Morgan Stanley Investment Funds

China A-shares Fund

EMERGING MARKETS EQUITY TEAM

Performance Review

In the one month period ending 31 January 2024, the Fund's Z shares returned -5.02% (net of fees)[1], while the benchmark returned -10.14%.

In the month of January, both our stock selections and sector allocation contributed to returns. Our stock selections in the financials and consumer discretionary sectors, along with our underweight to the information technology sector and overweight to the financials sector, contributed most to returns. Our stock selections in consumer staples and health care, however, detracted from returns.

At the stock level, our overweights to Gree Electric Appliance and large banks, including China Merchants Bank and Postal Savings Bank of China, were the largest contributors to returns. On the other hand, our overweights to iRay Technology, Anjoy Foods and WuXi AppTec detracted most.

Market Review

The China A-share market had a weak start to the year amid a sluggish macro outlook and bearish investor sentiment, despite continued policy attempts to revive the economy and the market. The MSCI China A Onshore Index slumped by 10.14% in U.S. dollar terms, trailing the regional MSCI All Country Asia ex Japan Index, which returned -5.45%. Information technology and health care led the decline on weak fund flows and regulatory concerns, while defensive sectors such as energy, utilities and financials outperformed.

China's macro data continued to paint a mixed picture of the economy, pointing to subpar growth in the near term. Fourth quarter real gross domestic product (GDP) growth was largely in line with market expectations at 5.2% year-over-year, taking 2023 full-year GDP growth to +5.2%. Industrial production growth ticked up in December, partly driven by stronger growth in automobile exports, while steel and cement production slowed, suggesting subdued construction activities. Retail sales growth slowed notably in December on weak discretionary consumption. Fixed asset investment growth accelerated modestly in December, driven by faster infrastructure investment while property sector investment continued to decline. Meanwhile, the January manufacturing purchasing managers' index (PMI) rose to 49.2 in January from 49.0 in December, and the services PMI also improved, increasing to 50.1 in January from 49.3 in December, likely boosted by the increased transportation sector activities amid rising travel demand ahead of the Chinese New Year holiday.

Against the backdrop of a still-challenging economic outlook, falling stock markets and subdued investor confidence, Chinese policymakers continued to ramp up policy supports. In a surprise move, the People's Bank of China (PBOC) announced a 50 basis point cut to the required reserve ratio (RRR), effective 5 February, which will release around 1 trillion renminbi into the financial system. The central bank also cut the rediscount rate and relending rate for agriculture and small and medium-sized enterprises (SMEs) by 25 basis points to 1.75% from 25 January onwards. This is expected to further motivate commercial banks to boost lending to the real economy and targeted areas such as SMEs and rural regions. Separately, to further ease property developers' liquidity crunch, regulators also relaxed the commercial property loan standards, allowing the maximum loan-to-value (LTV) ratio to reach 70%, up from 60% previously.

On the financial market, Beijing is reportedly seeking to mobilize a stabilization fund of about 2 trillion renminbi to support the onshore stock market. This came after the State Council urged more "forceful" measures to shore up the falling stock market. The onshore stock market exchange-traded funds (ETFs) witnessed sizable inflows in recent weeks, likely reflecting the purchase by state-backed funds as part of the market stabilization effort.

Portfolio Activity

We initiated a position in Zoomlion Heavy Industry, a leading construction machinery maker actively penetrating the overseas markets.

We initiated a position in Bank of Jiangsu, a quality regional bank focusing on the affluent province of Jiangsu, with above-industry earnings growth and attractive return on equity (15%) and dividend yield (7%).

We exited Vanke, given sluggish residential property sales and rising margin pressure.

Strategy and Outlook

We expect the Chinese economy to pick up momentum in the coming months, though overall growth is likely to remain subpar due to continued deleveraging in the property sector. Further policy support is needed to sustain a steady economic backdrop. We will watch for the upcoming government work report in March for any concrete policy measures and implementation progress.

[1] Source: Morgan Stanley Investment Management Limited. Data as of 31 January 2024.

Our China A portfolio has always been focused on long-term fundamentals, and we continue to seek structural growth opportunities in China. Meanwhile, we have also added quality companies with steady growth and attractive valuations or dividend yields amid the soft economic backdrop. In the near term, we are positioned with a defensive tilt in view of the macro headwinds.

Our medium-term view of the market hinges on whether China can take the external pressure to implement long-term structural reforms and achieve economic transformation that features more sustainable growth driven by technological innovation and productivity gains. The improved quality and sustainability of the economy could help boost China's corporate return on equity and valuation multiple. We also identify attractive investment themes in China that offer structural growth potential, including consumption upgrade, high-end manufacturing and renewable energy development. Against the macro backdrop of slower growth and lower interest rates in China, we believe high quality companies with resilient growth and sustainable total capital returns should outperform. As such, we believe bottom-up stock selection is important to generate alpha. We look for companies with structural growth, competitive advantages, strong corporate governance and financial strength.

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

Fund Facts

Launch date	29 December 2017
Base currency	U.S. dollars
Benchmark	MSCI China A Onshore Index

Calendar Year Returns (%)

Past performance is not a reliable indicator of future results.

	YTD	2023	2022	2021	2020	2019	2018	2017	2016	2015	2014
Class Z Shares	-5.02	-11.91	-23.34	-2.19	13.82	19.42	-16.60	--	--	--	--
MSCI China A Onshore Index	-10.14	-11.65	-27.23	4.03	40.04	37.48	-32.99	--	--	--	--

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.
- 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.
- Sustainability factors can pose risks to investments, for example: impact asset values, increased operational costs.
- There may be an insufficient number of buyers or sellers which may affect the funds ability to buy or sell securities.
- Investments in China involves a risk of a total loss due to factors such as government action or inaction, market volatility and reliance on primary trading partners.
- Investment in China A-Shares via Shanghai-Hong Kong and Shenzhen-Hong Kong Stock Connect programs may also entail additional risks, such as risks linked to the ownership of shares.
- There are increased risks of investing in emerging markets as political, legal and operational systems may be less developed than in developed markets.
- 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 January 2024 and subject to change daily.

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INDEX INFORMATION

The **MSCI China A Onshore Index** is a free float-adjusted market capitalization index that captures large and mid-cap representation across China securities listed on the Shanghai and Shenzhen exchanges.

The **MSCI All Country Asia Ex-Japan Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of Asia, excluding Japan. The performance of the Index is listed in U.S. dollars and assumes reinvestment of net dividends.

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