Morgan Stanley

INVESTMENT MANAGEMENT

Morgan Stanley Funds (UK) Global Balanced Sustainable Fund

Restriction Screening Policy

SOLUTIONS & MULTI ASSET | GLOBAL BALANCED RISK CONTROL TEAM | February 2022

MARKETING COMMUNICATION

Restriction screening is intentionally avoiding investments in certain sectors or issuers based on values or risk-based criteria. Our restriction screening process intends to avoid investment in issuers that are not aligned with our core investment principles or our sustainable investing philosophy, and screen out securities of issuers that are found to be in breach of minimum standards of responsible business practice based on international norms. To do so we utilise a global 3rd-party ESG data provider, supported by our own proprietary internal Environmental Social Governance (ESG) research. This policy applies to the **Morgan Stanley Funds (UK) Global Balanced Sustainable Fund**. If a company held within the portfolio subsequently qualifies to be excluded, we have an internal process in place to reflect the change in circumstances (see restriction policy compliance).

i) Fossil Fuels

We recognise that climate change poses significant risks to the global economy and therefore look to exclude issuers with high exposure to carbon-intensive activities, as listed below, to mitigate our climate-related financial risks.

Coal

We estimate that coal has the highest global warming potential of all fossil fuels and poses a significant stranded asset risk from climate policy.

We exclude issuers that derive **5% or more of their revenue** from the mining of thermal coal (including lignite, bituminous, anthracite and steam coal) and from the sale of coal to external parties.

Oil Sands

We estimate that oil sands require the most expensive and least efficient extraction/refining methods, such as surface mining or steam injection. Furthermore, we estimate that oil sands also have higher Green House Gas (GHG) potency (kg per GJ) than conventional fossil fuels and have significant negative environmental and social impacts, which can in turn generate complex legal, regulatory and social risks to shareholder value.

We exclude issuers that derive **5% or more of their revenues** from the extraction of oil sands.

ii) Controversial Weapons

In our view, controversial weapons are indiscriminate and excessively injurious, often resulting in civilian casualties and causing a disproportionate level of pain and suffering. These weapons may also pose a long-term risk to civilian population from unexploded ordnance, which can detonate long after its initial use.

Our approach to controversial weapons aims to be consistent with the following campaigns, conventions and treaties:

- **Anti-personnel mines** – Anti-Personnel Mine Ban Convention (or Ottawa Treaty)
- **Biological weapons** – Biological Weapons Convention
- **Blinding laser weapons** – Convention on Certain Conventional Weapons, Protocol IV on Blinding Laser Weapons
- **Chemical weapons** – Chemical Weapons Convention
- **Cluster munitions** – Convention on Cluster Munitions (or Oslo Treaty)
- **Depleted uranium weapons** - International Coalition to Ban Uranium Weapons
- **Incendiary weapons** – Convention on Certain Conventional Weapons Protocol III on Prohibitions or Restrictions on the Use of Incendiary Weapons

  Non-detectable fragments – Convention on Certain Conventional Weapons, Protocol I on Non-Detectable Fragments

We exclude issuers that have any tie to the manufacturing or production of controversial weapons or intended use components, or are a **majority owner of, or majority-owned by**, controversial weapons companies.

iii) Civilian Firearms

We take the view that although firearms can in some cases support rightful and peacekeeping activities, their use by civilians, particularly in the case of automatic and semi-automatic firearms, poses a threat to society as there is a high risk that they might end up being used illegally or indiscriminately against other people, causing mass wounding or death.

We exclude issuers that **manufacture** automatic firearms and/or semi-automatic firearms for the civilian market.

iv) Tobacco

We believe tobacco has significant negative social and economic impacts and is considered the single greatest preventable cause of death. As a result, tobacco companies are exposed to significant ongoing financial and reputational risk from increased regulation. Moreover, in our view, there is no reasonable level of tobacco consumption and we believe engagement with the tobacco industry will not lead to significant change.

We exclude issuers that manufacture tobacco products, and companies that derive **10% or more of their revenues** from the supply, distributions, or retail sales of tobacco products.

v) Gambling

Gambling activities embed a high risk of generating direct negative social impacts, in particular addiction and over-indebtedness, as well as indirect impacts especially for more vulnerable groups, including reduced familial stability and household income and increased propensity to crime.

We exclude issuers that derive **10% or more of their revenue** from gambling related business activities.

vi) Adult entertainment

We take the view that adult entertainment is associated with social risks in the form of the degradation of human rights and dignity, and potentially promotes negative behaviour involving physical and/or emotional duress and even violence, especially against women.

We exclude issuers that derive **10% of more of their revenue** from adult entertainment activities.

vii) ESG Controversies

We expect the issuers we invest in to comply with minimum standards and safeguards around human rights, labour rights, environment, business ethics and corruptions as defined by international norms such as the United Nations Global Compact.

We exclude issuers with the **most severe** ESG controversy cases, based on assessments from 3rd-party ESG providers and where we believe appropriate remedial action has not been taken. Additionally, we exclude issuers in ongoing **severe** structural controversy cases related to environmental harm and where we believe appropriate remedial action has not been taken.

Restriction Policy Compliance

This restriction screening policy applies to the physical investments held directly in the portfolios. The restriction screening criteria will not be applied to investments in which the portfolio managers do not have direct control of the underlying holdings, for example collective investment schemes or long derivatives exposures to indices. Investments that are held by the portfolios, but become restricted after they are acquired for the portfolios, will be sold. Such sales will take place over a period to be determined by the portfolio managers, taking into account the best interests of the shareholders of the portfolios.

We review this policy periodically and any changes will be reflected in this document. In addition to ongoing monitoring by the portfolio managers, Morgan Stanley Investment Management's Portfolio Surveillance team codes in the restricted criteria into the firm's surveillance system, and uses an automated process to monitor adherence to investment guidelines including pre and post-trade guideline monitoring and exception-based screening, and informs the Portfolio Surveillance team of possible guideline violations for this policy.

Engagement

Please note, in designing our restriction screening policy we considered whether there is an opportunity for engagement on ESG issues and whether an issuer may be able to transition its business activities or practices to a more sustainable model. We regularly engage with issuers on materially important corporate governance, environmental and/or social issues. For example, we engage with management teams broadly around the topics of decarbonisation and climate risk including those issuers involved in residual fossil fuel-related activities not covered by this policy.

RISK CONSIDERATIONS

Past performance is not a guarantee of future performance. The value of the investments and the income from them can go down as well as up and an investor may not get back the amount invested. 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.

The Asset Allocation strategies provide the Investment Adviser with wide discretion to allocate between different asset classes. From time to time, the Asset Allocation may have significant exposure to a single or limited number of fixed income or equity asset classes. Accordingly, the relative relevance of the risks associated with equity securities, Fixed Income Securities and derivatives will fluctuate over time.
Funds that specialise in a particular region or market sector are more risky than those which hold a very broad spread of investments. Where portfolio concentration is in one sector it is subject to greater risk and volatility than other portfolios that are more diversified and the value of its shares may be more substantially affected by economic events in the real estate industry.

Investments in derivative instruments carry certain inherent risks such as the risk of counter party default and before investing you should ensure you fully understand these risks. Use of leverage may also magnify losses as well as gains to the extent that leverage is employed.

These investments are designed for investors who understand and are willing to accept these risks. Performance may be volatile, and an investor could lose all or a substantial portion of his or her investment.

- The value of bonds are likely to decrease if interest rates rise and vice versa.
- The value of financial derivative instruments are highly sensitive and may result in losses in excess of the amount invested by the Sub-Fund.
- Issuers may not be able to repay their debts, if this happens the value of your investment will decrease. This risk is higher where the fund invests in a bond with a lower credit rating.
- The fund relies on other parties to fulfil 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.
- Commodity investments can change significantly and quickly in value as a large variety of factors affect them.
- There are increased risks of investing in emerging markets as political, legal and operational systems may be less developed than in developed markets.

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