Principal Asset Management℠

THE CASE FOR PREFERRED AND CAPITAL SECURITIES

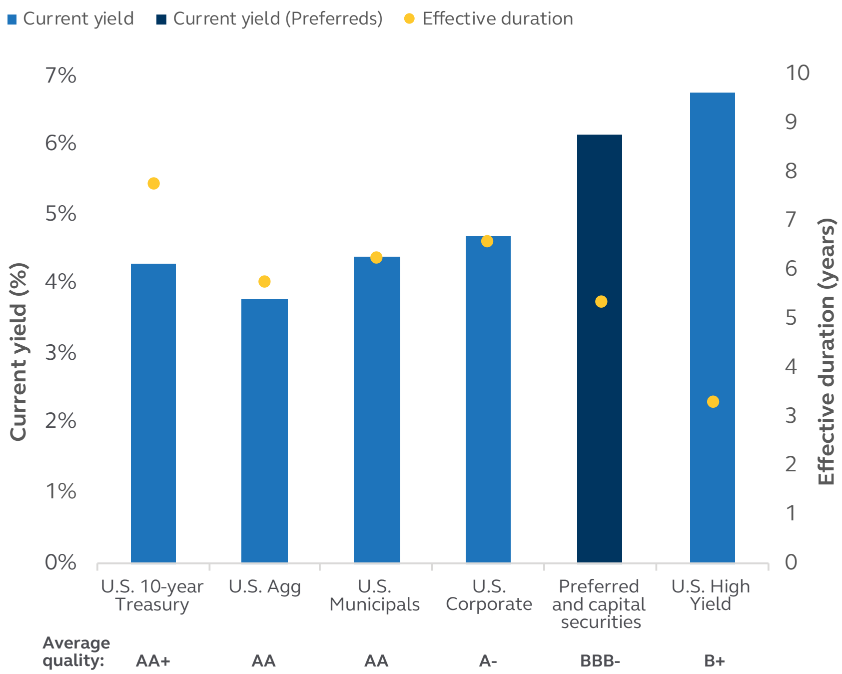
# Quality, defensive, tax-advantaged income

In today's uncertain interest rate environment, global preferred and capital securities may offer attractive yields, higher income potential, and favorable lower duration when compared to other fixed income asset classes. Additionally, their various adjustable-rate coupon structures may help cushion the impact of interest rates risk while their high credit quality may be beneficial when global economic conditions become challenging. For individual U.S. taxpayers, the availability of qualified dividend income from some preferred and capital securities may selectively further enhance the after-tax yield available from the asset class.

## Potential investor benefits

- Attractive income while maintaining a lower-duration, investment-grade portfolio
- Evolved security structures to help mitigate interest rate risk
- Reduced tax rates on qualified dividends for individual U.S. taxpayers

### Favorable yield relative to duration and credit quality




**Past index performance is not a reliable indicator of future performance.**

Source: Spectrum Asset Management, Inc., Bloomberg LLP, and Barclays. As of December 31, 2024.

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

## Active management based on specialized research and dynamic security selection to manage complex global markets

**Deep and broad experience:**

Specialized management of global high-quality preferred and capital securities across varied market, interest rate, and credit cycles for over 35 years.

**Conservative, risk-managed investment philosophy:**

Emphasis on high current income consistent with capital preservation equates to higher quality bias relative to many competitors.

**Dynamic management:**

Focus on seeking an optimal combination of preferred and capital securities sectors and structures under a variety of credit, interest rate, evolving regulatory, and market conditions.

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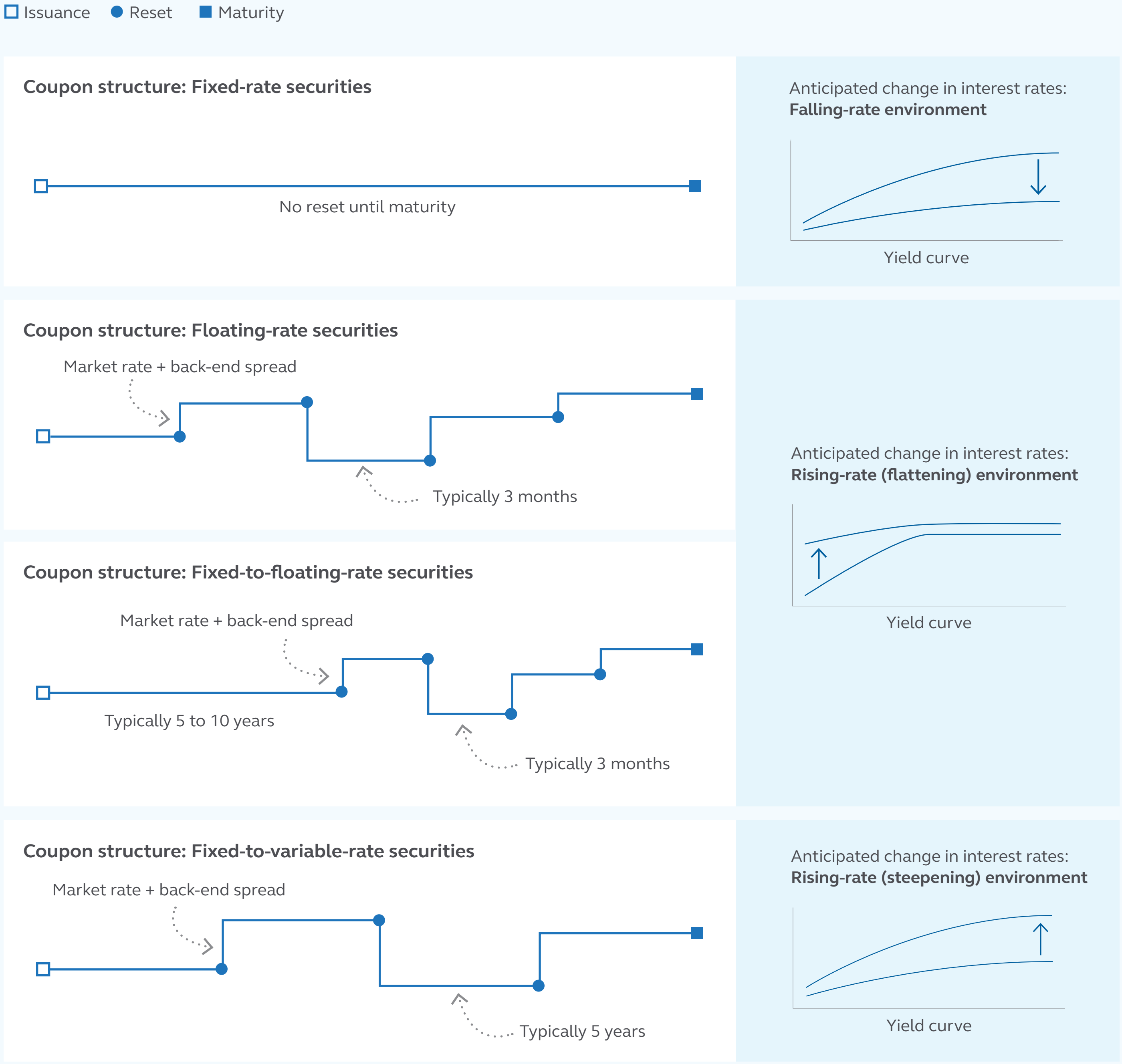
# Evolved tools to help portfolio managers manage interest rate risks

Today's preferred and capital securities markets offer investors varied coupon structures that can potentially benefit different types of interest rate movements. These structures include: fixed-rate, floating-rate, fixed-to-floating rate, and fixed-to-variable rate (i.e., re-fixed)—each having differing duration and call option features. Active portfolio management and security selection in anticipation of not only the overall direction on interest rates but the anticipated shape of the yield curve are valuable product flexibilities to help mitigate risks in both interest rate and credit cycles. By selecting securities with larger back-end spreads preferred and capital securities may help to cushion the effect of widening spreads or rate volatility.

## Strategic choices to manage interest rate risk



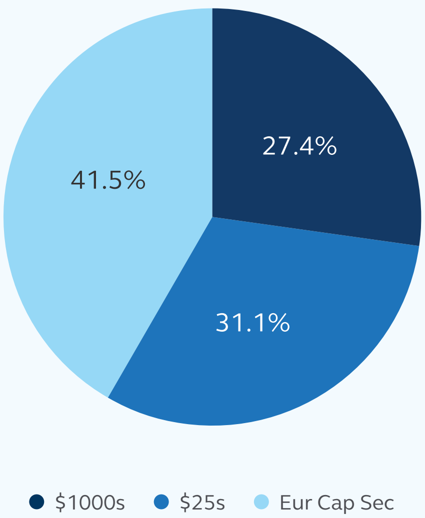

Source: Spectrum Asset Management, Inc. For illustrative purposes only. See last page for definitions.

# The preferred and capital securities market isn't what it used to be

The universe has vastly evolved due to regulation changes and with the introduction of contingent convertible securities (CoCos):

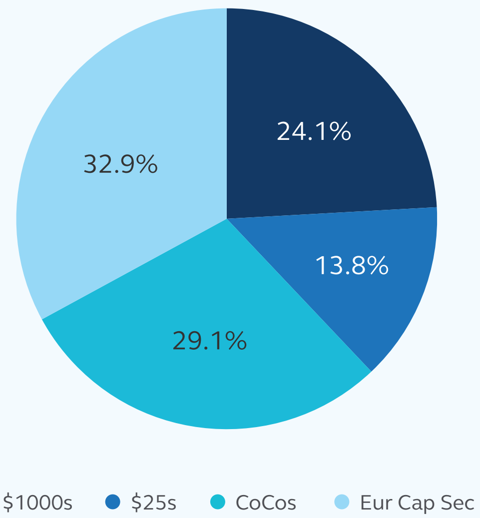
- The $25 par preferred securities market — generally heavily comprised of fixed-rate structures that are sensitive to interest rates — has shrunk over the years.
- The current landscape, with a smaller $25 par market, is made up of fewer fixed-rate structures and more adjustable-rate structures that are less interest-rate sensitive.
- Preferred and capital securities are better positioned to be more defensive, which may help in various rate environments.

**Preferred and capital securities market size**
as of December 31, 2012




**YIELD –** 6.12%
**EFFECTIVE DURATION –** 4.72 years

**Preferred and capital securities market size**
as of December 31, 2024



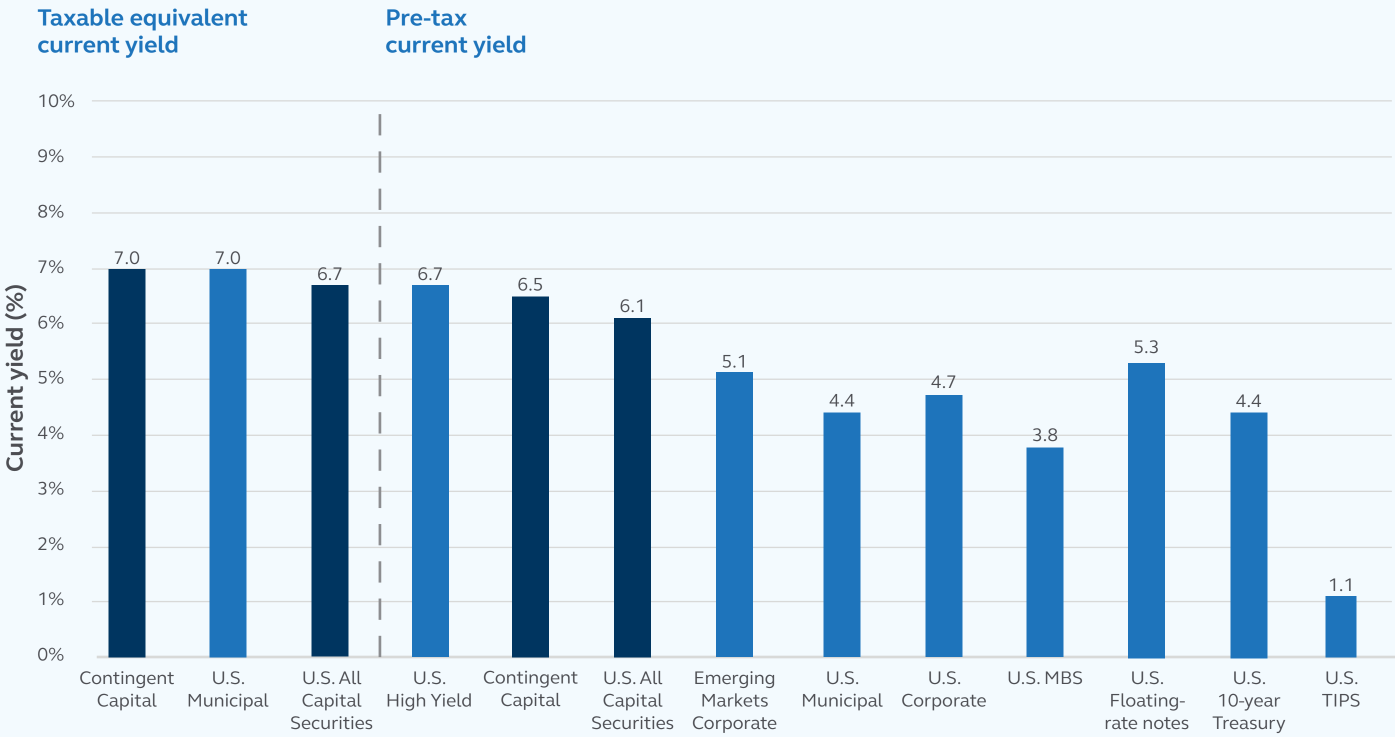

**YIELD –** 5.35%
**EFFECTIVE DURATION –** 4.22 years

Source: ICE Data Services, Bloomberg. $25s are represented by the ICE BofA Core Plus Fixed Rate Preferred Securities Index; $1000s are represented by the ICE BofA U.S. Investment Grade Institutional Capital Securities Index and ICE BofA U.S. High Yield Institutional Capital Securities Index; CoCos are represented by the ICE BofA Contingent Capital Index; Eur Capital Securities are represented by the ICE BofA Euro Non-Financial Subordinated Index and ICE BofA Subordinated Euro Financial Index. Indices are unmanaged and individuals cannot invest directly in an index. See last page for index descriptions and definitions. Past index performance is not a reliable indicator of future performance.

# Tax-advantaged dividends can potentially augment after-tax income for U.S. taxpayers

Global U.S. dollar denominated preferred and capital securities currently offer among the highest after-tax current yields for individual U.S. taxpayers. Because dividends from some preferred and capital securities may qualify for a tax preference at lower rates, certain security selections can be more attractive than their bond equivalents. One way to implement a preferred allocation for a U.S. taxpayer would be to switch less tax-efficient high-yield debt or lower yielding investment-grade corporate bonds for more tax-efficient preferred and capital securities.

**Qualified dividends favor individual U.S. taxpayers**

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Source: Spectrum Asset Management, Inc., Bloomberg LLP, Barclays. As of December 31, 2024.

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Note: Taxable equivalent current yields are calculated by segmenting the applicable index income paid by QDI-eligible securities from income paid by non-QDI-eligible securities, and tax adjusting such income by 20% and 37%, respectively. QDI-eligible income may be taxed at lower rates for investors in lower income tax brackets. Investors should consult their tax advisor.

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**Definitions**

- Fixed-rate securities: Fixed rate coupon for life of the security.
- Floating-rate securities: Floating rate coupon that typically resets in 3-month increments based on a spread vs a stated market rate1.
- Fixed-to-floating-rate securities: Coupon is initially fixed for a set period, typically 5, 7, or 10 years2. After initial fixed period, the coupon resets based on a stated market rate plus a predetermined back-end spread1. Then it will typically reset in 3-month increments.
- Fixed-to-variable (Fixed-to-re-fixed) rate securities: Coupon is initially fixed for a set period, 5, 7, or 10 years2. After initial fixed period, the coupon resets based on a stated market rate plus a predetermined back-end spread (most commonly a 5-year market rate plus a back-end spread)3. The security's coupon will be fixed for another set time period, typically 5 years2.

[1] Historically, the most common reset index has been LIBOR; however with LIBOR discontinuing, other rates such as SOFR have been and are expected to be used.

[2] Other fixed periods exist, however 5- and 10- year fixed rate coupon time frames are the most typical.

[3] The reset index is typically constant maturity treasuries for the same term as the fixed/re-fixed periods, but other reset indexes include swaps.

**Index descriptions**

- Bloomberg U.S. Aggregate Index (U.S. Agg) provides a broad-based measure of the U.S. investment-grade fixed income markets.
- Bloomberg Global-Aggregate Index (Global Agg) provides a broad-based measure of the global investment-grade fixed income markets.
- Bloomberg U.S. Treasury Inflation-Linked Bond Index: U.S. TIPS index (U.S. TIPS) measures the performance of the U.S. Treasury Inflation Protected Securities (TIPS) market.
- Bloomberg U.S. Mortgage Backed Securities Index (U.S. MBS) tracks fixed rate agency mortgage backed pass-through securities guaranteed by Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC).
- Bloomberg U.S. FRN Index (U.S. Floating-rate notes) measures the performance of USD denominated, investment-grade, floating-rate notes across corporate and government-related sectors.
- ICE BofA Core Fixed Rate Preferred Securities Index tracks the performance of fixed rate U.S. dollar denominated investment grade preferred securities issued in the U.S. domestic market.
- ICE BofA Core Plus Fixed Rate Preferred Securities Index tracks the performance of fixed rate U.S. dollar denominated preferred securities issued in the U.S. domestic market.
- ICE BofA U.S. Investment Grade Institutional Capital Securities Index tracks the performance of U.S. dollar denominated investment grade hybrid capital corporate and preferred securities publicly issued in the U.S. domestic market.
- ICE BofA Subordinated Euro Financial Index (Euro Capital Securities Financials) racks the performance of EUR denominated investment grade debt publicly issued by financial institutions in the eurobond or Euro member domestic markets.
- ICE BofA Euro Non-Financial Subordinated Index (Euro Capital Securities Non-Financials) tracks the performance of non-financial EUR denominated investment grade corporate debt publicly issued in the eurobond or Euro member domestic markets.
- ICE BofA U.S. High Yield Institutional Capital Securities Index tracks the performance of U.S. dollar denominated sub-investment grade hybrid capital corporate and preferred securities publicly issued in the U.S. domestic market.
- ICE BofA U.S. All Capital Securities Index (Preferred and capital securities) tracks the performance of fixed rate, U.S. dollar denominated hybrid corporate and preferred securities publicly issued in the U.S. domestic market.
- ICE BofA Contingent Capital Index (Contingent Capital) tracks the performance of investment grade and below investment grade contingent capital debt publicly issued in the major domestic and eurobond markets.
- ICE BofA U.S. High Yield Index (U.S. High Yield) tracks the performance of U.S. dollar denominated below investment grade corporate debt publicly issued in the U.S. domestic market.
- ICE BofA U.S. Corporate Index (U.S. Corporate) tracks the performance of U.S. dollar denominated investment grade corporate debt publicly issued in the U.S. domestic market.
- ICE BofA Emerging Markets Corporate Plus Index (Emerging Markets Corporate) tracks the performance of U.S. dollar and euro denominated emerging markets nonsovereign debt publicly issued in the major domestic and eurobond markets.
- ICE U.S. Broad Municipal Index (U.S. Municipal) tracks the performance of U.S. dollar denominated investment grade tax-exempt debt publicly issued by U.S. states and territories, and their political subdivisions, in the U.S. domestic market.
- ICE BofA Current 10-Year U.S. Treasury Index (U.S. 10-year Treasury) is a one-security index comprised of the most recently issued 10-year U.S. Treasury note.
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**Risk considerations**

Past performance is no guarantee of future results. Investing involves risk, including possible loss of principal. Fixed-income investment options are subject to interest rate risk, and their value will decline as interest rates rise. 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. Contingent capital securities (CoCos) may have substantially greater risk than other securities in times of financial stress. An issuer or regulators decision to write down, write off or convert a CoCo may result in complete loss on an investment.

**Important information**

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MM10496-17 | 02/2025 | 4152098-052025