PROLOGIS
Form 10-K
February 28, 2008

Table of Contents

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, 2007

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

PROLOGIS
(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
	New York Stock Exchange

Series G Cumulative Redeemable Preferred Shares of Beneficial
Interest par
value $0.01 per share

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. Yes o No þ

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, 2007, the aggregate market value of the voting common equity held by non-affiliates of the registrant was $14,561,373,852.

At February 22, 2008, there were outstanding approximately 258,202,700 common shares of beneficial interest of the registrant.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s definitive proxy statement for the 2008 annual meeting of its shareholders are incorporated by reference in Part III of this report.

TABLE OF CONTENTS

Table of Contents

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 of developed properties, general 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 and its consolidated subsidiaries.

PART I

ITEM 1. Business

ProLogis

We are the world s largest owner, manager and developer of industrial distribution facilities. We designed our business strategy to achieve long-term sustainable growth in cash flow and a high level of return for our shareholders. We manage our business by utilizing the ProLogis Operating System®, an organizational structure and service delivery system that we built around our customers. When combined with our international network of distribution properties, the ProLogis Operating System enables us to meet our customers needs for distribution space on a global basis. We believe that by integrating international scope and expertise with a strong local presence in our markets, we have become an attractive choice for our targeted customer base, the largest global users of distribution space.

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 offices in Asia are located in Tokyo, Japan and Shanghai, China.

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.

Business Strategy and Global Presence

We were formed in 1991 as an owner of industrial distribution space operating in the United States with a primary objective of differentiating 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. As our customers needs expanded to markets outside the United States, so did our portfolio and our management team. We currently have operations in North America, Europe and Asia. We are exploring opportunities in India and recently announced a development fee project in Dubai, United Arab Emirates. Our business strategy is to hold certain investments on a long-term basis and generate income from leasing space to our customers, develop properties primarily for contribution to property

Table of Contents

funds in which we maintain an ownership interest and manage those property funds and the properties they own. Since our inception, we have grown and expect continued growth through the development and selective acquisition of properties, individually and as portfolios, in targeted markets. In September 2005, we completed a merger whereby Catellus Development Corporation (Catellus) was merged into one of our subsidiaries (the Catellus Merger) and added approximately $4.5 billion of real estate assets to our direct owned investments. At that time, we added certain retail properties to our portfolio due to the similarities with our industrial distribution properties. This investment in retail, along with our investments in CDFS joint ventures that develop retail and mixed-use properties, gives us opportunities to diversify our revenue base, but also exposes us to the potential risks of the retail and mixed-use sector. As of December 31, 2007, our direct owned real estate investments totaled $16.6 billion.

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.

The primary business drivers across the globe continue to be the need for greater distribution network efficiency and state-of-the-art facilities to support the growing business of global trade. After 16 years in operation, our focus on our customers expanding needs and improving their supply-chain operations has enabled us to become the world s largest owner, manager and developer of industrial distribution facilities.

At December 31, 2007, our total portfolio of properties owned, managed and under development, including direct-owned properties and properties owned by property funds and CDFS joint ventures, consisted of 2,773 properties aggregating 510.2 million square feet and serving 4,912 customers in 118 markets in North America, Europe and Asia.

Our Operating Segments

Our business is primarily organized into three reportable business segments: (i) property operations, (ii) investment management and (iii) development or CDFS business. 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 18 to our Consolidated Financial Statements in Item 8.

Operating Segments Property Operations

Our property operations segment represents the direct long-term ownership of industrial distribution and retail properties. Our investment strategy in the property operations segment focuses primarily on the ownership and leasing of industrial distribution properties in key distribution markets. Included in this segment are operating properties we developed and acquired within the CDFS business segment with the intention of contributing the property to a property fund.

Investments

At December 31, 2007, our property operations segment consisted of 1,409 operating properties aggregating 208.5 million square feet in North America, Europe and Asia. The properties are primarily distribution properties, although we own 31 retail properties located in North America aggregating 1.2 million square feet.

During 2007, we increased our investments in our property operations segment through the acquisition of 66 properties, aggregating 12.9 million square feet representing an investment of $816.7 million, through various individual and/or portfolio acquisitions, excluding the 153 properties that we acquired from a property fund as discussed below in Operating Segments Investment Management . We acquired these properties primarily for future contribution to an unconsolidated property fund. It is our policy to hold acquired properties for long-term investment, although we often reduce our ownership to less than 100% through the contribution to a property fund resulting in the realization of a portion of the development or repositioning profits. We also acquire properties through tax-deferred exchanges that result in our holding the properties for long-term investment. In addition, we have increased our investment in the property operations segment through the development of 137 distribution and retail properties, which are primarily pending contribution to a property fund, as further discussed below. At December 31, 2007 we had 249 operating properties aggregating 56.9 million square feet at a total investment of $3.6 billion that were developed or acquired in the CDFS business segment but are included in the property operations segment s assets pending contribution or sale.

Also, during 2007, we disposed of 152 non-CDFS properties from this segment aggregating 14.3 million square feet with an investment of $413.5 million at the time of disposition. These properties were sold to third parties and included in discontinued operations (75 properties with an investment of $168.5 million) or contributed to property funds (77 properties with an investment of $245.0 million). In addition, we contributed 268 CDFS business properties to the property funds, as discussed in more detail below.

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.

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, 2007). We expect to grow our revenue through the acquisition and development of distribution and retail properties, continued focus on our customers global needs for distribution space, and use of the ProLogis Operating System to increase rental rates and, to a limited extent, increases in occupancy rates in our existing properties. The results of operations of properties we develop or acquire with the intention of contributing to a property fund are included in this segment during the period after completion of development or acquisition until contribution. 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 all reported in rental expenses in the property operations segment.

Market Presence

At December 31, 2007, our 1,409 properties aggregating 208.5 million square feet in the property operations segment were located in 38 markets in North America (32 markets in the United States, five markets in Mexico and one market in Canada), 20 markets in 11 countries in Europe and nine markets in three countries in Asia. Our largest markets for the property operations segment in North America (based on our investment in the properties) are Atlanta, Chicago, Dallas/Fort Worth, New Jersey, San Francisco (East and South Bay), Southern California and Washington D.C./Baltimore, Maryland. Our largest investments in Europe are in Poland and the United Kingdom and our largest investment in Asia is in Japan. The properties we own in Europe and Asia primarily consist of properties that were developed or acquired in the CDFS business segment and are pending contribution or sale. See Operating Segments CDFS Business and Item 2. Properties .

Competition

We compete primarily with local, regional, and national developers for the acquisition of land for future development and the acquisition of properties for future contributions to the property funds. The existence of competitive 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. We also face competition from other investment managers in attracting capital in the property funds to be utilized to acquire the properties we plan to contribute.

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

Table of Contents

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 members to give the proper level of attention to our customers throughout our network. 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, 2007, we had 2,955 customers occupying 175.6 million square feet of distribution and retail space. Our largest customer and 25 largest customers accounted for 2.6% and 19.7%, respectively, of our annualized collected base rents at December 31, 2007.

Employees

We employ 1,535 persons in our entire business. Our employees work in three countries in North America (860 persons), in 13 countries in Europe (385 persons) and in five countries in Asia (290 persons). Of the total, we have assigned 685 employees to the property operations segment. We have 445 employees who work in corporate positions that are not assigned to a segment who may assist with property operations 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.

Future Plans

Our current business plan allows for the expansion of our network 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.

We intend to fund our investment activities in the property operations segment in 2008 primarily with operating cash flow from this segment, borrowings under existing credit facilities, additional debt and equity issuances and proceeds from contributions and dispositions of properties.

Operating Segments Investment Management

The investment management segment represents the long-term investment management of unconsolidated property funds and the properties they own. We utilize our investment management expertise to manage the property funds and we utilize our leasing and property management expertise to manage the properties owned by the funds. We report the property management costs, for both our direct-owned portfolio and the properties owned by the property funds, in rental expenses in the property operations 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 the market presence and customer relationships that are the key drivers of the ProLogis Operating System;

allows us to maintain a long-term ownership position in the properties;

allows us to realize a portion of the development profits from our CDFS business activities by contributing our stabilized development properties to property funds (profits are recognized to the extent of third party ownership in the property fund);

provides diversified sources of capital;

Table of Contents

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.

Investments

As of December 31, 2007, we had investments in and advances to 17 property funds totaling $1.8 billion with ownership interests ranging from 20% to 50%. These investments are in North America 12 aggregating $818.0 million; Europe two aggregating $653.1 million; and Asia three aggregating $284.0 million. These property funds own, on a combined basis, 1,131 distribution properties aggregating 244.2 million square feet with a total entity investment (not our proportionate share) in operating properties of $19.1 billion. In addition to our equity interest in the property funds, we act as manager of the funds and the properties owned by the funds.

During 2007, we had the following activity in our investments in property funds (see Note 4 to our Consolidated Financial Statements in Item 8 for additional information on these transactions):

We contributed 339 properties aggregating 71.8 million square feet to the property funds for proceeds of $5.3 billion, net of deferred gains of $279.6 million, representing the portion of the gains related to our continuing ownership in the entities acquiring the properties.

On a combined basis, the property funds acquired 160 properties from third parties aggregating 33.0 million square feet and disposed of 51 properties to third parties aggregating 6.5 million square feet.

We repositioned one property fund, formed three new property funds and made the first acquisitions of properties in a property fund, as follows:

- On July 11, 2007, we completed the acquisition of all of the units in Macquarie ProLogis Trust, an Australian listed property trust (MPR). At the time of acquisition, MPR owned approximately 89% of ProLogis North American Properties Fund V and certain other assets. The total consideration was approximately $2.0 billion consisting of cash of $1.2 billion and assumed liabilities of $0.8 billion. The cash portion of the acquisition was financed primarily with a $473.1 million term loan and a $646.2 million convertible loan. As a result of the MPR transaction, on July 11, 2007, we owned 100% of, and began consolidating, ProLogis North American Properties Fund V.

  On August 27, 2007 the lender converted $546.2 million of the convertible loan into equity of a newly formed property fund, ProLogis North American Industrial Fund II. In addition, we made an equity contribution of $100.0 million into the fund, which was used to repay the remaining balance on the convertible loan. The conversion resulted in us owning 36.9% of the equity of ProLogis North American Industrial Fund II. We account for our investment under the equity method of accounting. Upon conversion, we recognized net gains of $68.6 million.

- We formed two new property funds, ProLogis European Properties II (PEPF II) and ProLogis Mexico Industrial Fund that will be the primary investment vehicles to acquire all of the properties we develop and stabilize in Europe and Mexico, respectively. We made contributions of properties to the new funds in 2007. ProLogis Korea Fund, which was formed in 2006 and will be the primary investment vehicle to acquire all the properties we develop and stabilize in South Korea, acquired six properties from a third party in 2007. As of December 31, 2007, we own 24.3% of the equity of PEPFII and 20% of the equity of both ProLogis Mexico Industrial Fund and ProLogis Korea Fund.

- In July 2007, we formed a new property fund, in which we own 20% of the equity, ProLogis North American Industrial Fund III, that completed the acquisition of 122 distribution properties in North America from a third party for $1.8 billion.

Results of Operations

We recognize our proportionate share of the earnings or losses from our investments in unconsolidated property funds. In addition to the income recognized under the equity method, we recognize fees and incentives earned for services performed on behalf of the property funds and interest earned on advances to the property funds, if any. We earn certain fees for services provided to the property funds, such as property management, asset management, acquisition, financing and development fees. We may also earn incentives depending on the return provided to the fund partners over a specified period. We expect growth in income recognized to come from newly created property funds and growth in existing property funds. We expect the growth in the existing property funds to come primarily from additional properties the funds will acquire, generally from us, and increased rental revenues in the property funds due, in part, to the leasing and property management efforts we provide as manager of the properties.

Market Presence

At December 31, 2007, the property funds on a combined basis owned 1,131 properties aggregating 244.2 million square feet located in 38 markets in North America (the United States and Mexico), 27 markets in 12 countries in Europe and 9 markets in Asia (Japan and South Korea).

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 distribution 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 Property Operations .

Property Management

We manage the properties owned by the property funds in our property operations segment utilizing our leasing and property management experience and the ProLogis Operating System. 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 members to give the proper level of attention to our customers throughout our network.

Customers

As in our property operations segment, we have developed a customer base in the property funds 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, 2007, the property funds, on a combined basis, had 1,792 customers occupying 234.3 million square feet of distribution space. The largest customer and 25 largest customers of the property funds, on a combined basis, accounted for 3.2% and 25.0%, respectively, of the total combined annualized collected base rents at December 31, 2007. In addition, in this segment our customers are also the investors in each of our property funds. As of December 31, 2007, we served a total of 41 investors, several of whom invest in multiple funds.

Employees

The property funds generally have no employees of their own. Employees in our property operations segment are responsible for the management of the properties owned by the property funds. We have 65 employees who work in corporate positions assigned to the management of the property funds in our investment management segment. Our other 445 corporate employees may assist with these activities as well.

Table of Contents

Future Plans

We expect to continue to increase our investments in property funds. We expect to achieve these increases through the existing property funds acquisition of properties that have been developed or acquired by us in the CDFS business segment, as well as from third parties. We also expect growth in our investments to come from property funds that may be formed in the future. 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 of the portfolios owned by the property funds grows.

Operating Segments CDFS Business

Our CDFS business segment primarily encompasses our development of real estate properties that are subsequently contributed to a property fund in which we have an ownership interest and act as manager, or sold to third parties. Additionally, we acquire properties with the intent to rehabilitate and/or reposition the property prior to it being contributed to a property fund. We may also acquire a portfolio of properties with the intent of contributing the portfolio to an existing or future property fund. We also engage in other development activities directly and through joint ventures in which we invest.

Investments

At December 31, 2007, we had 177 distribution and three retail properties aggregating 48.8 million square feet under development with a total expected cost at completion of $3.9 billion. Our properties under development at December 31, 2007, which are provided by country in Item 2, include:

North America: 57 properties in Canada, Mexico and the United States, for a combined total of 13.4 million square feet, with a total expected cost of $0.9 billion (approximately 23.5% of the total);

Europe: 80 properties in 13 countries, for a combined total of 21.0 million square feet, with a total expected cost of $1.8 billion (approximately 44.9% of the total); and

Asia: 43 properties in China, Japan and South Korea, for a combined total of 14.4 million square feet, with a total expected cost of $1.2 billion (approximately 31.6% of the total).

In addition, at December 31, 2007, we had 249 operating properties aggregating 56.9 million square feet with a current investment of $3.6 billion that we previously developed or acquired in the CDFS business segment. These properties and their results of operations are currently included in the property operations segment pending contribution or sale. This brings our total pipeline of potential CDFS business properties, both completed and under development, to $7.5 billion at December 31, 2007.

In addition to the properties we own directly, we invest in unconsolidated joint ventures that develop and own real estate properties. We refer to these entities as CDFS joint ventures. At December 31, 2007, the CDFS joint ventures in which we have an ownership interest had the following properties under development:

14 distribution properties under development in North America, Europe and China in joint ventures in which we have an approximately 50% ownership interest. Our proportionate share of the total expected investment at completion is $97.0 million.

39 retail and mixed use properties under development in joint ventures in which we have ownership interests of approximately 30% (China) and 25% (Europe). Our proportionate share of the total expected investment at completion is approximately $254.7 million.

At December 31, 2007, we owned 9,351 acres of land, or land use rights, for future development with a current investment of $2.2 billion. The land is in North America (6,031 acres), Europe (2,702 acres) and Asia (618 acres). This land is primarily held for the future development of properties to be contributed to a property fund, although some of the land will be sold as is or further developed and sold to third parties. In addition, we also control, through either a letter of intent or option, another 6,802 acres in North America (2,936 acres), Europe (3,537 acres) and Asia (329 acres). The CDFS joint ventures also own or control another 555 acres for the future development of distribution properties within the venture.

Table of Contents

During 2007, we had investment activity in the CDFS business segment as follows:

We started the development of 191 properties aggregating 50.5 million square feet with a total expected cost at completion of $3.8 billion.

We completed the development of 137 properties aggregating 32.8 million square feet with a total expected cost of $2.4 billion.

We generated $5.0 billion of proceeds and $763.7 million of gains from the contributions of CDFS developed and repositioned properties, acquired property portfolios and sales of land.

We disposed of five CDFS properties to third parties, including two parcels of land subject to ground leases, all of which were included in discontinued operations, generating net proceeds of $205.8 million and resulting in $28.7 million of gains.

We acquired 5,622 acres of land for future development for $1.5 billion.

We invested $299.0 million in the form of equity investments and advances in CDFS joint ventures operating in Asia ($57.4 million), Europe ($238.7 million) and North America ($2.9 million). This includes the 25% investment we made in the retail business of Parkridge Holdings Limited (Parkridge Retail) in February 2007. See Note 4 to our Consolidated Financial Statements in Item 8 for more information on our investments in CDFS joint ventures.

Results of Operations

We recognize income primarily from the contributions of developed and repositioned properties and acquired property portfolios to the property funds and from dispositions to third parties. In addition, we: (i) earn fees from our customers or other third parties for development activities that we provide on their behalf; (ii) recognize interest income on notes receivable related to asset dispositions; (iii) recognize net gains from the disposition of land parcels; and (iv) recognize our proportionate share of the earnings or losses generated by CDFS joint ventures in which we have an investment. We expect growth in income in this segment to come primarily from the continued development of high-quality distribution and retail properties in our key markets, resulting in the contribution to property funds or sale to third parties. Due to the nature of the income recognized in the CDFS business segment, the level and timing of income may vary significantly between periods.

Market Presence

Our CDFS business segment operates in substantially all of the markets as our property operations segment. At December 31, 2007, we had properties under development in 22 markets in North America (15 in the United States, six in Mexico and one in Canada), in 28 markets in 13 countries in Europe and in nine markets in three countries in Asia. At December 31, 2007, we owned land for development in 32 markets in North America (26 in the United States, five in Mexico and one in Canada), 28 markets in 11 countries in Europe and seven markets in three countries in Asia.

Competition

We compete primarily with local, regional and national developers for the acquisition of land for future development and the acquisition of properties for future contribution to the property funds. The existence of competitive 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. We also face competition from other investment managers in attracting capital in the property funds to be utilized to acquire the properties we plan to contribute.

We believe we have competitive advantages due to (i) the strategic locations of our land positions owned or under control; (ii) our personnel who are experienced in the land acquisition and entitlement process; (iii) our global experience in the development of distribution properties, (iv) our ability to quickly respond to customers needs for high-quality distribution space in key global distribution markets; (v) our relationships with key customers established and serviced by our local personnel; (vi) our ability to leverage our

Table of Contents

organizational structure to provide a single point of contact for our global customers; (vii) our property management and leasing expertise and; (viii) our relationships and proven track record with current and prospective investors in the property funds.

Customers

We use the customer relationships that we have developed in our property operations segment and the ProLogis Operating System in marketing our CDFS business. Approximately half of the space leased in newly developed properties in our CDFS business segment is with repeat customers.

Employees

We employ 340 employees that are assigned to the CDFS business segment. Our employees assigned to other segments or working at a corporate level may assist with CDFS business segment activities as well.

Seasonal Nature of the Business

The demand for the properties that are developed or acquired in the CDFS business segment is not seasonal in nature. However, development activities may be impeded by weather in certain markets, particularly during the winter months, affecting the scheduling of development activities and potentially delaying construction starts and completions.

Future Plans

We intend to conduct the CDFS business segment substantially as we have in the past, while evaluating and responding to current market conditions, as appropriate. To be successful in the CDFS business segment, we believe we must be able to: (i) develop, acquire and rehabilitate or reposition and lease properties on a timely basis; and (ii) have access to capital available to fund the acquisition of land and development costs and, within the property funds, to acquire our CDFS business properties. The ability to lease our properties is dependent on customer demand. We experienced stronger leasing activity in 2007 than in prior years. We expect continued growth in global trade to positively impact absorption of available space in our global development pipeline in 2008. Our market research and customer feedback indicate that consolidation and reconfiguration of supply chains driven by the need for distribution space to support continued growth in global trade will continue to favorably influence the demand for distribution properties that we plan to offer in the CDFS business segment in 2008. In addition, we believe the limited supply of state-of-the-art distribution space in locations that minimize transportation costs, but allow for high levels of service to the customer, and our position of being a single-source provider of distribution space will provide opportunities within this operating segment. We believe we have differentiated ourselves from our competitors by providing high quality customer service on a global basis. As of December 31, 2007, we had 12 customers that lease 37.4 million square feet of space from us on all three of the continents where we operate. Approximately half of the space leased in our newly developed CDFS business segment properties is leased to repeat customers.

We expect to increase our development activities in 2008 through our direct development, as well as investments in CDFS joint ventures. We currently invest in CDFS joint ventures in North America, Europe and Asia that develop and own distribution properties and retail properties. In addition, in 2008 we will continue to focus a larger portion of our development activities on properties that are developed for a specific customer and are leased 100% prior to the commencement of development, Build to Suit Properties . We will evaluate opportunities in new markets, such as India and the Middle East. We will also evaluate mixed-use development projects where we may complete the entitlement process and develop the land and infrastructure in return for development fees, profit participation on land sales, title to the land, or a combination thereof.

We intend to utilize the capital generated through contributions and sales of properties, the proceeds from private or public debt and equity issuances and borrowings on existing or new credit facilities to fund our future CDFS business activities. Further, we intend to actively pursue other sources of committed capital to form new property funds that will acquire our CDFS business properties not currently subject to exclusivity.

Table of Contents

We have commitments to contribute properties to certain existing property funds. See Note 4 to our Consolidated Financial Statements in Item 8 for further discussion.

There can be no assurance that if the existing property funds do not continue to acquire the properties we have available, we will be able to secure other sources of capital in a timely manner and continue to generate profits from our development activities in a particular reporting period. In addition, due to recent turmoil in the credit markets, it may be more difficult for the property funds to obtain financing for the acquisitions of properties from us.

Other

We have other segments that do not meet the threshold criteria to disclose as a reportable segment. At December 31, 2007, these operations include primarily the management of land subject to ground leases.

Our Management

Our Chief Executive Officer, Jeffrey H. Schwartz, our President and Chief Operating Officer, Walter C. Rakowich and our President and Chief Investment Officer, Ted R. Antenucci, head our management team. Mr. Schwartz and Mr. Rakowich also serve as members on our Board of Trustees (the Board). On February 7, 2008, we announced Mr. Rakowich s plan to retire effective January 2, 2009.

In addition to the leadership and oversight provided by Messrs. Schwartz, Rakowich, and Antenucci, William E. Sullivan is our Chief Financial Officer and Edward S. Nekritz is our General Counsel and Secretary. Our investments and operations are overseen by John R. Rizzo, Managing Director of Global Development, Charles Sullivan, Managing Director for North America Capital Management, Larry Harmsen, Managing Director for North America Capital Deployment, Silvano Solis, Regional Director Mexico, Gary E. Anderson, Europe President and Chief Operating Officer, Masato Miki and Mike Yamada, Japan Co-Presidents and Ming Z. Mei, China President. Further, in North America, two individuals lead each of our six regions (Central, Midwest, Mexico, 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.

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 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.

ProLogis Operating System

Our management team is responsible for overseeing the ProLogis Operating System, the cornerstone of our business strategy, designed to achieve long-term sustainable growth in cash flow and a high level of return for our shareholders. The ProLogis Operating System is a proprietary property management and customer service delivery system that we designed to assist our professional management team in providing a unique and disciplined approach to serving existing and prospective customers. We believe that, through the ProLogis Operating System, we are, and will continue to be, well positioned to leverage our customer relationships to generate additional business opportunities.

Capital Management and Capital Deployment

Within the ProLogis Operating System, we have a team of professionals who are 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 focus on ensuring 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 the 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.

Customer Service

The Global Solutions Group provides services to a targeted customer base that has been identified as large users of distribution space. The Global Solutions Group s primary focus is to position us as the preferred provider of distribution space to these targeted customers. 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.

Senior Management

*Jeffrey H. Schwartz** 48 Chief Executive Officer since January 2005 and Chairman of the Board since May 2007. Mr. Schwartz was President of International Operations of ProLogis from March 2003 to December 2004 and he was Asia - President and Chief Operating Officer from March 2002 to December 2004. Mr. Schwartz was President and Chief Executive Officer of Vizional Technologies, Inc., previously an unconsolidated investee of ProLogis from September 2000 to February 2002. From October 1994 to August 2000, Mr. Schwartz was with ProLogis, most recently as Vice Chairman for International Operations. Prior to originally joining ProLogis in October 1994, Mr. Schwartz was a founder and managing partner of The Krauss/Schwartz Company, an industrial real estate developer in Florida. Mr. Schwartz was appointed to the Board in August 2004.

*Walter C. Rakowich** 50 President and Chief Operating Officer since January 2005 and Chief Financial Officer from December 1998 until September 2005. Mr. Rakowich was Managing Director from December 1998 to December 2004. 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 was appointed to the Board in August 2004. On February 7, 2008, we announced Mr. Rakowich s plan to retire effective

January 2, 2009.

*Ted R. Antenucci** 43 President and Chief Investment Officer since May 2007. Mr. Antenucci was President of Global Development from September 2005 to May 2007. Prior to joining ProLogis, Mr. Antenucci was President of Catellus Commercial Development Corp. from September 2001 to September 2005, with responsibility for all development, construction and acquisition activities. Prior thereto, Mr. Antenucci served as Executive Vice President of Catellus Commercial Group from April 1999 to September 2001, where he managed the company s industrial development activities throughout the western United States, including northern and southern California, Denver, Chicago, Dallas and Portland.

*Edward S. Nekritz** 42 General Counsel 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 varying capacities since September 1995. Prior to joining ProLogis, Mr. Nekritz was an attorney with Mayer, Brown & Platt (now Mayer Brown LLP).

*William E. Sullivan** 53 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. Between 2001 and 2005, Mr. Sullivan served as chairman and CEO of SiteStuff, an online procurement company serving the real estate industry. As CEO, he supervised an effective effort to reduce costs, increase revenue and bring the company to sustained profitability. He stepped out of the CEO role following successful completion of the corporate turnaround. He continued as Chairman until June 30, 2007, at which time the company was sold. Between 1984 and 2001, Mr. Sullivan held several positions with the real estate firm of Jones Lang LaSalle, including chief financial officer.

Gary E. Anderson 42 Europe - President and Chief Operating Officer since November 2006 where he is responsible for investments and development in the European countries in which ProLogis operates. From 2003 to 2006, Mr. Anderson was the Managing Director responsible for investments and development in the Central and Mexico Regions. Prior to 2003, Mr. Anderson was a Market Officer from 1996 to 2003.

John C. Cutts 48 Vice Chairman Europe. Mr. Cutts joined ProLogis in February 2007 following the acquisition of the industrial development business of Parkridge, a European real estate development company based in the United Kingdom, which Mr. Cutts co-founded in 1998. In addition to his role at ProLogis, Mr. Cutts remains chairman and chief executive officer of Parkridge Retail, which continues to focus on the development of retail and mixed-use business centers throughout Europe. ProLogis owns a 25 percent interest in Parkridge Retail.

Ming Z. Mei 35 China President since January 2007, where he is responsible for capital management and development activities in China. Mr. Mei was a Managing Director from December 2005 to January 2007, a Senior Vice President from December 2004 to December 2005 and a First Vice President from 2003 to December 2004 with similar responsibilities in China. Prior to joining ProLogis in March 2003, Mr. Mei was Director of Finance and Business Development for the Asia Pacific Region of Owens Corning, a global building materials manufacturing company.

Masato Miki 43 Japan Co-President since March 2006, where he is responsible for acquisitions, finance operations and investment management in Japan. Mr. Miki was Managing Director from December 2004 to March 2006 and Senior Vice President from January 2004 to December 2004 with similar responsibilities in Japan and he has been with ProLogis since August 2002. Prior to joining ProLogis, Mr. Miki was Vice President of Mitsui Fudosan Investment Advisors, Inc., an affiliate of Mitsui Fudosa Co., Ltd., a comprehensive real estate company in Japan.

John P. Morland 49 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 with Barclays Global Investors at its San Francisco headquarters from April 2000 to March 2005, where he was the Global Head of Compensation.

Mike Yamada 54 Japan Co-President since March 2006, where he is responsible for development and leasing activities in Japan. Mr. Yamada was Managing Director from December 2004 to March 2006 and Senior Vice President from January 2004 to December 2004 with similar responsibilities in Japan and he has been with ProLogis 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 acquired by us 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 17 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:

<u>General Real Estate Risks</u>

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 22.0% of our 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 3.5% of our total investment before depreciation in operating properties) in certain markets located in Atlanta, Chicago, Dallas/Fort Worth, New Jersey, Japan, Poland, the United Kingdom and Washington D.C./Baltimore, Maryland. 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 CDFS joint ventures in which we have an ownership interest have concentrations of properties in the same 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 included a more significant portion of other sectors of the real estate industry.

Our real estate development strategies may not be successful.

We have developed a significant number of distribution properties since our inception and intend to continue to pursue development activities as opportunities arise. In addition, we currently own approximately 9,351 acres of land or land use rights for potential future development of distribution properties and other commercial real estate projects. Such development activities generally require various government and other approvals and we may not receive such approvals. We will be subject to risks associated with such development activities including, but not limited to:

- 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 we may not be able to obtain land or land use rights on which to develop or 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 make the project profitable.

Our business strategy associated with contributing properties to property funds or disposing of properties to third parties may not be successful.

We have contributed to property funds, or sold to third parties, a significant number of distribution properties in recent years and we intend to continue to contribute and sell properties, particularly from our CDFS business segment, which is an integral part of our business strategy. 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. Our ability to develop and timely lease properties will impact our ability to contribute or sell these properties. The property funds are required to have access to debt and equity capital, in the private and public markets, in order for us to continue our strategy of contributing properties to them. Should we not have sufficient properties available that meet the investment criteria of current or future property funds, or should the property funds have limited or no access to capital on favorable terms, then these contributions could be delayed resulting in adverse effects on our liquidity and on our ability

Table of Contents

to meet projected earnings levels in a particular reporting period. Failure to meet our projected earnings levels in a particular reporting period could have an adverse effect on our results of operations, distributable cash flow and on the value of our securities. Further, our inability to redeploy the proceeds from our divestitures in accordance with our investment strategy could have an adverse effect on our results of operations, distributable cash flow, our ability to meet our debt obligations in a timely manner and the value of our securities in subsequent periods.

Our growth will depend on future acquisitions of distribution properties, which involves risks that could adversely affect our operating results and the value of our securities.

We acquire distribution properties in both our property operations and CDFS business segments. 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 31.7 million square feet of distribution and retail space (out of a total of 175.6 million occupied square feet or 18.1%) with leases that expire in 2008, including 1.8 million square feet of leases that are on a month-to-month basis. In addition, our unconsolidated investees have a combined 33.2 million square feet of distribution space (out of a total 239.8 million occupied square feet or 13.8%) with leases that expire in 2008, including 2.0 million square feet of leases that are on a month-to-month basis. The number of distribution 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.

The fact that real estate investments are not as liquid as other types of assets 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 must comply with the safe harbor rules relating to the number of properties that can be disposed of in a year, the tax basis and the costs of improvements made to these properties and meet other tests that enable a REIT to avoid punitive taxation on the sale of assets. Thus, our ability at any time to sell assets or contribute assets to property funds or other entities in which we have an ownership interest may be restricted.

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 Catellus Merger, 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 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.

Risks Related to Financing and Capital

Our operating results and financial condition could be adversely affected if we do not continue to have access to capital through the property funds.

As a REIT, we are required to distribute at least 90% of our taxable income to our shareholders. Consequently, we are, as are all REITs, largely dependent on external capital to fund our development and acquisition activities. We have been accessing debt and equity capital, in both the private and public markets, through the establishment of property funds that acquire our properties. Our ability to access capital through the property funds is dependent upon a number of factors, including general market conditions and competition from other real estate companies. Further, we generate significant profits because of the contributions of properties to the property funds. To the extent that capital is not available to the property funds to allow them to acquire our properties, these profits may not be realized or realization may be delayed, which could result in an earnings stream that is less predictable than some of our competitors and may result in us not meeting our projected earnings and distributable cash flow levels in a particular reporting period. Our ability to contribute or sell properties from our development pipeline and recognize profits from our development

Table of Contents

activities will be jeopardized and our ability to meet projected earnings levels and generate distributable cash flow would be adversely affected should the existing equity commitments to the property funds not be available (due to investor default or otherwise) such that these property funds cannot acquire the properties that we expect to have available for contribution. This impact would occur in the short-term and would continue until we are able to sell the properties to third parties or until we could secure another source of capital to finance the properties. Failure to meet our projected earnings and distributable cash flow levels in a particular reporting period could have an adverse effect on our financial condition and on the market price of our securities.

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 adversely affect our financial condition.

The terms of our various credit agreements and other indebtedness require us to comply with a number of customary financial and other covenants, such as maintaining debt service coverage and leverage ratios and 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 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.

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

Table of Contents

unrealized gains in our assets as of the date of requalification and to make distributions to our shareholders equal to any earnings accumulated during the period of non-REIT status.

Potential adverse effect of REIT distribution requirements could adversely affect our financial condition.

To maintain qualification as a REIT under the Code, 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. The 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. See Note 7 to our Consolidated Financial Statements in Item 8.

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 Catellus Merger, 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.

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 2007, we generated approximately 42% of our revenue from operations outside the United States. 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, political activism or the continuation or escalation of terrorist activities; and

foreign ownership restrictions with respect to operations in countries, such as China.

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, 2007, approximately 45% of our total assets are invested in a currency other than the U.S. dollar, primarily the euro, Japanese yen, British pound sterling and Chinese renminbi. 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 distribution properties. In Japan, our distribution 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 property operations segment at December 31, 2007, our properties are 99.4% distribution properties, including 92.5% of properties used for bulk distribution, 6.1% used for light manufacturing and assembly and 0.8% for other purposes, primarily service centers, while the remaining 0.6% of our properties are retail.

At December 31, 2007, we own 1,409 operating properties, including 1,378 distribution properties located in North America, Europe and Asia and 31 retail properties in North America. In North America, our properties are located in

32 markets in 20 states and the District of Columbia in the United States, five markets in Mexico and one market in Canada. Our properties are located in 20 markets in 11 countries in Europe and nine markets in three countries in Asia.

Table of Contents

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, 2007 for the operating properties, properties under development and land we own, including 94 buildings owned by entities we consolidate but of which we own less than 100%. All of the operating properties are included in our property operations segment, including CDFS properties pending contribution to a property fund. Properties under development and land are included in the CDFS business segment. 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, 2007. No individual property or group of properties operating as a single business unit generated income equal to 10% or more of our consolidated gross revenues or total income for the year ended December 31, 2007. The table does not include properties that are owned by property funds or other unconsolidated investees which are discussed under Unconsolidated Investees.

Table of Contents

	No. of Bldgs.	Percentage Leased (1)	Rentable Square Footage	Investment Before Depreciation	Encumbrances (2)
Operating properties owned in the property operations segment at December 31, 2007 (dollars and rentable square footage in thousands):					
Distribution properties:					
North America by Market (38 markets) (3):					
United States:					
Atlanta, Georgia	81	89.49%	12,194	$ 423,776	$ 30,520
Austin, Texas	14	97.39%	983	37,064	
Charlotte, North Carolina	32	92.81%	3,883	123,536	35,924
Chicago, Illinois	88	83.93%	18,958	974,568	166,424
Cincinnati, Ohio	21	99.84%	3,927	117,541	22,711
Columbus, Ohio	32	87.53%	6,909	254,059	31,991
Dallas/Fort Worth, Texas	106	91.16%	15,260	614,050	54,289
Denver, Colorado	30	99.22%	4,700	232,644	65,700
El Paso, Texas	16	86.88%	2,051	62,360	
Houston, Texas	76	97.83%	7,216	246,407	
I-81 Corridor, Pennsylvania	12	70.91%	4,592	224,508	
Indianapolis, Indiana	30	96.01%	3,155	111,285	
Las Vegas, Nevada	17	98.79%	2,061	95,836	10,807
Louisville, Kentucky	11	100.00%	2,775	91,577	17,549
Memphis, Tennessee	23	62.92%	5,025	141,450	
Nashville, Tennessee	28	93.76%	2,694	71,078	
New Jersey	39	95.07%	7,814	483,411	47,405
Orlando, Florida	20	97.35%	1,902	82,274	3,270
Phoenix, Arizona	33	99.19%	2,700	125,812	13,886
Portland, Oregon	29	98.21%	2,479	142,069	28,789
Reno, Nevada	18	79.20%	3,210	129,183	5,289
Salt Lake City, Utah	5	100.00%	853	32,461	
San Antonio, Texas	45	92.37%	4,017	144,092	3,554
San Francisco (Central Valley), California	13	69.69%	3,486	163,940	34,616
San Francisco (East Bay), California	57	97.48%	4,902	309,565	87,852
San Francisco (South Bay), California	84	93.03%	5,516	457,654	65,671
Seattle, Washington	9	100.00%	1,036	45,741	296
South Florida	14	88.34%	1,288	78,912	6,291
Southern California	98	95.91%	18,641	1,559,196	463,566
St. Louis, Missouri	6	86.04%	685	22,218	
Tampa, Florida	53	96.11%	3,777	158,580	8,921
Washington D.C./Baltimore, Maryland	44	91.11%	5,717	314,381	36,913

Other	2	100.00%	367	19,170	
Subtotal United States	1,186	90.57%	164,773	8,090,398	1,242,234
Mexico:					
Guadalajara	2	81.11%	580	30,863	
Juarez	6	41.86%	589	21,205	
Mexico City	14	62.43%	2,537	135,979	
Monterrey	7	72.92%	711	26,743	
Reynosa	1	100.00%	160	7,790	
Subtotal Mexico	30	65.09%	4,577	222,580	
Canada Toronto	3	92.81%	987	81,624	
Subtotal North America	1,219	89.90%	170,337	8,394,602	1,242,234
Europe by Country (20 markets) (4):					
Czech Republic	5	68.05%	1,615	109,944	
France	16	55.91%	4,396	271,197	
Germany	3	87.28%	959	69,490	
Hungary	6	76.14%	1,111	96,093	
Italy	6	20.40%	1,774	117,304	
Netherlands	1	100.00%	191	13,499	
Poland	34	86.26%	7,220	416,458	
Romania	2	67.74%	578	35,215	
Slovakia	5	82.95%	1,352	88,835	
Sweden	2	100.00%	407	40,850	
United Kingdom	20	30.66%	4,686	556,546	
Subtotal Europe	100	63.31%	24,289	1,815,431	
Asia by Country (9 markets) (4):					
China	50	66.97%	7,560	192,227	16,142
Japan	7	66.99%	4,900	566,525	
Korea	2	77.44%	211	31,294	6,410
Subtotal Asia	59	67.15%	12,671	790,046	22,552
Total distribution properties	**1,378**	**85.39%**	**207,297**	**11,000,079**	**1,264,786**
Retail properties:					
North America by Country (4 markets):					
United States	31	94.01%	1,233	328,420	26,200
Total retail properties	**31**	**94.01%**	**1,233**	**328,420**	**26,200**
Total operating properties owned in the property operations segment at	**1,409**	**85.45%**	**208,530**	**$ 11,328,499**	**$ 1,290,986**

December 31, 2007

Table of Contents

	Land Held for Development		Properties Under Development			
	Acreage	Investment	No. of Bldgs.	Rentable Square Footage	Current Investment	Total Expected Cost (5)
Land held for development and properties under development at December 31, 2007 (dollars and rentable square footage in thousands):						
North America – by Market (35 total markets):						
United States:						
Atlanta, Georgia	468	$ 35,711			$	$
Austin, Texas			2	113	1,004	8,048
Charlotte, North Carolina	29	4,478				
Chicago, Illinois	750	77,954	2	563	24,310	47,783
Cincinnati, Ohio	85	7,968	1	416	12,841	17,840
Columbus, Ohio	233	9,053				
Dallas / Fort Worth, Texas	360	30,522	3	1,363	16,394	48,884
El Paso, Texas	68	3,855				
Houston, Texas	128	10,149	3	415	15,410	22,817
I-81 Corridor, Pennsylvania	267	37,163	1	870	13,594	56,537
Indianapolis, Indiana	93	5,029				
Jacksonville, Florida	82	9,658				
Las Vegas, Nevada	68	33,821				
Louisville, Kentucky	13	2,887	1	484	12,252	19,128
Memphis, Tennessee	159	12,502				
Nashville, Tennessee	24	1,220	1	288	11,408	12,208
New Jersey	204	104,571	1	270	434	20,548
Phoenix, Arizona	148	24,917				
Portland, Oregon	27	5,679	1	246	11,816	16,125
Reno, Nevada	202	24,231				
Salt Lake City, Utah	7	128				
San Antonio, Texas	62	6,262				
San Francisco (Central Valley), California	287	41,251	1	780	24,431	42,834
Seattle, Washington			2	246	20,517	30,766
Southern California	527	178,514	8	2,472	168,466	230,384
South Florida	70	46,358	5	443	24,457	51,378
Tampa, Florida	43	5,928	1	117	6,422	8,163
Washington D.C./Baltimore, Maryland	139	23,889				
Mexico:						
Guadalajara	48	14,902	2	273	4,340	12,850

Juarez	173	22,712	4	385	14,876	21,012
Mexico City	133	40,629	2	592	26,300	33,543
Monterrey	159	26,543	2	509	13,607	25,238
Reynosa	108	8,596	5	707	15,405	32,964
Tijuana			3	692	31,957	44,497
Canada - Toronto	113	72,366	3	817	55,610	67,005
Subtotal North America	5,277	929,446	54	13,061	525,851	870,552
Europe by Country (35 total markets):						
Belgium	13	1,353	1	187	5,061	15,371
Czech Republic	140	48,687	5	1,458	65,458	120,416
France	247	42,494	10	2,976	81,541	215,163
Germany	88	38,711	14	3,949	125,668	297,643
Hungary	197	35,325	4	974	20,521	71,947
Italy	81	32,875	1	327	18,581	21,640
Netherlands			2	402	12,096	29,392
Poland	717	137,200	21	4,363	139,328	330,846
Romania	90	16,803	2	540	10,193	39,884
Slovakia	157	31,384	4	1,085	30,579	84,828
Spain	44	14,782	4	1,607	48,187	105,697
Sweden			2	352	4,988	34,576
United Kingdom	928	554,798	10	2,847	203,996	398,249
Subtotal Europe	2,702	954,412	80	21,067	766,197	1,765,652
Asia by Country (10 total markets):						
China	555	90,569	31	7,314	83,842	268,892
Japan	41	89,967	11	6,898	593,435	959,961
Korea	22	12,788	1	181	8,985	14,072
Subtotal Asia	618	193,324	43	14,393	686,262	1,242,925
Total distribution properties	**8,597**	**2,077,182**	**177**	**48,521**	**1,978,310**	**3,879,129**
Retail and mixed-use properties:						
North America by Country (6 markets):						
United States	754	75,778	3	308	7,975	56,073
Total retail and mixed-use properties	**754**	**75,778**	**3**	**308**	**7,975**	**56,073**
Total land held for development and properties under development in the CDFS business segment at December 31, 2007	**9,351**	**$ 2,152,960**	**180**	**48,829**	**$ 1,986,285**	**$ 3,935,202**

The following is a summary of our direct-owned investments in real estate assets at December 31, 2007:

		Investment Before Depreciation (in thousands)
Operating properties	$	11,328,499
Land subject to ground leases and other (6)		458,782
Properties under development		1,986,285
Land held for development		2,152,960
Other investments (7)		652,319
Total	**$**	**16,578,845**

(1) Represents the percentage leased at December 31, 2007. Operating properties at December 31, 2007 include recently completed development properties and recently acquired properties that may be in the initial lease-up phase, including 166 properties aggregating 39.9 million square feet that were completed or acquired in 2007. The inclusion of properties in the initial lease-up phase can reduce the overall leased percentage.

(2) Certain properties are pledged as security under our secured debt and assessment bonds at December 31, 2007. 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 $35.9 million of encumbrances related to other real estate assets not included in the property operations 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 90 properties aggregating 19.9 million square feet at a total investment of $996.4 million that were developed or acquired in the CDFS business segment and are pending contribution to a property fund or sale to a third party.

(4) All of the operating properties in Europe and Asia were developed or acquired in the CDFS business segment and are pending contribution to a property fund or sale to a third party.

(5) Represents the total expected cost at completion for properties under development, including 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, rather than actual costs incurred to date.

(6) Amounts represent investments of $414.7 million in land subject to ground leases, $7.9 million in office properties and an investment of $36.2 million in railway depots.

(7) 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; (v) cost of land use rights on operating properties in China; and (vi) costs related to our corporate office buildings.

Unconsolidated Investees

At December 31, 2007, our investments in and advances to unconsolidated investees totaled $2.3 billion. The property funds in the investment management segment totaled $1.8 billion, CDFS joint ventures operating in the CDFS business segment totaled $483.5 million and other unconsolidated investees totaled $106.7 million, all at December 31, 2007.

Table of Contents

Property Funds

At December 31, 2007, we had ownership interests ranging from 20% to 50% in 17 property funds that are presented under the equity method. The property funds primarily own operating properties and our investments in the property funds are included in our investment management segment. We act as manager of each property fund. The information provided in the table below (dollars and square footage in thousands) is for the total entity in which we have an ownership interest, not just our proportionate share. See Item 1. Business and Note 4 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:					
ProLogis California	80	1	14,178	99.90%	$ 694,591
ProLogis North American Properties Fund I	36	16	9,406	94.71%	383,242
ProLogis North American Properties Fund VI	22	7	8,648	94.70%	515,179
ProLogis North American Properties Fund VII	29	8	6,055	92.04%	390,147
ProLogis North American Properties Fund VIII	24	9	3,064	97.34%	192,651
ProLogis North American Properties Fund IX	20	7	3,439	81.80%	195,949
ProLogis North American Properties Fund X	29	9	4,191	96.36%	222,506
ProLogis North American Properties Fund XI	13	2	4,112	100.00%	217,718
ProLogis North American Industrial Fund	217	30	37,188	99.06%	2,104,929
ProLogis North American Industrial Fund II	153	31	36,106	95.77%	2,146,594
ProLogis North American Industrial Fund III (2)	122	6	24,719	92.33%	1,743,595
ProLogis Mexico Industrial Fund	32	5	4,154	100.00%	269,130
Total North America	777	38(3)	155,260	96.08%	9,076,231
Europe:					
ProLogis European Properties	247	27	56,379	97.33%	4,900,914
ProLogis European Properties Fund II	41	14	10,391	99.65%	1,463,877
Total Europe	288	27(3)	66,770	97.69%	6,364,791
Asia:					
ProLogis Japan Properties Fund I	16	3	7,118	97.87%	1,236,099
ProLogis Japan Properties Fund II	44	8	14,566	99.96%	2,391,078
ProLogis Korea Fund	6	1	436	100.00%	49,983

Total Asia	66	9(3)	22,120	99.29%		3,677,160
Total property funds	1,131	74	244,150	96.81%	$	19,118,182

(1) Investment represents 100% of the carrying value of the properties, before depreciation, of each entity at December 31, 2007.

(2) Amounts include seven properties with a total investment of $103.9 million that are held for sale by the property fund.

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

Table of Contents

CDFS joint ventures

At December 31, 2007, we had ownership interests in several entities that perform CDFS business activities and are presented under the equity method. These entities develop and invest in distribution properties and retail and mixed-use properties. On a combined basis, these entities own 39 completed distribution properties and have 14 distribution properties under development. In addition, these entities have 39 retail and mixed-use properties under development. The information provided in the table below (dollars in thousands) is for the total entity in which we have an ownership interest, not just our proportionate share, as of December 31, 2007.

	Effective Ownership Percentage	Total Assets	Third Party Debt
Industrial CDFS Joint Ventures:			
North America	46%	$ 96,761	$ 53,292
Europe	50%	7,022	
Asia	50%	273,077	
Total Industrial CDFS Joint Ventures		$ 376,860	$ 53,292

	Type of Real Estate	Effective Ownership Percentage	Total Assets	Third Party Debt
Non-Industrial CDFS Joint Ventures:				
North America	Mixed-use	50%	$ 49,615	$ 8,365
Europe	Retail and Mixed-use	25%	556,635	304,366
Asia	Retail	30%	738,065	510,230
Total Non-Industrial CDFS Joint Ventures			$ 1,344,315	$ 822,961

See Note 4 to our Consolidated Financial Statements in Item 8 for additional 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.

Table of Contents

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 Distribution
2006:			
First Quarter	$ 56.31	$ 46.29	$ 0.40
Second Quarter	53.85	46.66	0.40
Third Quarter	58.86	52.05	0.40
Fourth Quarter	65.81	56.07	0.40
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 (through February 22)	$ 64.00	$ 51.71	$ 0.5175

On February 22, 2008, we had approximately 258,202,700 common shares outstanding, which were held of record by approximately 9,000 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.

We announce the following year s projected annual common share distribution level after the Board performs its annual budget review and approves a common share distribution level, generally in December of each year. In December 2007, the Board announced an increase in the annual distribution level for 2008 from $1.84 to $2.07 per common share. The payment of common share distributions is subject to the discretion of the Board, is dependent on 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, 2007, 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

Table of Contents

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,	
	2007	**2006**
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 9 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 5 and 14 to our Consolidated Financial Statements in Item 8.

Other Shareholder Matters

Other Issuances of Common Shares

In 2007, we issued 128,000 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 2008 Proxy Statement for further information relative to our equity compensation plans.

Table of Contents

ITEM 6. Selected Financial Data

The following table sets forth selected financial data relating to our historical financial condition and results of operations for 2007 and the four preceding years. Certain amounts for the years prior to 2007 presented in the table below have been reclassified to conform to the 2007 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,				
	2007	2006	2005 (1)	2004	2003
Operating Data:					
Total revenues	$ 6,205	$ 2,446	$ 1,817	$ 1,838	$ 1,444
Total expenses	$ 5,069	$ 1,686	$ 1,393	$ 1,493	$ 1,120
Operating income	$ 1,136	$ 760	$ 424	$ 345	$ 324
Interest expense	$ 368	$ 294	$ 178	$ 153	$ 154
Earnings from continuing operations	$ 987	$ 713	$ 300	$ 216	$ 232
Discontinued operations (2)	$ 87	$ 162	$ 96	$ 17	$ 19
Net earnings	$ 1,074	$ 874	$ 396	$ 233	$ 251
Net earnings attributable to common shares	$ 1,049	$ 849	$ 371	$ 203	$ 212
Net earnings per share attributable to common shares Basic:					
Continuing operations	$ 3.74	$ 2.79	$ 1.35	$ 1.02	$ 1.08
Discontinued operations	0.34	0.66	0.47	0.09	0.10
Net earnings per share attributable to common shares Basic	$ 4.08	$ 3.45	$ 1.82	$ 1.11	$ 1.18
Net earnings per share attributable to common shares Diluted:					
Continuing operations	$ 3.61	$ 2.69	$ 1.31	$ 0.99	$ 1.06
Discontinued operations	0.33	0.63	0.45	0.09	0.10
Net earnings per share attributable to common shares Diluted	$ 3.94	$ 3.32	$ 1.76	$ 1.08	$ 1.16
Weighted average common shares outstanding:					
Basic	257	246	203	182	179
Diluted	267	257	214	192	187
Common Share Distributions:					
Common share cash distributions paid	$ 473	$ 393	$ 297	$ 266	$ 258
Common share distributions paid per share	$ 1.84	$ 1.60	$ 1.48	$ 1.46	$ 1.44
FFO (3):					
Reconciliation of net earnings to FFO:					
Net earnings attributable to common shares	$ 1,049	$ 849	$ 371	$ 203	$ 212
Total NAREIT defined adjustments	150	149	161	196	159
Total our defined adjustments	28	(53)	(2)	1	29
FFO attributable to common shares as defined by us	$ 1,227	$ 945	$ 530	$ 400	$ 400

Cash Flow Data:					
Net cash provided by operating activities	$ 1,225	$ 687	$ 488	$ 484	$ 367
Net cash used in investing activities	$ (4,053)	$ (2,069)	$ (2,223)	$ (620)	$ (115)
Net cash provided by (used in) financing activities	$ 2,742	$ 1,645	$ 1,713	$ 37	$ (31)

	As of December 31,				
	2007	**2006**	**2005 (1)**	**2004**	**2003**
Financial Position:					
Real estate owned, excluding land held for development, before depreciation	$ 14,426	$ 12,500	$ 10,830	$ 5,738	$ 5,343
Land held for development	$ 2,153	$ 1,397	$ 1,045	$ 596	$ 511
Investments in and advances to unconsolidated investees	$ 2,345	$ 1,300	$ 1,050	$ 909	$ 677
Total assets	$ 19,724	$ 15,904	$ 13,126	$ 7,098	$ 6,367
Total debt	$ 10,506	$ 8,387	$ 6,678	$ 3,414	$ 2,991
Total liabilities	$ 12,209	$ 9,453	$ 7,580	$ 3,929	$ 3,271
Minority interest	$ 79	$ 52	$ 58	$ 67	$ 37
Total shareholders equity	$ 7,436	$ 6,399	$ 5,488	$ 3,102	$ 3,059
Number of common shares outstanding	258	251	244	186	180

(1) On September 15, 2005, we completed the Catellus Merger with an aggregate purchase price of $5.3 billion. See Note 3 to our Consolidated Financial Statements in Item 8 for additional information.

(2) Discontinued operations include income attributable to assets disposed of and net gains recognized on the disposition of assets to third parties. See Note 8 to our Consolidated Financial Statements in Item 8 for additional information. Amounts are net of losses 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 .

Management s Overview

We are a self-administered and self-managed REIT that operates a global network of real estate properties, primarily industrial distribution properties. The primary business drivers continue to be the need for greater distribution network efficiency and the continued growth in global trade. Our focus on our customers expanding needs has enabled us to become the world s largest owner, manager and developer of industrial distribution properties.

Our business is organized into three reportable business segments: (i) property operations; (ii) investment management; and (iii) development or CDFS business. Our property operations segment represents the direct long-term ownership of distribution and retail properties. Our investment management segment represents the long-term investment management of property funds and the properties they own. Our CDFS business segment primarily encompasses our development or acquisition of real estate properties that are subsequently contributed to a property fund in which we have an ownership interest and act as manager, or sold to third parties.

We generate and seek to increase revenues, earnings, FFO and cash flows through our segments primarily as follows:

Property Operations Segment We earn rent from our customers, including reimbursements of certain operating costs, under long-term operating leases in the distribution and retail properties that we own directly. We expect to grow our revenue through the selective acquisition of properties and increases in rental rates and, to a limited extent, increases in occupancy rates in our existing properties. Our strategy is to achieve the increases in rental rates and occupancy primarily through continued focus on our customers global needs for distribution space on the three continents in which we operate and use of the ProLogis Operating System.

Investment Management Segment We recognize our proportionate share of the earnings or losses from our investments in unconsolidated property funds. Along with the income recognized under the equity method, we recognize fees and incentives earned for services performed on behalf of the property funds and interest earned on advances to the property funds. We earn fees for services provided to the property funds, such as property management, asset management, acquisition, financing, leasing and development fees. We may earn incentives based on the return provided to our fund partners. We expect growth in income recognized to come from newly created property funds, such as those discussed below, and growth in existing property funds. The growth in the existing property funds is expected to come primarily from additional properties the funds will acquire, generally from us, and increased rental revenues in the property funds due, in part, to the leasing and property management efforts we provide as manager of the properties.

CDFS Business Segment We recognize income primarily from the contributions of developed, rehabilitated and repositioned properties and acquired portfolios of properties to the property funds and from dispositions to third parties. In addition, we: (i) earn fees from our customers or other third parties for development activities that we perform on their behalf; (ii) recognize interest income on notes receivable related to asset dispositions or development; (iii) recognize net gains from the disposition of land parcels, including land subject to ground leases; and (iv) recognize our proportionate share of the earnings or losses generated by development joint ventures in which we have an investment. We expect growth in income in this segment to come primarily from the continued development of high-quality distribution and retail properties in our key markets in North America, Europe and Asia, resulting in the contribution to property funds or sale to third parties.

Summary of 2007

The fundamentals of our business continued to be strong in each of our business segments in 2007.

We increased our net operating income from our property operations segment to $737.3 million for the year ended December 31, 2007 from $648.4 million for the same period in 2006. The increase of 13.7% was primarily a result of us owning a larger operating portfolio during 2007 over 2006, as well as an increase in same store net operating income (as defined below) for these properties. Our direct-owned operating portfolio increased due to acquisitions and development of 356 operating properties and decreased due to contributions and dispositions of 420 properties, resulting in a direct-owned operating portfolio of 1,409 properties at December 31, 2007. The timing of our contributions impacts the net operating income recognized in this segment.

Our net operating income from the investment management segment was $199.2 million for the year ended December 31, 2007, compared to $305.0 million for 2006. In 2007, we recognized $38.2 million that represented our proportionate share of the gain recognized by ProLogis European Properties (PEPR) upon the sale of certain properties. In 2006, we recognized $168.3 million of earnings and incentive returns associated with PEPR s initial public offering (IPO) ($109.2 million) and the termination of three of the property funds in North America as further discussed below ($59.1 million). Excluding these items from 2007 and 2006, net operating income from this segment increased $24.3 million, or 17.8%, due primarily to the new property funds created in 2007 and 2006 and an increase in the number of properties managed by us on behalf of the property funds.

We increased our total operating portfolio of distribution and retail properties owned or managed, including direct-owned properties and properties owned by the property funds and CDFS joint ventures, to 459.5 million square feet at December 31, 2007 from 391.4 million square feet at December 31, 2006. This increase is primarily in the portfolio of properties owned by the property funds, which increased from 843 properties at December 31, 2006 to 1,131 properties at December 31, 2007 due to the formation of new property funds, contributions by us and acquisitions from third parties. Our stabilized leased percentage (as defined below) was 95.6% at December 31, 2007, compared with 95.3% at December 31, 2006. Our same store net operating income increased by 5.2% and our same store average occupancy increased by 2.9% for the year ended December 31, 2007 over the same period in 2006. In 2007, same store rental rates on new leases increased 8.0% over the previous rental rates on that space.

Net operating income of the CDFS business segment increased for the year ended December 31, 2007 to $789.9 million from $379.5 million for the same period in 2006. This increase of 108% was due primarily to increased levels of contributions brought about by increased development activity, the creation of two new property funds that acquired properties from us, as well as the acquisition of MPR and subsequent formation of a new fund that resulted in gains of $68.6 million in 2007 and is further discussed below. During the year ended December 31, 2007, we started development on projects with a total expected cost at completion of $3.9 billion and completed development projects with a total expected cost of $2.4 billion, most of which will be contributed to property funds in future periods. We believe our strong development and leasing activity, along with the access to capital through the property funds, will continue to support our contribution activity to the property funds.

Key Transactions in 2007

In February 2007, we purchased the industrial business and made a 25% investment in the retail business of Parkridge, a European real estate development company. The total purchase price was $1.3 billion and resulted in the addition of 6.3 million square feet of operating distribution properties and 1,139 acres of land for future development (see Note 3 to our Consolidated Financial Statements in Item 8).

During 2007, we issued $2.4 billion of convertible senior notes due 2037. In March 2007, we issued $1.25 billion with a coupon rate of 2.25% and in November, we issued $1.12 billion with a coupon rate of 1.875% (see Note 13 to our Consolidated Financial Statements in Item 8).

In 2007, we generated aggregate proceeds of $5.8 billion and recognized aggregate gains of $991.9 million from contributions and dispositions of properties, net of amounts deferred, as follows:

- We generated $2.5 billion of proceeds and $695.1 million of gains from the contributions of CDFS developed and repositioned properties and sales of land. This is net of the deferral of $189.7 million of gains related to our ongoing ownership in the property funds that acquired the properties.

- We contributed acquired CDFS property portfolios generating $2.5 billion of proceeds and $68.6 million of gains. This is net of the deferral of $53.7 million of gains related to our continuing ownership in the three property funds that acquired these portfolios of properties. We acquired these portfolios of properties in 2007 and 2006 with the intent to contribute them to a new or existing property fund at, or slightly above, our cost.

- We disposed of 80 CDFS and non-CDFS properties, as well as land subject to ground leases, to third parties, all of which are included in discontinued operations, generating proceeds of $426.8 million and $81.5 million of gains.

- We generated proceeds of $391.7 million and gains of $146.7 million from the contribution of 77 non-CDFS properties to the property funds, net of the deferral of $36.2 million of gains related to our ongoing ownership in the property funds that acquired the properties.

We repositioned one property fund, formed three new property funds and made the first acquisitions of properties in a property fund, as follows (see Note 4 to our Consolidated Financial Statements in Item 8 for additional information):

¡ On July 11, 2007, we completed the acquisition of 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 until August 27, 2007, when the lender converted certain of the bridge debt, used to finance the acquisition, into equity of a new property fund, ProLogis North American Industrial Fund II, in which we have a 36.9% equity interest.

Table of Contents

- We formed two new property funds, ProLogis European Properties II (PEPF II) and ProLogis Mexico Industrial Fund that will be the primary investment vehicles to acquire all of the properties we develop and stabilize in Europe and Mexico, respectively. We made contributions of properties to the new funds in 2007. ProLogis Korea Fund, which was formed in 2006 and will be the primary investment vehicle to acquire all the properties we develop and stabilize in South Korea, acquired six properties from a third party in 2007.
- In July 2007, we formed a new property fund, ProLogis North American Industrial Fund III, that completed the acquisition of $1.8 billion of distribution properties in North America from a third party.

During the year ended December 31, 2007, in addition to the Parkridge and MPR acquisitions, we acquired an aggregate 7.3 million square feet of operating properties with a total expected investment of $382.7 million. These properties were primarily acquired for future contribution to a property fund, although we may hold certain properties for long-term investment.

In 2007, we started development on projects with a total expected cost at completion of $3.9 billion and completed development projects with a total expected cost of $2.4 billion. We also acquired 4,482 acres of land (or land use rights) for future development for an aggregate purchase price of $1.3 billion, excluding the land acquired in the Parkridge acquisition.

We invested $152.1 million in the form of equity investments and advances in CDFS joint ventures operating in North America, Europe and Asia, excluding the investment in a joint venture through the Parkridge acquisition discussed above. These joint ventures primarily develop and operate distribution and retail properties. These joint ventures, including the Parkridge retail joint venture, started development on projects with a total expected cost of $223.8 million, representing our proportionate share, in 2007 since our initial investment.

Our Board approved an increase in our annual distribution in 2008 to $2.07 per common share, from $1.84 per common share, or an increase of 12.5%. The common share distribution is declared quarterly and may be adjusted at the discretion of the Board.

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 about the effect of matters that are inherently uncertain. Estimates are prepared using management s best judgment, after considering past and current economic conditions. 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.

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.

Table of Contents

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.

Impairment of Long-Lived Assets

We assess the carrying value of our long-lived assets whenever events or changes in circumstances indicate that the carrying amount of these assets may not be recoverable and, with respect to goodwill, at least annually applying a fair-value-based test. The determination of the fair value of long-lived assets, including goodwill, involves significant judgment. This judgment is based on our analysis and estimates of the future operating results and resulting cash flows of each long-lived asset. Our ability to accurately predict future operating results and cash flows affects the determination of fair value.

If there is a decline in the fair value of a long-lived asset or a history of the asset generating operating losses, we determine whether the operating losses associated with the asset will continue. Our assessment as to the nature of a decline in fair value is primarily based on estimates of future operating results, the resulting cash flows and our intent to either hold or dispose of the long-lived asset. If an investment is considered impaired, an impairment charge is recognized based on these analyses.

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 earnings, other than adjustments to income tax liabilities due to tax uncertainties acquired in a business combination, which are adjusted to goodwill. Effective January 1, 2007, we adopted Financial Accounting Standards Board (FASB) Interpretation No. 48, *Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109* (FIN 48), which changed our methodology for estimating potential liabilities for income tax related matters. 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.

Results of Operations

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

	December 31, 2007	2006	2005
Net earnings attributable to common shares (in millions)	$ 1,048.9	$ 849.0	$ 370.7
Net earnings per share attributable to common shares Basic	$ 4.08	$ 3.45	$ 1.82
Net earnings per share attributable to common shares Diluted	$ 3.94	$ 3.32	$ 1.76

The increase in net earnings in 2007 over 2006 is primarily due to increased gains on contributions of CDFS and non-CDFS properties to property funds, 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. The increase in gains on contributions was fueled by the creation of two new property funds who acquired properties from us in 2007 and the repositioning of one property fund with a new partner. The increase in net earnings attributable to common shares in 2006 over 2005 was due to increases in the earnings of each of our reportable business segments driven by the PEPR IPO, the liquidation of certain property funds, improved property operating performance, gains on dispositions of properties and the Catellus Merger.

Portfolio Information

In the discussion that follows, we present the results of operations by reportable business segment. See Note 18 to our Consolidated Financial Statements in Item 8 for further description of our segments. Our total operating portfolio of properties includes distribution and retail properties owned by us and distribution properties owned by the property funds and CDFS joint ventures. Our operating portfolio also includes properties that were developed or acquired in our CDFS business segment and are pending contribution to a property fund or disposition to a third party. The operating portfolio does not include properties under development or any other properties owned by the CDFS joint ventures, other than distribution properties, and was as follows (square feet in thousands):

	December 31,					
	2007		2006		2005	
Reportable Business Segment	Number of Properties	Square Feet	Number of Properties	Square Feet	Number of Properties	Square Feet
Property operations (1)	1,409	208,530	1,473	204,674	1,461	186,663
Investment management	1,131	244,150	843	181,273	752	159,769
CDFS business (2)	39	6,801	32	5,474	23	3,283
Totals	2,579	459,481	2,348	391,421	2,236	349,715

(1) Our operating portfolio includes properties that were developed or acquired in our CDFS business segment and are pending contribution to a property fund or disposition to a third party as follows (square feet in thousands):

	Number of Properties	Square Feet
2007	249	56,861
2006	205	49,792
2005	124	29,383

(2) Only includes distribution properties owned by the CDFS joint ventures. We include our wholly owned CDFS properties in the property operations segment (see above).

The stabilized operating properties owned by us, the property funds and the CDFS joint ventures were 95.6% leased at December 31, 2007, 95.3% leased at December 31, 2006 and 94.5% leased at December 31, 2005. The stabilized properties are those properties where the capital improvements, repositioning efforts, new management and new marketing programs for acquisitions or the marketing programs in the case of newly developed properties, have been completed and in effect for a sufficient period of time to achieve stabilization. A property generally enters the stabilized pool at the earlier of 12 months from acquisition or completion or when it becomes substantially occupied, which we generally define as 93.0%.

Same Store Analysis

We evaluate the operating performance of the operating properties included in each of our three reportable business segments 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, the property funds and the CDFS joint ventures, in the same store analysis. Accordingly, we define the same store portfolio of operating properties for each period as those properties that have been in operation throughout the full period in both the current and prior year. When a property is disposed of to a third party, it is removed from the population for all periods presented. The same store portfolio aggregated 332.1 million square feet at December 31, 2007.

Same store results were as follows:

Net operating income generated by the same store portfolio (defined for the same store analysis as rental income, excluding termination and renegotiation fees, less rental expenses) increased 5.2% in 2007 over 2006, due to a 5.5% increase in rental income, partially offset by a 6.5% increase in rental expenses. The increase in rental expenses was primarily driven by increases in property insurance and property taxes, which are largely recovered from our customers as rental recoveries included in rental income. For 2006, the net operating income of the same store portfolio increased by 3.1% over 2005. Rental income increased 3.3% in 2006 and rental expenses increased 4.2% in 2006, both over 2005.

Average occupancy in the same store portfolio increased 2.9% in 2007 over 2006. This compares with an increase of 2.6% in average occupancy in 2006 over 2005.

Within the same store portfolio rental rates on new leases in 2007 increased 8.0%, as compared with the previous rental rates in that same space. In 2006, the rental rates on new leases in the same store portfolio increased by 2.6%.

We believe the factors that impact net operating income, rental rates and average occupancy in the same store portfolio are the same as for the total portfolio. In order to derive an appropriate measure of period-to-period operating performance, the percentage change computation removes the effects of foreign currency exchange rate movements by computing each property s components in that property s functional currency.

Rental income computed under GAAP applicable to the properties included in the same store portfolio is adjusted to remove the net termination and renegotiation fees recognized in each period. Net termination and renegotiation fees excluded from rental income for the same store portfolio (including properties directly owned and properties owned by the property funds and CDFS joint ventures) were $2.9 million and $5.5 million for the year ended December 31, 2007 and 2006, respectively. 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. Removing the net termination fees from the same store calculation of rental income allows 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.

In computing the percentage change in rental expenses, the rental expenses applicable to the properties in the same store portfolio include property management expenses for our direct-owned properties. These expenses are based on the property management fee that is provided for in the individual agreements under which our wholly owned management company 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 direct costs of providing property management services are recognized as part of our rental expenses reported under GAAP.

Operational Outlook

Changes in economic conditions will generally affect customer leasing decisions and absorption of new distribution properties. Since late 2004, we have experienced strong customer demand and continued strengthening in occupancies across our global markets. Growth in global trade continues to support our market fundamentals, which in turn, support the leasing activity in our global development pipeline. During the year ended December 31, 2007, in our total operating portfolio, including properties owned by our unconsolidated investees and managed by us, we executed 108.6 million square feet of leases. This includes 32.9 million square feet of initial leasing activity in new developments and repositioned acquisitions, bringing our stabilized portfolio to 95.6% leased at December 31, 2007. We consider our stabilized portfolio to be substantially occupied and, therefore, do not expect our overall leased percentage to increase much above the current level. Market rental rates are increasing in many of our markets and we have experienced positive rental rate growth, in the aggregate, for the past seven quarters. As a result, we expect to continue to see increasing rents in most of our markets and we expect absorption of available space in our global development pipeline to continue to be healthy in 2008. An important fundamental to our long-term growth is repeat business with our global customers. Historically, approximately half of the space leased in our newly developed properties is with repeat customers (54% for 2007).

Property Operations Segment

The net operating income of the property operations segment consists of rental income and rental expenses from the distribution and retail operating properties that we own directly. The costs of our property management function for both our direct-owned portfolio and the properties owned by the property funds are all reported in rental expenses in the property operations segment. The rental income and expenses of operating properties that we developed or acquired in the CDFS business segment are included in the property operations segment during the interim period from the date of completion or acquisition through the date the properties are contributed or sold. See Note 18 to our Consolidated Financial Statements in Item 8 for a reconciliation of net operating income to earnings before minority interest. The net operating income from the property operations segment, excluding amounts presented as discontinued operations in our Consolidated Financial Statements, was as follows (in thousands):

	Years Ended December 31, 2007	2006	2005
Rental income	$ 1,023,640	$ 873,393	$ 574,588
Rental expenses	286,352	224,947	160,041
Total net operating income property operations segment	$ 737,288	$ 648,446	$ 414,547

The number and composition of operating properties that we own throughout the periods and the timing of contributions impact rental income and rental expenses for each period. As discussed earlier, on July 11, 2007, we completed the acquisition of MPR, which resulted in us consolidating the operating results until August 27, 2007, at which point the lender converted certain of the bridge debt into equity in ProLogis North American Industrial Fund II, thereby reducing our ownership to 36.9% of the equity of the property fund. At this time, we no longer controlled the property fund and began to account for our investment under the equity method of accounting in our investment management segment. The property operations segment includes the rental income and expenses of those properties, during the time we owned them in our direct owned portfolio. 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.

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 MPR acquisition and the timing of contributions, as well as increases in the net operating income of the same store properties we own directly. The increases in rental income and rental expenses in 2006 over 2005 are due primarily to the increase in properties owned resulting from the Catellus Merger in the third quarter of 2005 and other acquisitions and increases in the net operating income of the same store properties we directly own. Under the terms of our lease agreements, some or all of our rental expenses are recovered from customers. These rental expense recoveries of $217.8 million, $180.0 million and $112.5 million for the years ended December 31, 2007, 2006 and 2005, respectively, are included in rental income and offset some of the increases in rental expenses. The increase in the number of properties under management has also contributed to the increase in rental expenses.

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 the property funds; (ii) fees and incentives earned for services performed on behalf of the property funds; and (iii) interest earned on advances to the property funds, if any. The net earnings or losses of the property funds may include the following income and expense items of the property funds, 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; and (vi) gains on dispositions of properties. 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 property funds; (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 are reported in the property operations segment and the costs of the investment management function are included in our general and administrative expenses. See Notes 4 and 18 to our Consolidated Financial Statements in Item 8 for additional information on the property funds and for a reconciliation of net operating income to earnings before minority interest.

Table of Contents

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

	Years Ended December 31, 2007	2006	2005
ProLogis North American property funds (1)	$ 64,325	$ 117,532	$ 56,348
ProLogis European property funds (2)	104,665	167,227	44,002
ProLogis Asian property funds (3)	30,182	20,225	12,662
Total net operating income investment management segment	$ 199,172	$ 304,984	$ 113,012

(1) Represents the income earned by us from our investments in property funds in North America. We had interests in 12, 10 and 12 funds at December 31, 2007, 2006 and 2005, respectively. This includes two new property funds and one repositioned property fund in 2007. One property fund, ProLogis Mexico Industrial Fund, acquired 35 properties from us in 2007 while the other new property fund acquired 122 properties from a third party concurrent with its formation. Our ownership interests ranged from 20.0% to 50.0% at December 31, 2007. These property funds on a combined basis owned 777, 535 and 471 properties at December 31, 2007, 2006 and 2005, respectively. Beginning in August 2007, we own 36.9% of a property fund that owns 100% of the real estate assets previously owned by ProLogis North American Properties Fund V.

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 2007, represents the income earned by us from our investments in two property funds in Europe, PEPR and PEPF II and prior to 2007 represents the income from our investment in PEPR. PEPF II was formed in the third quarter of 2007 and made acquisitions of 38 properties from us in 2007. On a combined basis, these funds owned 288 properties at December 31, 2007. Our ownership interest in PEPR and PEPF II was 24.9% and 24.3%, respectively at December 31, 2007. Our ownership interest in PEPF II is due to our direct ownership interest of 16.85% and our indirect 7.45% interest through our ownership in PEPR, which owns a 30% interest in PEPF II. In July 2007, PEPR sold a portfolio of 47 properties that resulted in our recognition of additional earnings of $38.2 million, representing our proportionate share of the gain recognized by PEPR.

Our ownership interest in PEPR was 24.0% and 21.0% at December 31, 2006 and 2005, respectively. In connection with PEPR s IPO in 2006, we recognized $109.2 million in incentive return based fees on the internal rate of return that the pre-IPO unit holders earned. During 2006, PEPR incurred professional fees and other expenses related to the completion of its IPO, which resulted in a decrease of approximately $8.9 million in the earnings we recognized. PEPR owned 277 and 263 properties at December 31, 2006 and 2005, respectively.

(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, which made its first acquisition of properties from third parties during 2007. These property funds on a combined basis owned 66, 31 and 18 properties at December 31, 2007, 2006 and 2005, respectively, including a portfolio of 17 properties in Japan that were purchased from a third party during

the third quarter of 2007.

CDFS Business Segment

Net operating income from the CDFS business segment consists 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; (iii) fees earned for development services provided to customers and third parties; (iv) interest income earned on notes receivable related to property dispositions or development; (v) our proportionate share of the earnings or losses of CDFS joint ventures; and (vi) certain costs associated with the potential acquisition of CDFS business assets and land holding costs. See Note 18 to our Consolidated Financial Statements in Item 8 for a reconciliation of net operating income to earnings before minority interest.

For 2007, our net operating income in this segment, excluding amounts presented as discontinued operations in our Consolidated Financial Statements, was $789.9 million, as compared to $379.5 million in 2006, an increase of $410.4 million or 108%. The increased net operating income in this segment 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, 32.6% of the net operating income of this operating segment was generated in North America, 36.0% was generated in Europe and 31.4% was generated in Asia.

For 2006, our net operating income in this segment, excluding amounts presented as discontinued operations in our Consolidated Financial Statements, was $379.5 million, as compared to $252.6 million in 2005, an increase of $126.9 million or 50.2%. The increased net operating income in this segment in 2006 over 2005 was primarily due to increased levels of dispositions brought about by increased development activity, increased earnings from CDFS joint ventures, development fees and interest income. In 2006, 46.5% of the net operating income of this operating segment was generated in North America, 28.5% was generated in Europe and 25.0% was generated in Asia.

We attribute the strong performance in 2007 to increased development activity and improved leasing activity for CDFS business properties, as well as our ability to create new property funds to acquire our properties. We believe the economic conditions in 2007 positively affected our customers decisions with respect to changes in their distribution networks. Increased demand is driven by the need for distribution efficiencies and on-going growth in global trade. Our geographically diverse portfolio helps to mitigate the impact of slowing economies in any one area in which we operate. There can be no assurance we will be able to maintain or increase the current level of net operating income in this segment. See Item 1A. Risk Factors for factors that may affect our performance in this business segment.

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

	Years Ended December 31,		
	2007	**2006**	**2005**
CDFS transactions in continuing operations:			
Disposition proceeds, prior to deferral (1)	$ 5,230,788	$ 1,337,278	$ 1,190,264
Proceeds deferred and not recognized (2)	(243,411)	(65,542)	(52,770)
Recognition of previously deferred amounts (2)	18,035	15,105	2,963
Cost of dispositions (1)	(4,241,700)	(993,926)	(917,782)
Net gains	763,712	292,915	222,675
Development management and other income (3)	26,670	37,420	25,464
Interest income on notes receivable (4)	8,066	16,730	6,781
Net earnings from CDFS joint ventures (5)	3,371	44,974	5,671
Other expenses and charges (6)	(11,905)	(12,554)	(7,983)
Total net operating income - CDFS business segment	$ 789,914	$ 379,485	$ 252,608

CDFS transactions recognized as discontinued operations (7):

Disposition proceeds	$	205,775	$	245,500	$	100,494
Cost of dispositions		(177,054)		(211,986)		(89,878)
Net CDFS gains in discontinued operations	$	28,721	$	33,514	$	10,616

(1) During 2007, we contributed 87 developed and repositioned properties to the property funds (41 in North America, 41 in Europe and five in Japan) and we contributed 175 properties that were acquired

property portfolios to the property funds, including the MPR acquisition (162 in North America and 13 in Europe). This compares with 2006 when we contributed 55 developed and repositioned properties (30 in North America, 19 in Europe and six in Japan) and 2005 when we contributed 42 developed and repositioned properties (20 in North America, 19 in Europe and three in Japan). In addition, we recognized net gains of $93.3 million, $24.6 million and $14.5 million from the disposition of land parcels to third parties during 2007, 2006 and 2005, 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 .

(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 proceeds 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 proceeds by recognizing a reduction to our investment in the applicable unconsolidated investee. We adjust our proportionate share of the earnings or losses that we recognize under the equity method in later periods to reflect the entity s depreciation expense as if the depreciation expense was computed on our lower basis in the contributed property rather than on the entity s basis in the contributed property. 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 to a third party, we recognize a gain during the period that the disposition occurs related to the proceeds we had previously deferred, in addition to our proportionate share of the gain or loss recognized by the entity. Further, during periods when our ownership interest in a property fund decreases, we recognize gains to the extent that proceeds 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) Amounts represent interest income earned on notes receivable related to previous property sales that were primarily acquired through the Catellus Merger, most of which have been substantially repaid as of December 31, 2007.

(5) Represents the net earnings or losses we recognize under the equity method from our investments in CDFS joint ventures. Included in the earnings for 2006 was $35.0 million, representing our proportionate share of the earnings of a CDFS joint venture, LAAFB JV that redeveloped and sold land parcels. As our investment in LAAFB JV is held in a taxable subsidiary, we also recognized $27.0 million of current income tax expense and a deferred tax benefit of $12.4 million (see further discussion in Income Taxes below). This entity substantially completed its operations at the end of 2006.

(6) Includes land holding costs and charges for previously capitalized costs related to potential CDFS business segment projects when the acquisition is no longer probable.

(7) Includes five CDFS business properties aggregating 0.6 million square feet, 15 CDFS business properties aggregating 1.9 million square feet and eight CDFS business properties aggregating 1.1 million square feet that were sold to third parties during 2007, 2006 and 2005, respectively, that met the criteria to be presented as discontinued operations.

The level and timing of income generated from the CDFS business segment is dependent on several factors, including but not limited to: (i) our ability to develop and timely lease properties; (ii) our ability to acquire properties that eventually can be contributed to property funds after rehabilitating or repositioning; (iii) our ability to identify and secure sites for redevelopment; (iv) our ability to generate a profit from these activities; and (v) our success in raising capital to be used by the property funds to acquire the properties we have to contribute. The margins earned in this segment may vary quarter to quarter depending on a number of factors, including the type of property contributed, the market in which the land parcel and property are located, and other market conditions. There can be no assurance we will be able to maintain or increase the current level of net operating income in this segment. Overall, we believe that the continued demand for state-of-the-art distribution properties resulted in positive leasing activity in 2007 in our global development pipeline, which helps support our CDFS business segment. We continue to monitor leasing activity and general economic conditions as it pertains to the CDFS business segment.

In North America, in 2007, we acquired 2,193 acres of land for future potential development in Canada, Mexico and the United States. We created a property fund that acquired certain properties that we had developed or acquired in Mexico. We have one property fund that is committed to acquire all the properties we develop and stabilize in the United States and Canada (as discussed below).

In Europe, during 2007, we acquired 2,619 acres of land for future potential development. This included 1,139 acres of land that was acquired as part of the Parkridge acquisition as discussed above. We formed a new property fund in Europe that acquired certain operating properties that we had developed and a portfolio of properties we acquired in the Parkridge acquisition. This property fund is committed to acquire all the properties we develop and stabilize in Europe (as discussed below).

In Asia, during 2006, we established a property fund that will acquire the properties we develop and stabilize in South Korea. In Japan, we have one property fund that will acquire properties we develop and stabilize in Japan (as discussed below). In China, we are positioning ourselves to meet what we believe will be significant future demand for distribution space due to the expected growth in manufacturing and consumer demand for goods and we have increased our direct-owned development and our investments in CDFS joint ventures operating in China. Also, we have begun to evaluate potential development opportunities in India and the Middle East. In Asia, we acquired 810 acres of land or land use rights for future development activity.

Other Components of Operating Income

General and Administrative Expenses

General and administrative expenses were $204.6 million in 2007, $153.5 million in 2006 and $118.2 million in 2005. The increases in general and administrative expenses are due primarily to our continued investment in the infrastructure necessary to support our business growth and continued expansion into new and existing international markets, the increase in our investment management business, our growing portfolio of properties through acquisitions and development and the growth in our CDFS business segment. This increase in infrastructure includes additional headcount and a higher level of performance-based compensation. Strengthening foreign currencies account for a portion of the increase when our international operations are translated into U.S. dollars at consolidation. Also in 2007, we recognized $8.0 million of employee departure costs, including $5.0 million related to the departure of our Chief Financial Officer in March 2007 and $3.0 million related to employees whose responsibilities became redundant after the acquisition of Parkridge. In each of 2007 and 2006, we recognized $5.0 million of expense related to a contribution to our charitable foundation. Included in 2006 and 2005 are merger integration costs of $2.6 million and $12.2 million, respectively. These costs are indirect costs associated with the Catellus Merger, such as employee transition costs as well as severance costs for certain of our employees whose responsibilities became redundant after the merger.

Depreciation and Amortization

Depreciation and amortization expenses were $309.0 million in 2007, $286.8 million in 2006 and $186.6 million in 2005. The increases in all periods is due to acquired real estate assets and intangible lease assets, improvements made to the properties in our property operations segment and increased leasing activity. The increase in 2006 over 2005 is also due to the depreciable assets acquired through the Catellus Merger.

Other Expenses

During 2007, we recognized an impairment charge of $12.6 million related to certain properties held and used in our property operations segment.

Interest Expense

Interest expense was $368.1 million in 2007, $294.4 million in 2006 and $177.6 million in 2005. The increases in interest expense in all periods as compared with the prior year are due to increases in our borrowings, resulting from individual and portfolio acquisitions, including the MPR and Parkridge acquisitions in 2007 and the Catellus Merger in 2005, increased development activity and our increased investments in property funds and CDFS joint ventures, offset somewhat by a decrease in our overall weighted average interest rates and additional capitalized interest. The decrease in our weighted average interest rates is due to our issuance of debt at lower interest rates, including the $2.4 billion of convertible senior notes issued in 2007 ($1.25 billion issued in March 2007 with a coupon rate of 2.25% and $1.12 billion issued in November 2007 with a coupon rate of 1.875%). The increase in capitalized interest for all periods when compared to the prior year is due to our increased development activities. See Note 13 to our Consolidated Financial Statements in Item 8 for additional information on our interest expense and debt and Note 2 for potential changes in accounting that may impact our reported interest expense.

Gains Recognized on Dispositions of Certain Non-CDFS Business Assets

In 2007 and 2006, we recognized gains of $146.7 million and $81.5 million on the disposition of 77 properties and 39 properties, respectively, from our property operations 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, 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 can 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 shareholders equity. 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. Additionally, we may utilize derivative financial instruments to manage certain foreign currency exchange risks, including put option contracts with notional amounts corresponding to a portion of our projected net operating income from our operations in Europe and Japan and forward contracts designed to manage foreign currency fluctuations of certain intercompany loans. See Note 16 to our Consolidated Financial Statements in Item 8 for more information on our derivative financial instruments.

We recognized net foreign currency exchange gains of $7.9 million, $21.1 million and $16.0 million during 2007, 2006 and 2005, respectively. These primarily relate to our third party and intercompany debt transactions and related derivative contracts. Also included in our 2007 foreign currency exchange gains are 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. As contracts used to manage the foreign currency fluctuations of an anticipated business combination do not qualify for hedge accounting treatment, the settlement of these contracts in 2007 resulted in net gains of $26.6 million recognized in earnings.

Income Taxes

During, 2007, 2006 and 2005, our current income tax expense was $68.3 million $84.3 million and $14.8 million, respectively. We recognize current income tax expense for income taxes incurred by our taxable REIT subsidiaries and in certain foreign jurisdictions, primarily related to our CDFS business, 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.

During 2007, we recognized a deferred tax expense of $0.6 million, compared with a deferred tax benefit of $53.7 million in 2006 and deferred tax expense of $12.0 million in 2005. The deferred tax expense in 2007 relates primarily to a tax indemnification agreement we entered into in 2007 in connection with the formation of PEPF II and the indemnification agreement we entered into with PEPR in connection with its IPO in 2006 related to the contribution of certain properties, all of which were contributed in 2007. These charges were partially offset with the benefit we recognized from the termination of the indemnification previously provided to ProLogis North American Properties Fund V and other deferred tax benefits due primarily to timing.

The deferred tax benefit recognized in 2006 was caused primarily by the reversal of deferred tax liabilities recorded in connection with our investments in CDFS joint ventures 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. The deferred tax expense in 2005 related primarily to the indemnification agreements related to property contributions to PEPR and ProLogis North American Properties Fund V. The current tax indemnification agreements are discussed in more detail in Note 7 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.

During 2007, 2006 and 2005, we disposed of 80, 89 and 72 CDFS and non-CDFS properties, respectively, as well as land subject to ground leases, to third parties. The results of operations for these properties, as well as the gain recognized upon disposition, are included in discontinued operations. As of December 31, 2007 and 2006, we had 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.

In 2005, we sold our temperature-controlled distribution assets in France, which resulted in the recognition of $25.2 million of losses in discontinued operations in 2005.

See Note 8 to our Consolidated Financial Statements in Item 8 for further discussion of discontinued operations.

Environmental Matters

For a discussion of environmental matters, see Note 17 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.

Our credit facilities provide liquidity and financial flexibility, which allows us to efficiently respond to market opportunities and execute our business strategy on a global basis. Regular repayments of our credit facilities are necessary to allow us to maintain adequate liquidity. We anticipate future repayments of the borrowings under our credit facilities will be funded primarily through cash flow from operations, the proceeds from future property contributions and dispositions and from proceeds generated by future issuances of debt or equity securities, depending on market conditions.

We continually assess our capital structure and look for ways to reduce our interest expense while financing our growing operations. As part of this assessment, we access the capital markets through the issuance of debt or equity securities at such time as we believe the market conditions to be favorable to do so.

This may include refinancing of maturing indebtedness, including borrowings on credit facilities that were used to fund acquisitions and development. Due to the recent turmoil in the credit markets, we may not be able to finance maturing debt on terms that are as favorable as the terms on the maturing debt. As a part of our CDFS business strategy, we are able to fund much of our on-going development and acquisition costs with the proceeds from the contribution and or disposition of properties. This strategy makes us less dependent on accessing the capital markets, although the property funds that primarily acquire our properties may also be affected by the current condition of the credit markets. In 2008, we have scheduled principle payments of $964 million of debt, including maturing debt. We expect to repay these amounts with the issuance of unsecured debt under our current indenture or with borrowings under our existing credit facilities as discussed below.

Our credit facilities provide aggregate borrowing capacity of $3.7 billion at December 31, 2007. This includes our Global Line, where a syndicate of 38 banks allows us to draw funds in U.S. dollar, euro, Japanese yen, British pound sterling, Chinese renminbi, South Korean won and Canadian dollar. The total commitment under the Global Line fluctuates in U.S. dollars based on the underlying currencies. Based on our public debt ratings, interest on the borrowings under the Global Line primarily accrues at a variable rate based upon the interbank offered rate in each respective jurisdiction in which the borrowings are outstanding. The majority of the Global Line matures in October 2009, however, it contains provisions for an extension, at our option subject to certain conditions, to October 2010. The renminbi tranche accrues interest based upon the People s Bank of China rate and matures in May 2009. As of December 31, 2007, under these facilities, we had outstanding borrowings of $2.0 billion and $148.2 million of letters of credit outstanding with participating lenders resulting in remaining borrowing capacity of $1.6 billion.

In February 2007 in connection with the Parkridge acquisition, as discussed earlier, we entered into a new multi-currency senior credit facility. The total commitment under this facility fluctuates in U.S. dollars based on the underlying currencies and the funds may be drawn in U.S. dollar, euro, Japanese yen and British pound sterling. Borrowings under this facility bear interest at a variable rate based upon the interbank offered rate in each respective jurisdiction in which the borrowings are outstanding, plus a margin, and the facility matures in October 2009. This debt can be repaid at our option prior to maturity. The facility provides us the ability to re-borrow, within a specified period of time, any amounts repaid on the facility. As of December 31, 2007, the outstanding balance was $626.6 million and is included in senior notes and other unsecured debt and we had no available capacity to borrow additional funds under this facility.

During 2007 we issued $2.4 billion of convertible senior notes. In March, we issued $1.25 billion with a coupon rate of 2.25% due in March 2037 and in November we issued $1.12 billion with a coupon rate of 1.875% due in November 2037. The proceeds of these issuances were used to pay down borrowings under our lines of credit and other debt and for general corporate purposes. The convertible notes are senior unsecured obligations of ProLogis and are convertible, under certain circumstances, for cash, our common shares or a combination of cash and our common shares, at our option, at a specified conversion price. The initial conversion price represents a premium of 20% over the closing price of our common shares at the date of first sale. The notes are redeemable at our option after five years for the principal amount plus accrued and unpaid interest and at any time prior to maturity to the extent necessary to preserve our status as a REIT. Holders of the notes have the right to require us to repurchase their notes every five years beginning after the first five years and at any time prior to their maturity upon certain limited circumstances.

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 2008 and future years:

- development of properties directly and additional investment in joint ventures in the CDFS business segment;
- acquisitions of properties or portfolios of properties in the CDFS business segment primarily for future contribution to property funds;

acquisitions of land for future development in the CDFS business segment;

investments in current or future unconsolidated property funds;

direct acquisitions of operating properties and/or portfolios of operating properties in key distribution markets for direct, long-term investment in the property operations segment;

capital expenditures on properties; and

scheduled principal payments, including $964 million that is due in 2008.

We expect to fund cash needs for 2008 and future years primarily with cash from the following sources, all subject to market conditions:

property operations;

fees and incentives earned for services performed on behalf of the property funds;

proceeds from the contributions of properties to current or future property funds;

proceeds from the disposition of land parcels and properties to third parties;

borrowing capacity under our Global Line or other credit facilities ($1.6 billion available as of December 31, 2007);

assumption of debt in connection with acquisitions; and

proceeds from the issuance of equity or debt securities, including sales under various common share plans, all subject to market conditions.

Commitments related to future contributions to Property Funds

We are committed to offer to contribute substantially all of the properties we develop and stabilize in Canada and the United States to the North American Industrial Fund. The North American Industrial Fund has equity commitments, which expire in February 2009, aggregating approximately $1.4 billion from third party investors, of which $729.7 million was unfunded at December 31, 2007. In addition, we are committed to make additional capital contributions in cash of $25.5 million through February 2009 as the fund acquires assets, primarily from us. This capital contribution represents our three percent ownership interest in the North American Industrial Fund that we acquired in July 2007 as part of the MPR acquisition.

We are committed to offer to contribute all of the properties we develop and stabilize in Mexico and, in certain circumstances properties we acquire, to ProLogis Mexico Industrial Fund. ProLogis Mexico Industrial Fund has equity commitments, which expire in August 2010, aggregating approximately $500.0 million from third party investors, of which $411.5 million was unfunded at December 31, 2007.

We are committed to offer to contribute substantially all of the properties we develop and stabilize in Europe and, in certain circumstances properties we acquire, to PEPF II. PEPF II has equity commitments, which expire in August 2010, aggregating approximately 2.5 billion ($3.6 billion as of December 31, 2007) from third party investors and PEPR, of which 2.1 billion ($3.1 billion as of December 31, 2007) was unfunded at December 31, 2007.

We are committed to offer to contribute all of the properties we develop and stabilize in Japan to ProLogis Japan Properties Fund II through September 2010. ProLogis Japan Properties Fund II has an equity commitment of

$600.0 million from our fund partner, which expires in August 2008, and under which $28.2 million was unfunded at December 31, 2007. In February 2008, ProLogis Japan Properties Fund II received an additional equity commitment of $400.0 million from our fund partner that expires in September 2010.

We are committed to offer to contribute substantially all of the properties we develop and stabilize in South Korea and, in certain circumstances properties we acquire, to ProLogis Korea Fund. ProLogis Korea Fund has an equity commitment from our fund partner of $200.0 million, which expires in June 2010, and under which $179.4 million was unfunded at December 31, 2007.

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 believe that, while the current capital commitments and borrowing capacities of these property funds may be expended prior to the expiration dates of these commitments, each property fund will have sufficient debt and/or equity capital to acquire the properties that we expect to offer to contribute during 2008, however, there can be no certainty until the contributions are completed. Should the property funds not acquire, because of insufficient capital available to acquire a property that meets the specified criteria or other reason, the rights under the agreement with regard to that specific property will terminate. We continually explore our options related to both new and existing property funds to support the business objectives of our CDFS business segment.

There can be no assurance that if these property funds do not acquire the properties we have available, we will be able to secure other sources of capital such that we can contribute or sell these properties in a timely manner and continue to generate profits from our development activities in a particular reporting period.

In addition, to the extent a property fund acquires properties from a third party, we may be required to contribute our proportionate share of the equity component in cash to the property fund.

Cash Provided by Operating Activities

Net cash provided by operating activities was $1.2 billion for 2007, $687.3 million for 2006, and $488.1 million for 2005. 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 2007, 2006 and 2005, investing activities used net cash of $4.1 billion, $2.1 billion and $2.2 billion, respectively. The following are the more significant activities for all periods presented:

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.

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. In 2006, we invested cash of $113.0 million in the form of a loan. See Note 3 to our Consolidated Financial Statements in Item 8 for more details of this transaction.

We invested $5.3 billion in real estate during the year ended December 31, 2007, excluding the MPR and Parkridge acquisitions; $3.8 billion for the same period in 2006, excluding the purchase of ownership interests in property funds; and $2.5 billion for the same period in 2005, excluding the Catellus Merger. These amounts include the acquisition of operating properties (41 properties, 74 properties and 25 properties with an aggregate purchase price of $351.6 million, $735.4 million and $453.9 million in 2007, 2006 and 2005, 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, 2007, we had 180 distribution and retail properties aggregating 48.8 million square feet under development, with a total expected investment of $3.9 billion.

We invested cash of $661.8 million, $217.9 million and $16.7 million in 2007, 2006 and 2005, respectively, in new and existing unconsolidated investees. The 2007 investments include the

$100.0 million invested in ProLogis North American Industrial Fund II, our proportionate share of the equity component for third-party acquisitions made by the property funds and investments and advances to CDFS joint ventures, excluding the initial investment in the Parkridge retail business. The 2006 investments were primarily in the North American Industrial Fund and CDFS joint ventures in China, including amounts escrowed for potential investments that are subject to the attainment of certain performance criteria. In January 2006, we invested $55.0 million in a preferred interest in ProLogis North American Properties Fund V, which we subsequently sold in August 2006.

We generated net cash from contributions and dispositions of properties and land parcels of $3.6 billion, $2.1 billion and $1.5 billion in 2007, 2006 and 2005, respectively. See further discussion in - Results of Operations-CDFS Business Segment .

We received proceeds from unconsolidated investees as a return of investment of $50.2 million, $146.2 million and $48.7 million in 2007, 2006 and 2005, respectively. The proceeds in 2007 include $18.7 million received from the liquidation of an investment in an unconsolidated investee and the proceeds in 2006 include $42.0 million from LAAFB JV and $55.0 million related to the sale of a preferred interest in ProLogis North American Properties Fund V discussed above.

We invested cash of $259.2 million in connection with the purchase of our fund partner s ownership interests in ProLogis North America Properties Funds II, III and IV during the first quarter of 2006. See Note 4 to our Consolidated Financial Statements in Item 8 for more details of this transaction.

Generated net cash proceeds from payments on notes receivable related to dispositions of assets of $97.4 million and $60.0 million in 2007 and 2005, respectively, and net cash payments for advances on notes receivable of $41.7 million in 2006.

Used $1.3 billion of cash (net of Catellus cash on the merger date) as partial consideration related to the Catellus Merger in 2005.

For 2007, 2006 and 2005, financing activities provided net cash of $2.7 billion, $1.6 billion and $1.7 billion, respectively. The following are the more significant activities for all periods presented as summarized below:

During 2007, we issued $2.4 billion of convertible senior notes. In March, we issued $1.25 billion with a coupon rate of 2.25% due in March 2037 and in November, 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. Also in 2007, on our lines of credit including the Global Line, we made net payments of $431.5 million and we made net payments of $392.5 million on our other debt.

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 3 and Note 13 to our Consolidated Financial Statements in Item 8).

We received proceeds of $1.9 billion and made payments of $588.8 million on our senior notes and other secured and unsecured debt, resulting in net proceeds of $1.4 billion during 2006. We received net proceeds from issuance of other debt of $368.2 million for 2006.

In 2005, we received proceeds from borrowings on credit facilities and short-term borrowings of $1.3 billion, which were used primarily for the cash consideration for the Catellus Merger and repayment of

$106.4 million of debt assumed in the Catellus Merger. We also received proceeds from the issuance of senior notes of $890.0 million.

We paid distributions to holders of common shares of $472.6 million, $393.3 million and $297.4 million in 2007, 2006 and 2005, respectively. We paid dividends on preferred shares of $31.8 million, $19.1 million and $25.4 million in 2007, 2006 and 2005, respectively.

Table of Contents

The sale and issuance of common shares generated proceeds of $46.9 million, $358.0 million and $45.6 million in 2007, 2006 and 2005, respectively. This includes $320.8 million received in 2006 for the issuance of 5.4 million common shares under our Controlled Equity Offering Program.

Off-Balance Sheet Arrangements

Liquidity and Capital Resources of Our Unconsolidated Investees

We had investments in and advances to unconsolidated investees of $2.3 billion at December 31, 2007, of which $1.8 billion relates to our investments in the property funds. Summarized financial information for the property funds (for the entire entity, not our proportionate share) at December 31, 2007 is presented below (dollars in millions):

Property Fund	Total Assets	Third Party Debt (1)(2)	2008 Maturities	Weighted Average Interest Rate	Our Ownership
ProLogis California	$ 591.2	$ 319.8	$ 5.6	7.5%	50.0%
ProLogis North American Properties Fund I	324.2	242.3		7.6%	41.3%
ProLogis North American Properties Fund VI	495.9	307.0		5.4%	20.0%
ProLogis North American Properties Fund VII	375.2	228.7	0.2	5.5%	20.0%
ProLogis North American Properties Fund VIII	185.7	112.0		5.3%	20.0%
ProLogis North American Properties Fund IX	189.8	120.4	1.7	5.7%	20.0%
ProLogis North American Properties Fund X	216.8	135.0		5.7%	20.0%
ProLogis North American Properties Fund XI	217.2	60.2	0.8	4.5%	20.0%
ProLogis North American Industrial Fund	2,135.6	1,259.2	48.3	5.7%	23.2%
ProLogis North American Industrial Fund II (3)	2,205.5	1,283.9	102.1	5.5%	36.9%
ProLogis North American Industrial Fund III (3)	1,792.7	1,090.2	988.0	5.8%	20.0%
ProLogis Mexico Industrial Fund (3)	304.8	146.4	146.4	5.8%	20.0%
ProLogis European Properties	4,975.2	2,744.9		5.2%	24.9%
ProLogis European Properties Fund II (3)	1,551.2	711.4	711.4	6.0%	24.3%
ProLogis Japan Properties Fund I	1,235.3	554.3		1.6%	20.0%
ProLogis Japan Properties Fund II	2,523.6	1,309.6	1.0	1.9%	20.0%
ProLogis Korea Fund	51.7	25.6		6.2%	20.0%

Total property funds	$	19,371.6	$	10,650.9	$	2,005.5

(1) As of December 31, 2007, we had not guaranteed any of the third party debt.

(2) The approximate principal payments due on the third party debt of the property funds during each of the years in the five year period ending December 31, 2012 and thereafter are as follows: 2008 $2,005.5 million; 2009 $1,524.2 million; 2010 $2,039.4 million; 2011 $570.8 million; 2012 $2,204.8 million; and thereafter $2,306.2 million.

(3) The principal payments reflected as 2008 maturities in these property funds primarily represent short-term financing done in 2007 to acquire properties from us or third parties. The refinancing of this debt with long-term debt is in varying stages of completion.

See Note 4 to our Consolidated Financial Statements in Item 8 for additional information on the property funds and derivative contracts related to this debt.

Table of Contents

Contractual Obligations

Long-Term Contractual Obligations

We had long-term contractual obligations at December 31, 2007 related to long-term debt (senior and other unsecured debt, secured debt and assessment bonds), unfunded commitments on development projects, acquisitions and capital to unconsolidated investees and amounts due on lines of credit 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	$ 8,550	$ 964	$ 2,076	$ 3,469	$ 2,041
Interest on debt obligations, other than credit facilities	2,010	387	895	345	383
Unfunded commitments on development projects (1)	1,949	1,949			
Unfunded commitments on acquisitions	226	226			
Unfunded capital commitments to unconsolidated investees	26	26			
Amounts due on credit facilities (2)	1,955		1,955		
Interest on lines of credit (2)	183	63	120		
Totals (3)	$ 14,899	$ 3,615	$ 5,046	$ 3,814	$ 2,424

(1) We had properties under development at December 31, 2007 with a total expected investment of $3.9 billion. The unfunded commitments presented include all costs necessary to place the property into service, including the costs of tenant improvements and marketing and leasing costs, not only those costs that we are obligated to fund under construction contracts.

(2) The maturity date of the credit agreements assumes that we exercise our option to extend.

(3) Amounts do not include any of our FIN 48 liabilities. The majority of the FIN 48 liability of $192.4 million at December 31, 2007 represents items currently under audit, for which we can not reasonably estimate the period of settlement. See Note 7 to our Consolidated Financial Statements in Item 8.

Other Commitments

From time to time, we enter into Special Limited Contribution Agreements (SLCAs) in connection with certain of our contributions of properties to property funds. The potential obligations under the SLCAs aggregate $1.2 billion at December 31, 2007 and the combined book value of the assets in the property funds, before depreciation, that are subject to the provisions of SLCAs was approximately $6.3 billion at December 31, 2007. See Note 17 to our Consolidated Financial Statements in Item 8.

As of December 31, 2007, we have advanced $115.8 million to two of our CDFS joint ventures to fund development activities and one of the joint ventures may borrow an additional £7.5 million (or $15.1 million).

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 2007, 2006 and 2005 were $1.84, $1.60 and $1.48, respectively. In December 2007, the Board approved an increase in the annual distribution for 2008 from $1.84 to $2.07 per common share. The payment of common share distributions is dependent upon our financial condition and operating results and may be adjusted at the discretion of the Board during the year. A distribution of $0.5175 per common share for the first quarter of 2008 was declared on February 1, 2008. This distribution will be paid on February 29, 2008 to holders of common shares on February 15, 2008. We have increased our common share distribution level every year since our common shares became publicly traded in 1994.

Table of Contents

At December 31, 2007, 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.

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 properties acquired or developed in our CDFS business segment and 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 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 risks.

FFO of our unconsolidated investees is calculated on the same 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 measure is an important supplemental measure, neither NAREIT s nor our measure 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 measure 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 distribution 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.

Table of Contents

The deferred income tax benefits and expenses that are excluded from our defined FFO measure 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 measure does 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 measure 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 measure is limited in that it does not reflect the current period changes in these net assets that result from periodic foreign currency exchange rate movements.

We compensate for these limitations by using the FFO measure only in conjunction with net earnings computed under GAAP. To further compensate, we reconcile our defined FFO measure 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 attributable to common shares as defined by us was $1,227.0 million, $945.1 million and $530.5 million for the years ended December 31, 2007, 2006 and 2005, respectively. The reconciliations of net earnings attributable to common shares computed under GAAP to FFO attributable to common shares as defined by us are as follows for the periods indicated (in thousands):

	Years Ended December 31,		
	2007	**2006**	**2005**
FFO:			
Reconciliation of net earnings to FFO:			
Net earnings attributable to common shares	$ 1,048,917	$ 848,951	$ 370,747
Add (deduct) NAREIT defined adjustments:			
Real estate related depreciation and amortization	298,089	277,481	184,792
Adjustments to CDFS dispositions for depreciation	(6,196)	466	
Gains recognized on dispositions of certain non-CDFS business assets	(146,667)	(81,470)	
Reconciling items attributable to discontinued operations:			
Gains recognized on dispositions of non-CDFS business assets	(52,776)	(103,729)	(86,444)
Real estate related depreciation and amortization	2,896	11,535	11,399
Totals discontinued operations	(49,880)	(92,194)	(75,045)
Our share of reconciling items from unconsolidated investees:			
Real estate related depreciation and amortization	99,026	68,151	57,766
Gains on dispositions of non-CDFS business assets	(35,672)	(7,124)	(1,114)
Other amortization items	(8,731)	(16,000)	(5,134)
Totals unconsolidated investees	54,623	45,027	51,518
Totals NAREIT defined adjustments	149,969	149,310	161,265

Subtotals NAREIT defined FFO	1,198,886	998,261	532,012
Add (deduct) our defined adjustments:			
Foreign currency exchange losses (gains), net	16,384	(19,555)	(14,065)
Current income tax expense	3,038	23,191	
Deferred income tax expense (benefit)	550	(53,722)	12,045
Reconciling items attributable to discontinued operations deferred income tax benefit			(213)
Our share of reconciling items from unconsolidated investees:			
Foreign currency exchange losses (gains), net	1,823	(45)	298
Deferred income tax expense (benefit)	6,327	(2,982)	395
Totals unconsolidated investees	8,150	(3,027)	693
Totals our defined adjustments	28,122	(53,113)	(1,540)
FFO attributable to common shares, as defined by us	$ 1,227,008	$ 945,148	$ 530,472

Table of Contents

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. 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.

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. In anticipation of financings expected to occur in 2007, we entered into several interest rate swap contracts that were designated as cash flow hedges to fix the interest rate on a portion of the expected financing. We had no interest rate derivative contracts outstanding at December 31, 2007.

Our primary interest rate risk is created by the variable rate lines of credit. During the year ended December 31, 2007, we had weighted average daily outstanding borrowings of $2.5 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 $8.7 million of cash flow for the year ended December 31, 2007.

We also have $1.1 billion 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 $5.5 million on our cash flow for the year ended December 31, 2007.

The unconsolidated property funds that we manage, and in which we have an equity ownership, may enter into interest rate swap contracts that are designated as cash flow hedges to mitigate interest expense volatility associated with movements of interest rates for the debt they expect to issue. In 2007, certain of the property funds issued short-term bridge financing to finance their acquisitions of properties from us and third parties. Based on the anticipated refinancing of these bridge financings with longer-term debt issuances, the property funds have the following interest rate swap contracts outstanding at December 31, 2007 (amounts are for the entire entity and dollars are in thousands):

Entity	Our Ownership	Notional Amounts	Swap Rate	Maturity	Fair Value
ProLogis North American Industrial Fund II	36.9%	$ 1,005,900	5.31 5.83%	2009 - 2018	($68,757)
ProLogis North American Industrial Fund III	20.0%	$ 642,000	5.79%	2017	($58,577)

ProLogis Mexico Industrial Fund	20.0%	$ 137,000	5.24 - 5.56%	2017	($8,650)

We have recorded our proportionate share of the liabilities of the funds related to these instruments in Other Comprehensive Income in Shareholders Equity. Once these contracts are settled, the amount of the gain or loss upon settlement, which is recorded by the property funds in other comprehensive income, will be amortized over the life of the hedged debt issuance. We guarantee our proportionate share of the ProLogis North American Industrial Fund III contracts. See also Item 1A. for risk factors related to financing.

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 forecasted net income of our foreign subsidiaries into U.S. dollars, principally euro, pound sterling, yen and renminbi. 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, 2007, we had no put option contracts outstanding. For the year ended December 31, 2007, approximately 42% of our revenues were generated outside of the United States.

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, 2007, we had forward contracts outstanding with an aggregate notional amount of £181.5 million ($360.7 million at December 31, 2007).

Fair Value of Financial Instruments

See Note 16 to our Consolidated Financial Statements in Item 8.

ITEM 8. Financial Statements and Supplementary Data

Our Consolidated Balance Sheets as of December 31, 2007 and 2006, our Consolidated Statements of Earnings, Shareholders Equity and Comprehensive Income and Cash Flows for each of the years in the three-year period ended December 31, 2007, 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 20 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). Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that our disclosure controls and procedures are effective as of December 31, 2007 to ensure that information required to be disclosed by us in reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms. Subsequent to December 31, 2007, 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, 2007 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, 2007, our internal control over financial reporting was effective.

Table of Contents

The effectiveness of our internal control over financial reporting as of December 31, 2007 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

None.

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 Jeffrey H. Schwartz, 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 2008 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 2008 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 Equity Compensation Plans in our 2008 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 2008 Proxy Statement.

Table of Contents

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 2008 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 60 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 135 to 139 of this report, which is incorporated herein by reference.

(c) Financial Statements: See Index to Consolidated Financial Statements and Schedule III on page 60 of this report, which is incorporated by reference.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULE III

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, 2007 and 2006, and the related consolidated statements of earnings, shareholders equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2007. 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, 2007 and 2006, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2007, 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, 2007, 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, 2008 expressed an unqualified opinion on the effectiveness of ProLogis internal control over financial reporting.

KPMG LLP

Denver, Colorado
February 27, 2008

Table of Contents

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, 2007, 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, 2007, 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, 2007 and 2006, and the related consolidated statements of earnings, shareholders equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2007, and our report dated February 27, 2008 expressed an unqualified opinion on those consolidated financial statements.

KPMG LLP

Denver, Colorado
February 27, 2008

Table of Contents

PROLOGIS

CONSOLIDATED STATEMENTS OF EARNINGS
Years Ended December 31, 2007, 2006 and 2005
(In thousands, except per share data)

	2007	2006	2005
Revenues:			
Rental income	$ 1,067,865	$ 910,202	$ 584,352
CDFS disposition proceeds:			
Developed and repositioned properties	2,530,377	1,286,841	1,140,457
Acquired property portfolios	2,475,035		
Property management and other fees and incentives	104,719	211,929	66,934
Development management and other income	26,670	37,420	25,464
Total revenues	6,204,666	2,446,392	1,817,207
Expenses:			
Rental expenses	288,569	239,221	162,245
Cost of CDFS dispositions:			
Developed and repositioned properties	1,835,274	993,926	917,782
Acquired property portfolios	2,406,426		
General and administrative	204,558	153,516	118,166
Depreciation and amortization	308,971	286,807	186,605
Other expenses	24,963	13,013	8,633
Total expenses	5,068,761	1,686,483	1,393,431
Operating income	1,135,905	759,909	423,776
Other income (expense):			
Earnings from unconsolidated property funds	94,453	93,055	46,078
Earnings from CDFS joint ventures and other unconsolidated investees	11,165	50,703	6,421
Interest expense	(368,065)	(294,403)	(177,562)
Interest income on notes receivable	8,066	16,730	6,781
Interest and other income, net	25,935	18,248	10,724
Total other income (expense)	(228,446)	(115,667)	(107,558)
Earnings before minority interest	907,459	644,242	316,218
Minority interest	(6,003)	(3,457)	(5,243)
Earnings before certain net gains	901,456	640,785	310,975
Gains recognized on dispositions of certain non-CDFS business assets	146,667	81,470	
Foreign currency exchange gains, net	7,915	21,086	15,979

Earnings before income taxes			1,056,038		743,341		326,954
Income taxes:							
Current income tax expense			68,349		84,250		14,847
Deferred income tax expense (benefit)			550		(53,722)		12,045
Total income taxes			68,899		30,528		26,892
Earnings from continuing operations			987,139		712,813		300,062
Discontinued operations:							
Income attributable to disposed properties and assets held for sale			5,704		24,311		24,191
Losses related to temperature-controlled distribution assets							(25,150)
Gains recognized on dispositions:							
Non-CDFS business assets			52,776		103,729		86,444
CDFS business assets			28,721		33,514		10,616
Total discontinued operations			87,201		161,554		96,101
Net earnings			1,074,340		874,367		396,163
Less preferred share dividends			25,423		25,416		25,416
Net earnings attributable to common shares		$	1,048,917	$	848,951	$	370,747
Weighted average common shares outstanding	Basic		256,873		245,952		203,337
Weighted average common shares outstanding	Diluted		267,226		256,852		213,713
Net earnings per share attributable to common shares	Basic:						
Continuing operations		$	3.74	$	2.79	$	1.35
Discontinued operations			0.34		0.66		0.47
Net earnings per share attributable to common shares	Basic	$	4.08	$	3.45	$	1.82
Net earnings per share attributable to common shares	Diluted:						
Continuing operations		$	3.61	$	2.69	$	1.31
Discontinued operations			0.33		0.63		0.45
Net earnings per share attributable to common shares	Diluted	$	3.94	$	3.32	$	1.76
Distributions per common share		$	1.84	$	1.60	$	1.48

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

Table of Contents

PROLOGIS

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

	December 31, 2007	December 31, 2006
ASSETS		
Real estate	$ 16,578,845	$ 13,897,091
Less accumulated depreciation	1,368,458	1,264,227
	15,210,387	12,632,864
Investments in and advances to unconsolidated investees	2,345,277	1,299,697
Cash and cash equivalents	418,991	475,791
Accounts and notes receivable	340,039	439,791
Other assets	1,389,733	998,224
Discontinued operations assets held for sale	19,607	57,158
Total assets	$ 19,724,034	$ 15,903,525
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Debt	$ 10,506,068	$ 8,386,886
Accounts payable and accrued expenses	933,075	518,651
Other liabilities	769,408	546,129
Discontinued operations assets held for sale	424	1,012
Total liabilities	12,208,975	9,452,678
Minority interest	78,661	52,268
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, 2007 and 2006	100,000	100,000