Principal Global Investors Funds

Islamic Global Responsible Equity Fund

I Class December 2025

Market Review

It was a highly anticipated last month of 2025 as investors focused on a slew of economic data releases as well as take cues from the latest Federal Reserve (Fed) meeting on 2026's rate cut path. All seemingly met expectations as equity markets advanced further in December closing out a strong 2025 with most regions and sectors posting double-digit returns.

At its December meeting, the Federal Open Market Committee (FOMC) decided to lower its benchmark policy rate by 25 basis points (bps) to 3.50%-3.75%. Three officials voted to dissent—two preferred to keep rates unchanged today, while one voted for a larger 50 bps cut.

The decision marks the third interest rate cut this year, bringing policy rates down by 175 bps from the start of the easing cycle in September 2024. Chair Jerome Powell emphasized that policy is now "well-positioned" to await greater clarity in the data and to carefully assess labor market conditions and inflation trends. This signals that an extended pause is likely before the Fed resumes its easing cycle and delivers a few additional cuts.

The outcome of the December FOMC meeting remained a key source of market debate. In late September, consensus expectations indicated a likely December cut. However, a strong September employment report, combined with more hawkish commentary from several FOMC members, saw markets reduce the probability of a cut to just 20%. Ultimately, dovish communication ahead of the blackout period—without any pushback from Chair Powell—led markets to fully price in a cut, making the decision widely anticipated.

Interestingly though, there was a bit of mini-quantitative easing that came out of the meeting as the Fed announced plans to begin purchasing Treasury bills on December 12 to maintain ample reserves, underscoring its ability to leverage tools beyond rate policy to ensure market stability.

The second half of December featured two influential economic releases for Fed policy: employment and inflation. After limited visibility due to the U.S. government shutdown, investors are heading into the new year with a clearer picture of the Fed's likely path ahead.

Headline payroll weakness was driven by deferred resignations in federal jobs, though offset by gains in private payrolls. Overall, it reinforces the view that the labor market is cooling but not collapsing. Still, the unemployment rate is at a four-year high, a development that the Fed is unlikely to dismiss.

The absence of October data, combined with distortions in the November data collection, has made it more challenging than usual to accurately gauge the true direction of inflation. Nevertheless, headline and core inflation were much softer than expected, with core inflation near a four-year low. While some tariff-related caution remains warranted, there's little evidence of a sharp reacceleration in prices.

Taken together, the latest economic readings are likely to give doves in the Fed the upper hand, though uncertainty remains with one more inflation and employment report due before the Fed's next meeting in January 2026.

Across the pond, the European Central Bank (ECB) held policy rates steady, extending its pause for a fourth straight meeting in the current easing cycle. Economic activity has continued to grow, aided by fiscal spending and increased business capex. While ECB President Christine Lagarde reiterated that they remain in a very good place with policy, given this positive backdrop, she also noted that this place is "not static."

To conclude, the December period brought healthy returns and closed out a strong 2025 for investors. The S&P 500 was flat, while the MSCI EM Index was higher by 3.0%. The MSCI Europe Index was up 3.9%, while the MSCI Japan Index was higher by 0.5%.

Fund Review

The portfolio posted a positive absolute return of 1.8% in the month of December while outperforming its respective index. From a sector perspective, the IT and consumer staples sectors were places of strength while were partially offset by weakness in communication services and consumer discretionary. South Korea and Canada were top contributors from a country perspective while the United States and Japan lagged overall.

Portfolio Outlook and Strategy

The adage "stocks follow earnings" has never been more true than in recent years, particularly during a decade characterized by American exceptionalism. U.S. stocks have outperformed global counterparts, buoyed by superior free cash flow, earnings growth, and higher valuation multiples. However, 2025 brought a normalization of this exceptionalism and leads to the question, is there staying power for international equity leadership? The answer appears to be yes, as international fiscal policy initiatives coupled with structural changes are broadening out and increasing earnings and cash flow growth.

U.S. earnings growth and valuation multiples reached extraordinary levels, largely led by mega-cap companies, and concentration risk in the U.S. has never been more prevalent. As we head into 2026, there is a resounding case for diversification, not diworsification, to international equities and a more normal allocation to the U.S.

A decade of strong earnings growth has led the United States to be at its largest weighting in the MSCI World Index in over 30 years at >70%. Notably, 5 stocks make up a quarter of the index highlighting the efficiency of the US market and reduced opportunity for differentiated alpha. It is no longer just an innovation and earnings growth story in the U.S. as "America First" policies have prompted other nations to focus on internal development in pursuit of economic growth.

This shift is fostering a more conducive environment for local businesses. A prime example is Germany's renewed commitment to invest in physical and digital infrastructure to stimulate short-term economic growth and enhance Berlin's long-term competitiveness. Let's not forget defense spending which isn't in isolation to Germany as global counterparts, led by NATO countries, are ratcheting up this initiative to be at least 2% of GDP.

Structural change opportunities like these are driving earnings growth higher internationally and have hit an inflection point to keep pace with the U.S. Broadening earnings growth of double-digits lays the foundation for international equity leadership to stay.

Furthermore, the earnings growth of ACWI ex. US is similar to ex. Mag 7. So what? International stocks are a better diversifier than the S&P 493 for those looking to reduce Mag 7. Why? Similar growth rate but 30% lower multiple.

Risk Considerations

Investing involves risk, including possible loss of principal. Past Performance does not guarantee future return. All financial investments involve an element of risk. Therefore, the value of the investment and the income from it will vary and the initial investment amount cannot be guaranteed.

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