

Principal Funds, Inc. 2017 Tax Reporting Supplement

The enclosed information is provided to assist shareholders in preparing their 2017 tax returns. The information contained herein should not be deemed to be tax advice. Please consult your tax advisor to determine impacts to you, if any. If you have questions concerning the information we have furnished, please call us at 1-800-222-5852.

Government Obligations Percentage

A portion of the dividends paid by the following funds during 2017 was derived from investments in obligations of the U.S. government or its agencies. Some of these dividends may be exempt from state and local taxes depending on the tax laws of your individual state or local taxing authority. Some states treat income from federal agency obligations differently than income from direct federal obligations.

Fund	Direct Federal Obligations	Indirect Federal Obligations	Repurchase Agreements
PFI Bond Market Index Fund	25.37%	29.20%	0.00%
PFI Core Plus Bond Fund	5.34%	15.96%	0.00%
PFI Diversified Real Asset Fund	8.64%	0.01%	0.00%
PFI Finisterre Unconstrained Emerging Markets Bond Fund	0.02%	0.00%	0.00%
PFI Global Diversified Income Fund	0.00%	0.89%	0.00%
PFI Global Multi-Strategy Fund	0.42%	0.01%	0.00%
PFI Government & High Quality Bond Fund	3.67%	53.98%	0.00%
PFI High Yield Fund	0.03%	0.00%	0.00%
PFI Income Fund	8.42%	17.72%	0.00%
PFI Inflation Protection Fund	92.76%	0.00%	0.00%
PFI Money Market Fund	0.00%	0.00%	4.84%
PFI Multi-Manager Equity Long/Short Fund	0.62%	0.00%	0.00%
PFI Principal LifeTime 2010 Fund	6.66%	5.34%	0.00%
PFI Principal LifeTime 2015 Fund	5.63%	5.05%	0.00%
PFI Principal LifeTime 2020 Fund	4.89%	4.65%	0.00%
PFI Principal LifeTime 2025 Fund	3.97%	4.19%	0.00%
PFI Principal LifeTime 2030 Fund	3.21%	3.40%	0.00%
PFI Principal LifeTime 2035 Fund	1.89%	3.44%	0.00%
PFI Principal LifeTime 2040 Fund	1.57%	2.85%	0.00%
PFI Principal LifeTime 2045 Fund	1.23%	2.16%	0.00%
PFI Principal LifeTime 2050 Fund	0.88%	1.59%	0.00%
PFI Principal LifeTime 2055 Fund	0.62%	1.06%	0.00%
PFI Principal LifeTime 2060 Fund	0.52%	0.89%	0.00%
PFI Principal LifeTime 2065 Fund	0.52%	0.73%	0.00%
PFI Principal LifeTime Hybrid 2015 Fund	11.92%	8.72%	0.00%
PFI Principal LifeTime Hybrid 2020 Fund	10.58%	8.53%	0.00%
PFI Principal LifeTime Hybrid 2025 Fund	9.40%	8.07%	0.00%
PFI Principal LifeTime Hybrid 2030 Fund	7.84%	6.85%	0.00%
PFI Principal LifeTime Hybrid 2035 Fund	5.08%	5.85%	0.00%
PFI Principal LifeTime Hybrid 2040 Fund	3.88%	4.47%	0.00%
PFI Principal LifeTime Hybrid 2045 Fund	3.00%	3.44%	0.00%
PFI Principal LifeTime Hybrid 2050 Fund	2.16%	2.48%	0.00%
PFI Principal LifeTime Hybrid 2055 Fund	1.55%	1.78%	0.00%
PFI Principal LifeTime Hybrid 2060 Fund	1.08%	1.24%	0.00%
PFI Principal LifeTime Hybrid 2065 Fund	1.37%	1.58%	0.00%
PFI Principal LifeTime Hybrid Income Fund	14.57%	11.81%	0.00%
PFI Principal LifeTime Strategic Income Fund	6.71%	6.47%	0.00%
PFI SAM Balanced Portfolio	2.99%	6.72%	0.00%
PFI SAM Conservative Balanced Portfolio	3.90%	10.16%	0.00%
PFI SAM Conservative Growth Portfolio	0.98%	2.96%	0.00%
PFI SAM Flexible Income Portfolio	6.78%	11.94%	0.00%
PFI SAM Strategic Growth Portfolio	0.03%	0.48%	0.00%
PFI Short-Term Income Fund	0.25%	0.03%	0.00%

PFI = Principal Funds, Inc.

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Alternative Minimum Tax

The percentage of 2017 exempt interest dividends subject to the Federal Alternative Minimum Tax is summarized below.

Fund	AMT
PFI California Municipal Fund	8.28%
PFI Opportunistic Municipal Fund	16.14%
PFI Tax-Exempt Bond Fund	10.35%

Qualified Dividend Income & Dividends Received Deduction

Qualified Dividend Income ("QDI"). QDI received and distributed by a fund is eligible to be taxed at lower rates. QDI is generally distributed from domestic corporations and certain qualified foreign corporations that meet certain holding requirements. The ordinary dividends that may qualify for the lower tax rates are shown in Box 1b of Form 1099-DIV. Shareholders must meet the holding period requirement to qualify for the lower ordinary dividend tax rates. To be eligible to treat all or a portion of the fund's dividend as qualified, a shareholder must have held the fund's shares for at least 61 days during the 121-day period surrounding the ex-dividend date. For additional information, see IRS Publication 550 at www.irs.gov.

Dividends Received Deduction ("DRD"). For corporate shareholders, the percentage of ordinary income distributions (dividend income and short-term gains, if any) for 2017, that qualifies for the DRD are as follows:

Fund	QDI	DRD	Fund	QDI	DRD
PFI Blue Chip Fund	100.00%	100.00%	PFI Principal LifeTime 2020 Fund	33.86%	17.20%
PFI Capital Securities Fund	59.95%	27.24%	PFI Principal LifeTime 2025 Fund	37.17%	18.68%
PFI Core Plus Bond Fund	9.03%	5.42%	PFI Principal LifeTime 2030 Fund	34.74%	15.19%
PFI Diversified International Fund	74.39%	0.00%	PFI Principal LifeTime 2035 Fund	36.71%	17.81%
PFI Diversified Real Asset Fund	38.79%	11.23%	PFI Principal LifeTime 2040 Fund	41.12%	20.02%
PFI Dynamic Floating Rate High Income Fund	0.09%	0.00%	PFI Principal LifeTime 2045 Fund	41.63%	19.81%
PFI EDGE MidCap Fund	100.00%	100.00%	PFI Principal LifeTime 2050 Fund	44.84%	21.62%
PFI Equity Income Fund	100.00%	81.77%	PFI Principal LifeTime 2055 Fund	43.75%	20.58%
PFI Finisterre Unconstrained Emerging Markets Bond Fund	4.33%	0.00%	PFI Principal LifeTime 2060 Fund	40.44%	17.63%
PFI Global Diversified Income Fund	21.37%	10.51%	PFI Principal LifeTime 2065 Fund	42.93%	21.60%
PFI Global Multi-Strategy Fund	27.89%	15.10%	PFI Principal LifeTime Hybrid 2015 Fund	28.70%	18.41%
PFI Global Opportunities Equity Hedged Fund	100.00%	97.20%	PFI Principal LifeTime Hybrid 2020 Fund	38.02%	24.87%
PFI Global Opportunities Fund	27.47%	13.87%	PFI Principal LifeTime Hybrid 2025 Fund	43.37%	28.56%
PFI Global Real Estate Securities Fund	6.19%	0.46%	PFI Principal LifeTime Hybrid 2030 Fund	49.03%	32.49%
PFI High Yield Fund	2.93%	2.21%	PFI Principal LifeTime Hybrid 2035 Fund	50.44%	33.96%
PFI High Yield Fund I	0.28%	0.22%	PFI Principal LifeTime Hybrid 2040 Fund	54.83%	36.71%
PFI Income Fund	5.68%	5.68%	PFI Principal LifeTime Hybrid 2045 Fund	58.65%	39.50%
PFI International Emerging Markets Fund	85.49%	0.00%	PFI Principal LifeTime Hybrid 2050 Fund	58.87%	38.90%
PFI International Equity Index Fund	73.87%	0.00%	PFI Principal LifeTime Hybrid 2055 Fund	59.04%	38.70%
PFI International Fund I	100.00%	0.00%	PFI Principal LifeTime Hybrid 2060 Fund	39.17%	22.19%
PFI International Small Company Fund	30.99%	0.00%	PFI Principal LifeTime Hybrid 2065 Fund	65.87%	47.75%
PFI LargeCap Growth Fund	39.75%	34.48%	PFI Principal LifeTime Hybrid Income Fund	18.62%	11.61%
PFI LargeCap Growth Fund I	100.00%	100.00%	PFI Principal LifeTime Strategic Income Fund	18.37%	9.11%
PFI LargeCap Growth Fund II	19.62%	18.98%	PFI Real Estate Allocation Fund	2.81%	0.21%
PFI LargeCap S&P 500 Index Fund	100.00%	100.00%	PFI Real Estate Securities Fund	5.34%	0.00%
PFI LargeCap Value Fund	42.98%	41.40%	PFI SAM Balanced Portfolio	44.47%	26.84%
PFI LargeCap Value Fund III	87.81%	77.64%	PFI SAM Conservative Balanced Portfolio	29.23%	18.08%
PFI MidCap Fund	100.00%	100.00%	PFI SAM Conservative Growth Portfolio	46.21%	26.31%
PFI MidCap Growth Fund III	15.96%	15.06%	PFI SAM Flexible Income Portfolio	23.18%	16.85%
PFI MidCap S&P 400 Index Fund	84.09%	81.27%	PFI SAM Strategic Growth Portfolio	42.83%	20.14%
PFI MidCap Value Fund I	35.19%	33.23%	PFI Short-Term Income Fund	0.32%	0.32%
PFI MidCap Value Fund III	53.45%	44.43%	PFI SmallCap Fund	28.07%	24.95%
PFI Multi-Manager Equity Long/Short Fund	37.40%	27.53%	PFI SmallCap Growth Fund I	6.87%	6.17%
PFI Origin Emerging Markets Fund	100.00%	0.00%	PFI SmallCap S&P 600 Index Fund	55.82%	55.37%
PFI Overseas Fund	83.99%	0.36%	PFI SmallCap Value Fund II	41.05%	38.70%
PFI Preferred Securities Fund	75.89%	42.22%	PFI Small-MidCap Dividend Income Fund	75.27%	57.46%
PFI Principal Capital Appreciation Fund	100.00%	100.00%	PFI SystematEx International Fund	79.06%	0.00%
PFI Principal LifeTime 2010 Fund	25.18%	12.80%	PFI SystematEx Large Value Fund	100.00%	100.00%
PFI Principal LifeTime 2015 Fund	28.79%	14.76%			

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Foreign Tax

Foreign source income is the income earned by a fund from investments in foreign securities. Many countries impose a tax on income earned by investors beyond their borders. These taxes are paid by the fund. The following funds have elected to pass-through to shareholders the foreign taxes paid. Accordingly, this permits a shareholder to either take a federal income tax credit or a deduction from gross income. The amount of foreign tax credit that is utilized by a shareholder may be limited due to general credit limitation rules as well as a reduction in foreign source income associated with qualified dividend income. The percentage of the foreign source income that is qualified dividend income is shown in the Qualified Dividend Income table of this Tax Reporting Supplement. Refer to the IRS Form 1116 instructions for additional information regarding foreign tax credits.

The information below summarizes the portion of income that was derived from foreign sources with regard to the applicable fund.

<u>Fund</u>	<u>Foreign Source Income</u>	<u>Foreign Tax Paid</u>
PFI Diversified International Fund	99.33%	\$ 0.0315
PFI International Emerging Markets Fund	98.85%	\$ 0.0404
PFI International Equity Index Fund	89.54%	\$ 0.0261
PFI International Fund I	98.90%	\$ 0.0314
PFI International Small Company Fund	43.94%	\$ 0.0220
PFI Origin Emerging Markets Fund	99.00%	\$ 0.0357
PFI Overseas Fund	80.07%	\$ 0.0259
PFI Principal LifeTime 2010 Fund	8.20%	\$ 0.0034
PFI Principal LifeTime 2015 Fund	9.95%	\$ 0.0032
PFI Principal LifeTime 2020 Fund	12.81%	\$ 0.0054
PFI Principal LifeTime 2025 Fund	14.90%	\$ 0.0050
PFI Principal LifeTime 2030 Fund	16.86%	\$ 0.0074
PFI Principal LifeTime 2035 Fund	21.28%	\$ 0.0074
PFI Principal LifeTime 2040 Fund	23.76%	\$ 0.0100
PFI Principal LifeTime 2045 Fund	24.95%	\$ 0.0085
PFI Principal LifeTime 2050 Fund	26.66%	\$ 0.0107
PFI Principal LifeTime 2055 Fund	27.33%	\$ 0.0095
PFI Principal LifeTime 2060 Fund	28.49%	\$ 0.0101
PFI Principal LifeTime 2065 Fund	31.48%	\$ 0.0073
PFI Principal LifeTime Hybrid 2015 Fund	13.56%	\$ 0.0035
PFI Principal LifeTime Hybrid 2020 Fund	16.68%	\$ 0.0045
PFI Principal LifeTime Hybrid 2025 Fund	19.94%	\$ 0.0054
PFI Principal LifeTime Hybrid 2030 Fund	22.26%	\$ 0.0062
PFI Principal LifeTime Hybrid 2035 Fund	24.61%	\$ 0.0069
PFI Principal LifeTime Hybrid 2040 Fund	27.10%	\$ 0.0075
PFI Principal LifeTime Hybrid 2045 Fund	28.62%	\$ 0.0079
PFI Principal LifeTime Hybrid 2050 Fund	30.20%	\$ 0.0083
PFI Principal LifeTime Hybrid 2055 Fund	31.27%	\$ 0.0085
PFI Principal LifeTime Hybrid 2060 Fund	28.62%	\$ 0.0086
PFI Principal LifeTime Hybrid 2065 Fund	32.68%	\$ 0.0070
PFI Principal LifeTime Hybrid Income Fund	6.74%	\$ 0.0018
PFI Principal LifeTime Strategic Income Fund	5.37%	\$ 0.0021
PFI SAM Balanced Portfolio	11.47%	\$ 0.0050
PFI SAM Conservative Balanced Portfolio	6.50%	\$ 0.0026
PFI SAM Conservative Growth Portfolio	16.15%	\$ 0.0093
PFI SAM Flexible Income Portfolio	0.58%	\$ 0.0002
PFI SAM Strategic Growth Portfolio	21.55%	\$ 0.0139
PFI SystematEx International Fund	93.35%	\$ 0.0287

Reallocation of Principal Funds, Inc. Distributions: Return of Capital Redesignation

A portion of the ordinary income and/or long-term capital gains dividends paid by Principal Funds, Inc. – Global Opportunities Equity Hedged Fund and Principal Funds, Inc. - Money Market Fund have been redesignated as non-taxable return of capital. Your Form 1099-DIV reports the proper amount of “nondividend distribution” for income tax purposes. If a return of capital was reported to you, an adjustment to the basis of your shares will be necessary.

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Tax-Exempt Income by State

A portion of the dividends you received in 2017 may be exempt from state and local taxes, depending on the tax laws of your individual state or local taxing authority. For this purpose, a percentage breakdown of income by state or U.S. possession for 2017 is provided below. For shareholders residing in the state of California, payments of exempt interest-dividends on federally tax-exempt non-California municipal bonds are being reported to the California Franchise Tax Board (FTB) as required under Revenue & Taxation Code (R&TC) Section 18639.

State	PFI California Municipal Fund	PFI Opportunistic Municipal Fund	PFI Tax- Exempt Bond Fund	State	PFI California Municipal Fund	PFI Opportunistic Municipal Fund	PFI Tax- Exempt Bond Fund
Alabama	0.62%	2.44%	3.33%	Nebraska	0.00%	0.00%	0.99%
Alaska	0.00%	0.00%	0.51%	Nevada	0.00%	1.66%	1.45%
Arizona	0.00%	3.95%	1.90%	New Hampshire	0.00%	0.00%	0.32%
Arkansas	0.00%	0.00%	0.00%	New Jersey	0.00%	7.07%	3.22%
California	97.75%	12.64%	17.86%	New Mexico	0.00%	0.00%	0.00%
Colorado	0.00%	3.13%	1.20%	New York	0.00%	5.09%	7.98%
Connecticut	0.00%	3.20%	2.89%	North Carolina	0.00%	1.12%	0.35%
Delaware	0.00%	0.00%	0.00%	North Dakota	0.00%	0.00%	0.00%
District of Columbia	0.00%	0.02%	1.76%	Northern Mariana Islands	0.00%	0.00%	0.00%
Florida	0.00%	1.09%	1.77%	Ohio	0.00%	6.52%	5.34%
Georgia	0.00%	1.55%	0.93%	Oklahoma	0.00%	1.60%	0.63%
Guam	0.60%	0.00%	0.00%	Oregon	0.00%	0.53%	0.00%
Hawaii	0.00%	0.00%	0.00%	Pennsylvania	0.00%	3.67%	2.04%
Idaho	0.00%	0.00%	0.83%	Puerto Rico	0.00%	0.00%	0.00%
Illinois	0.00%	14.78%	14.90%	Rhode Island	0.00%	0.00%	0.00%
Indiana	0.00%	0.68%	1.24%	South Carolina	0.00%	1.15%	1.74%
Iowa	0.00%	0.00%	0.44%	South Dakota	0.00%	0.55%	0.55%
Kansas	0.00%	0.00%	0.35%	Tennessee	0.00%	2.34%	1.31%
Kentucky	0.00%	0.00%	1.26%	Texas	0.00%	9.16%	8.67%
Louisiana	0.00%	3.39%	3.08%	Utah	0.00%	0.42%	0.22%
Maine	0.00%	0.91%	0.03%	Vermont	0.00%	0.03%	0.00%
Maryland	0.00%	1.04%	0.59%	Virgin Islands	1.03%	0.71%	0.38%
Massachusetts	0.00%	0.00%	2.09%	Virginia	0.00%	1.13%	1.74%
Michigan	0.00%	1.25%	0.82%	Washington	0.00%	1.04%	1.60%
Minnesota	0.00%	0.88%	0.95%	West Virginia	0.00%	0.16%	0.47%
Mississippi	0.00%	0.00%	0.00%	Wisconsin	0.00%	2.90%	1.85%
Missouri	0.00%	1.36%	0.42%	Wyoming	0.00%	0.00%	0.00%
Montana	0.00%	0.84%	0.00%				

Long-Term Capital Gain Distribution

Certain funds distributed long-term capital gain dividends during the calendar year ended December 31, 2017. Unless otherwise designated, long-term capital gain dividends are subject to a maximum tax rate of 20-percent, 15-percent, or 0-percent, depending on the shareholder's taxable income. To the extent necessary to distribute such capital gains, certain funds may also utilize, and hereby designate, earnings and profits distributed to shareholders on redemptions of shares as part of the Dividends Paid Deduction.

Unrecaptured Section 1250 Gain Distribution

Principal Funds, Inc. – Real Estate Securities Fund distributed Unrecaptured Section 1250 gains, in addition to long-term capital gains in 2017. Unrecaptured Section 1250 gains are gains from the sale of depreciable property that are subject to a maximum tax rate of 25%.

Tax Information Disclosure

Certain funds may invest in securities that reclassify income distributions after you have received your original Form 1099-DIV. Although at the time of mailing we supplied you with the most current information, reclassifications from income to return of capital, may occur as a result of REIT (real estate investment trust) or MLP (master limited partnership) investments. Once the REITs or MLPs notify Principal Funds, Inc., of any reclassifications, a determination will be made if such reclassifications require 1099-DIVs to be amended. Amended 1099-DIVs will be sent by March 20, 2018.

The latest tax reporting supplement is available on Principal's Tax Center website.
Website: <https://www.principalfunds.com/taxcenter>