Morgan Stanley Investment Funds

Calvert Sustainable Climate Aligned Fund

Calvert

Performance Review

In the three month period ending 30 September 2023, the Fund's Z shares returned -4.51% (net of fees)[1], while the benchmark returned -3.46%.

Calvert Sustainable Climate Aligned Fund (the Fund) is designed to provide long-term capital appreciation by investing in companies that are involved in economic activities that address climate transition and/or are aligned with the long-term decarbonization objectives of the 2015 Paris Agreement. The Fund uses a proprietary quantitative and qualitative investment process to identify environmental leaders and companies aligned with these climate objectives. The Fund is optimized to manage active risk and to maintain a substantially lower carbon footprint than the benchmark, the MSCI World Index.

The biggest detractor from portfolio returns in the third quarter was an underweight to the communication services sector. The portfolio does not hold Alphabet or Meta Platforms, which had positive returns during the period. Alphabet does not meet the portfolio's methodology for environmental or climate leadership, and Meta Platforms is not considered eligible for investment according to the Calvert Principles for Responsible Investment due to ongoing data privacy and governance concerns.

The portfolio's underweight to the energy sector also impacted returns negatively. The underweight is driven by the portfolio's alignment with the Paris-Aligned benchmark methodology, which requires the exclusion of companies with significant revenue derived from fossil fuels.

Positive drivers of the portfolio's performance were its overweight and relative stock selection in the information technology and health care sectors. Within information technology, our stock picks in the IT services and software industries boosted returns. Through our Principles for Responsible Investment and the Fund's environmental and climate leadership methodology, we avoided certain names like Unity Software, WiseTech Global and Fortinet that had negative performance during the period, but homed in on names like Atlassian and Intuit that performed strongly over the quarter and boosted our overall performance. Atlassian is a leader among peers for its greenhouse gas (GHG) reduction strategy, while Intuit is an overall environmental leader for its efforts on GHG efficiency and reducing GHGs — the company has net-zero targets aligned with limiting global warming to 1.5 degrees according to the Science Based Targets Initiative. In IT services, IBM and Cognizant Technology Solutions drove positive returns. IBM is a leader in providing energy-efficient products and services to help clients reduce energy consumption and costs, and Cognizant has a strong net-zero strategy with demonstrated interim progress.

In health care, relative stock selection in the pharmaceuticals and health care equipment and supplies industries boosted performance. In pharmaceuticals, Eli Lilly and Company and Chugai Pharmaceutical Co. had strong returns. Eli Lilly is a member of the RE100 global corporate renewable energy initiative, with a commitment to secure 100% of its electricity from renewable sources by 2030 and to make its own operations carbon neutral within the same time frame. It has also reduced its Scope 1 and 2 emissions more than 7% year-over-year. Chugai Pharmaceutical is targeting 100% renewable energy by 2025, absolute emissions reduction targets for Scope 1 and 2, and is working toward zero waste and reduced water consumption.

In health care equipment and services, returns were bolstered by relative stock selection, such as holding Cochlear Limited, a leader in GHG emissions reduction and efficiency, and avoiding underperforming names such as Medtronic and Intuitive Surgical, which do not meet the portfolio's environmental and climate leadership methodology.

Market Review

In the third quarter of 2023, the equity rally that had previously defied rising interest rates and shaken off three of the largest bank failures in U.S. history ended, as many investors — lured by higher interest rates, particularly for long-term U.S. Treasuries — deserted riskier stocks in favor of relatively risk-free government bonds.

The period saw record-low unemployment, strong job creation and robust consumer spending. While these trends are typically good news stories, in this environment they have been seen as bad news for inflation and fuel for further rate hikes that would weigh on stock prices. As the U.S. Federal Reserve (Fed) repeatedly confirmed its intent to bring inflation down to 2%, investors' anticipation of "higher for longer" interest rates intensified during the quarter.

In the first month of the period, however, the global stock rally that had started in January — fueled largely by exuberance over artificial intelligence (AI) technology — continued. The number of economists and pundits predicting a soft landing for the U.S. economy grew larger. When the Fed hiked interest rates 25 basis points on 26 July, many observers expected it might be the final hike of this tightening cycle.

[1] Source: Morgan Stanley Investment Management Limited. Data as of 30 September 2023.

But the end of July would prove to be the high-water mark for U.S. and global equity indexes for the first three quarters of 2023. In early August, as investors came around to the view that the Fed might leave rates higher for longer than they had expected just a month or two earlier, a rise in longer-term bond rates gathered steam. In mid-August, the release of minutes from the Fed's July meeting showed that further rate hikes to quell inflation were under consideration. At the Fed's August conference in Jackson Hole, Wyoming, European Central Bank (ECB) President Christine Lagarde expressed the sentiment that higher rates would persist for some time in Europe as well.

Things got worse for equity investors in September, the toughest month of 2023 so far. Government interest rates continued to rise around the world and global equity prices tumbled, as long-term government bond yields and even money market funds offered attractive alternatives to stocks for the first time in years. While the Fed left rates unchanged at its September meeting, it appeared to predict at least one more rate hike this year, and it pushed out expectations for a return to falling rates later into 2024.

In response, stocks fell further as investors also weighed the negative effects of a potential U.S. government shutdown in November, ongoing labor strikes by the United Auto Workers and SAG-AFTRA actors, and the resumption of college loan payments that could impinge on consumer spending. The energy sector, boosted by a significant rise in oil prices that pushed up gasoline prices for consumers, was one of only two sectors in the S&P 500 Index with a positive return during the quarter.

Outside of the U.S., September inflation data for the euro area looked promising, indicating weaker growth and declining inflation. Morgan Stanley analysts are of the view that the ECB will hold further interest rate action in the coming months and that its next likely move will be a cut, likely in mid-2024. This view is backed by declining wage data and a receding energy shock; however, analysts note that another shock to the European economy could derail this outlook. Similarly, in the U.K., data shows that underlying price pressures are softening, and at the end of September the Bank of England paused its almost two-year straight succession of rate increases. While there is no guarantee that there won't be further rate hikes, many analysts believe they are likely to be done.

The good news was that, despite a tough quarter that saw nearly all major global indexes deliver negative returns, most of those same indexes were still solidly in positive territory for the year-to-date as of 30 September.

We remain cautiously optimistic about continued inflation reduction in the U.S., U.K. and eurozone, and we believe a full-fledged recession in the U.S. is unlikely. However, there are several factors at play in the U.S. that could slow the economy's progress. Further, the slow growth rates in China and Japan, combined with the renewed Israel-Gaza conflict, present uncertainty for the global economy for the remainder of this year and into 2024.

Portfolio Activity

There was no significant portfolio activity during the quarter.

Strategy and Outlook

The Climate Aligned strategy is designed to provide exposure to companies that offer protection from climate risk through decarbonization and climate transition strategies, as well as upside potential associated with offering climate solutions, all while managing active risk and seeking a factor-balanced portfolio. The strategy is built around Calvert's views on addressing the climate crisis and the risks and opportunities this presents for long-term oriented, responsible investors.

The transition to a low-carbon economy has created a complex environmental, social and governance (ESG) landscape where long-term environmental risks are being precariously balanced against short-term social risks. We believe companies with the highest potential long-term returns will be those that have credible net-zero strategies and that provide solutions to help the economy as a whole decarbonize.

We continue to see legislation and proposed legislation as a positive tailwind for companies active in the climate transition value chain. In February, the European Commission presented The Green Deal Industrial Plan for discussion, as a first response to the U.S. Inflation Reduction Act (IRA). With the plan, the Commission aims to enhance the attractiveness of the European Union as an investment location for industry and manufacturing, while also addressing permit-related issues. The proposal will further expedite the climate transition.

Meanwhile, the U.S. is doubling down on "buy American" policies: After seeing the initial results of the IRA, the Biden administration proposed that all federally funded construction projects use materials made in the United States. The American Clean Power Association reported that clean energy investments in the U.S. totaled $40 billion in the three-month period following passage of the IRA, which is equivalent to the total estimated investment in all clean energy projects installed in 2021.

Asian companies that are leaders in the climate transition and deployment of green solutions will have the opportunity to benefit from the restructuring of global supply chains.

We continue to see significant demand for increasing volumes of clean water. Greater demand combined with the impact of accelerating global warming is intensifying water shortages. Without more efficient water management, international demand for freshwater is expected to exceed supplies by 40% by 2030.[2] Water scarcity will affect crops and food supply, create health issues and even hamper economic growth. We believe water investment is needed, including better infrastructure and technologies that are focused on addressing the water shortage and worldwide water pollution challenges, in order to solve current and future water crises.

2 Source: "Turning the Tide: A Call to Collective Action," Global Commission on the Economics of Water, March 2023.

The investment risks and opportunities presented by the transition to a low-carbon economy must be factored into long-term investment decisions. While there are clear contributors and benefactors in industries like utilities and mining and metals, which provide products and services that can directly facilitate the necessary energy system changes, all industries are dependent on the energy system and will be affected by the transition. The portfolio seeks to invest in companies with leading decarbonization and net-zero strategies, as well as climate solutions providers, as these companies are better positioned to weather the transition.

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

Fund Facts

Launch date	08 April 2022
Base currency	U.S. dollars
Benchmark	MSCI World Index Net Index (USD)

Calendar Year Returns (%)

Past performance is not a reliable indicator of future results.

	YTD	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013
Class Z Shares	8.93	--	--	--	--	--	--	--	--	--	--
MSCI World Index Net Index (USD)	11.10	--	--	--	--	--	--	--	--	--	--

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 to see the latest performance returns for the fund's other share classes.**

Share Class Z Risk and Reward Profile

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.

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.
- Sustainability factors can pose risks to investments, for example: impact asset values, increased operational costs.
- 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 30 September 2023 and subject to change daily.

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INDEX INFORMATION

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The **Standard & Poor's 500® Index (S&P 500®)** measures the performance of the large cap segment of the U.S. equities market, covering approximately 80% of the U.S. equities market. The Index includes 500 leading companies in leading industries of the U.S. economy.

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