

## Principal Asset Allocation (PAA)

# Sustainable Investing Policy Statement

### Philosophy

Principal Asset Allocation (PAA) believes sustainable investing is a principles and values-based continuum that can be customized to reflect our clients' priorities and goals. We believe that active consideration of material environmental, social, and governance (ESG) factors has the potential to enhance our ability to add value from a long-term risk/return perspective. Finally, we believe that integrating ESG considerations into our investment process helps facilitate our clients' desire to leverage their capital to drive meaningful change.

### Measure: Assessing the Building Blocks

PAA builds ESG awareness into the asset allocation investment process. As asset allocators, the building blocks, or betas, that we select when constructing portfolios can be very influential in determining the overall ESG sensitivity of a strategy. As such, when building portfolios, we first determine the ESG rating for each asset class in our investment universe, using the representative indices as our baseline. This analysis allows us to understand, at a high level, what the ESG implications might be of emphasizing certain asset classes in order to achieve a desired investment outcome.

### Activate: Implementation

Once we progress to the implementation of those selected asset classes, we rely on multi-pronged approach to ensure that we are building portfolios that reflect our sustainable investing philosophy. We generally prefer that our sub-advisors be signatories to the Principles for Responsible Investment (PRI). This ensures that we are engaging with investment partners that share our belief that ESG issues may affect the performance of investment portfolios. Further, we require that each sub-advisor submit an ESG policy, which details their individual philosophy and ESG methodology.

Finally, all sub-advisors must complete our annual ESG questionnaire, which delves into the level that ESG is being incorporated into the day-to-day management of the portfolio. The questionnaire is a proprietary tool developed by the Principal Asset Management Investment & Platform Oversight and Manager Alpha Research & Selection teams that allows us to compare the ESG awareness across sub-advisors, disciplines, and asset classes. This comparison is formalized in the Manager Alpha Research & Selection team internal ranking system which assesses each sub-advisor according to their level of ESG integration.

This ESG integration ranking is primarily qualitative in nature and attempts to capture the depth and breadth of the sub-advisors ESG discipline. To complement this qualitative assessment, we employ a holdings-based ESG analysis across our portfolios. Specifically, we rely on ESG Manager from MSCI ESG Research, LLC as our primary tool to evaluate ESG criteria. We use the MSCI analysis to gain a detailed understanding of how an individual holding (company) is rated according to ESG principles. We examine the overall ESG rating and the individual E, S, and G ratings in absolute measure as well as index- or peer-group relative, as applicable. We focus specifically on the trend of those ratings over time versus any one reading.

This qualitative and quantitative assessment of the ESG profile of a sub-advisor or a strategy helps us identify attractive ESG profiles. For example, when selecting a large cap value manager for our equity allocation, we may prefer one that has the higher ESG rating or alternatively, the option that may have a lower overall rating but, according to MSCI analysis, has higher exposure to ESG leaders that may be on a path for an ESG rating upgrade. Note that the ESG profile would just be one of many factors considered in the above hypothetical illustration.

## Manage

Each month we review the overall ESG ratings of the investment options on the Principal platform, as well as any of the indices or betas in our investment universe. Many of our sub-advisors have developed a proprietary methodology for reviewing and quantifying ESG risk in their portfolios. In those cases, a comparison of our third-party assessment to their proprietary assessment can often be informative in understanding the trajectory and overall ESG sensitivity of the portfolio.

We have integrated the MSCI ESG tool into our holdings-based attribution system (FactSet) and our holdings-based risk system (BarraOne). This allows us to examine the performance attribution that was generated from the ESG sensitivity within the portfolio. We can then use that information to better understand how our asset allocation and manager selection decisions impact our ESG bias and ultimately our desired investment outcome.

In most cases we do not have any hard restrictions on ESG investing (meaning, no explicit exclusions or minimum quality) at the portfolio level. From the sub-advisor perspective, we do monitor adherence to their ESG policy as part of our standard quarterly monitoring. Any significant deviations would be flagged for review.

## Feedback: ESG reporting process

The sixth PRI Principle states that we will report on our activities and progress towards implementing the Principles. To this end, the PAA team can provide the reporting and feedback on current sustainable investing positioning across all existing strategies as well as the performance attribution according to ESG rating.

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