Second Quarter 2010

Quarterly Commentary

Investment Advisor	Benchmark	Morningstar Category	Investment Objective
Principal Global Investors	Barclays Capital Aggregate Bond Index	Intermediate-Term Bond	Corp Bond - High Quality

Economy & Market Overview

Following four positive quarters in a row, both U.S. and international stocks fell in the second quarter of 2010. The rally ended as investor concerns mounted about economic stability in Europe, slowing growth in China and the sustainability of the U.S. recovery.[1]

Europe's troubles, which started with the revelation of Greece's staggering deficit and debt load, broadened as it became apparent other countries (such as Spain and Portugal) faced similar issues. Markets reacted negatively to the exposure of European banks to the sovereign and corporate debt of these countries, despite the nearly $1 trillion bail-out plan put in effect by the European Union and International Monetary Fund. In China, the government's decision to reign in real estate growth weighed on international investors, as did new data indicating a slowdown in China's pace of economic growth.[2]

Negative economic data reported during the quarter pointed to slowing growth across the U.S. economy: Employers continued their reluctance to add staff; May payrolls were meager, following gains in April and March.[3] Gross Domestic Product (GDP) for the first quarter came in lower than expected; the 2.7% gain was a sharp drop from the 5.6% increase for fourth quarter 2009.[4] After rising for three consecutive months, consumer confidence fell unexpectedly in June, reflecting consumers' uncertainty about jobs and income.[5] Following expiration of the home buyer tax credit in April, new-home sales fell in May to a seasonally adjusted, annual rate of 300,000 (the lowest number since the government began tracking the figure in 1963);[6] meanwhile, existing-home sales fell 2.2% in May after gaining 8% in April.[7]

After its June meeting, the Federal Reserve reaffirmed its belief that economic recovery is proceeding, but also acknowledged that "financial conditions have become less supportive of economic growth" and restated its intention to keep the fed funds interest rate very low "for an extended period."[8]

For the quarter, the broad U.S. stock market posted a return of -11.3% as all sectors within the Russell 3000 Index delivered negative performance. The economically sensitive materials sector struggled the most. Financial stocks also were under acute pressure, as investors grappled with the changing landscape of regulatory reform and how it might impact the industry. In this environment, growth and value performed similarly among large- and mid-cap stocks, while within small-caps, value slightly underperformed growth. From a market-cap perspective, small-caps outperformed large-caps.[9]

International stocks in developed markets returned -14.0%,[10] reflecting in part the precarious financial situation in Europe. Emerging markets performed better, but still delivered -8.37%.[11]

Real estate investment trusts returned -4.0%[12] to outperform the broad U.S. stock market. Although real estate fundamentals were still unfavorable, access to capital for commercial real estate had improved, which drew investors hoping to participate in the asset class's recovery.

Within fixed income, risk aversion was apparent as many investors turned to the "safe haven" of U.S. Treasuries, which outperformed other fixed-income sectors. By quarter-end, the yield on the benchmark 10-year Treasury had fallen from 3.84% to 2.95%. (Bond prices and yields move in opposite directions.) Meanwhile, investment-grade corporate bonds fell -2.25% relative to duration-adjusted Treasuries. Returns were slightly worse in the financial segment of the corporate bond market (down 2.97% relative to duration-adjusted Treasuries), due in part to uncertainty and anxiety surrounding financial regulation reform. Commercial mortgage-backed securities and asset-backed securities also lagged Treasuries, while mortgage-backed securities managed to outperform Treasuries by 0.01%.[13] Finally, high-yield bonds returned -3.86% relative to duration-adjusted Treasuries, with the lowest-rated (highest risk) high-yield bonds performing the worst.[14]

Performance Contributors

Positive Contributors

During last quarter:

The portfolio performed in line with the benchmark index, Barclays Capital Aggregate Bond Index, driven by positive sector allocation as well as positive security selection. An overweight to commercial mortgage-backed securities (CMBS) and an overweight to mortgage-backed securities were the largest contributors to positive sector allocation. The portfolio's long duration versus the index also contributed positively to performance as interest rates rallied.

During last 12 months:

Portfolio performance largely benefited from positive sector allocation over the 12-month period. The portfolio's overweight to CMBS was the largest driver of positive sector selection. An overweight allocation to investment-grade bonds (which varied between 120% and 160% of the index's weighting) added to performance. Additionally, the portfolio was long in duration, benefiting performance as interest rates (though volatile) fell over the period.

Negative Contributors

During last quarter:

The portfolio held an underweight to U.S. Treasuries (which outperformed the index), resulting in a slight negative to performance. An overweight to investment-grade corporate bonds detracted from performance as well. Additionally, the portfolio's underweight to U.S. agencies resulted in a slight negative impact on performance, because agencies outperformed during the period as investors became more risk-averse.

During last 12 months:

The portfolio's allocation to cash, while providing a liquidity cushion, was also a detractor to performance. Additionally, while the total sector allocation to investment-grade bonds was a positive, the portfolio's overweight to the consumer and industrial sector within corporate bonds was a negative because the sector underperformed the U.S. Corporate Investment Grade Index.

Changes to the investment option's structure or portfolio:

No material changes occurred in the portfolio structure.

High Quality Intermediate-Term Bond Separate Account-R6

Performance

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

In situations where the net and gross expense figures are different, the investment manager has contractually agreed to limit the investment option's expense. Differences may also be shown due to the investment manager choosing to pay certain expenses that would normally be payable by the investment option. The gross total investment expense figure does not reflect any waivers or caps on the mutual fund or underlying mutual fund in which a Separate Account invests. Returns displayed are always based on net total investment expense.

Average Annual Total Returns (%) as of 06/30/2010	QTR	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception
High Quality Intermediate-Term Bond Separate Account-R6	3.31	5.87	14.80	1.69	1.99	4.51	4.30
Barclays Capital Aggregate Bond Index	3.49	5.33	9.50	7.55	5.54	6.47	-
Intermediate-Term Bond Category	2.71	5.21	13.11	6.03	4.51	5.75	-
Morningstar Percentile Ranking	-	-	31	92	92	91	-
Total Funds in Category	1202	1186	1149	1011	880	515	-

Inception Date	03/15/1998
Ext. Perf. Inc. Date	03/15/1998
Total Inv. Exp Gross	0.56
Total Inv Exp Net	0.56
Waiver Date	-
Contractual Cap Date	-

Risk and Return Statistics Summary as of 06/30/2010

	3 Year Return vs. Rank						5 Year Return vs. Risk					
	Alpha	Beta	R2	Sharpe Ratio	Info Ratio	Std Dev	Alpha	Beta	R2	Sharpe Ratio	Info Ratio	Std Dev
High Quality Intermediate-Term Bond Separate Account-R6	-5.52	1.00	39.14	0.05	-1.14	6.47	-3.20	0.94	43.85	-0.12	-0.88	5.29

Relative to Barclays Capital Aggregate Bond Index

Risk and return statistical data is provided by Markov Processes International (MPI). Percentile rankings are based on total returns in accordance with the appropriate Morningstar peer group. Please see Important Notes section for definitions of Risk and Return Statistics.

Upside/Downside Capture Ratio Summary as of 06/30/2010

	3 Year Upside/Downside Capture Ratio						5 Year Upside/Downside Capture Ratio					
	# of Months		Avg Returns %		Market Benchmark %		# of Months		Avg Returns %		Market Benchmark %	
	Up	Down	Up	Down	Up	Down	Up	Down	Up	Down	Up	Down
High Quality Intermediate-Term Bond Separate Account-R6	23	13	0.83	-1.59	72.13	205.94	36	24	0.83	-1.04	79.32	162.44
Barclays Capital Aggregate Bond Index	26	10	1.15	-0.77	100.00	100.00	39	21	1.05	-0.64	100.00	100.00

Top Ten Holdings as of 05/31/2010

Security	Net Assets (%)
FNMA	3.53
United States Treas Nts 4.25%	3.10
FHLMC	2.82
United States Treas Nts	2.31
United States Treas Bds 6.25%	2.10
United States Treas Nts 3.125%	2.06
United States Treas Nts 3.375%	2.02
United States Treas Bds 4.5%	1.93
FHLMC	1.85
GNMA 5.5%	1.67
Total % in Top 10	**23.38**

Information is current as of the date noted. Keep in mind that portfolio holdings are subject to risk.

Manager(s)	Start Date	Degree	Alma Mater
William C. Armstrong	11/01/2002	M.B.A.	University of Iowa
Timothy R. Warrick	11/01/2002	M.B.A.	Drake University
Mark A. Lieb	07/01/2009	M.B.A.	University of Hartford

Investment Strategy

The investment seeks current income by investing primarily in intermediate-term fixed income securities rated A or higher. It normally invests the majority of assets in U.S. government debt, U.S. dollar-denominated Canadian or British government debt, mortgage-backed securities, and taxable municipal obligations and other debt rated BBB or higher. The average portfolio duration of the Separate Account normally varies between three and six years. The Separate Account may enter into reverse repurchase agreements to attempt to enhance portfolio return and income.

About Principal Global Investors

Principal Global Investors' fixed income capabilities emphasize a broad array of global credit, mortgage, asset-backed and government debt markets worldwide. The firm also offers extensive capabilities in structured fixed income strategies. Principal Global Investors manages $80.8 billion in fixed income assets as of December 31, 2009. Its global fixed income research efforts span sovereign and corporate debt markets worldwide and draw from 161 fixed income professionals. The disciplined and repeatable investment process combines bottom-up and top-down portfolio construction techniques with a strong focus on relative value and broad diversification. Principal Global Investors is a member of the Principal Financial Group®.

Important Notes

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

The value of the investment options will fluctuate so that when redeemed, shares or units may be worth more or less than the original cost.

Returns shown for periods of less than one year are not annualized. All returns displayed here are after Total Investment Expense of the investment option. Any operating expenses of a mutual fund or underlying mutual fund that are part of net Total Investment Expense are obtained from the mutual fund's most recent prospecuts. The operating expenses shown as part of the Total Investment Expense include voluntary expense limits and fee credit.

Fixed-income investment options are subject to interest rate risk, and their value will decline as interest rates rise. Neither the principal of bond investment options nor their yields are guaranteed by the U.S. government.

Fixed-income and asset allocation investment options that invest in mortgage securities are subject to increased risk due to real estate exposure.

Barclays Capital Aggregate Bond Index represents securities that are domestic, taxable, and dollar denominated. The index covers the U. S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis.

Risk and Return Statistics:
Alpha - The difference between an investment's actual returns and its expected performance, given its level of risk (as measured by beta).
Beta - An investment's sensitivity to market movements.
R-squared - Ranges from 0 to 100 and reveals how closely an investment's returns track those of a benchmark index.
Standard Deviation - Measures how much an investment's returns are likely to fluctuate.
Sharpe Ratio - Measures how an investment balances risks and rewards. The higher the Sharpe ratio, the better the investment's historical risk-adjusted performance.
Information Ratio - A risk-adjusted measure commonly used to evaluate an active manager's involvement skill. It's defined as the manager's excess return divided by the variability or standard deviation of the excess return.

About Principal Financial Group

The Principal Financial Group® (The Principal®) is a leading global financial company offering businesses, individuals and institutional clients a wide range of financial products and services. Our range of products and services includes retirement solutions, life and health insurance, wellness programs, and investment and banking products through our diverse family of financial services companies and national network of financial professionals.

Important Notes

[1] Source: On the Other Hand: Economic Insights, Second Quarter 2010, by Bob Baur and the Principal Global Investors Economic Committee

[2] Source: The Conference Board Leading Economic Index® (LEI) for China, measuring economic activity, increased 0.3% in April following increases of 1.2% in March and 0.4% in February.

[3] Source: U.S. Bureau of Labor Statistics: Employment Situation Summary 6/4/2010 (available at www.bls.gov)

[4] Source: Bureau of Economic Analysis, US Dept of Commerce (data available at www.bea.gov)

[5] Source: Data available at www.conference-board.org

[6] Source: National Association of Home Builders (data available at www.nahb.com)

[7] Source: National Association of Realtors (data available at www.realtor.org)

[8] Source: Federal Reserve press release dated 6/23/10 (available at www.federalreserve.gov)

[9] Source: As measured by Russell family of indexes

[10] Source: As measured by the MSCI EAFE Index

[11] Source: As measured by the MSCI EM Index

[12] Source: As measured by the MSCI U.S. REIT Index

[13] Source: As measured by components of Barclays Capital Aggregate Bond Index

[14] Source: As measured by components of Barclays Capital High Yield Index

This report is not complete unless all pages, as noted below, are included.

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