not repurchased our common shares since 2003.

Debt Covenants

Under the terms of certain of our debt agreements, we are currently subject to six different sets of financial covenants that include leverage ratios, fixed charge and debt service coverage ratios, investments and indebtedness to total asset value ratios, minimum consolidated net worth and restrictions on distributions and redemptions. The most restrictive covenants relate to the total leverage ratio and the fixed charge coverage ratio. All covenants are calculated based on the definitions and calculations included in the respective debt agreements.

As of December 31, 2008, we were in compliance with all of our debt covenants.

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Commitments Related to Future Contributions to Property Funds

The following table outlines acquisitions made by the property funds from ProLogis and third parties during the year ended December 31, 2008, including the related financing of such acquisitions, and the remaining equity commitments of the property fund as of December 31, 2008 (dollars in millions):

	Fund Acquisitions					Remaining Equity Commitments			Available
					Equity				Under
		Third			and		Fund	Expiration	Credit
	ProLogis	Parties	Total	Debt	Other	ProLogis	Partners	Date	Facility
ProLogis North American Industrial Fund (1)	$ 815.2	$	$ 815.2	$ 243.0	$ 572.2	$ 72.5	$ 211.7	2/10	$ 223.4
ProLogis Mexico Industrial Fund (2)	155.0	189.8	344.8	155.8	189.0	44.3	246.7	8/10	
ProLogis European Properties Fund II (2)(3)	2,604.3	84.0	2,688.3	1,172.1	1,516.2	830.4(4)	1,253.1(4)	8/10	77.7
ProLogis Japan Properties Fund II (5)	876.8	83.7	960.5	555.0	405.5				
ProLogis Korea Fund (2)	11.1	119.1	130.2	25.2	105.0	23.2	92.8	6/10	
Total	$ 4,462.4	$ 476.6	$ 4,939.0	$ 2,151.1	$ 2,787.9	$ 970.4	$ 1,804.3		$ 301.1

(1) The investor agreements were modified in early 2009 to extend the remaining equity commitments through 2010, which were originally scheduled to expire in February 2009. In connection with the modifications, the commitments related to property contributions were eliminated and one investor did not extend its commitment. Amounts presented reflect these changes. We expect the remaining equity commitments to be used to pay down existing debt or to make opportunistic acquisitions, depending on market conditions and other factors.

(2) We are committed to offer to contribute substantially all of the properties that we develop and stabilize in Europe, Mexico and South Korea to these respective funds. These property funds are committed to acquire such properties, subject to certain exceptions, including that the properties meet certain specified leasing and other criteria, and that the property funds have available capital. We are not obligated to contribute properties at a loss.

Dependent on market conditions, we expect to make contributions of properties to these property funds in 2009. Given the current debt markets, it is likely that the acquisitions will be financed by the property funds with all equity. Generally, the properties are contributed based on third-party appraised value (see Note 3 below).

(3) During the fourth quarter, we modified the determination of the contribution value related to 2009 contributions to PEPF II. After the capitalization rate is determined based on a third party appraisal, a margin of 0.25 to 0.75 percentage points is added depending on the quarter contributed. This modification was made due to the belief that appraisals were lagging true market conditions. The agreement provides for an adjustment in our favor if the appraised values at the end of 2010 are higher than those used to determine contribution values.

(4) PEPF II s equity commitments are denominated in euro and include ProLogis of 568.1 million, PEPR of 136.1 million and remaining fund partners of 721.3 million. Our equity commitments include the 20% interest in PEPF II we acquired from PEPR in December 2008.

(5) In connection with the sale of our investments in the Japan property funds, we entered into an agreement to sell a property in Japan to our fund partner in 2009, which will utilize the remaining equity commitment from our fund partner. This property is included in assets held for sale at December 31, 2008 in our Consolidated Financial Statements in Item 8.

Generally, we fulfill our equity commitment with a portion of the proceeds from properties we contribute to the property fund. However, to the extent a property fund acquires properties from a third party or requires cash to pay-off debt or has other cash needs, we may be required to contribute our proportionate share of the equity component in cash to the property fund.

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Cash Provided by Operating Activities

Net cash provided by operating activities was $843.6 million for 2008, $1.2 billion for 2007, and $687.3 million for 2006. The decrease in cash provided by operating activities in 2008 over 2007 is due to the decrease in net earnings primarily as a result of lower gains on contributions and dispositions of properties and changes in our operating assets and liabilities. Cash provided by operating activities exceeded the cash distributions paid on common shares and dividends paid on preferred shares in both periods. As discussed earlier, we do not expect gains from CDFS contributions in 2009 and as a result, expect cash flow from operations to also decrease in 2009 over 2008.

The increase in cash provided by operating activities in 2007 over 2006 is due primarily to higher CDFS gains on contributions of properties to the property funds in 2007, adjusted for non-cash items. Operational items that impact net cash provided by operating activities are more fully discussed in - Results of Operations. Cash provided by operating activities exceeded the cash distributions paid on common shares and dividends paid on preferred shares in all periods.

Cash Investing and Cash Financing Activities

For 2008, 2007 and 2006, investing activities used net cash of $1.3 billion, $4.1 billion and $2.1 billion, respectively. The following are the more significant activities for all periods presented:

We invested $5.6 billion in real estate during the year ended December 31, 2008; $5.3 billion for the same period in 2007, excluding the MPR and Parkridge acquisitions; and $3.8 billion for the same period in 2006, excluding the purchase of ownership interests in property funds. These amounts include the acquisition of operating properties (25 properties, 41 properties and 74 properties with an aggregate purchase price of $324.0 million, $351.6 million and $735.4 million in 2008, 2007 and 2006, respectively); acquisitions of land or land use rights for future development; costs for current and future development projects; and recurring capital expenditures and tenant improvements on existing operating properties. At December 31, 2008, we had 65 distribution and retail properties aggregating 19.8 million square feet under development, with a total expected investment of $1.9 billion.

In February 2007, we purchased the industrial business and made a 25% investment in the retail business of Parkridge. The total purchase price was $1.3 billion of which we paid cash of $733.9 million and the balance in common shares or assumption of liabilities.

On July 11, 2007, we completed the acquisition of MPR for total consideration of approximately $2.0 billion, consisting of $1.2 billion of cash and the assumption of debt and other liabilities of $0.8 billion. The cash portion was financed by the issuance of a $473.1 million term loan and a $646.2 million convertible loan with an affiliate of Citigroup. On August 27, 2007, when Citigroup converted $546.2 million of the convertible loan into equity of a newly created property fund, ProLogis North American Industrial Fund II, we made a $100.0 million cash equity contribution to the property fund, which it used to repay the remaining balance on the convertible loan and included in the $661.8 million of investments to unconsolidated investees.

We generated net cash from contributions and dispositions of properties and land parcels of $4.5 billion, $3.6 billion and $2.1 billion in 2008, 2007 and 2006, respectively. See further discussion in - Results of Operations-CDFS Business Segment .

We invested cash of $329.6 million, $661.8 million and $175.7 million in 2008, 2007 and 2006, respectively, in new and existing unconsolidated investees. These investments principally include our proportionate share of the equity component for third-party acquisitions made by the property funds and investments and advances to

development joint ventures. In 2008, our investments include $167.3 million in PEPF II and $68.5 million in joint ventures operating in China. In 2007, our investments include $100.0 million in ProLogis North American Industrial Fund II, $360.0 million in ProLogis North American Industrial Fund III, and excludes the initial investment in the Parkridge retail business, which is detailed separately. The 2006 investments include $34.6 million in North American Industrial Fund, $56.5 million

in joint ventures operating in China, along with $54.6 million in a preferred interest in ProLogis North American Properties Fund V, which we subsequently sold in August 2006.

We invested cash of $259.2 million in connection with the purchase of our fund partner s ownership interests in three of our North America property funds during the first quarter of 2006.

We received proceeds from unconsolidated investees as a return of investment of $127.0 million, $50.2 million and $146.2 million in 2008, 2007 and 2006, respectively. The proceeds in 2006 include $54.6 million related to the sale of a preferred interest in ProLogis North American Properties Fund V discussed above.

We generated net cash proceeds from payments on notes receivable of $4.2 million and $97.4 million in 2008 and 2007, respectively, and net cash payments for advances on notes receivable of $41.7 million in 2006.

For 2008, 2007 and 2006, financing activities provided net cash of $358.1 million, $2.7 billion and $1.6 billion, respectively. The following are the more significant activities for all periods presented as summarized below:

In May 2008 we closed on $550.0 million of 2.625% convertible senior notes due in 2038. The proceeds were used to repay secured debt and borrowings on our credit facilities and for general corporate purposes. In March 2007, we issued $1.25 billion with a coupon rate of 2.25% due in March 2037 and in November 2007, we issued $1.12 billion with a coupon rate of 1.875% due in November 2037. We used the net proceeds of the offerings to repay a portion of the outstanding balance under our Global Line and senior notes that were maturing in November 2007 and for general corporate purposes.

On our lines of credit and other credit facilities, including the Global Line and the Credit Facility, we had net proceeds from borrowings of $743.9 million and $368.2 million in 2008 and 2006, respectively, and net payments of $431.5 million in 2007.

During 2007, we received proceeds of $1.1 billion and $600.1 million under facilities used to partially finance the MPR and Parkridge acquisitions, respectively (see Note 5 and Note 8 to our Consolidated Financial Statements in Item 8).

On our other debt, we had net payments of $1.2 billion, $1.2 billion and $588.8 million for the year ended December 31, 2008, 2007 and 2006, respectively. In May 2008, we issued $600.0 million of 6.625% senior notes due 2018. In 2007 and 2006, we received proceeds of $781.8 million and $1.9 billion from the issuance of senior notes and other secured and unsecured debt, respectively.

We paid distributions to holders of common shares of $542.8 million, $472.6 million and $393.3 million in 2008, 2007 and 2006, respectively. We paid dividends on preferred shares of $25.4 million, $31.8 million and $19.1 million in 2008, 2007 and 2006, respectively.

We generated proceeds from the sale and issuance of common shares of $222.2 million, $46.9 million and $358.0 million in 2008, 2007 and 2006, respectively. This includes $196.4 million received in 2008 for the issuance of 3.4 million common shares and $320.8 million received in 2006 for the issuance of 5.4 million common shares, both under our Controlled Equity Offering Program.

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Off-Balance Sheet Arrangements

Liquidity and Capital Resources of Our Unconsolidated Investees

We had investments in and advances to property funds at December 31, 2008, of $2.0 billion. The property funds had total third party debt of $13.5 billion (for the entire entity, not our proportionate share) at December 31, 2008 that matures as follows (dollars in millions):

	2009	2010	2011	2012	2013	Thereafter	Total (1)
ProLogis European Properties (2)	$ 490.9	$ 1,460.6	$	$ 378.4	$	$ 730.8	$ 3,060.7
ProLogis European Properties Fund II (3)		1,383.9			385.3		1,769.2
ProLogis California LLC (4)	314.2						314.2
ProLogis North American Properties Fund I		130.6	111.7				242.3
ProLogis North American Properties Fund VI-X	2.1	2.2	2.4	882.1	12.4		901.2
ProLogis North American Properties Fund XI	14.8	42.7	0.7	0.7	0.4		59.3
ProLogis North American Industrial Fund (5)		26.6	190.0	78.0	169.5	1,047.7	1,511.8
ProLogis North American Industrial Fund II (6)	454.1	108.6	(1.9)	153.0	63.1	548.3	1,325.2
ProLogis North American Industrial Fund III (7)	167.3	2.0	120.1	2.3	385.0	426.2	1,102.9
ProLogis Mexico Industrial Fund (8)				99.1	170.0		269.1
ProLogis Korea Fund			14.0	28.2			42.2
	$ 1,443.4	$ 3,157.2	$ 437.0	$ 1,621.8	$ 1,185.7	$ 2,753.0	$ 10,598.1
Japan property funds (9)							2,864.3
Total property funds							$ 13,462.4

(1) As of December 31, 2008, we had not guaranteed any of the third party debt. In our role as the manager of the property funds, we work with the property funds to refinance their maturing debt. There can be no assurance that the property funds will be able to refinance any maturing indebtedness at terms as favorable as the maturing debt, or at all. If the property funds are unable to refinance the maturing indebtedness with newly issued debt, they may be able to otherwise obtain funds by capital contributions from us and our fund partners, in proportion to our ownership interest in such funds, or by selling assets. Certain of the property funds also have credit facilities, which may be used to obtain funds. Generally, the property funds issue long-term debt and utilize the proceeds to repay borrowings under the credit facilities. See above for information on remaining equity commitments of the property funds.

(2) PEPR has $490.9 million of Collateralized Mortgage Backed Securities (CMBS) maturing in July 2009. We are currently in negotiations with German mortgage banks to refinance the debt. PEPR has a credit facility that matures in May 2010, with aggregate borrowing capacity of 900 million (or $1.3 billion) under which $816.9 million was outstanding with $498.6 million remaining capacity, all at December 31, 2008. The facility has three tranches; (i) a 300 million revolving credit facility that matures December 13, 2010; (ii) a 300 million term loan facility that matures December 13, 2010; and (iii) a 300 million term loan facility that matures December 11, 2012. In addition, PEPR has cash of $112.7 million at December 31, 2008, primarily due to the sale of its equity investment in PEPF II to us. No assurances can be given that this property fund will be able to refinance this debt on favorable terms or at all.

(3) PEPF II has a 1 billion credit facility (approximately $1.46 billion) to partially fund property acquisitions. As of December 31, 2008, approximately $1.38 billion was outstanding and $77.7 million was available to borrow under this facility. The property fund is in discussions with a group of German mortgage banks for a five-year loan for 350 million.

(4) ProLogis California LLC has $314.2 million maturing in 2009 (approximately half in March and half in August). We have term sheets from existing lenders to extend the 2009 maturities for one to five years and we have rate lock agreements on a new $120 million, ten year financing. No assurances can be given that this property fund will be able to refinance this debt on favorable terms or at all.

(5) ProLogis North American Industrial Fund has a $250.0 million credit facility that matures July 17, 2010, under which approximately $26.6 million was outstanding and $223.4 million was available at December 31, 2008. Capital was called on February 10, 2009 to repay the outstanding balance.

(6) The maturities in 2009 include a term loan for $411.4 million that was issued by our fund partner in July 2007 when this property fund was formed and matures in July 2009. We are in active discussions with our fund partner regarding an extension of the term loan, as well as their underlying equity investment in the property fund. No assurances can be given that this property fund will be able to refinance this debt on favorable terms or at all.

(7) The 2009 maturities include a $165.4 million that represents a bridge loan that was issued by a subsidiary of our fund partner, Lehman Brothers Holding, Inc., at the formation of the fund in July 2007 that was due in 2008. We have been in discussions with the lender and hope to extend the maturity date for three years. No assurances can be given that this property fund will be able to refinance this debt on favorable terms or at all.

(8) In addition to its existing third party debt, this property fund has a note payable to us for $15.2 million at December 31, 2008.

(9) In 2009, we sold our investments in the Japan property funds to our fund partner.

Contractual Obligations

Long-Term Contractual Obligations

We had long-term contractual obligations at December 31, 2008 as follows (in millions):

		Payments Due By Period			
	Total	**Less than 1 year**	**1 to 3 years**	**3 to 5 years**	**More than 5 years**
Debt obligations, other than credit facilities	$ 7,795	$ 339	$ 811	$ 4,001	$ 2,644
Interest on debt obligations, other than credit facilities	1,941	342	629	413	557
Unfunded commitments on development projects (1)	701	701			
Unfunded commitments on acquisitions	7	7			
Unfunded capital commitments to unconsolidated investees (2)	971		971		
Amounts due on credit facilities (3)	3,218		3,218		
Interest on lines of credit (3)	127	79	48		
Tax liabilities (4)	285	50	100	135	
Totals	$ 15,045	$ 1,518	$ 5,777	$ 4,549	$ 3,201

(1) We had properties under development at December 31, 2008 with a total expected investment of $1.9 billion. The unfunded commitments presented include not only those costs that we are obligated to fund under construction

contracts, but all costs necessary to place the property into service, including the costs of tenant improvements and marketing and leasing costs.

(2) Generally, we fulfill our equity commitment with a portion of the proceeds from properties we contribute to the property fund. However, to the extent a property fund acquires properties from a third party or requires cash to pay-off debt or has other cash needs, we may be required to contribute our proportionate share of the equity component in cash to the property fund.

(3) For purposes of this table, we have assumed that we exercise our option to extend these facilities.

(4) These amounts represent our Financial Accounting Standards Board Interpretation No. 48, *Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109* (FIN 48) liabilities, which include an estimate of the period of settlement. See Note 14 to our Consolidated Financial Statements in Item 8.

Other Commitments

On a continuing basis, we are engaged in various stages of negotiations for the acquisition and/or disposition of individual properties or portfolios of properties.

Distribution and Dividend Requirements

Our common share distribution policy is to distribute a percentage of our cash flow to ensure we will meet the distribution requirements of the Code relative to maintaining our REIT status, while still allowing us to maximize the cash retained to meet other cash needs such as capital improvements and other investment activities. Because depreciation is a non-cash expense, cash flow typically will be greater than operating income and net earnings.

Cash distributions per common share paid in 2008, 2007 and 2006 were $2.07, $1.84 and $1.60, respectively. In November 2008, the Board set the expected annual distribution rate for 2009 at $1.00 per common share, subject to market conditions and REIT distribution requirements. The payment of common share distributions, as well as whether the distribution will be payable in cash or shares of beneficial interest, or some combination, is dependent upon our financial condition and operating results and may be adjusted at the discretion of the Board during the year. A cash distribution of $0.25 per common share for the first quarter of 2009 was declared on February 9, 2009. This distribution will be paid on February 27, 2009 to holders of common shares on February 19, 2009.

At December 31, 2008, we had three series of preferred shares outstanding. The annual dividend rates on preferred shares are $4.27 per Series C Preferred Share, $1.69 per Series F Preferred Share and $1.69 per Series G Preferred Share.

Pursuant to the terms of our preferred shares, we are restricted from declaring or paying any distribution with respect to our common shares unless and until all cumulative dividends with respect to the preferred shares have been paid and sufficient funds have been set aside for dividends that have been declared for the then current dividend period with respect to the preferred shares.

Critical Accounting Policies

A critical accounting policy is one that is both important to the portrayal of an entity s financial condition and results of operations and requires judgment on the part of management. Generally, the judgment requires management to make estimates and assumptions about the effect of matters that are inherently uncertain. Estimates are prepared using management s best judgment, after considering past and current economic conditions and expectations for the future. The current economic environment has increased the degree of uncertainty inherent in these estimates and assumptions. Changes in estimates could affect our financial position and specific items in our results of operations that are used by shareholders, potential investors, industry analysts and lenders in their evaluation of our performance. Of the accounting policies discussed in Note 2 to our Consolidated Financial Statements in Item 8, those presented below have been identified by us as critical accounting policies.

Impairment of Long-Lived Assets

We assess the carrying values of our respective long-lived assets, including goodwill, whenever events or changes in circumstances indicate that the carrying amounts of these assets may not be fully recoverable.

Recoverability of real estate assets is measured by comparison of the carrying amount of the asset to the estimated future undiscounted cash flows. In order to review our real estate assets for recoverability, we consider current market conditions, as well as our intent with respect to holding or disposing of the asset. Fair value is determined through various valuation techniques; including discounted cash flow models, quoted market values and third party appraisals, where considered necessary. If our analysis indicates that the carrying value of the long-lived asset is not recoverable on an undiscounted cash flow basis, we recognize an impairment charge for the amount by which the carrying value exceeds the current estimated fair value of the real estate property.

Generally, we use a net asset value analyses to estimate the fair value of the reporting unit where the goodwill is allocated. We estimate the current fair value of the assets and liabilities in the reporting unit through various valuation techniques; including discounted cash flow models, applying a capitalization rate to estimated net operating income of a property, quoted market values and third-party appraisals, as considered necessary. The fair value of the reporting unit also includes an enterprise value that we estimate a third party would be willing to pay for the particular reporting unit. The fair value of the reporting unit is then compared with the corresponding book value, including goodwill, to determine whether there is a potential impairment of the

goodwill. If the carrying amount of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss shall be recognized in an amount equal to that excess.

The use of projected future cash flows and other estimates of fair value are based on assumptions that are consistent with our estimates of future expectations and the strategic plan we use to manage our underlying business. However, assumptions and estimates about future cash flows, discount rates and capitalization rates are complex and subjective. Use of other estimates and assumptions may result in changes in the impairment charges recognized. Changes in economic and operating conditions that occur subsequent to our impairment analyses could impact these assumptions and result in future impairment charges of our real estate properties and/or goodwill. In addition, our intent with regard to the underlying assets might change as market conditions change, as well as other factors, especially in the current global economic environment.

Investments in Unconsolidated Investees

When circumstances indicate there may have been a loss in value of an equity investment, we evaluate the investment for impairment by estimating our ability to recover our investments from future expected cash flows. If we determine the loss in value is other than temporary, we recognize an impairment charge to reflect the investment at fair value. The use of projected future cash flows and other estimates of fair value, the determination of when a loss is other than temporary, and the calculation of the amount of the loss, is complex and subjective. Use of other estimates and assumptions may result in different conclusions. Changes in economic and operating conditions that occur subsequent to our review could impact these assumptions and result in future impairment charges of our equity investments.

Revenue Recognition

We recognize gains from the contributions and sales of real estate assets, generally at the time the title is transferred, consideration is received and we have no future involvement as a direct owner of the real estate asset contributed or sold. In many of our transactions, an entity in which we have an ownership interest will acquire a real estate asset from us. We make judgments based on the specific terms of each transaction as to the amount of the total profit from the transaction that we recognize given our continuing ownership interest and our level of future involvement with the investee that acquires the assets. We also make judgments regarding the timing of recognition in earnings of certain fees and incentives when they are fixed and determinable.

Business Combinations

We acquire individual properties, as well as portfolios of properties or businesses. When we acquire a property for investment purposes, we allocate the purchase price to the various components of the acquisition based upon the fair value of each component. The components typically include land, building, debt and other assumed liabilities, and intangible assets related to above and below market leases, value of costs to obtain tenants and goodwill, deferred tax liabilities and other assets and liabilities in the case of an acquisition of a business. In an acquisition of multiple properties, we must also allocate the purchase price among the properties. The allocation of the purchase price is based on our assessment of estimated fair value and often times based upon the expected future cash flows of the property and various characteristics of the markets where the property is located. The initial allocation of the purchase price is based on management s preliminary assessment, which may differ when final information becomes available. Subsequent adjustments made to the initial purchase price allocation are made within the allocation period, which typically does not exceed one year.

Consolidation

Our consolidated financial statements include the accounts of ProLogis and all entities that we control, either through ownership of a majority voting interest or as the general partner, and variable interest entities when we are the primary beneficiary. Investments in entities in which we do not control but over which we have the ability to exercise significant influence over operating and financial policies are presented under the equity

method. Investments in entities that we do not control and over which we do not exercise significant influence are carried at the lower of cost or fair value, as appropriate. Our judgment with respect to our level of influence or control of an entity and whether we are the primary beneficiary of a variable interest entity involve the consideration of various factors including the form of our ownership interest, our representation on the entity s governing body, the size of our investment (including loans), estimates of future cash flows, our ability to participate in policy making decisions and the rights of the other investors to participate in the decision making process and to replace us as manager and/or liquidate the venture, if applicable. Our ability to correctly assess our influence or control over an entity affects the presentation of these investments in our consolidated financial statements.

Capitalization of Costs and Depreciation

We capitalize costs incurred in developing, renovating, acquiring and rehabilitating real estate assets as part of the investment basis. Costs incurred in making certain other improvements are also capitalized. During the land development and construction periods, we capitalize interest costs, insurance, real estate taxes and certain general and administrative costs of the personnel performing development, renovations, rehabilitation and leasing activities if such costs are incremental and identifiable to a specific activity. Capitalized costs are included in the investment basis of real estate assets except for the costs capitalized related to leasing activities, which are presented as a component of other assets. We estimate the depreciable portion of our real estate assets and related useful lives in order to record depreciation expense. We generally do not depreciate properties during the period from the completion of the development, rehabilitation or repositioning activities through the date the properties are contributed or sold. Our ability to accurately assess the properties to depreciate and to estimate the depreciable portions of our real estate assets and useful lives is critical to the determination of the appropriate amount of depreciation expense recorded and the carrying value of the underlying assets. Any change to the assets to be depreciated and the estimated depreciable lives of these assets would have an impact on the depreciation expense recognized.

Income Taxes

As part of the process of preparing our consolidated financial statements, significant management judgment is required to estimate our current income tax liability, the liability associated with open tax years that are under review and our compliance with REIT requirements. Our estimates are based on interpretation of tax laws. We estimate our actual current income tax due and assess temporary differences resulting from differing treatment of items for book and tax purposes resulting in the recognition of deferred income tax assets and liabilities. These estimates may have an impact on the income tax expense recognized. Adjustments may be required by a change in assessment of our deferred income tax assets and liabilities, changes in assessments of the recognition of income tax benefits for certain non-routine transactions, changes due to audit adjustments by federal and state tax authorities, our inability to qualify as a REIT, the potential for built-in-gain recognition, changes in the assessment of properties to be contributed to TRSs and changes in tax laws. Adjustments required in any given period are included within the income tax provision in the statements of operations, other than adjustments to income tax liabilities due to tax uncertainties acquired in a business combination, which are adjusted to goodwill through December 31, 2008. We recognize the tax benefit from an uncertain tax position only if it is more-likely-than-not that the tax position will be sustained on examination by taxing authorities.

New Accounting Pronouncements

See Note 2 to our Consolidated Financial Statements in Item 8.

Funds from Operations

FFO is a non-GAAP measure that is commonly used in the real estate industry. The most directly comparable GAAP measure to FFO is net earnings. Although NAREIT has published a definition of FFO, modifications to the NAREIT calculation of FFO are common among REITs, as companies seek to provide financial measures that meaningfully reflect their business. FFO, as we define it, is presented as a supplemental financial measure.

We do not use FFO as, nor should it be considered to be, an alternative to net earnings computed under GAAP as an indicator of our operating performance or as an alternative to cash from operating activities computed under GAAP as an indicator of our ability to fund our cash needs.

FFO is not meant to represent a comprehensive system of financial reporting and does not present, nor do we intend it to present, a complete picture of our financial condition and operating performance. We believe net earnings computed under GAAP remains the primary measure of performance and that FFO is only meaningful when it is used in conjunction with net earnings computed under GAAP. Further, we believe our consolidated financial statements, prepared in accordance with GAAP, provide the most meaningful picture of our financial condition and our operating performance.

NAREIT s FFO measure adjusts net earnings computed under GAAP to exclude historical cost depreciation and gains and losses from the sales of previously depreciated properties. We agree that these two NAREIT adjustments are useful to investors for the following reasons:

(a) historical cost accounting for real estate assets in accordance with GAAP assumes, through depreciation charges, that the value of real estate assets diminishes predictably over time. NAREIT stated in its White Paper on FFO since real estate asset values have historically risen or fallen with market conditions, many industry investors have considered presentations of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. Consequently, NAREIT s definition of FFO reflects the fact that real estate, as an asset class, generally appreciates over time and depreciation charges required by GAAP do not reflect the underlying economic realities.

(b) REITs were created as a legal form of organization in order to encourage public ownership of real estate as an asset class through investment in firms that were in the business of long-term ownership and management of real estate. The exclusion, in NAREIT s definition of FFO, of gains and losses from the sales of previously depreciated operating real estate assets allows investors and analysts to readily identify the operating results of the long-term assets that form the core of a REIT s activity and assists in comparing those operating results between periods. We include the gains and losses from dispositions of land, development properties and properties acquired in our CDFS business segment, as well as our proportionate share of the gains and losses from dispositions recognized by the property funds, in our definition of FFO.

At the same time that NAREIT created and defined its FFO concept for the REIT industry, it also recognized that management of each of its member companies has the responsibility and authority to publish financial information that it regards as useful to the financial community. We believe financial analysts, potential investors and shareholders who review our operating results are best served by a defined FFO measure that includes other adjustments to net earnings computed under GAAP in addition to those included in the NAREIT defined measure of FFO.

Our defined FFO, including significant non-cash items, measure excludes the following items from net earnings computed under GAAP that are not excluded in the NAREIT defined FFO measure:

(i) deferred income tax benefits and deferred income tax expenses recognized by our subsidiaries;

(ii) current income tax expense related to acquired tax liabilities that were recorded as deferred tax liabilities in an acquisition, to the extent the expense is offset with a deferred income tax benefit in GAAP earnings that is excluded from our defined FFO measure;

(iii) certain foreign currency exchange gains and losses resulting from certain debt transactions between us and our foreign consolidated subsidiaries and our foreign unconsolidated investees;

(iv) foreign currency exchange gains and losses from the remeasurement (based on current foreign currency exchange rates) of certain third party debt of our foreign consolidated subsidiaries and our foreign unconsolidated investees; and

(v) mark-to-market adjustments associated with derivative financial instruments utilized to manage foreign currency and interest rate risks.

FFO, including significant non-cash items, of our unconsolidated investees is calculated on the same basis.

In addition, we present FFO excluding significant non-cash items. In order to derive FFO excluding significant non-cash items, we add back certain charges or subtract certain gains. The items that were currently excluded were impairment charges that we incurred directly or through our investment in unconsolidated investees, as well as a gain from the early extinguishment of debt. The impairment charges were related to certain of our real estate properties (including land), goodwill and other assets and our China operations that were sold in February 2009. These items are a reflection of decreases in current values driven by increases in current estimated capitalization rates and other declines in market conditions. We believe it is meaningful to remove the effects of significant non-cash items to more appropriately present our results on a comparative basis.

The items that we exclude from net earnings computed under GAAP, while not infrequent or unusual, are subject to significant fluctuations from period to period that cause both positive and negative effects on our results of operations, in inconsistent and unpredictable directions. Most importantly, the economics underlying the items that we exclude from net earnings computed under GAAP are not the primary drivers in management s decision-making process and capital investment decisions. Period to period fluctuations in these items can be driven by accounting for short-term factors that are not relevant to long-term investment decisions, long-term capital structures or long-term tax planning and tax structuring decisions. Accordingly, we believe investors are best served if the information that is made available to them allows them to align their analysis and evaluation of our operating results along the same lines that our management uses in planning and executing our business strategy.

Real estate is a capital-intensive business. Investors analyses of the performance of real estate companies tend to be centered on understanding the asset value created by real estate investment decisions and understanding current operating returns that are being generated by those same investment decisions. The adjustments to net earnings computed under GAAP that are included in arriving at our FFO measure are helpful to management in making real estate investment decisions and evaluating our current operating performance. We believe these adjustments are also helpful to industry analysts, potential investors and shareholders in their understanding and evaluation of our performance on the key measures of net asset value and current operating returns generated on real estate investments.

While we believe our defined FFO measures are an important supplemental measures, neither NAREIT s nor our measures of FFO should be used alone because they exclude significant economic components of net earnings computed under GAAP and are, therefore, limited as an analytical tool. Some of these limitations are:

The current income tax expenses that are excluded from our defined FFO measures represent the taxes that are payable.

Depreciation and amortization of real estate assets are economic costs that are excluded from FFO. FFO is limited, as it does not reflect the cash requirements that may be necessary for future replacements of the real estate assets. Further, the amortization of capital expenditures and leasing costs necessary to maintain the operating performance of industrial properties are not reflected in FFO.

Gains or losses from property dispositions represent changes in the value of the disposed properties. By excluding these gains and losses, FFO does not capture realized changes in the value of disposed properties arising from changes in market conditions.

The deferred income tax benefits and expenses that are excluded from our defined FFO measures result from the creation of a deferred income tax asset or liability that may have to be settled at some future point. Our defined FFO measures do not currently reflect any income or expense that may result from such settlement.

The foreign currency exchange gains and losses that are excluded from our defined FFO measures are generally recognized based on movements in foreign currency exchange rates through a specific point in time. The ultimate settlement of our foreign currency-denominated net assets is indefinite as to timing and

amount. Our FFO measures are limited in that they do not reflect the current period changes in these net assets that result from periodic foreign currency exchange rate movements.

The non-cash impairment charges that we exclude from our FFO, excluding significant non-cash items, measure may be realized in the future upon the ultimate disposition of the related real estate properties or other assets.

We compensate for these limitations by using the FFO measures only in conjunction with net earnings computed under GAAP. To further compensate, we reconcile our defined FFO measures to net earnings computed under GAAP in our financial reports. Additionally, we provide investors with (i) our complete financial statements prepared under GAAP; (ii) our definition of FFO, which includes a discussion of the limitations of using our non-GAAP measure; and (iii) a reconciliation of our GAAP measure (net earnings) to our non-GAAP measure (FFO, as we define it), so that investors can appropriately incorporate this measure and its limitations into their analyses.

FFO, including significant non-cash items, attributable to common shares as defined by us was $180.9 million, $1,227.0 million and $945.1 million for the years ended December 31, 2008, 2007 and 2006, respectively. FFO, excluding significant non-cash items, attributable to common shares as defined by us was $991.9 million, $1,227.0 million and $945.1 million for the years ended December 31, 2008, 2007 and 2006, respectively. The reconciliations of net earnings attributable to common shares computed under GAAP to both FFO, including

significant non-cash items, attributable to common shares and FFO, excluding significant non-cash items, attributable to common shares as defined by us are as follows for the periods indicated (in thousands):

	Years Ended December 31,		
	2008	2007	2006
FFO:			
Reconciliation of net earnings to FFO:			
Net earnings attributable to common shares	$ (432,196)	$ 1,048,917	$ 848,951
Add (deduct) NAREIT defined adjustments:			
Real estate related depreciation and amortization	323,159	291,531	273,980
Adjustments to gains on CDFS dispositions for depreciation	(2,866)	(6,196)	466
Gains recognized on dispositions of certain non-CDFS business assets	(11,620)	(146,667)	(81,470)
Reconciling items attributable to discontinued operations:			
Gains recognized on dispositions of non-CDFS business assets	(9,718)	(52,776)	(103,729)
Real estate related depreciation and amortization	11,485	9,454	15,036
Total discontinued operations	1,767	(43,322)	(88,693)
Our share of reconciling items from unconsolidated investees:			
Real estate related depreciation and amortization	155,067	99,026	68,151
Gains on dispositions of non-CDFS business assets	(492)	(35,672)	(7,124)
Other amortization items	(15,840)	(8,731)	(16,000)
Total unconsolidated investees	138,735	54,623	45,027
Total NAREIT defined adjustments	449,175	149,969	149,310
Subtotal NAREIT defined FFO	16,979	1,198,886	998,261
Add (deduct) our defined adjustments:			
Foreign currency exchange losses (gains), net	144,364	16,384	(19,555)
Current income tax expense	9,656	3,038	23,191
Deferred income tax expense (benefit)	4,073	550	(53,722)
Our share of reconciling items from unconsolidated investees:			
Foreign currency exchange losses (gains), net	2,331	1,823	(45)
Unrealized losses on derivative contracts, net	23,005		
Deferred income tax expense (benefit)	(19,538)	6,327	(2,982)
Total unconsolidated investees	5,798	8,150	(3,027)
Total our defined adjustments	163,891	28,122	(53,113)
FFO, including significant non-cash items, attributable to common shares, as defined by us	180,870	1,227,008	945,148
Impairment of goodwill and other assets	320,636		
Impairment related to assets held for sale China operations	198,236		
Impairment of real estate properties	274,705		
Our share of the loss/impairment recorded by PEPR	108,195		

Gain on early extinguishment of debt	(90,719)		
FFO, excluding significant non-cash items, attributable to common shares, as defined by us	$ 991,923	$ 1,227,008	$ 945,148

ITEM 7A. Quantitative and Qualitative Disclosure About Market Risk

We are exposed to the impact of interest rate changes and foreign-exchange related variability and earnings volatility on our foreign investments. We have used certain derivative financial instruments, primarily foreign currency put option and forward contracts, to reduce our foreign currency market risk, as we deem appropriate. Currently, we do not have any such instruments outstanding. We have also used interest rate swap agreements to reduce our interest rate market risk. We do not use financial instruments for trading or speculative purposes and all financial instruments are entered into in accordance with established polices and procedures.

We monitor our market risk exposures using a sensitivity analysis. Our sensitivity analysis estimates the exposure to market risk sensitive instruments assuming a hypothetical 10% adverse change in year end interest rates and foreign currency exchange rates. The results of the sensitivity analysis are summarized below. The sensitivity analysis is of limited predictive value. As a result, our ultimate realized gains or losses with respect to interest rate and foreign currency exchange rate fluctuations will depend on the exposures that arise during a future period, hedging strategies at the time and the prevailing interest and foreign currency exchange rates.

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Interest Rate Risk

Our interest rate risk management objective is to limit the impact of future interest rate changes on earnings and cash flows. To achieve this objective, we primarily borrow on a fixed rate basis for longer-term debt issuances. We had no interest rate swap contracts outstanding at December 31, 2008.

Our primary interest rate risk is created by the variable rate lines of credit. During the year ended December 31, 2008, we had weighted average daily outstanding borrowings of $3.2 billion on our variable rate lines of credit. Based on the results of the sensitivity analysis, which assumed a 10% adverse change in interest rates, the estimated market risk exposure for the variable rate lines of credit was approximately $10.6 million of cash flow for the year ended December 31, 2008.

We also have $250 million of variable interest rate debt in which we have a market risk of increased rates. Based on a sensitivity analysis with a 10% adverse change in interest rates our estimated market risk exposure for this issuance is approximately $0.6 million on our cash flow for the year ended December 31, 2008.

In addition, as a result of a change in accounting effective January 1, 2009, we expect our non-cash interest expense to increase between $73 million and $83 million per annum, prior to capitalization of interest as a result of our development activities. See Note 2 to our Consolidated Financial Statements in Item 8 for further information.

The unconsolidated property funds that we manage, and in which we have an equity ownership, may enter into interest rate swap contracts. See Note 5 to our Consolidated Financial Statements in Item 8 for further information on these derivatives.

Foreign Currency Risk

Foreign currency risk is the possibility that our financial results could be better or worse than planned because of changes in foreign currency exchange rates.

Our primary exposure to foreign currency exchange rates relates to the translation of the net income of our foreign subsidiaries into U.S. dollars, principally euro, pound sterling and yen. To mitigate our foreign currency exchange exposure, we borrow in the functional currency of the borrowing entity, when appropriate. We also may use foreign currency put option contracts to manage foreign currency exchange rate risk associated with the projected net operating income of our foreign consolidated subsidiaries and unconsolidated investees. At December 31, 2008, we had no put option contracts outstanding and, therefore, we may experience fluctuations in our earnings as a result of changes in foreign currency exchange rates.

We also have some exposure to movements in exchange rates related to certain intercompany loans we issue from time to time and we may use foreign currency forward contracts to manage these risks. At December 31, 2008, we had no forward contracts outstanding and, therefore, we may experience fluctuations in our earnings from the remeasurement of these intercompany loans due to changes in foreign currency exchange rates.

Fair Value of Financial Instruments

See Note 17 to our Consolidated Financial Statements in Item 8.

ITEM 8. Financial Statements and Supplementary Data

Our Consolidated Balance Sheets as of December 31, 2008 and 2007, our Consolidated Statements of Operations, Shareholders Equity and Comprehensive Income (Loss) and Cash Flows for each of the years in the three-year period ended December 31, 2008, Notes to Consolidated Financial Statements and Schedule III Real Estate and Accumulated Depreciation, together with the reports of KPMG LLP, Independent Registered Public Accounting Firm, are included under Item 15 of this report and are incorporated herein by reference. Selected unaudited quarterly financial data is presented in Note 22 of our Consolidated Financial Statements.

ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

ITEM 9A. Controls and Procedures

An evaluation was carried out under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the Exchange Act)) as of December 31, 2008. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of December 31, 2008 to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms. Subsequent to December 31, 2008, there were no significant changes in our internal controls or in other factors that could significantly affect these controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

Management s Report on Internal Control over Financial Reporting

We are responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934.

Under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, an evaluation of the effectiveness of our internal control over financial reporting was conducted as of December 31, 2008 based on the criteria described in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management determined that, as of December 31, 2008, our internal control over financial reporting was effective.

The effectiveness of our internal control over financial reporting as of December 31, 2008 has been audited by KPMG LLP, an independent registered public accounting firm, as stated in their report which is included herein.

Limitations of the Effectiveness of Controls

Management s assessment included an evaluation of the design of our internal control over financial reporting and testing of the operational effectiveness of our internal control over financial reporting. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

ITEM 9B. Other Information

On February 27, 2009, the Board approved Articles of Amendment (the Amendment) to ProLogis Amended and Restated Declaration of Trust. The Amendment increases the total number of shares of beneficial interest that ProLogis has the authority to issue from 375,000,000 to 750,000,000 shares, including an increase in the number of common shares of beneficial interest that we have authority to issue from 362,580,000 common shares of beneficial interest to 737,580,000 common shares of beneficial interest.

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PART III

ITEM 10. Directors, Executive Officers and Corporate Governance

Trustees and Officers

The information required by this item is incorporated herein by reference to the description under Item 1 Our Management Senior Management (but only with respect to Walter C. Rakowich, Ted R. Antenucci, Edward S. Nekritz and William E. Sullivan), and to the descriptions under the captions Election of Trustees Nominees, Additional Information Section 16(a) Beneficial Ownership Reporting Compliance, Corporate Governance Code of Ethics and Business Conduct, and Board of Trustees and Committees Audit Committee in our 2009 Proxy Statement.

ITEM 11. Executive Compensation

The information required by this item is incorporated herein by reference to the descriptions under the captions Compensation Matters and Board of Trustees and Committees Compensation Committee Interlocks and Insider Participation in our 2009 Proxy Statement.

ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by this item is incorporated herein by reference to the descriptions under the captions Information Relating to Trustees, Nominees and Executive Officers Common Shares Beneficially Owned and Compensation Matters Equity Compensation Plans in our 2009 Proxy Statement.

ITEM 13. Certain Relationships and Related Transactions, and Director Independence

The information required by this item is incorporated herein by reference to the descriptions under the captions Information Relating to Trustees, Nominees and Executive Officers Certain Relationships and Related Transactions and Corporate Governance Trustee Independence in our 2009 Proxy Statement.

ITEM 14. Principal Accounting Fees and Services

The information required by this item is incorporated herein by reference to the description under the caption Independent Registered Public Accounting Firm in our 2009 Proxy Statement.

PART IV

ITEM 15. Exhibits, Financial Statement Schedules

The following documents are filed as a part of this report:

(a) Financial Statements and Schedules:

1. Financial Statements:

See Index to Consolidated Financial Statements and Schedule III on page 64 of this report, which is incorporated herein by reference.

2. Financial Statement Schedules:

Schedule III Real Estate and Accumulated Depreciation

All other schedules have been omitted since the required information is presented in the Consolidated Financial Statements and the related Notes or is not applicable.

(b) Exhibits: The Exhibits required by Item 601 of Regulation S-K are listed in the Index to Exhibits on pages 144 to 148 of this report, which is incorporated herein by reference.

(c) Financial Statements: See Index to Consolidated Financial Statements and Schedule III on page 64 of this report, which is incorporated by reference.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULE III

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Trustees and Shareholders
ProLogis:

We have audited the accompanying consolidated balance sheets of ProLogis and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of operations, shareholders equity and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2008. These consolidated financial statements are the responsibility of ProLogis management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the 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 referred to above present fairly, in all material respects, the financial position of ProLogis and subsidiaries as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), ProLogis internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 27, 2009 expressed an unqualified opinion on the effectiveness of ProLogis internal control over financial reporting.

KPMG LLP

Denver, Colorado
February 27, 2009

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Trustees and Shareholders
ProLogis:

We have audited ProLogis internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). ProLogis management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on ProLogis internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, ProLogis maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of ProLogis and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of operations, shareholders equity and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2008, and our report dated February 27, 2009 expressed an unqualified opinion on those consolidated financial statements.

KPMG LLP

Denver, Colorado
February 27, 2009

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PROLOGIS

CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)

	December 31, 2008	December 31, 2007
ASSETS		
Real estate	$ 15,706,172	$ 16,578,845
Less accumulated depreciation	1,583,299	1,368,458
	14,122,873	15,210,387
Investments in and advances to unconsolidated investees	2,269,993	2,345,277
Cash and cash equivalents	174,636	399,910
Accounts and notes receivable	244,778	340,039
Other assets	1,129,182	1,408,814
Discontinued operations assets held for sale	1,310,754	19,607
Total assets	$ 19,252,216	$ 19,724,034
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Debt	$ 11,007,636	$ 10,506,068
Accounts payable and accrued expenses	658,868	933,075
Other liabilities	751,238	769,408
Discontinued operations assets held for sale	389,884	424
Total liabilities	12,807,626	12,208,975
Minority interest	19,878	78,661
Shareholders equity:		
Series C preferred shares at stated liquidation preference of $50 per share; $0.01 par value; 2,000 shares issued and outstanding at December 31, 2008 and 2007	100,000	100,000
Series F preferred shares at stated liquidation preference of $25 per share; $0.01 par value; 5,000 shares issued and outstanding at December 31, 2008 and 2007	125,000	125,000
Series G preferred shares at stated liquidation preference of $25 per share; $0.01 par value; 5,000 shares issued and outstanding at December 31, 2008 and 2007	125,000	125,000
Common shares; $0.01 par value; 267,005 shares issued and outstanding at December 31, 2008 and 257,712 shares issued and outstanding at December 31, 2007	2,670	2,577
Additional paid-in capital	6,688,615	6,412,473

Accumulated other comprehensive income (loss):		
Unrealized losses on derivative contracts, net	(52,219)	(27,091)
Foreign currency translation gains, net	22,845	302,413
(Distributions in excess of net earnings) retained earnings	(587,199)	396,026
Total shareholders equity	6,424,712	7,436,398
Total liabilities and shareholders equity	$ 19,252,216	$ 19,724,034

The accompanying notes are an integral part of these Consolidated Financial Statements.

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PROLOGIS

CONSOLIDATED STATEMENTS OF OPERATIONS
Years Ended December 31, 2008, 2007 and 2006
(In thousands, except per share data)

	2008	2007	2006
Revenues:			
Rental income	$ 1,002,493	$ 1,052,219	$ 901,954
CDFS disposition proceeds:			
Developed and repositioned properties	4,206,446	2,530,377	1,286,841
Acquired property portfolios	289,019	2,475,035	
Property management and other fees and incentives	131,011	104,719	211,929
Development management and other income	25,857	26,322	37,443
Total revenues	5,654,826	6,188,672	2,438,167
Expenses:			
Rental expenses	325,049	284,421	236,054
Cost of CDFS dispositions:			
Developed and repositioned properties	3,547,500	1,835,274	993,926
Acquired property portfolios	289,019	2,406,426	
General and administrative	204,300	193,204	147,193
Reduction in workforce	23,131		
Impairment of real estate properties	274,705	12,600	
Depreciation and amortization	339,491	302,413	283,306
Other expenses	28,104	12,363	13,013
Total expenses	5,031,299	5,046,701	1,673,492
Operating income	623,527	1,141,971	764,675
Other income (expense):			
Earnings (loss) from unconsolidated property funds, net	(69,116)	94,453	93,055
Earnings from other unconsolidated investees, net	13,342	4,573	47,748
Interest expense	(341,305)	(368,512)	(295,629)
Impairment of goodwill and other assets	(320,636)		
Gain on early extinguishment of debt	90,719		
Interest and other income, net	16,522	32,129	34,625
Total other income (expense)	(610,474)	(237,357)	(120,201)
Earnings before minority interest	13,053	904,614	644,474
Minority interest share in earnings, net	(3,837)	(4,814)	(3,451)
Earnings before certain net gains (losses)	9,216	899,800	641,023

Gains recognized on dispositions of certain non-CDFS business assets		11,668		146,667		81,470
Foreign currency exchange gains (losses), net		(148,281)		8,132		21,444
Earnings (loss) before income taxes		(127,397)		1,054,599		743,937
Income taxes:						
Current income tax expense		63,441		66,339		83,508
Deferred income tax expense (benefit)		4,570		516		(53,722)
Total income taxes		68,011		66,855		29,786
Earnings (loss) from continuing operations		(195,408)		987,744		714,151
Discontinued operations:						
Income (loss) attributable to assets held for sale and disposed properties, net		(32,630)		5,099		22,973
Impairment related to assets held for sale China operations		(198,236)				
Gains recognized on dispositions:						
Non-CDFS business assets		9,718		52,776		103,729
CDFS business assets		9,783		28,721		33,514
Total discontinued operations		(211,365)		86,596		160,216
Net earnings (loss)		(406,773)		1,074,340		874,367
Less preferred share dividends		25,423		25,423		25,416
Net earnings (loss) attributable to common shares	$	(432,196)	$	1,048,917	$	848,951
Weighted average common shares outstanding Basic		262,729		256,873		245,952
Weighted average common shares outstanding Diluted		262,729		267,226		256,852
Net earnings (loss) per share attributable to common shares Basic:						
Continuing operations	$	(0.85)	$	3.74	$	2.80
Discontinued operations		(0.80)		0.34		0.65
Net earnings (loss) per share attributable to common shares Basic	$	(1.65)	$	4.08	$	3.45
Net earnings (loss) per share attributable to common shares Diluted:						
Continuing operations	$	(0.85)	$	3.62	$	2.69
Discontinued operations		(0.80)		0.32		0.63
Net earnings (loss) per share attributable to common shares Diluted	$	(1.65)	$	3.94	$	3.32
Distributions per common share	$	2.07	$	1.84	$	1.60

The accompanying notes are an integral part of these Consolidated Financial Statements.

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PROLOGIS

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY AND COMPREHENSIVE INCOME (LOSS)
Years Ended December 31, 2008, 2007 and 2006
(In thousands)

	2008	2007	2006
Common shares number of shares at beginning of year	257,712	250,912	243,781
Issuance of common shares in connection with acquisitions		4,781	
Issuances of common shares under common share plans	5,381	1,891	6,951
Conversions of limited partnership units	3,912	128	180
Common shares number of shares at end of year	267,005	257,712	250,912
Common shares par value at beginning of year	$ 2,577	$ 2,509	$ 2,438
Issuance of common shares in connection with acquisitions		48	
Issuances of common shares under common share plans	54	19	69
Conversions of limited partnership units	39	1	2
Common shares par value at end of year	$ 2,670	$ 2,577	$ 2,509
Preferred shares at stated liquidation preference	$ 350,000	$ 350,000	$ 350,000
Additional paid-in capital at beginning of year	$ 6,412,473	$ 6,000,119	$ 5,606,017
Issuance of common shares in connection with acquisitions		339,449	
Issuances of common shares under common share plans	219,012	37,417	357,448
Conversions of limited partnership units	17,126	4,444	6,475
Cost of issuing common shares	(199)	(106)	(76)
Change in receivable from timing differences on equity transactions	113	247	244
Cost of share-based compensation awards	40,090	30,903	30,011
Additional paid-in capital at end of year	$ 6,688,615	$ 6,412,473	$ 6,000,119
Accumulated other comprehensive income at beginning of year	$ 275,322	$ 216,922	$ 149,586
Foreign currency translation gains (losses), net	(279,568)	90,015	70,777
Unrealized losses on derivative contracts, net	(25,128)	(31,615)	(3,441)
Accumulated other comprehensive income (loss) at end of year	$ (29,374)	$ 275,322	$ 216,922
Retained earnings (distributions in excess of net earnings) at beginning of year	$ 396,026	$ (170,971)	$ (620,018)
Net earnings (loss)	(406,773)	1,074,340	874,367
Effect of adoption of FIN 48		(9,272)	

Preferred share dividends	(25,423)	(25,423)	(25,416)
Common share distributions	(551,029)	(472,648)	(399,904)
Retained earnings (distributions in excess of net earnings) at end of year	$ (587,199)	$ 396,026	$ (170,971)
Total shareholders equity at end of year	$ 6,424,712	$ 7,436,398	$ 6,398,579
Comprehensive income (loss) attributable to common shares:			
Net earnings (loss)	$ (406,773)	$ 1,074,340	$ 874,367
Preferred share dividends	(25,423)	(25,423)	(25,416)
Foreign currency translation gains (losses), net	(279,568)	90,015	70,777
Losses on derivative contracts, net	(25,128)	(31,615)	(3,441)
Comprehensive income (loss) attributable to common shares	$ (736,892)	$ 1,107,317	$ 916,287

The accompanying notes are an integral part of these Consolidated Financial Statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2008, 2007 and 2006
(In thousands)

	2008	2007	2006
Operating activities:			
Net earnings (loss)	$ (406,773)	$ 1,074,340	$ 874,367
Adjustments to reconcile net earnings (loss) to net cash provided by operating activities:			
Minority interest share in earnings (loss), net	(6,231)	6,003	3,457
Straight-lined rents	(34,063)	(44,403)	(36,418)
Cost of share-based compensation awards	28,321	23,934	21,567
Depreciation and amortization	350,976	311,867	298,342
Equity in (earnings)/share of loss from unconsolidated investees	71,956	(105,618)	(143,758)
Changes in operating receivables and distributions from unconsolidated investees	19,956	74,348	99,062
Amortization of deferred loan costs	12,759	10,555	7,673
Amortization of debt premium, net	(702)	(7,797)	(13,861)
Gains recognized on dispositions of non-CDFS business assets	(21,386)	(199,443)	(185,199)
Gains recognized on dispositions of CDFS business assets included in discontinued operations	(9,783)	(28,721)	(33,514)
Impairment of goodwill and other assets	320,636		
Impairment related to assets held for sale China operations	198,236		
Impairment of real estate properties	274,705	13,259	
Gain on early extinguishment of debt	(90,719)		
Unrealized foreign currency exchange losses (gains)	144,364	16,229	(18,774)
Deferred income tax expense (benefit)	4,072	550	(53,722)
(Increase) decrease in accounts and notes receivable and other assets	63,769	(155,486)	(204,096)
Increase (decrease) in accounts payable and accrued expenses and other liabilities	(76,472)	216,338	72,201
Net cash provided by operating activities	843,621	1,205,955	687,327
Investing activities:			
Real estate investments	(5,482,792)	(5,213,870)	(3,695,799)
Tenant improvements and lease commissions on previously leased space	(58,076)	(67,317)	(66,787)
Non-development capital expenditures	(36,902)	(37,948)	(29,437)
Cash consideration paid in Parkridge acquisition, net of cash acquired		(700,812)	
Purchase of Macquarie ProLogis Trust (MPR), net of cash acquired		(1,137,028)	

Proceeds from dispositions of real estate assets	4,474,228	3,618,622	2,095,231
Investments in and advances to unconsolidated investees	(329,553)	(661,796)	(175,677)
Purchase of ownership interests in property funds			(259,248)
Return of investment from unconsolidated investees	126,983	50,243	146,206
Advances on notes receivable		(18,270)	(115,417)
Proceeds from repayments of notes receivable	4,200	115,620	73,723
Increase in restricted cash for potential investment			(42,174)
Net cash used in investing activities	(1,301,912)	(4,052,556)	(2,069,379)
Financing activities:			
Proceeds from sales and issuances of common shares under various common share plans	222,162	46,855	358,038
Distributions paid on common shares	(542,792)	(472,645)	(393,317)
Dividends paid on preferred shares	(25,423)	(31,781)	(19,062)
Minority interest redemptions (distributions), net	23,827	(9,341)	(11,576)
Debt and equity issuance costs paid	(12,121)	(15,830)	(13,840)
Net proceeds from (payments on) credit facilities	743,934	(431,506)	368,158
Proceeds from issuance of debt to finance MPR and Parkridge acquisitions		1,719,453	
Proceeds from issuance of senior convertible notes	544,500	2,329,016	
Proceeds from issuance of senior notes, secured and unsecured debt	606,044	781,802	1,945,325
Payments on senior notes, secured debt, unsecured debt and assessment bonds	(1,202,028)	(1,174,335)	(588,844)
Net cash provided by financing activities	358,103	2,741,688	1,644,882
Effect of exchange rate changes on cash	(13,950)	29,032	9,161
Net increase (decrease) in cash and cash equivalents	(114,138)	(75,881)	271,991
Cash and cash equivalents, beginning of year	399,910	475,791	203,800
Cash and cash equivalents, assets held for sale	(111,136)		
Cash and cash equivalents, end of year	$ 174,636	$ 399,910	$ 475,791

See Note 20 for information on non-cash investing and financing activities and other information.

The accompanying notes are an integral part of these Consolidated Financial Statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Description of Business:

ProLogis, collectively with our consolidated subsidiaries (we , our , us , the Company or ProLogis), is a publicly h real estate investment trust (REIT) that owns, operates and develops (directly and through our unconsolidated investees) primarily industrial properties in North America, Europe and Asia. Through 2008, our business consisted of three reportable business segments: (i) direct owned (previously referred to as property operations); (ii) investment management; and (iii) CDFS business. Our direct owned segment represents the direct long-term ownership of industrial properties. Our investment management segment represents the long-term investment management of property funds and joint ventures and the properties they own. Our CDFS business segment primarily encompasses our development or acquisition of real estate properties that are generally contributed to a property fund in which we have an ownership interest and act as manager, or sold to third parties. Recent economic conditions have resulted in changes in our business strategy. As a result, as of December 31, 2008, our business strategy no longer includes the CDFS Business segment. See Note 19 for further discussion of our business segments.

2. Summary of Significant Accounting Policies:

Basis of Presentation and Consolidation. The accompanying consolidated financial statements are presented in our reporting currency, the U.S. dollar. All material intercompany transactions with consolidated entities have been eliminated.

We consolidate all entities that are wholly owned and those in which we own less than 100% but control, as well as any variable interest entities in which we are the primary beneficiary. We evaluate our ability to control an entity and whether the entity is a variable interest entity and we are the primary beneficiary through the consideration of the following factors:

(i) the form of our ownership interest and legal structure;

(ii) our representation on the entity s governing body;

(iii) the size of our investment (including loans);

(iv) estimates of future cash flows;

(v) our ability to participate in policy making decisions, including but not limited to, the acquisition or disposition of investment properties and the incurrence or refinancing of debt;

(vi) the rights of other investors to participate in the decision making process; and

(vii) the ability for other partners or owners to replace us as manager and/or liquidate the venture, if applicable.

Use of Estimates. The accompanying consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (GAAP). GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as of the date of the financial statements and revenue and expenses during the reporting period. Although we believe the assumptions and estimates we made are reasonable and appropriate, as discussed in the applicable sections throughout these Consolidated Financial Statements, different assumptions and estimates could materially impact our reported results. The current economic environment has increased the degree of uncertainty inherent in these estimates and assumptions and changes in market conditions could impact our future operating results.

Foreign Operations. The U.S. dollar is the functional currency for our consolidated subsidiaries and unconsolidated investees operating in the United States and Mexico and certain of our consolidated

PROLOGIS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

subsidiaries that operate as holding companies for foreign investments. The functional currency for our consolidated subsidiaries and unconsolidated investees operating in countries other than the United States and Mexico is the principal currency in which the entity s assets, liabilities, income and expenses are denominated, which may be different from the local currency of the country of incorporation or the country where the entity conducts its operations. The functional currencies of our consolidated subsidiaries and unconsolidated investees generally include the British pound sterling, Canadian dollar, Chinese renminbi, euro, Japanese yen and Korean won. We are parties to business transactions denominated in these and other currencies.

For our consolidated subsidiaries whose functional currency is not the U.S. dollar, we translate their financial statements into U.S. dollars at the time we consolidate those subsidiaries financial statements. Generally, assets and liabilities are translated at the exchange rate in effect as of the balance sheet date. Certain balance sheet items, primarily equity-related accounts, are reflected at the historical exchange rate. Income statement accounts are translated using the average exchange rate for the period and income statement accounts that represent significant non-recurring transactions are translated at the rate in effect as of the date of the transaction. We translate our share of the net earnings or losses of our unconsolidated investees whose functional currency is not the U.S. dollar at the average exchange rate for the period. The resulting translation adjustments are included in the Accumulated Other Comprehensive Income (Loss) in Shareholders Equity.

We and certain of our consolidated subsidiaries have intercompany and third party debt that is not denominated in the entity s functional currency. When the debt is remeasured against the functional currency of the entity, a gain or loss can result. The resulting adjustment is generally reflected in results of operations unless it is intercompany debt that is deemed to be long-term in nature. The remeasurement of such long-term debt results in the recognition of a cumulative translation adjustment in Accumulated Other Comprehensive Income (Loss) in Shareholders Equity.

Gains or losses are included in results of operations when transactions with a third party, denominated in a currency other than the entity s functional currency, are settled. We occasionally utilize derivative financial instruments to manage certain foreign currency exchange risks.

We are subject to foreign currency risk due to potential fluctuations in exchange rates between certain foreign currencies and the U.S. dollar. A significant change in the value of the foreign currency of one or more countries where we have a significant investment would have an effect on our reported results of operations and financial position. Although we attempt to mitigate adverse effects by borrowing under debt agreements denominated in foreign currencies and, on occasion and when deemed appropriate, through the use of derivative contracts, there can be no assurance that those attempts to mitigate foreign currency risk will be successful. See our policy footnote on financial instruments and Note 17 for more information related to our derivative financial instruments.

Business Combinations. When we acquire a business or individual properties, with the intention to hold the investment for the long term, we allocate the purchase price to the various components of the acquisition based upon the fair value of each component. We estimate:

- the fair value of the buildings on an as-if-vacant basis. The fair value allocated to land is generally based on relevant market data;

the market value of above and below market leases based upon our best estimate of current market rents. The value of each lease is recorded in either other assets or other liabilities, as appropriate;

the value of costs to obtain tenants, primarily leasing commissions. These costs are recorded in other assets;

PROLOGIS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

the value of debt based on quoted market rates for the same or similar issues, or by discounting future cash flows using rates currently available for debt with similar terms and maturities. Any discount or premium is included in the principal amount;

the value of any management contracts by discounting future expected cash flows under these contracts; and

the value of all other assumed assets and liabilities based on the best information available.

We amortize the acquired assets or liabilities as follows:

Above and below market leases are charged to rental income over the average remaining estimated life of the lease.

Leasing commissions are charged to amortization expense over the average remaining estimated life of the lease.

Debt discount or premium is charged to interest expense using the effective interest method over the remaining term of the related debt.

Management contracts are charged against income over the remaining term of the contract.

Goodwill represents the excess of the purchase price over the fair value of net tangible and intangible assets acquired in a business combination. See the discussion below for the change in accounting for business combinations that is effective as of January 1, 2009.

Long-Lived Assets

Real Estate Assets. Real estate assets are carried at depreciated cost. Costs incurred that are directly associated with the successful acquisition of real estate assets are capitalized as part of the investment basis of the real estate assets. Costs that are associated with unsuccessful acquisition efforts are expensed at the time the acquisition is abandoned. Costs incurred in developing, renovating, rehabilitating and improving real estate assets are capitalized as part of the investment basis of the real estate assets. Costs incurred in making repairs and maintaining real estate assets are expensed as incurred.

During the land development and construction periods of qualifying projects, we capitalize interest costs, insurance, real estate taxes and general and administrative costs of the personnel performing the development, renovation, rehabilitation and leasing activities; if such costs are incremental and identifiable to a specific activity. Capitalized costs are included in the investment basis of real estate assets except for the costs capitalized related to leasing activities, which are included in other assets. When a municipal district finances costs we incur for public infrastructure improvements, we record the costs in real estate until we are reimbursed.

The depreciable portions of real estate assets are charged to depreciation expense on a straight-line basis over their respective estimated useful lives. We generally use the following useful lives: seven years for capital improvements, 10 years for standard tenant improvements, 30 years for industrial properties acquired, 40 years for office and retail properties acquired and 40 years for properties we develop. Capitalized leasing costs are amortized over the respective lease term. Our average lease term for all leases in effect at December 31, 2008 was between six and seven years. Previously, if we developed properties with the intent to contribute the property to a property fund, we did not depreciate these properties during the period from the completion of the development through the date the property was contributed. With the changes in our business strategy, and the uncertainty with respect to the timing of future contributions to the property funds, we may hold these properties long-term and have begun to depreciate them.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In accordance with Statement of Financial Accounting Standards (SFAS) 144 Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144), we assess the carrying values of our respective long-lived assets, whenever events or changes in circumstances indicate that the carrying amounts of these assets may not be fully recoverable. Recoverability of the assets is measured by comparison of the carrying amount of the asset to the estimated future undiscounted cash flows. In order to review our assets for recoverability, we consider current market conditions, as well as our intent with respect to holding or disposing of the asset. Fair value is determined through various valuation techniques; including discounted cash flow models, quoted market values and third party appraisals, where considered necessary. If our analysis indicates that the carrying value of the long-lived asset is not recoverable on an undiscounted cash flow basis, we recognize an impairment charge for the amount by which the carrying value exceeds the current estimated fair value of the real estate property.

We estimate the future undiscounted cash flows based on management s intent as follows: (i) for real estate properties that we intend to hold long-term, including land held for development, properties currently under development and operating buildings, recoverability is assessed based on the estimated future net rental income from operating the property; (ii) for real estate properties that we intend to sell, including land parcels, properties currently under development and operating buildings, recoverability is assessed based on estimated proceeds from disposition that are estimated based on future net rental income of the property and expected market capitalization rates; and (iii) for costs incurred related to the potential acquisition or development of a real estate property, recoverability is assessed based on the probability that the acquisition or development is likely to occur as of the measurement date.

The use of projected future cash flows is based on assumptions that are consistent with our estimates of future expectations and the strategic plan we use to manage our underlying business. However assumptions and estimates about future cash flows, discount rates and capitalization rates are complex and subjective. Changes in economic and operating conditions and our ultimate investment intent that occur subsequent to our impairment analyses could impact these assumptions and result in future impairment charges of our real estate properties.

Goodwill. Goodwill represents the excess of the purchase price over the fair value of net tangible and intangible assets acquired in a business combination. In accordance with SFAS 142 Goodwill and other Intangible Assets (SFAS 142), we perform an annual impairment test for goodwill at the reporting unit level. The annual review is performed during the third quarter for the reporting units in our CDFS business segment and during the fourth quarter for the reporting units in our direct owned and investment management segments. Additionally, we will evaluate the recoverability of goodwill whenever events or changes in circumstances indicate that the carrying amounts of goodwill may not be fully recoverable.

Generally, we use a net asset value analyses to estimate the fair value of the reporting unit where the goodwill is allocated. We estimate the current fair value of the assets and liabilities in the reporting unit through various valuation techniques; including discounted cash flow models, applying a capitalization rate to estimated net operating income of a property, quoted market values and third-party appraisals, as considered necessary. The fair value of the reporting unit also includes an enterprise value that we estimate a third party would be willing to pay for the particular reporting unit. The fair value of the reporting unit is then compared with the corresponding book value, including goodwill, to determine whether there is a potential impairment of the goodwill. If the carrying amount of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss shall be recognized in an amount equal to

that excess.

The use of projected future cash flows is based on assumptions that are consistent with our estimates of future expectations and the strategic plan we use to manage our underlying business. However assumptions and

PROLOGIS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

estimates about future cash flows, discount rates and capitalization rates are complex and subjective. Changes in economic and operating conditions that occur subsequent to our impairment analyses could impact these assumptions and result in future impairment charges of our goodwill.

Assets Held for Sale and Discontinued Operations. Discontinued operations represent a component of an entity that has either been disposed of or is classified as held for sale if both the operations and cash flows of the component have been or will be eliminated from ongoing operations of the entity as a result of the disposal transaction and the entity will not have any significant continuing involvement in the operations of the component after the disposal transaction. The results of operations of a component of our business or properties that have been classified as discontinued operations are also reported as discontinued operations for all periods presented. We classify a component of our business or property as held for sale when certain criteria are met. At such time, the respective assets and liabilities are presented separately on our Consolidated Balance Sheets and depreciation is no longer recognized. Assets held for sale are reported at the lower of their carrying amount or their estimated fair value less the estimated costs to sell the assets.

Properties disposed of to third parties are considered discontinued operations unless such properties were developed under a pre-sale agreement. Properties contributed to property funds in which we maintain an ownership interest and act as manager are not considered discontinued operations due to our continuing involvement with the properties. The contribution of properties to the property funds is reflected in our Consolidated Statements of Operations based on the nature of the properties contributed, either CDFS or non-CDFS.

Investments in Unconsolidated Investees. Our investments in certain entities are presented under the equity method. The equity method is used when we have the ability to exercise significant influence over operating and financial policies of the investee but do not have control of the investee. Under the equity method, these investments (including advances to the investee) are initially recognized in the balance sheet at our cost and are subsequently adjusted to reflect our proportionate share of net earnings or losses of the investee, distributions received, deferred gains from the contribution of properties and certain other adjustments, as appropriate. When circumstances indicate there may have been a loss in value of an equity investment, we evaluate the investment for impairment by estimating our ability to recover our investment from future expected cash flows. If we determine the loss in value is other than temporary, we recognize an impairment charge to reflect the investment at fair value.

Cash and Cash Equivalents. We consider all cash on hand, demand deposits with financial institutions and short-term, highly liquid investments with original maturities of three months or less to be cash equivalents. Our cash and cash equivalents are financial instruments that are exposed to concentrations of credit risk. We invest our cash with high-credit quality institutions. Cash balances may be invested in money market accounts that are not insured. We have not realized any losses in such cash investments or accounts and believe that we are not exposed to any significant credit risk.

Minority Interest. We recognize the minority interests in real estate partnerships in which we consolidate at each minority holder s respective share of the estimated fair value of the real estate as of the date of formation. Minority interest that was created or assumed as a part of a business combination is recognized at the underlying book value as of the date of the transaction. Minority interest is subsequently adjusted for additional contributions, distributions to

minority holders and the minority holders proportionate share of the net earnings or losses of each respective entity. See the discussion below for the change in accounting for minority interests that is effective as of January 1, 2009.

Certain limited partnership interests issued by us in connection with the formation of a real estate partnership and as consideration in a business combination are exchangeable into our common shares. Common shares issued upon exchange of a holder s minority interest are accounted for at our carrying value of the surrendered minority interest.

PROLOGIS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Costs of Raising Capital. Costs incurred in connection with the issuance of both common shares and preferred shares are treated as a reduction to additional paid-in capital. Costs incurred in connection with the issuance or renewal of debt are capitalized in other assets, and amortized to interest expense over the term of the related debt.

Revenue Recognition.

Rental and other income. We lease our operating properties to customers under agreements that are classified as operating leases. We recognize the total minimum lease payments provided for under the leases on a straight-line basis over the lease term. Generally, under the terms of our leases, some or all of our rental expenses are recovered from our customers. We reflect amounts recovered from customers as a component of rental income. A provision for possible loss is made if the collection of a receivable balance is considered doubtful. Some of our retail and ground leases provide for additional rent based on sales over a stated base amount during the lease year. We recognize this additional rent when each customer s sales exceed their sales threshold. We recognize interest income and management, development and other fees and incentives when earned, fixed and determinable.

Gains on Disposition of Real Estate. Gains on the disposition of real estate are recorded when the recognition criteria have been met, generally at the time title is transferred, and we no longer have substantial continuing involvement with the real estate sold.

When we contribute a property to a property fund or joint venture in which we have an ownership interest, we do not recognize a portion of the gain realized. The amount of gain not recognized, based on our ownership interest in the entity acquiring the property, is deferred by recognizing a reduction to our investment in the applicable unconsolidated investee. We adjust our proportionate share of net earnings or losses recognized in future periods to reflect the investees recorded depreciation expense as if it were computed on our lower basis in the contributed properties rather than on the entity s basis. We reflect the gains recognized from contributions of CDFS properties to property funds and CDFS joint ventures in operating cash flows and we include the costs related to the CDFS properties and the recovery of those costs through the proceeds we receive upon contribution in investing cash flows in our Consolidated Statements of Cash Flows.

When a property that we originally contributed to a property fund or joint venture is disposed of to a third party, we recognize the amount of the gain we had previously deferred, along with our proportionate share of the gain recognized by the investee. During periods when our ownership interest in an investee decreases, we recognize gains relating to previously deferred gains to coincide with our new ownership interest in the investee.

Rental Expenses. Rental expenses primarily include the cost of on-site property management personnel, utilities, repairs and maintenance, property insurance and real estate taxes. Also included are direct expenses associated with our management of the property funds operations.

Share-Based Compensation. We account for stock-based compensation in accordance with SFAS 123R *Share Based Payment* (SFAS 123R). This standard requires companies to measure the cost of employee services received in exchange for an award of an equity instrument based on the fair value of the award on the grant date and recognize the cost over the period during which an employee is required to provide service in exchange for the award, generally the

vesting period. We treat dividend equivalent units (DEUs) as dividends, which are charged to retained earnings and factored into the computation of the fair value of the underlying share award at grant date. See Note 11 for more information on our stock based compensation.

Income Taxes. ProLogis was formed as a Maryland REIT in January 1993 and we have, along with our consolidated REIT subsidiary, elected to be taxed as a REIT under the Internal Revenue Code of 1986, as

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

amended (the Code). Under the Code, REITs are generally not required to pay federal income taxes if they distribute 100% of their taxable income and meet certain income, asset and shareholder tests. If we fail to qualify as a REIT in any taxable year, we will be subject to federal income taxes at regular corporate rates (including any alternative minimum tax) and may not be able to qualify as a REIT for the four subsequent taxable years. Even as a REIT, we may be subject to certain state and local taxes on our own income and property, and to federal income and excise taxes on our undistributed taxable income.

We have elected taxable REIT subsidiary (TRS) status for some of our consolidated subsidiaries. This allows us to provide services that would otherwise be considered impermissible for REITs. Many of the foreign countries in which we have operations do not recognize REITs or do not accord REIT status under their respective tax laws to our entities that operate in their jurisdiction. In the United States, we are taxed in certain states in which we operate. Accordingly, we recognize income tax expense for the federal and state income taxes incurred by our TRSs, taxes incurred in certain states and foreign jurisdictions and interest and penalties, associated with our unrecognized tax benefit liabilities.

In July 2006, Financial Accounting Standards Board (FASB) Interpretation No. 48 *Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109* (FIN 48) was issued. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS No. 109 *Accounting for Income Taxes* . FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and provides guidance on various income tax accounting issues, including derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Under FIN 48, we may recognize the tax benefit from an uncertain tax position only if it is more-likely-than-not that the tax position will be sustained on examination by taxing authorities. We adopted the provisions of FIN 48 in 2007 and, as a result, we recognized a $9.3 million increase in the liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007 balance of distributions in excess of net earnings.

Deferred income tax is generally a function of the period s temporary differences (items that are treated differently for tax purposes than for financial reporting purposes), the utilization of tax net operating losses generated in prior years that had been previously recognized as deferred income tax assets and deferred income tax liabilities related to indemnification agreements related to certain contributions to property funds. A valuation allowance for deferred income tax assets is provided if we believe all or some portion of the deferred income tax asset may not be realized. Any increase or decrease in the valuation allowance that results from a change in circumstances that causes a change in the estimated realizability of the related deferred income tax asset is included in income. See Note 14 for further discussion of income taxes.

Financial Instruments. In the normal course of business, we use certain types of derivative financial instruments for the purpose of managing our foreign currency exchange rate and interest rate risk. We reflect our derivative financial instruments at fair value and record changes in the fair value of these derivatives each period in earnings, unless specific hedge accounting criteria are met. To qualify for hedge accounting treatment, certain criteria must be met. Generally, the derivative instruments used for risk management purposes must effectively reduce the risk exposure that they are designed to hedge (primarily interest rate swaps) and, if a derivative instrument is utilized to hedge an

anticipated transaction, the anticipated transaction must be probable of occurring. Derivative instruments meeting these hedging criteria are formally designated as hedges at the inception of the contract.

The unrealized gains and losses resulting from changes in fair value of an effective hedge are recorded in accumulated other comprehensive income and are amortized to earnings over the remaining term of the hedged items. The ineffective portion of a hedge, if any, is immediately recognized in earnings to the extent that the

PROLOGIS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

change in value of the derivative instrument does not perfectly offset the change in value of the item being hedged.

We estimate the fair value of our financial instruments through a variety of methods and assumptions that are based on market conditions and risks existing at each balance sheet date. Primarily, we use quoted market prices or quotes from brokers or dealers for the same or similar instruments. These values represent a general approximation of possible value and may never actually be realized.

We adopted SFAS No. 157 *Fair Value Measurements* (SFAS 157) on January 1, 2008 for our financial assets and liabilities, primarily derivative instruments to which either we or our unconsolidated investees are a party. SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with GAAP and expands disclosures about fair value measurements. SFAS 157 applies to other accounting pronouncements that require or permit fair value measurements but does not require any new fair value measurements. The provisions of SFAS 157 relating to non-financial assets and liabilities that are not required or permitted to be measured at fair value on a recurring basis was delayed in February 2008 with the issuance of FASB Staff Position No. FAS 157-2 Effective Date of FASB Statement No. 157 (FSP FAS 157-2). Fair value measurements identified in FSP FAS 157-2 will be effective for our fiscal year beginning January 1, 2009. Adoption of FSP FAS 157-2 will not have a material impact on our financial position and results of operations.

Environmental costs. We incur certain environmental remediation costs, including cleanup costs, consulting fees for environmental studies and investigations, monitoring costs, and legal costs relating to cleanup, litigation defense, and the pursuit of responsible third parties. Costs incurred in connection with operating properties and properties previously sold are expensed. Costs related to undeveloped land are capitalized as development costs. Costs incurred for properties to be disposed are included in the cost of the properties upon disposition. We maintain a liability for the estimated costs of environmental remediation expected to be incurred in connection with undeveloped land, operating properties and properties previously sold that we adjust as appropriate as information becomes available.

Recent Accounting Pronouncements. In December 2007, the FASB issued SFAS No. 141R *Business Combinations* (SFAS 141R) and SFAS No. 160 *Noncontrolling Interests in Consolidated Financial Statements An Amendment of ARB No. 51* (SFAS 160). SFAS 141R and SFAS 160 require most identifiable assets, liabilities, noncontrolling interests, and goodwill acquired in a business combination to be recorded at full fair value and require noncontrolling interests (previously referred to as minority interests) to be reported as a component of equity, which changes the accounting for transactions with noncontrolling interest holders. The provisions of SFAS 141R and SFAS 160 are effective for our fiscal year beginning January 1, 2009. SFAS 141R will be applied to business combinations occurring after the effective date and SFAS 160 will be applied prospectively to all changes in noncontrolling interests, including any that existed at the effective date. The initial adoption of SFAS 141R will have a nominal impact on our financial position or results of operations but will impact us in the future. SFAS 141R broadens the scope of what qualifies as a business combination to include the acquisition of an operating property by us and our unconsolidated investees. Transaction costs related to the acquisition of a business that were previously capitalized will be expensed under SFAS 141R. The transaction costs related to the acquisition of land and equity method investments will continue to be capitalized. SFAS 141R will require subsequent adjustments of tax uncertainties that occur after the purchase price allocation period to be recognized in earnings. Previously, these adjustments were recognized in the purchase price as an adjustment to goodwill.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133* (SFAS 161). SFAS 161 requires enhanced disclosures related to derivative instruments and hedging activities. SFAS 161 will require disclosures relating to: (i) how and why an entity uses derivative instruments; (ii) how derivative instruments and related hedge

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

items are accounted for under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* ; and (iii) how derivative instruments and related hedged items affect an entity s financial position, financial performance and cash flows. SFAS 161 must be applied prospectively and is effective for our fiscal year beginning January 1, 2009. The adoption of SFAS 161 will not have a material impact on our consolidated financial statements.

In May 2008, the FASB issued FASB Staff Position APB 14-1 *Accounting for Convertible Debt Instruments that May Be Settled in Cash Upon Conversion (Including Partial Cash Settlement)* that requires separate accounting for the debt and equity components of convertible debt. The value assigned to the debt component is the estimated fair value of a similar bond without the conversion feature, which would result in the debt being recorded at a discount. The resulting debt discount would be amortized over the period during which the debt is expected to be outstanding (for example, through the first optional redemption date) as additional non-cash interest expense. The effective date of this accounting change is January 1, 2009 with the application of the new accounting applied retrospectively to both new and existing convertible instruments, including the convertible notes we issued in 2007 and 2008. As a result of the new accounting, we expect our non-cash interest expense to increase between $73 million and $83 million per year, prior to capitalization as a result of our development activities. In addition, we will restate our 2007 and 2008 results to reflect the additional interest expense. This restatement will also include an adjustment to the interest capitalized related to our development activities to both properties we currently own, as well as properties that were contributed during the periods the convertible notes were outstanding.

The following table illustrates the impact on our Consolidated Balance Sheets and Consolidated Statements of Operations for these periods (in thousands):

	December 31, 2008		December 31, 2007	
	As Reported	**As Adjusted**	**As Reported**	**As Adjusted**
Consolidated Balance Sheets (1):				
Real estate	$ 15,706,172	$ 15,725,069	$ 16,578,845	$ 16,581,119
Debt	$ 11,007,636	$ 10,711,350	$ 10,506,068	$ 10,217,168
Shareholders equity	$ 6,424,712	$ 6,739,895	$ 7,436,398	$ 7,727,572
Consolidated Statements of Operations (1):				
Total cost of CDFS dispositions	$ 3,836,519	$ 3,839,923	$ 4,241,700	$ 4,241,716
Interest expense	$ 341,305	$ 384,715	$ 368,512	$ 390,256
Loss from discontinued operations	$ (211,365)	$ (212,360)	$ 86,596	$ 86,596
Net earnings (loss)	$ (406,773)	$ (454,582)	$ 1,074,340	$ 1,052,580

(1) Amounts do not include adjustments to previously deferred gains or depreciation expense due to immateriality.

In November 2008, the FASB s Emerging Issues Task Force (EITF) reached a consensus on EITF Issue No. 08-6 Equity Method Investment Accounting Considerations . EITF 08-6 continues to follow the accounting for the initial carrying value of equity method investments in APB Opinion No. 18 *The Equity Method of Accounting for Investments in Common Stock* , which is based on a cost accumulation model and generally excludes contingent consideration. EITF 08-6 also specifies that other-than-temporary impairment testing by the investor should be performed at the investment level and that a separate impairment assessment of the underlying assets is not required. An impairment charge by the investee should result in an adjustment of the investor s basis of the impaired asset for the investor s pro-rata share of such impairment. In addition, EITF 08-6 reached a consensus on how to account for an issuance of shares by an investee that reduces the investor s ownership share of the investee. An investor should account for such transactions as if it had sold a proportionate share of its investment with any gains or losses recorded through earnings. EITF 08-6 also addresses the accounting for a change in an investment from the equity method to the cost method after

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adoption of SFAS 160. EITF 08-6 is effective for fiscal years beginning on or after December 15, 2008. We do not expect the adoption of EITF 08-6 to have a material impact on our financial position or results of operations.

Reclassifications. Certain amounts included in our consolidated financial statements for prior years have been reclassified to conform to the 2008 financial statement presentation.

3. Real Estate:

Real Estate Assets

Real estate assets are presented at cost, and consist of the following (in thousands):

	December 31,	
	2008	2007
Investments in real estate assets:		
Industrial properties (1):		
Improved land	$ 2,414,023	$ 2,247,013
Buildings and improvements	8,542,445	8,799,318
Retail and mixed use properties (2):		
Improved land	81,117	77,536
Buildings and improvements	277,875	258,743
Properties under development (3)	1,163,610	1,986,285
Land held for development (4)	2,481,216	2,152,960
Land subject to ground leases and other (5)	424,489	404,671
Other investments (6)	321,397	652,319
Investment before depreciation	15,706,172	16,578,845
Less accumulated depreciation	1,583,299	1,368,458
Net real estate assets	$ 14,122,873	$ 15,210,387

(1) At December 31, 2008 and 2007, we had 1,297 and 1,378 industrial operating properties consisting of 195.7 million square feet and 207.3 million square feet, respectively.

(2) At December 31, 2008 and 2007, we had 34 and 32 retail operating properties consisting of 1.4 million square feet and 1.3 million square feet, respectively. Amounts include an office property with a cost of $7.9 million at both December 31, 2008 and 2007.

(3) Properties under development consisted of 65 industrial properties aggregating 19.8 million square feet at December 31, 2008 and 180 properties aggregating 48.8 million square feet at December 31, 2007. At December 31, 2008, our total expected investment upon completion of the properties under development is approximately $1.9 billion, of which $1.2 billion was incurred.

(4) Land held for future development consisted of 10,134 and 9,351 acres of land or land use rights at December 31, 2008 and 2007, respectively.

(5) At December 31, 2008 and 2007, amount represents investments of $389.2 million and $368.5 million in land we own and lease to our customers under long-term ground leases and an investment of $35.3 million and $36.2 million in railway depots, respectively.

(6) Other investments primarily include: (i) restricted funds that are held in escrow pending the completion of tax-deferred exchange transactions involving operating properties ($9.0 million and $94.5 million at

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 2008 and 2007, respectively.); (ii) earnest money deposits associated with potential acquisitions; (iii) costs incurred during the pre-acquisition due diligence process; (iv) costs incurred during the pre-construction phase related to future development projects, including purchase options on land and certain infrastructure costs; (v) cost of land use rights on operating properties in China (2007 only); and (vi) costs related to our corporate office buildings.

At December 31, 2008, we owned real estate assets in North America (Canada, Mexico and the United States), Europe (Austria, Belgium, the Czech Republic, France, Germany, Hungary, Italy, the Netherlands, Poland, Romania, Slovakia, Spain, Sweden, and the United Kingdom) and Asia (Japan and South Korea). In addition, we owned assets in China that were sold in early 2009 and are classified as held for sale at December 31, 2008.

During the last three years, we completed individual and portfolio acquisitions of industrial properties, other than those discussed in Note 4 and Note 5, as follows (aggregated, dollars and square feet in thousands):

	Number of Properties	Aggregate Square Feet	Aggregate Purchase Price	Debt Assumed
2008	25	5,812	$ 324,029	$ 6,599
2007	41	7,347	$ 351,639	$ 27,305
2006	74	13,529	$ 735,427	$ 87,919

During the years ended December 31, 2008, 2007 and 2006, we recognized gains of $11.7 million, $146.7 million and $81.5 million, respectively, in Gains Recognized on Dispositions of Certain Non-CDFS Business Assets in our Consolidated Statements of Operations for properties contributed to the property funds (2 in 2008, 77 in 2007 and 39 in 2006), from our direct owned segment. In addition, we recognized previously deferred proceeds related to non-CDFS properties sold to a third party by a property fund. Due to our continuing involvement through our ownership in the property funds, these dispositions are not included in discontinued operations and the gains recognized include only the portion attributable to the third party ownership in the property funds that acquired the properties.

During the year ended December 31, 2008, we recognized impairment charges of $274.7 million related to real estate properties in our direct owned segment. See Note 13 for further discussion.

We previously identified properties that were developed or acquired with the intent to contribute them to an unconsolidated property fund. Our policy is to not depreciate these properties during the period from completion or acquisition until their contribution to the property fund. In 2008, in connection with changes in our business strategy, including uncertainty as to when, or if, these properties will be contributed and our intent to hold and operate these properties for our own use, we no longer identify specific properties for contribution to property funds. As a result, we recorded a $30.9 million adjustment to depreciation expense to depreciate these properties through December 31,

2008.

Operating Lease Agreements

We lease our operating properties and certain land parcels to customers under agreements that are generally classified as operating leases. Our largest customer and 25 largest customers accounted for 1.89% and 11.84%, respectively, of our annualized collected base rents at December 31, 2008. At December 31, 2008, minimum lease payments on leases with lease periods greater than one year for space in our operating properties,

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

excluding properties held for sale, and including leases of land under ground leases, during each of the years in the five-year period ending December 31, 2013 and thereafter are as follows (in thousands):

2009	$ 680,611
2010	586,893
2011	472,766
2012	356,025
2013	248,955
Thereafter	1,255,467
	$ 3,600,717

These amounts do not reflect future rental revenues from the renewal or replacement of existing leases and exclude reimbursements of operating expenses. In addition to minimum rental payments, certain customers pay reimbursements for their pro rata share of specified operating expenses, which amounted to $231.8 million, $217.0 million and $180.0 million for the years ended December 31, 2008, 2007 and 2006, respectively. These reimbursements are reflected as rental income and rental expenses in the accompanying Consolidated Statements of Operations.

4. Acquisitions:

In February 2007, we purchased the industrial business and made a 25% investment in the retail business of Parkridge Holdings Limited (Parkridge), a European developer. The total purchase price was $1.3 billion, which was financed with $733.9 million in cash, including amounts settled in cash subsequent to the purchase date, the issuance of 4.8 million common shares (valued for accounting purposes at $71.01 per share for a total of $339.5 million) and the assumption of $191.5 million in debt and other liabilities. The cash portion of the acquisition was funded with borrowings under our credit facilities.

The acquisition included 6.3 million square feet of operating distribution properties, including developments under construction, and 1,139 acres of land, primarily in Central Europe and the United Kingdom. We allocated the purchase price based on estimated fair values and recorded approximately $724.7 million of real estate assets, $156.3 million of investments in joint ventures and other unconsolidated investees, $58.1 million of cash and other tangible assets and $325.8 million of goodwill and other intangible assets, which are included in Other Assets in our Consolidated Balance Sheet. During 2008, we recognized an impairment charge of $175.4 million related to this allocated goodwill. See Note 13. The Parkridge acquisition would not have had a material impact on our consolidated results of operations for the years ended December 31, 2007, and 2006, and as such, we have not presented any pro forma financial information.

See also Note 3 for information on real estate property acquisitions.

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5. Unconsolidated Investees:

Summary of Investments

We have ownership interests in several unconsolidated property funds and joint ventures that we account for using the equity method. Our investments in and advances to these unconsolidated investees are summarized as follows (in thousands):

	December 31,	
	2008	**2007**
Property funds	$ 1,957,977	$ 1,755,113
Other investees	312,016	590,164
Totals	$ 2,269,993	$ 2,345,277

Property Funds

We have investments in several property funds that own portfolios of operating industrial properties. Many of these properties were originally developed by ProLogis and contributed to these property funds, although certain of the property funds have also acquired properties from third parties. When we contribute a property to a property fund, we generally receive ownership interests (based on our pre-contribution ownership in the fund) as part of the proceeds generated by the contribution. We earn fees for acting as manager of the property funds and the properties they own. We may earn additional fees by providing other services including, but not limited to, acquisition, development, construction management, leasing and financing activities. We may also earn incentive performance returns based on the investors returns over a specified period.

Summarized information regarding our proportionate share of net earnings or losses and fees and incentives related to our investments in property funds is as follows (in thousands):

	Years Ended December 31,		
	2008	**2007**	**2006**
Earnings (loss) from unconsolidated property funds:			
North America	$ 3,271	$ 17,161	$ 59,732
Europe	(94,429)	60,913	21,605
Asia	22,042	16,379	11,718
Total earnings (loss) from unconsolidated property funds	$ (69,116)	$ 94,453	$ 93,055

Property management and other fees and incentives:			
North America	$ 61,753	$ 47,164	$ 57,800
Europe	51,969	43,752	145,622
Asia	17,289	13,803	8,507
Total property management and other fees and incentives	$ 131,011	$ 104,719	$ 211,929

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Information about our property funds (the names in parentheses represent the legal names of the entities) is as follows:

	As of December 31,					
Fund Names	**Number of properties owned 2008**	**Square feet (in millions) 2008**	**Ownership Percentage 2008**	**Ownership Percentage 2007**	**Investment in and advances to (in thousands) 2008**	**Investment in and advances to (in thousands) 2007**
ProLogis California (ProLogis California I LLC) (1)	80	14.2	50.0%	50.0%	$ 102,685	$ 106,630
ProLogis North American Properties Fund I (ProLogis North American Properties Fund I LLC) (1)	36	9.4	41.3%	41.3%	25,018	27,135
ProLogis North American Properties Fund VI (Allagash Property Trust) (1)	22	8.6	20.0%	20.0%	35,659	37,218
ProLogis North American Properties Fund VII (Brazos Property Trust) (1)	29	6.2	20.0%	20.0%	32,679	31,321
ProLogis North American Properties Fund VIII (Cimmaron Property Trust) (1)	24	3.1	20.0%	20.0%	13,281	14,982
ProLogis North American Properties Fund IX (Deerfield Property Trust) (1)	20	3.4	20.0%	20.0%	13,375	13,986
ProLogis North American Properties Fund X (Elkhorn Property Trust) (1)	29	4.2	20.0%	20.0%	15,567	15,721
ProLogis North American Properties Fund XI (KPJV, LLP) (1)	13	4.1	20.0%	20.0%	28,322	30,712
ProLogis North American Industrial Fund (2)	258	49.6	23.1%	23.2%	191,088	104,277
ProLogis North American Industrial Fund II (ProLogis NA2 LP) (1)(3)	150	35.8	36.9%	36.9%	265,575	274,238
ProLogis North American Industrial Fund III (ProLogis NA3 LP) (1)(4)	120	24.7	20.0%	20.0%	122,148	123,720
ProLogis Mexico Industrial Fund (ProLogis MX Fund LP) (5)	73	9.5	24.2%	20.0%	96,320	38,085
PEPR (ProLogis European Properties) (6)	246	56.3	24.9%	24.9%	321,984	494,593
PEPF II (ProLogis European Properties II) (7)	153	38.9	36.9%	24.3%	312,600	158,483

ProLogis Japan Properties Fund I (PLD/RECO Japan TMK Property Trust) (1)(8)	16	7.1	20.0%	20.0%	114,111	87,663
ProLogis Japan Properties Fund II (ProLogis Japan Properties Trust) (1)(8)	54	19.9	20.0%	20.0%	245,698	189,584
ProLogis Korea Fund (ProLogis Korea Properties Trust) (1)	13	1.9	20.0%	20.0%	21,867	6,765
Totals	1,336	296.9			$ 1,957,977	$ 1,755,113

(1) We have one fund partner in each of these property funds.

(2) We refer to the combined entities in which we have ownership interests with ten institutional investors as one property fund named ProLogis North American Industrial Fund. Our ownership percentage is based on our levels of ownership interest in these different entities. In connection with the contribution of properties in 2008, we advanced the property fund $7.5 million, all of which was repaid in 2008.

(3) In July 2007, we acquired all of the units in Macquarie ProLogis Trust, an Australian listed property trust (MPR) which had an 88.7% ownership interest in ProLogis North American Properties Fund V. The total consideration was approximately $2.0 billion consisting of cash in the amount of $1.2 billion and assumed liabilities of $0.8 billion. We entered into foreign currency forward contracts to economically hedge the purchase price of MPR. As this type of contract does not qualify for hedge accounting treatment, we recognized gains of $26.6 million in 2007 when the contract settled that are included in Foreign Currency Exchange Gains and Losses, Net in our Consolidated Statements of Operations.

As a result of the MPR acquisition, we owned 100% and consolidated the results of the assets for approximately two months, at which time the lender converted certain of the bridge debt into equity of a new property fund, ProLogis North American Industrial Fund II, in which we have a 36.9% equity interest. Upon conversion by the lender in the third quarter of 2007, we recognized net gains of $68.6 million that are reflected in CDFS Acquired Property Portfolios in our Consolidated Statements of Operations.

(4) In July 2007, we formed a new property fund to acquire a portfolio of industrial properties from a third party. We refer to the combined entities in which we have ownership interests as one property fund named

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

ProLogis North American Industrial Fund III. The total consideration for the acquisition was approximately $1.8 billion, including transaction costs.

(5) On September 11, 2007, we contributed properties to a new property fund formed with several institutional investors. We refer to the combined entities in which we have ownership interests as one property fund named ProLogis Mexico Industrial Fund. During 2008, we loaned this property fund $153.1 million that was used to repay bridge financing that had matured and for a portion of the costs related to a third party acquisition. Through December 31, 2008, the fund had repaid $137.9 million of this loan with proceeds obtained from third party financing. The loan bears interest at LIBOR plus a margin and is payable upon demand.

(6) In December 2008, we purchased units in ProLogis European Properties Fund II (PEPF II) from ProLogis European Properties (PEPR) that represented a 20% interest for 43 million ($61.1 million) and assumed 348 million of PEPR s future equity commitments related to these units. The units were purchased at a discount to net asset value due to PEPR s near-term liquidity needs.

In January 2009, PEPR received offers for their remaining 10.4% interest in PEPF II for 10.5 million and recorded the resulting impairment as of December 31, 2008. As a result of the sale of units to us and the impairment of their remaining ownership (based on offers received), PEPR recognized a total loss of 310.9 million. Our share of this loss, reflected as Earnings (Loss) from Unconsolidated Property Funds in our Consolidated Statements of Operations, was $108.2 million.

In connection with the purchase of PEPR s interest in PEPF II, PEPR has a 12-month option to repurchase the 20% interest from us at our cost per unit (including any capital contributions we have made related to these units).

In September 2006, PEPR completed an initial public offering (IPO), and as the manager of the property fund, we received an incentive return of $109.2 million.

(7) In July 2007, we formed a new European property fund, PEPF II with several third party investors. From July 2007 through December 2008 PEPR owned approximately 30% of PEPF II. During that same period we owned approximately 24% of PEPF II, which included an indirect interest through PEPR. As a result of the additional 20% investment we made in December and contributions made in December, as of December 31, 2008, we own a 34.3% direct interest in PEPF II. PEPR owned a 10.4% interest in PEPF II, which due to our ownership in PEPR, results in us owning an additional 2.6% of PEPF II indirectly (combined direct and indirect ownership in PEPF II at December 31, 2008 was 36.9%).

(8) On December 23, 2008, we entered into an agreement to sell our interests in the Japan property funds (see Note 21).

Several property funds have equity commitments from us and our fund partners. We may fulfill our equity commitment with a portion of the proceeds from the properties we contribute to the property fund or cash. Our fund partners fulfill the commitment with the contribution of cash. The following table outlines acquisitions made by these property funds from ProLogis and third parties during the year ended December 31,

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2008, including the related financing of such acquisitions, and the remaining equity commitments of each property fund as of December 31, 2008 (in millions):

	Fund Acquisitions					Remaining Equity Commitments			Available Under Credit Facility
	ProLogis	Third Parties	Total	Debt	Equity and Other	ProLogis	Fund Partners	Expiration Date	
ProLogis North American Industrial Fund (1)	$ 815.2	$	$ 815.2	$ 243.0	$ 572.2	$ 72.5	$ 211.7	2/10	$ 223.4
ProLogis Mexico Industrial Fund (2)	155.0	189.8	344.8	155.8	189.0	44.3	246.7	8/10	
ProLogis European Properties Fund II (2)(3)	2,604.3	84.0	2,688.3	1,172.1	1,516.2	830.4(4)	1,253.1(4)	8/10	77.7
ProLogis Japan Properties Fund II (5)	876.8	83.7	960.5	555.0	405.5				
ProLogis Korea Fund (2)	11.1	119.1	130.2	25.2	105.0	23.2	92.8	6/10	
Total	$ 4,462.4	$ 476.6	$ 4,939.0	$ 2,151.1	$ 2,787.9	$ 970.4	$ 1,804.3		$ 301.1

(1) The investor agreements were modified in early 2009 to extend the remaining equity commitments through 2010, which were originally scheduled to expire in February 2009. In connection with the modifications, the commitments related to property contributions were eliminated and one investor did not extend its commitment. Amounts presented reflect these changes. We expect the remaining equity commitments to be used to pay down existing debt or to make opportunistic acquisitions, depending on market conditions and other factors.

(2) We are committed to offer to contribute substantially all of the properties that we develop and stabilize in Europe, Mexico and South Korea to these respective funds. These property funds are committed to acquire such

properties, subject to certain exceptions, including that the properties meet certain specified leasing and other criteria, and that the property funds have available capital. We are not obligated to contribute properties at a loss.

Dependent on market conditions, we expect to make contributions of properties to these property funds in 2009. Given the current debt markets, it is likely that the acquisitions will be financed by the property funds with all equity. Generally, the properties are contributed based on third-party appraised value (see note 3 below).

(3) During the fourth quarter, we modified the determination of the contribution value related to 2009 contributions to PEPF II. Once the capitalization rate is determined based on a third party appraisal, a margin of 0.25 to 0.75 percentage points is added depending on the quarter contributed. This modification was made due to the belief that appraisals were lagging true market conditions. The agreement provides for an adjustment in our favor if capitalization rates at the end of 2010 are lower than those used to determine contribution values.

(4) PEPF II s equity commitments are denominated in euro and include ProLogis of 568.1 million, PEPR of 136.1 million and remaining fund partners of 721.3 million. Our equity commitments include the 20% interest in PEPF II we acquired from PEPR in December 2008.

(5) In connection with the sale of our investments in the Japan property funds, we entered into an agreement to sell a property in Japan to our fund partner in 2009, which will utilize the remaining equity commitment from our fund partner. This property is included in assets held for sale at December 31, 2008.

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Summarized financial information of the property funds (for the entire entity, not our proportionate share) and our investments in such funds are presented below as of and for the years ended December 31, 2008 and 2007 (dollars in millions):

	2008			
	North America	Europe	Asia	Total
Revenues	$ 835.8	$ 665.6	$ 299.6	$ 1,801.0
Net earnings (loss) (1)(2)	$ (24.2)	$ (404.6)	$ 82.8	$ (346.0)
Total assets	$ 9,979.2	$ 8,982.9	$ 5,821.6	$ 24,783.7
Amounts due to us	$ 30.2	$ 22.4	$ 147.4	$ 200.0
Third party debt (3)	$ 5,726.0	$ 4,829.9	$ 2,906.5	$ 13,462.4
Total liabilities	$ 5,985.4	$ 5,581.1	$ 3,855.1	$ 15,421.6
Minority interest	$ 10.7	$ 19.8	$	$ 30.5
Equity	$ 3,983.1	$ 3,382.0	$ 1,966.5	$ 9,331.6
Our weighted average ownership at end of period (4)	27.5%	30.2%	20.0%	26.9%
Our investment balance (5)	$ 941.7	$ 634.6	$ 381.7	$ 1,958.0
Deferred proceeds, net of amortization(6)	$ 246.7	$ 299.0	$ 163.3	$ 709.0

	2007			
	North America	Europe	Asia	Total
Revenues	$ 634.1	$ 493.2	$ 180.4	$ 1,307.7
Net earnings (1)(7)	$ 27.6	$ 234.1	$ 64.4	$ 326.1
Total assets	$ 9,034.7	$ 6,526.4	$ 3,810.5	$ 19,371.6
Amounts due to us	$ 24.8	$ 70.0	$ 109.1	$ 203.9
Third party debt (3)	$ 5,305.2	$ 3,456.2	$ 1,889.5	$ 10,650.9
Total liabilities	$ 5,678.5	$ 4,057.7	$ 2,550.7	$ 12,286.9
Minority interest	$ 17.4	$ 10.8	$	$ 28.2
Equity	$ 3,338.8	$ 2,457.9	$ 1,259.8	$ 7,056.5
Our weighted average ownership at end of period (4)	27.9%	24.8%	20.0%	25.5%
Our investment balance (5)	$ 818.0	$ 653.1	$ 284.0	$ 1,755.1
Deferred proceeds, net of amortization (6)	$ 216.4	$ 193.9	$ 127.0	$ 537.3

(1) In North America, two of the property funds issued short-term bridge financing in 2007 to finance their acquisitions of properties from us and third parties and entered into interest rate swap contracts, designated as

cash flow hedges, to mitigate interest expense volatility associated with movements of interest rates. Based on the anticipated refinancing of the bridge financings with long-term debt issuances, certain of these derivative contracts no longer met the requirements for hedge accounting and, therefore, the change in fair value of these contracts was recorded through earnings, along with the gain or loss on settlement. Included in net earnings (loss) from North America for 2008 are net losses of $77.0 million, which represent the losses recognized from the change in value and settlement of these contracts. We included our proportionate share of these losses of $28.2 million in Earnings (Loss) from Unconsolidated Property Funds for the year ended December 31, 2008 in our Consolidated Statements of Operations.

We have recorded our proportionate share of the losses of the North America funds in the amount of $38.0 million that relate to the instruments that qualify for hedge accounting, including the outstanding contracts discussed above in Accumulated Other Comprehensive Income in Shareholders Equity. Once these contracts are settled, the amount of the gain or loss upon settlement that is recorded by the property funds in comprehensive income will be amortized over the life of the forecasted transaction. As discussed above, for the contracts that did not qualify for hedge accounting, we recognized our share of the gains or

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

losses in earnings. As of December 31, 2008, ProLogis North American Industrial Fund II has outstanding interest rate swap contracts, with notional amounts aggregating $223.2 million resulting in a liability at fair value of $48.0 million and swap rates ranging from 5.73% to 5.83%.

In Japan, the property funds entered into swap contracts that fixed the interest rate of their variable rate debt. These contracts did not qualify for hedge accounting and any change in value of these contracts is recognized as an unrealized gain or loss in earnings over the term of the contract. These contracts have no cash settlement at the end of the contract term. Included in net earnings from Asia for the year ended December 31, 2008 are net losses of $20.3 million, which represent the change in value of these contracts. We included our proportionate share of these losses of $4.1 million in Earnings (Loss) from Unconsolidated Property Funds for the year ended December 31, 2008 in our Consolidated Statements of Operations.

(2) Included in net loss for Europe in 2008 is the loss on sale and impairment of PEPR s ownership in PEPF II, as discussed above, of $434.3 million, of which $108.2 million was our share.

(3) As of December 31, 2008 and 2007, we had not guaranteed any of the debt of the property funds.

(4) Represents the weighted average of our ownership interests in all property funds at December 31, based on each entity s contribution to total assets, before depreciation, net of other liabilities.

(5) The difference between our percentage ownership interest of the property fund s equity and our investment balance results principally from three types of transactions: (i) deferring a portion of the proceeds we receive from a contribution of one of our properties to a property fund as a result of our continuing ownership in the property (see below); (ii) additional costs we incur associated with our investment in the property fund; and (iii) advances we have made to the property funds, generally timing related to fees.

(6) This amount is recorded as a reduction to our investment and represents the proceeds that we defer when we contribute a property to a property fund due to our continuing ownership in the property.

(7) Included in net earnings for Europe in 2007 is a net gain of $155.8 million from the disposition of 47 properties by PEPR, of which $38.2 million was our proportionate share.

Other unconsolidated investees

At December 31, 2008, we had investments in entities that develop and own industrial and retail properties, perform land and mixed-use development activity, own a hotel and own office properties. The amounts we have recognized as our proportionate share of the earnings (loss) from our investments in other unconsolidated investees, are summarized as follows (in thousands):

	Years Ended December 31,	
	2008	2007