

Manager profile



Principal MidCap Value III Portfolio

Co-sub-advised by Principal Global Investors and Barrow Hanley



Principal Global Investors—a member of the Principal Financial Group®—uses a unified investment philosophy and process that emphasize independent fundamental research and superior stock selection. The firm's capabilities encompass large-, mid-, and small-cap stocks in developed and emerging markets worldwide.

> Investment philosophy and process

Philosophy: The equity investment philosophy of Principal Global Investors is based on the beliefs that **1) stock selection** is the most reliable and repeatable source of consistent performance and that **2) integration** of traditional and quantitative fundamental research is superior to either in isolation.

The firm seeks to identify the most compelling investment opportunities within a clearly defined focus universe. It believes superior stocks are characterized by companies consistently demonstrating three key characteristics:

- 1. Positive and sustainable fundamental change.** Principal Global Investors seeks companies offering improving and sustainable business fundamentals, with a particular emphasis on accelerating earnings trends.
- 2. Rising investor expectations.** The objective of Principal Global Investors is to be early—but not alone—in identifying positive fundamental change and improving investor sentiment.
- 3. Attractive relative valuations.** The firm's research shows that performance potential of positive fundamental change is greatest when accompanied by discounted valuations relative to peers.

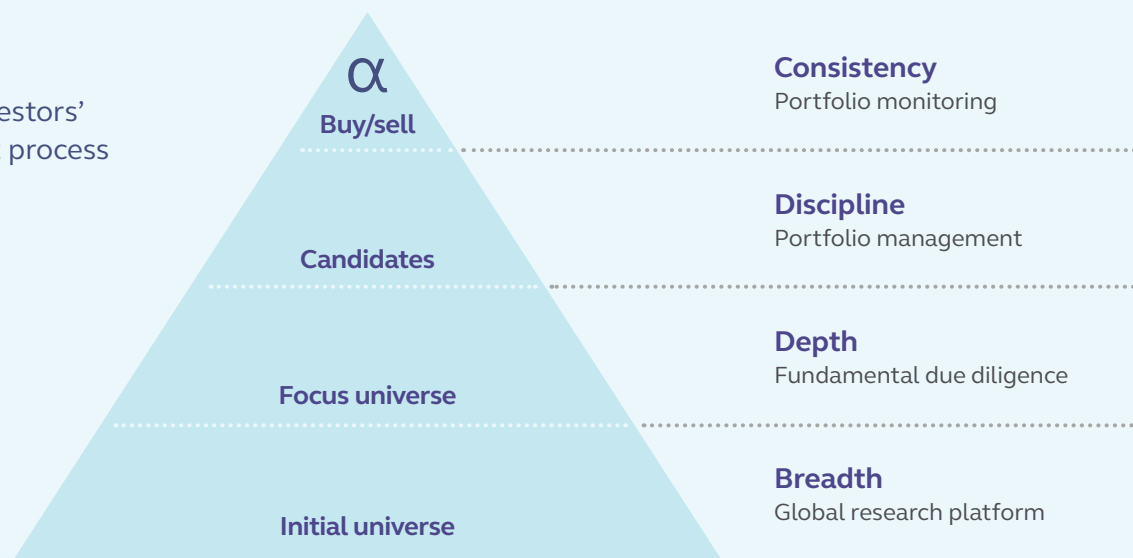
The investment advisor's investment philosophy and strategy may not perform as intended and could result in a loss or gain.

Process: To maximize global information advantages, Principal Global Investors employs a uniform and globally integrated process (Figure 1) combining fundamental research analytics, systematic disciplines, and risk management tools.

The firm's proprietary stock ranking framework—the Global Research Platform (GRP)—serves as a cornerstone of a disciplined stock selection approach by providing breadth and objectivity within the research process. The GRP systematically covers a universe of more than 10,000 companies, large and small, in both developed and emerging markets. The models underlying the GRP framework combine hundreds of complex stock evaluation tools and proprietary factors that are customized to ensure alignment with the group's investment philosophy.

Not FDIC insured | May lose value | No bank guarantee

Figure 1:
Principal Global Investors’
equities investment process



As an information management framework, the GRP is used to isolate a manageable focus-universe of stocks by providing analysts with rankings of each company’s fundamental characteristics relative to regional sector peers. This helps to make efficient use of analysts’ time as they focus their due diligence efforts on a condensed list of top-ranked companies that the firm believes have the most performance potential and are aligned with its investment philosophy.

The fundamental research analyst team provides the depth of research coverage driving the firm’s stock selection discipline over time. Organized primarily by economic sector and industry specialization, analysts are responsible for conducting fundamental analysis in their areas of specialty. They provide essential insights into industry trends and company-specific considerations. Their forward-looking professional judgment includes qualitative considerations such as intangibles, event-driven opportunities, management credibility, the quality and transparency of company financial reporting, and data integrity.

The focus universe centers on the top-ranked stocks, primarily those in the upper 20 percent among their regional sector peers. Analysts are responsible for reviewing the specific characteristics underlying the GRP ranking for each company to determine the most promising subset that

warrants further due diligence and analysis; preference is for those demonstrating the key characteristics the firm seeks. Generally, an analyst’s fundamental evaluation includes a review of financial statements, regulatory filings, news flow, independent research sources, and select sell-side research. Analysts also engage company management and industry contacts to develop a complete assessment of key business drivers, corporate operating performance, and competitive position. Also, analysts carefully evaluate sell-side estimate revisions and rating changes to determine the consensus base-case, and probe key areas of dispute in order to identify opportunities for positive earnings surprise.

Based on the rigorous multi-stage process of company due diligence, the analysts identify and recommend a subset of well-ranked companies that warrant the highest degree of consideration by the portfolio managers. Analysts communicate their stock recommendations directly to the portfolio managers, who have final authority on all buy/sell decisions.

All portfolios are well-diversified, with active positions deliberately limited relative to the benchmark. The firm’s disciplined approach is intended to provide consistency and isolate stock selection as the primary driver of relative performance over time.



**Principal Global Investors
portfolio management team**

Christopher Ibach has been with Principal Global Investors since 2000. He earned a Bachelor’s Degree in Electrical Engineering and an M.B.A. in Finance from the University of Iowa. Mr. Ibach has earned the right to use the Chartered Financial Analyst designation and is a member of the CFA Institute.

Joel Fortney has been with Principal Global Investors since 2001. He earned a Bachelor’s Degree in Finance from the University of Iowa and an M.B.A. from University of Chicago Booth School of Business. Mr. Fortney has earned the right to use the Chartered Financial Analyst designation.

BARROW, HANLEY, MEWHINNEY & STRAUSS, LLC

Barrow, Hanley, Mewhinney & Strauss (Barrow Hanley), founded in Dallas in 1979, is one of the largest value-oriented investment managers in the U.S. Barrow Hanley provides U.S. and international equity, fixed-income, and balanced investment management services. In all strategies, the firm seeks to exploit market inefficiencies through adherence to a value-oriented investment process dedicated to the selection of securities on a bottom-up basis.

> Investment philosophy and process

Philosophy: Barrow Hanley has a strict definition of value in its equity strategies. The goal of its mid-cap value equity portfolios is to exhibit below-market price-to-earnings ratios, below-market price-to-book ratios, and above-market dividend yields—regardless of market conditions—helping to ensure the integrity of the client’s asset allocation.

The firm’s approach to the mid-cap equity market is based on the underlying philosophy that markets are inefficient. These inefficiencies can best be exploited through adherence to a value-oriented investment process dedicated to the selection of securities on a bottom-up basis. Barrow Hanley’s mid-cap value equity strategy focuses on securities that are not widely followed by industry analysts—providing a greater opportunity to seek out undervalued companies utilizing first-hand, internally generated research. The firm does not attempt to time the market or rotate in and out of broad market sectors, as Barrow Hanley believes it is difficult—if not impossible—to add incremental value on a consistent basis by market timing.

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Process: Barrow Hanley does not deviate from its time-tested investment process (Figure 2). Barrow Hanley stays fully invested with a defensive, conservative orientation based on the belief that superior

Figure 2:
Barrow Hanley’s mid-cap value investment process



returns can be achieved while taking below-average risks. This strategy is implemented by constructing portfolios of individual stocks that reflect all three value characteristics: price/earnings and price/book ratios below the market and dividend yields above the market (Russell Midcap Index). While exacting in the firm's definition of value, Barrow Hanley is equally demanding in its pursuit of quality companies. The firm seeks companies with profitability and earnings growth greater than the market.

Barrow Hanley's equity portfolio managers and analysts work as a team for the purposes of generating and researching investment ideas. Portfolio managers have broad research responsibilities, although they focus their efforts on particular sectors. Analysts have specific industry assignments for more specialized, in-depth research. Approximately 75 percent of the firm's equity research is produced internally.

Barrow Hanley's mid-cap value portfolios generally consist of 35 to 45 stocks, with a primary emphasis on companies with market capitalizations of \$1 billion to \$15 billion. Sector weightings are a residual of the firm's bottom-up stock selection process. However, sector weightings are limited to 35 percent of the portfolio, at cost. The firm will not take more than a 15 percent weighting, at cost, in any industry group.

Barrow Hanley has assembled a solid base of investment professionals to continue its longstanding commitment to the value investment style. The staff of experienced equity investment professionals includes portfolio managers, research analysts, and traders. The vast experience of the firm's investment team is the distinguishing factor in the success of its security selection process.



Barrow Hanley portfolio management team

James P. Barrow, founding partner of Barrow Hanley, has been with the firm since 1979. He earned a B.S. from the University of South Carolina.

Mark Giambrone has been with Barrow Hanley since 1998. He earned a B.S. from Indiana University and an M.B.A. from the University of Chicago, and is a C.P.A.

> About Principal Portfolio Strategies

Principal Portfolio Strategies¹ is a specialized boutique that engages exclusively in the creation of asset allocation solutions. Principal Portfolio Strategies has responsibility for portfolio management of the core portion for all of the core-satellite investment options. In managing the core portion, Principal Portfolio Strategies utilizes a team approach overseen by a portfolio manager. Additionally, the boutique oversees the proprietary due diligence process for identifying, selecting, and monitoring investment managers. The philosophy of Principal Portfolio Strategies is to design innovative strategies that address specific portfolio risks, rather than simply aligning with an investment style.

¹Principal Portfolio Strategies is involved in the creation of asset allocation solutions and is responsible for the initial selection and ongoing monitoring of affiliated and unaffiliated investment managers. Principal Portfolio Strategies is a specialized investment management group within Principal Global Investors, the investment adviser to Principal Funds.

Additional information

Carefully consider a fund's objectives, risks, charges, and expenses. Contact your financial professional or visit principal.com or principalfunds.com for a prospectus, or summary prospectus if available, containing this and other information. Please read it carefully before investing.

Before directing retirement funds to a separate account, investors should carefully consider the investment objectives, risks, charges and expenses of the separate account as well as their individual risk tolerance, time horizon and goals. For additional information contact us at 1-800-547-7754 or by visiting principal.com.

Investing involves risk, including possible loss of principal.

This investment option is available through a separate account or Principal Funds, Inc. mutual fund. Separate accounts are made available through a group annuity contract with the Principal Life Insurance Company, Des Moines, IA 50392.

The Russell Midcap Index measures the performance of the mid-cap segment of the U.S. equity universe. The Russell Midcap is a subset of the Russell 1000[®] Index. It includes approximately 800 of the smallest securities based on a combination of their market cap and current index membership. The Russell Midcap represents approximately 31% of the total market capitalization of the Russell 1000[®] companies. Investors cannot invest directly in an index.

Small and mid-cap stocks may have additional risks including greater price volatility.

Sub-Advised Investment Options include separate accounts available through a group annuity contract with Principal Life Insurance Company and mutual funds available through Principal Funds, Inc.

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