

## Morgan Stanley Investment Funds

# European Equity Alpha Fund

ACTIVE FUNDAMENTAL EQUITY | EUROPEAN EQUITY TEAM | MONTHLY COMMENTARY | 31 OCTOBER 2019

### Performance Review

In the one month period ending 31 October 2019, the Fund's I shares returned 2.08% (net of fees)<sup>1</sup>, while the benchmark returned 0.86%.

The portfolio's stock selection in information technology (SAP, ASML), financials (Prudential, Lloyds, BNP), materials (Sika) and health care (Fresenius, Bayer, Novo Nordisk) all contributed positively to performance in the month. The main detractor from performance was an overweight position in the consumer staples sector.

### Market Review

The eurozone economy managed a modest expansion in the third quarter of 2019. According to Eurostat's flash estimate, gross domestic product grew 0.2% in the euro area and 0.3% in the European Union (EU) quarter-over-quarter, beating expectations that the region was stagnating. However, data in October showed a further loss of momentum. The IHS Markit Eurozone Manufacturing PMI registered 45.9 in October, up slightly from 45.7 in September, as new orders fell sharply, production and purchasing activity were cut, and job shedding accelerated. Germany remained the hardest hit by weakening international and domestic demand, Brexit concerns and U.S. trade policy uncertainty. The eurozone's services sector continued to expand but at an overall weak pace. The IHS Markit Eurozone PMI Services Business Activity Index recorded a small improvement from 51.6 in September to 52.2 in October.

Inflation fell further below the European Central Bank's (ECB) target. Eurostat's flash estimate shows consumer prices increased 0.7% from October a year earlier, compared to 0.8% in September. Excluding food, energy, alcohol and tobacco, core inflation is estimated at 1.1% for the annual period ended October, a slight uptick from 1.0% in September. In a separate report, Eurostat said unemployment was 7.5% in the euro area and 6.3% in the EU in September, stable from the August readings for each bloc.

The October ECB meeting was President Draghi's final meeting, as Christine Lagarde's term begins on November 1. The ECB left rates unchanged, as expected, and maintained its forward guidance that rates would stay low until inflation rises toward the 2% target.

In the U.K., manufacturing and services sector activity remained under pressure from Brexit. Although the IHS Markit/CIPS U.K. Manufacturing PMI rose to 49.6 in October from 48.3 in September, much of the improvement was due to Brexit stockpiling ahead of the October 31 deadline, which was later postponed. Service sector activity was stagnant, with the IHS Markit/CIPS U.K. Services PMI Business Activity Index increasing slightly to 50.0 in October from 49.5 in September. New business continued to decline and firms cut jobs, as Brexit concerns continued to stifle international and domestic demand.

U.K. unemployment increased fractionally in the July to August period to 3.9% from 3.8% in the prior three months but remained below the 4.0% rate a year ago, according to the Office for National Statistics (ONS). The ONS also estimated annual growth in wages including bonuses was 3.8% before inflation and 1.9% after adjusting for inflation. Excluding bonuses, workers' annual pay growth was 3.8% before inflation and 2.0% in inflation-adjusted terms. Inflation was unchanged in September from August, up 1.7% from a year earlier, and remained below the Bank of England's 2% target. (There was no Monetary Policy Committee meeting in October.)

European equities stayed positive in October, although currency effects had a large impact on returns. The MSCI Europe Index was up 3.21% in USD and up 0.86% in euros. Prime Minister Johnson and the EU agreed to a deal, but Parliament withheld its support to force an extension, which the EU granted until January 31, 2020. Additionally, the U.K. will hold a general election in December. Sterling rallied sharply as a no-deal Brexit appeared to be off the table. Macro indicators remain under pressure from trade war and Brexit woes, with signs of labour market weakness now taking hold in the U.K. and the eurozone. As Christine Lagarde takes leadership of the ECB, the limitations of monetary policy remain a concern.

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<sup>1</sup> Source: Morgan Stanley Investment Management Limited. Data as of 31 October 2019.

European government bond yields rose over the month in response to internal dissent within the ECB over the forthcoming bond buying programme, easing trade tensions and progress in Brexit negotiations. U.K., German, French, Spanish and Italian 10-year yields ended the month higher.

## Portfolio Activity

There was no significant activity over the month.

## Strategy and Outlook

We continue to believe that careful stock selection can be an important source of investment performance. We apply a disciplined and proven investment process to identify individual stocks that we feel are attractively valued relative to their future prospects. Typically, the companies on which we focus are characterised by strong business models, financial strength and management teams of demonstrable competence.

**For further information, please contact your Morgan Stanley Investment Management representative.**

### FUND FACTS

#### Launch date

05 March 1991

#### Base currency

Euro

#### Index

MSCI Europe (Net) Index

### 12 Month Performance Periods to Latest Month End (%)

	OCTOBER '18 - OCTOBER '19	OCTOBER '17 - OCTOBER '18	OCTOBER '16 - OCTOBER '17	OCTOBER '15 - OCTOBER '16	OCTOBER '14 - OCTOBER '15
MS INV European Equity Alpha Fund - I Shares	12.63	-7.72	17.55	-9.40	9.06
MSCI Europe (Net) Index	12.63	-5.76	19.52	-6.76	13.19

**Past performance is not a reliable indicator of future results.** Returns may increase or decrease as a result of currency fluctuations. All performance data is calculated NAV to NAV, net of fees, and does not take account of commissions and costs incurred on the issue and redemption of units. The sources for all performance and Index data is Morgan Stanley Investment Management. **Please visit our website [www.morganstanley.com/im](http://www.morganstanley.com/im) to see the latest performance returns for the fund's other share classes.**

### Share Class I Risk and Reward Profile

Lower Risk

Higher Risk



Potentially Lower Rewards

Potentially Higher Rewards

The risk and reward category shown is based on historic data.

- Historic figures are only a guide and may not be a reliable indicator of what may happen in the future.
- As such this category may change in the future.
- The higher the category, the greater the potential reward, but also the greater the risk of losing the investment. Category 1 does not indicate a risk free investment.
- The fund is in this category because it invests in company shares and the fund's simulated and/or realised return has experienced high rises and falls historically.
- The fund may be impacted by movements in the exchange rates between the fund's currency and the currencies of the fund's investments.

This rating does not take into account other risk factors which should be considered before investing, these include:

- The fund relies on other parties to fulfill certain services, investments or transactions. If these parties become insolvent, it may expose the fund to financial loss.
- There may be an insufficient number of buyers or sellers which may affect the fund's ability to buy or sell securities.
- Past performance is not a reliable indicator of future results. Returns may increase or decrease as a result of currency fluctuations. The value of investments and the income from them can go down as well as up and investors may lose all or a substantial portion of his or her investment.
- The value of the investments and the income from them will vary and there can be no assurance that the Fund will achieve its investment objectives.
- Investments may be in a variety of currencies and therefore changes in rates of exchange between currencies may cause the value of investments to decrease or increase. Furthermore, the value of investments may be adversely affected by fluctuations in exchange rates between the investor's reference currency and the base currency of the investments.

Please refer to the Prospectus for full risk disclosures. All data as of 31 October 2019 and subject to change daily.

## INDEX INFORMATION

The **MSCI Europe (Net) Index** is a free float-adjusted market capitalization index that is designed to measure developed market equity performance in Europe. As of September 2002, the MSCI Europe Index consisted of the following 16 developed market country indices: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, and the United Kingdom.

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