

# Manager profile



## Principal High Yield I Portfolio

Sub-advised by J.P. Morgan Asset Management and Neuberger Berman

### J.P.Morgan Asset Management

J.P. Morgan Asset Management is one of the largest and most comprehensive investment management firms. J.P. Morgan offers the breadth and depth of the firm's global research capabilities, with career analysts located throughout the world.

### > Investment philosophy and process

**Philosophy:** J.P. Morgan's philosophy incorporates a value-oriented approach to fixed-income investment management. The firm's strategy combines active investment management and disciplined risk control. Central to this approach is the identification of securities that are priced inefficiently, using a bottom-up, value-oriented methodology with a secondary emphasis on strategic macro insight. J.P. Morgan's fixed-income strategies combine the consistent application of a value-oriented framework and the ongoing review, monitoring, and control of key portfolio characteristics.

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

**Process:** The firm's rigorous fundamental investment process (Figure 1)—driven by the portfolio managers working with the large investment staff—seeks to generate excess returns through the selection of undervalued securities and sectors that offer attractive total-return and risk characteristics.

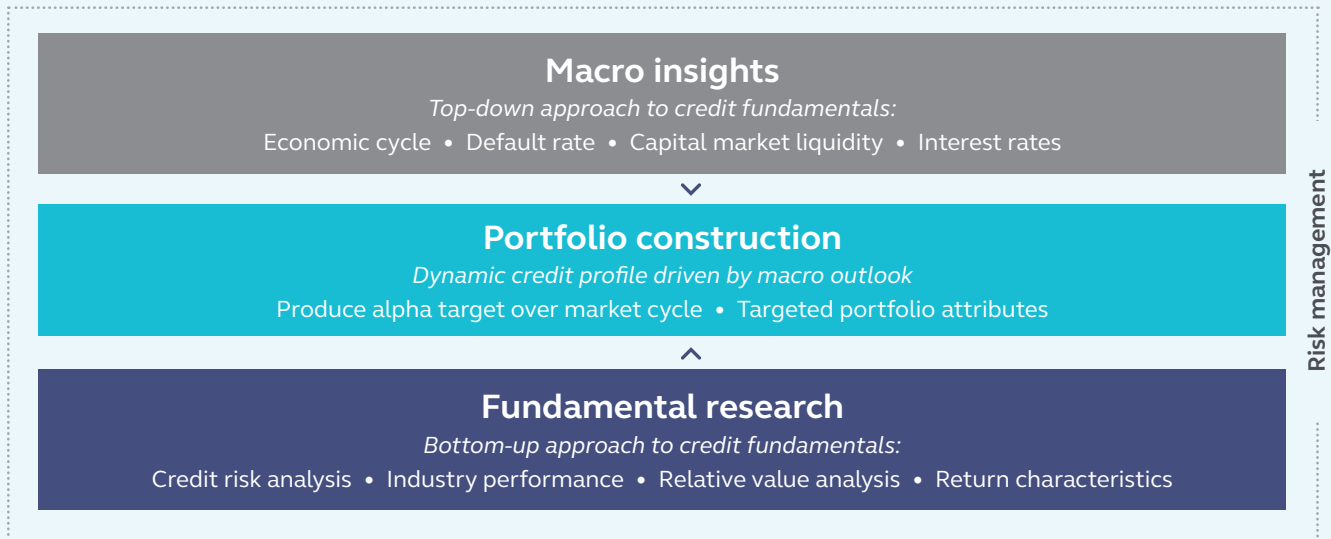
Successful implementation of the process leads to potentially favorable total-portfolio returns relative to a benchmark index and superior risk-adjusted results.

The portfolio is managed versus the Barclays Capital High Yield Index, 2% Issuer Constrained and will invest in the full range of credit ratings included in the Index. The majority of the portfolio's assets are invested in BB- and B-rated securities—although J.P. Morgan will invest in lower-rated and higher-rated securities that satisfy the yield and return criteria. The portfolio may overweight or underweight allocations to the various credit rating groups within the framework of the allocation guidelines. J.P. Morgan also participates in the "busted" convertible\* market, the leveraged loan market, high-yield private placements, post-reorganization securities, and high-yield preferred stocks.

\*Busted convertible: A convertible security, typically from debt to stock, that currently is trading below its conversion value. The security remains valued as debt based on lower likelihood the convertible price will be reached before maturity.

Not FDIC insured | May lose value | No bank guarantee

**Figure 1:**  
J.P. Morgan's investment process



The J.P. Morgan high yield management team has successfully managed portfolios using its fundamental approach to credit analysis and portfolio construction for more than 20 years.

**Three characteristics clearly distinguish J.P. Morgan's high yield management:**

1. Each portfolio manager brings a depth of experience to the critical areas associated with high yield.
2. The portfolio managers act as the head of credit and focus primarily on the security selection process with the team's credit analysts.
3. J.P. Morgan's high-yield portfolio utilizes an active and dynamic credit profile driven by security selection opportunities and the portfolio manager's outlook for high-yield credit fundamentals.

J.P. Morgan has a team of industry-aligned credit analysts who focus solely on high yield. The primary driver of returns in the high-yield market generally is the management of credit risk. Therefore, the firm's credit analysts are an integral part of the decision-making team with respect to their industry sectors—and, they have significant influence on security buy/sell decisions, industry sector weighting, and the risk profile within the sector. The analysts also play a critical role in the ongoing risk management and portfolio monitoring process.



**J.P. Morgan portfolio management team**

**James E. Gibson, Managing Director,** is a member of the Global Fixed Income, Currency & Commodities (GFICC) group. Based in Cincinnati, Jim is the head trader for the Cincinnati High Yield team and is responsible for overseeing all high-yield trading for the group. An employee since 1988, he held the same role at Banc One High Yield Partners, LLC and Pacholder Associates, Inc. Jim began his career as a high-yield analyst and also worked on a number of special projects in the corporate finance area. He holds a B.S. in Finance from the University Of Cincinnati College of Business Administration.

**William J. Morgan, Managing Director,** is a member of the Global Fixed Income, Currency & Commodities (GFICC) group. Based in Cincinnati, Bill is the team leader and senior portfolio manager for the Cincinnati High Yield team and is responsible for overseeing high yield, loans, and distressed strategies. An employee since 1984, he held the same role at Banc One High Yield Partners, LLC and Pacholder Associates, Inc. Bill holds a B.A. in History from Kenyon College and an M.B.A from Xavier University.

**James P. Shanahan, Jr., Managing Director,** is a member of the Global Fixed Income, Currency & Commodities (GFICC) group. Based in Cincinnati, Jim is the team leader and senior portfolio manager for the Cincinnati High Yield team and focuses on higher risk credits, including leveraged loans, distressed and special situations investments in high yield mandates. An employee since 1986, he held the same role at Banc One High Yield Partners, LLC and Pacholder Associates, Inc. He graduated from Xavier University and holds a J.D. from the University Of Cincinnati College Of Law.

Formed in 1939, Neuberger Berman is a leading provider of global equity, fixed-income, and alternative investment strategies to institutions and individuals through customized separately managed accounts and funds.

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## > Investment philosophy and process

**Philosophy:** Neuberger Berman has an experienced high-yield team that seeks to add value through 1) issue selection and 2) industry and quality rotation. The issue selection process focuses on securities that offer a combination of solid credit fundamentals and potential for capital appreciation. The sector rotation strategy seeks to take advantage of sector and credit-tier volatility by altering the portfolio's exposure to industries and quality tiers. The strategy seeks to take opportunistic advantage of the full high-yield credit-quality spectrum.

Neuberger Berman recognizes that the high-yield market is inherently volatile due to global economic developments, issuer operating performance, and supply/demand fundamentals. This volatility offers opportunities for experienced portfolio managers using a disciplined process to identify compelling investment opportunities. The goal is to create a diversified portfolio that can produce the opportunity for superior long-term performance based on avoidance of credit deterioration, industry and quality rotation, and relative value analysis.

Neuberger Berman takes a proactive approach to high-yield management and integrates detailed security and industry analysis within the context of a global economic outlook. The firm's research analysts are industry specialists who carry out independent primary research on companies and industries. When the research analysts purchase securities, they initiate close monitoring of all factors relevant to the investment thesis supporting buy decisions. The team's goal is to purchase issuers with solid credit profiles that offer the

potential for capital appreciation. In addition to seeking value from issue selections, they also implement strategies to take advantage of valuation opportunities across industry sectors and credit-quality tiers.

The research discipline requires the team to evaluate reported results and employ scenario analysis to project likely credit profiles going forward. The team's goal is to select companies having debt service plans that are achievable—even under extreme circumstances. The analysts believe it is extremely important to know the borrowers, not just their financials. Therefore, the analysts visit with managements at least twice per year and have regular company contact.

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**Process:** Neuberger Berman's investment process (Figure 2) begins with a screening methodology to identify the securities the firm will consider for purchase.

From the broad high-yield-issue universe, Neuberger Berman eliminates issues that do not meet the firm's standards—such as illiquid issues and defaulted securities. After the first screen issues are sorted, the results are reviewed according to credit standing (ratings and credit statistics) and relative yield. Once the team members have identified the most promising investment candidates, they apply their in-depth fundamental credit analysis and valuation process to select actual portfolio holdings.

The team seeks to manage individual issuer risk through diversification. The portfolio generally holds 100–150 issues, and the maximum security weighting is 5 percent (however, generally 1 percent per issuer, on average, is held). The issue limits result in sufficient diversification, while allowing the flexibility to concentrate on the most promising investment opportunities.

For industries, the maximum weight generally is three times the industry weight (as represented in the benchmark index). The team also employs a proprietary liquidity coding system with a liquidity score ascribed to each security. This system allows the team to monitor the overall liquidity of the portfolio.

The co-portfolio managers have broad experience in the high-yield market and extensive experience managing high-yield assets together. The co-portfolio managers rely on the input provided by their high-yield team members, who assist in asset allocation, portfolio construction, research, and security selection ideas. The high-yield team includes dedicated traders responsible for executing all buy and sell recommendations (as communicated by the portfolio managers).



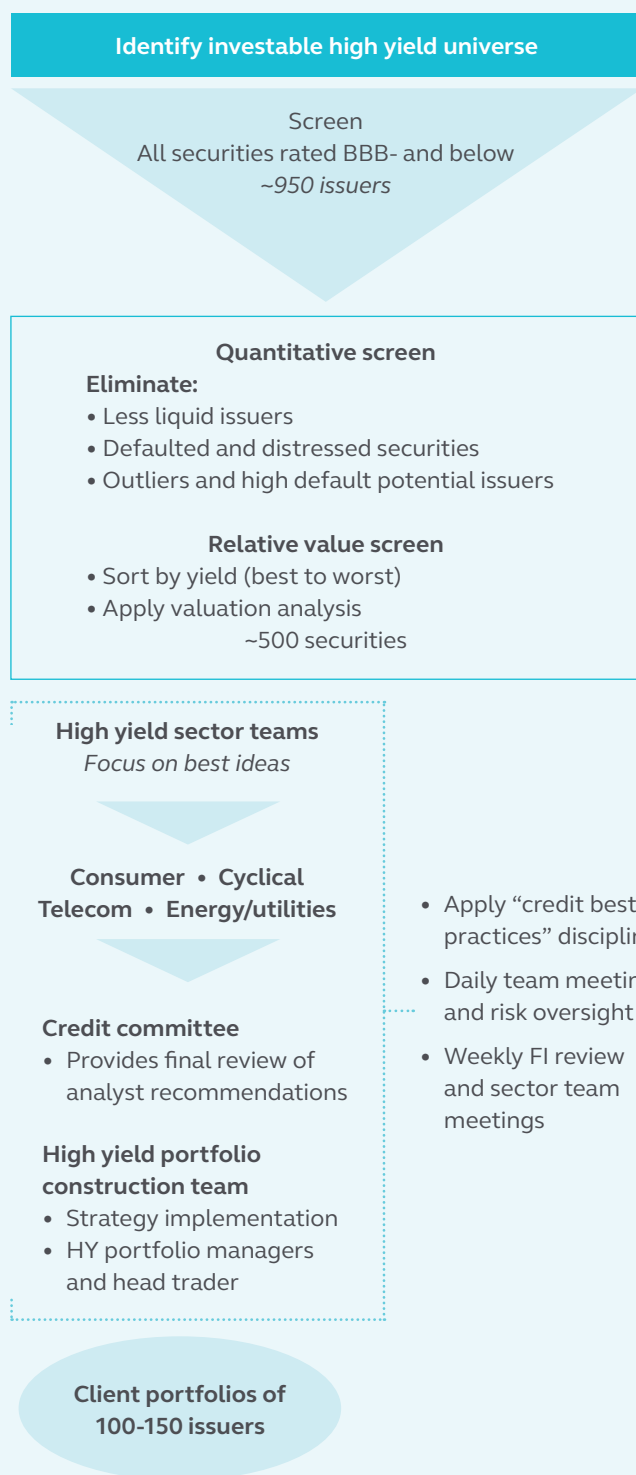
**Neuberger Berman portfolio management team**

**Ann H. Benjamin** has been with Neuberger Berman (and its predecessors) since 1997. She earned a B.A. in Economics from Chatham College and a Master’s in Finance from Carnegie Mellon University.

**Thomas P. O’Reilly** has been with Neuberger Berman (and its predecessors) since 1997. He earned a B.S. in Finance from Indiana University and an M.B.A. from Loyola University. He has earned the right to use the Chartered Financial Analyst designation.

**William (Russ) Covode** has been with Neuberger Berman since 2006. He earned a B.A. in Economics from Colorado College and an M.B.A. from the University of Chicago.

**Figure 2:**  
Neuberger Berman’s investment process



## Additional information

Carefully consider a fund's objectives, risks, charges, and expenses. Contact your financial professional or visit [principal.com](http://principal.com) or [principalfunds.com](http://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](http://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.

Fixed-income investments are subject to interest rate risk; as interest rates rise their value will decline.

Fixed-income and asset allocation investment options that invest in mortgage securities are subject to increased risk due to real estate exposure.

Lower-rated securities are subject to additional credit and default risks.

Barclays US Corporate High Yield 2% Issuer Capped Index is an unmanaged index comprised of fixed rate, non-investment grade debt securities that are dollar denominated. The index limits the maximum exposure to any one issuer to 2%.

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