Principal Asset Allocation

Principal Asset Management℠

PRINCIPAL DIVERSIFIED INCOME FUND

Quarterly commentary

SECOND QUARTER 2024

Market review

TICKER:

Class I: PGDIX
Class A: PGBAX
Class C: PGDCX
Class R6: PGBLX

The U.S. economy moderated while other developed markets enjoyed cyclical upturns. Global financial conditions were marginally tighter, driven by wider credit spreads and weaker equity momentum.

Central bank cutting cycles were delayed and are expected to be slow and shallow. A first Federal Reserve (Fed) rate cut could occur in September, provided inflation and economic surprises continue to decelerate. Other central banks already eased but their next moves will align with Fed actions.

Elevated fixed income yields continue drawing investor interest. Global credit rating upgrades to total changes was stable at 50%, a bit improved from the 43% measured as of year-end 2023. Ratings momentum could improve further if the expected earnings growth materializes.

Investors who stayed in cash are meaningfully exposed to reinvestment risk. Assets in money market funds ballooned to a record $6 trillion. This cash now represents a potential tailwind to risk assets.

Credit risk outperformed rate and liquidity risk. High yield (HY) bonds and floating rate debt delivered strong returns in the second quarter (Q2) primarily due to their higher yield as spreads on both asset classes only widened by 8 and 10 basis points (bps), respectively. Macro resilience should ensure a gradual rise in defaults versus a sudden spike, meaning credit spreads are unlikely to widen significantly from current levels.

Interest rate risk (i.e., duration) weighed on fixed income returns in Q2. Although rates were somewhat volatile during the quarter, the U.S. 10-year Treasury ended the quarter only modestly higher from first quarter (Q1) 2024 levels. Longer duration and more interest rate sensitive fixed income struggled to generate a positive return in this environment.

Preferred securities and emerging markets (EM) debt securities outperformed the highest quality sectors within fixed income due to their compelling yields. Both sectors out-yielded the Bloomberg Barclays U.S. Aggregate Index by more than 1%.

Market indices	Quarterly returns (%)	1-year returns (%)
Bloomberg U.S. Aggregate Bond Index	0.07	2.63
Bloomberg Global Aggregate Index	-1.10	0.93
Bloomberg Global High Yield Index	1.04	11.82
Bloomberg Global Credit Index	-0.02	5.48
Bloomberg EM Aggregate TR Index	0.68	7.95
ICE BofA US All Captl TR Index	0.49	11.63
Morningstar LSTA US LL 100 TR Index	2.07	10.78

As of June 30, 2024. Source: Morningstar. Indices are unmanaged and do not take into account fees, expenses, and transaction costs and it is not possible to invest in an index.

Portfolio commentary

The Principal Diversified Income Fund (I-shares) returned 0.58% for the quarter, outperforming the Diversified Income Blended Index (Linked) which returned 0.07% for the quarter ending June 30, 2024.

What helped?

- The Fund's outperformance was largely driven by its allocation to HY. Despite the slight widening of spreads, the asset class benefited from favorable market conditions, including a resilient consumer and positive momentum within risk markets leading to a move higher in rates. Leveraged loans showed a notable rebound during Q2 with a resurgence in loan issuance as an increase in corporate buyouts and merger and acquisition (M&A) activity drove demand. Nuveen, our dedicated leveraged loan manager, delivered the highest absolute performance, as well as outperformed the Morningstar U.S. LSTA LL Index through solid issuer selection, in aggregate.
- Our allocation to preferred securities delivered robust returns on an absolute and benchmark-relative basis as Spectrum Asset Management, Inc. (Spectrum) outperformed the Bloomberg U.S. Aggregate Bond Index as well as its primary benchmark, the Ice BofA All Capital Securities Index. This segment of the market continues to benefit from investors' ongoing appetite for riskier fixed income sectors amid elevated valuations across HY and investment-grade (IG) credit, coupled with a resilient economic backdrop.
- The portfolio benefited from our allocation to the securitized segment of the fixed income market, predominantly through our recently launched opportunistic securitized sleeve, managed by Grantham, Mayo, Van Otterloo & Co. LLC (GMO). This sleeve allows us to gain exposure to some of the more non-traditional, esoteric areas of the securitized market such as asset-backed securities (ABS), commercial mortgage-backed securities (CMBS), collateralized loan obligations (CLOs), and non-agency mortgage-backed securities (MBS), where valuations remain quite attractive. The broader securitized market has also benefited from the downward trajectory surrounding rate volatility as the market gains more confidence around the Fed's rate-cutting path.

What hurt?

- The portfolio was negatively impacted by one of our HY managers, Polen Capital Credit, LLC (Polen), as they underperformed for the quarter. The disappointing quarterly results were mainly attributed to one of their less liquid holdings, Atd New Holdings Inc, which suffered from a valuation write-down due to deteriorating fundamentals and poor management execution.
- Our allocation to private credit was a detractor over the quarter, albeit by a small margin, driven by negative manager selection effect. The underperformance was isolated to one underlying holding within a private credit fund which, due to unforeseen events, was written down to zero. We held several calls with the manager to understand the details around the write-down and maintain a positive view on the private credit fund and strategy.
- Lastly, our allocation to global IG credit detracted as the asset class posted a marginally negative return as the U.S. dollar continued its upward trend putting pressure on foreign currency valuations.

What's next?

- We continue to believe spread sectors offer an attractive risk/income profile in today's economic backdrop with yields at extremely attractive levels. Allocating across the various spread sectors will provide investors the necessary diversification and complementary positioning to investors' core bond holdings.

Allocation update

	Q2 2024 (%)	Q1 2024 (%)
Investment-grade credit	**27.5**	**29.0**
Global investment-grade credit	**9.1**	**9.9**
BlackRock Financial Management, Inc.	9.1	9.9
U.S. investment-grade credit	**18.4**	**19.2**
PineBridge Investments LLC	18.4	19.2
Securitized	**12.3**	**12.0**
Agency mortgage-backed securities	**7.2**	**7.0**
Principal Fixed Income	7.2	7.0
Opportunistic securitized	**5.2**	**5.0**
Grantham, Mayo, Van Otterloo & Co. LLC	5.2	5.0
High yield	**32.7**	**31.6**
Polen Capital Credit, LLC	15.5	15.3
Post Advisory Group, LLC	17.2	16.4
Floating rate debt	**7.4**	**7.0**
Nuveen Asset Management, LLC	7.4	7.0
Preferred and capital securities	**7.2**	**7.0**
Spectrum Asset Management, Inc.	7.2	7.0
Emerging market debt	**9.1**	**7.6**
Principal Finisterre	9.1	7.6
Commercial mortgage-backed securities	**—**	**1.3**
Principal Real Estate	—	1.3
Private credit	**2.2**	**2.2**
Cliffwater Enhanced Lending Fund	1.1	1.1
Variant Alternative Income Fund	1.1	1.1
Liquidity	**1.5**	**2.3**
Principal Asset Allocation	1.5	2.3

As of June 30, 2024. May not reflect current allocation or investment managers. Percentages may not add up to 100% due to rounding. A Tactical asset allocation sleeve was added in the second quarter of 2023. At times, there may not be any tactical views reflected through this sleeve, so allocations may be zero. Tactical aset allocations will reflect under their respective asset classes.

PRINCIPAL DIVERSIFIED INCOME FUND as of June 30, 2024

Performance

	Average annual total returns (%)									Yields (%)	
	3-month	Year-to-date	1-year	3-year	5-year	10-year	Since inception (12/15/2008)	Expense ratio (net/gross)	Expense limit expiration date	30-day SEC (unsubsidized/ subsidized)	12-month distribution
Class I	0.58	1.99	7.44	0.39	2.49	3.07	7.57	0.70/0.78	02/28/2025	6.24/6.33	6.72
DI Blended Index (Linked)	0.07	-0.71	2.63	-3.00	0.18	1.52	—	—	—	—	—
Morningstar category average	0.79	2.17	7.35	0.09	2.03	2.55	—	—	—	—	—

Morningstar rankings and ratings	3-month	Year-to-date	1-year	3-year	5-year	10-year	Overall
Category and number of funds in category: Multisector Bond	359	355	353	316	262	177	316
Class I percentile rankings	—	—	54	40	34	25	—
Class I ratings	—	—	—	★★★	★★★	★★★	★★★

Calendar year returns (%)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Class I	6.55	-2.23	9.62	10.23	-5.39	13.77	1.87	8.66	-11.20	8.52
DI Blended Index (Linked)	1.86	-3.94	10.25	12.24	-5.70	9.84	7.58	0.26	-12.92	5.53
Morningstar category average	3.63	-2.18	7.52	6.07	-1.52	9.80	4.84	2.49	-9.85	8.13

Morningstar percentile rankings are based on total returns. Morningstar rankings are based on risk-adjusted returns.

Returns represent past performance and do not guarantee future results. Share price, principal value, and return will vary and you may have a gain or loss when shares are sold. Current performance may be lower or higher than quoted. For the most recent month-end performance, visit www.PrincipalAM.com.

The net expense ratio reflects contractual expense limits, if any, which may lower net expenses and cause the gross and net expense ratios to differ. In such cases a date is listed through which expense limits are expected to apply; however, Principal Funds and the investment advisor may mutually agree to terminate the expense limits prior to the end of the period. Returns displayed are based on net total investment expense.

Performance assumes reinvestment of all dividends and capital gains.

DI Blended Index (Linked) benchmark description: March 1, 2022 and after, 100% Bloomberg U.S. Aggregate Bond Index (covers the U.S. investment-grade fixed rate bond market and represents securities that are domestic, taxable, and dollar denominated), for the period prior to March 1, 2022, 80% Bloomberg Global Aggregate Index (a broad-based measure of global investment-grade fixed income) and 20% MSCI World Value Index NTR (includes large- and mid-cap securities across developed markets that exhibit overall value style), and for the period prior to January 1, 2019, 40% Bloomberg Global Credit Index (represents global investment-grade, fixed-rate, taxable corporate and government-related bonds), 30% Bloomberg Global High Yield Index (represents the global high yield bond market), and 30% MSCI ACWI Value Index NTR (a market cap weighted index that is a broad measure of global equity markets).

Index performance information reflects no deduction for fees, expenses, or taxes. Indices are unmanaged and individuals cannot invest directly in an index.

Returns shown for periods of less than one year are not annualized.

The Morningstar Rating™ for funds, or "star rating," is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history. Exchange traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics. The weights are: 100% three-year rating for 36-59 months of total returns, 60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10-year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods. Morningstar ratings do not reflect the inclusion of sales charges. If sales charges were reflected, ratings could be lower.

30-day SEC yield represents net investment income earned by a fund over a 30-day period, stated as an annual percentage. Unsubsidized yield reflects the SEC yield when some fund expenses are not waived. Subsidized yield reflects a fund's yield when all expense waivers are included. 12-month yield is based on actual distributions paid over a trailing 12-month period, stated as an annual percentage.

Bloomberg U.S. Aggregate Bond Index: The index is the most widely followed broad market U.S. bond index. It measures the investment-grade, U.S. dollar-denominated, fixed-rate taxable bond market.

Bloomberg Global Aggregate Index: The index measures global investment-grade debt from 24 local currency markets. This multi-currency benchmark includes treasury, government-related, corporate, and securitized fixed-rate bonds from both developed and emerging markets issuers.

Bloomberg Global High Yield Index: The index is a multi-currency flagship measure of the global high yield debt market. The index represents the union of the U.S. High Yield, the Pan-European High Yield, and Emerging Markets Hard Currency High Yield indices. The high yield and emerging markets sub-components are mutually exclusive.

Bloomberg Global Credit Index: The index measures the credit sector of the global investment-grade fixed-rate bond market, including corporate, government, and agency securities.

Bloomberg EM Aggregate TR Index: The index is a flagship hard currency emerging market debt benchmark that includes fixed- and floating-rate U.S. dollar-denominated debt issued from sovereign, quasi-sovereign, and corporate emerging markets issuers.

ICE BofA US All Captl TR Index: The index represents investment-grade and below- investment-grade instruments in both the retail $25 par market and the institutional $1,000 par market.

Morningstar LSTA US LL 100 TR Index: The index measures the performance of the 100 largest facilities in the U.S. leveraged loan market. Index constituents are market-value weighted, subject to a single loan facility weight cap of 2%.

Not authorized for distribution unless preceded or accompanied by a current prospectus, or a summary prospectus if available, that includes information about the fund's objectives, risks, charges, and expenses. Please read it carefully before investing.

Commentary reflects the opinions of Principal Global Investors, is believed to come from reliable sources, and reflects the opinions of the investment advisor at the time of publication. The opinions may not come to pass.

Past performance is no guarantee of future results and should not be relied upon to make an investment decision. Investing involves risk, including possible loss of principal.

Asset allocation and diversification do not ensure a profit or protect against a loss.

Fixed-income investments are subject to interest rate risk; as interest rates rise their value will decline. Lower-rated securities are subject to additional credit and default risks, as are mortgage-backed securities, which carry pre-payment risk and increased risk due to real estate exposure. Risks of preferred securities differ from risks inherent in other investments. In particular, in a bankruptcy preferred securities are senior to common stock but subordinate to other corporate debt. International investing involves greater risks such as currency fluctuations, political/social instability, and differing accounting standards. These risks are magnified in emerging markets, which have increased liquidity risk. Floating rate debt instruments are subject to credit risk, interest rate risk, and impaired collateral risk, which means that the value of the collateral used to secure a loan held by the fund could decline over the course of the loan. Private credit involves an investment in non-publicly traded securities which are subject to illiquidity risk. Portfolios that invest in private credit may be leveraged and may engage in speculative investment practices that increase the risk of investment loss. Investing in derivatives entails specific risks relating to liquidity, leverage, and credit, which may reduce returns and/or increase volatility.

Liquidity allocation may not be held as cash and may be invested on a short- term basis in ETFs that represent asset classes in the Fund, seeking to align with the target weights in the Fund's index.

Class I shares are available only to eligible investors, including various institutional investors and investors in certain mutual fund wrap or asset allocation programs. See the prospectus for eligibility requirements.

Principal Asset Allocation, Principal Fixed Income, and Principal Finisterre are investment teams within Principal Global Investors.

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