A Sub-Fund of Morgan Stanley Investment Funds

Emerging Leaders Equity Fund

EMERGING MARKETS EQUITY TEAM

Investors should note that, relative to the expectations of the Autorité des Marchés Financiers, this UCITS presents disproportionate communication on the consideration of extra-financial criteria in its management.

Performance Review

In the one month period ending 31 December 2025, the Fund's Z shares returned -1.46% (net of fees)[1], while the benchmark returned 2.99%.

Emerging markets (EM) finished the year on a strong note, outperforming key indexes including the S&P 500 Index and MSCI All Country World Index.

Though the Fund's fourth quarter 2025 return was positive overall, it lagged the benchmark return given 1) the strong rally in semiconductor stocks across Korea and Taiwan, and (2) a wider correction in e-commerce platform stocks (such as Sea Limited, MercadoLibre and Coupang, partly due to the rotation into semiconductors and other artificial intelligence [AI] plays). This offset the benefit of our underweight selection to China and Middle Eastern markets in the quarter.

On a full-year basis, our overweight allocation to India was the biggest detractor in the year, driving 8.5% of underperformance. India ended the year on a weak note after four years of outperformance as the U.S. trade issue lingered along with rupee weakness and the lack of AI-related trades. Our underweight allocation to and stock selection in Korea and Taiwan also detracted as both tech-heavy markets ended the year on a strong note driven by surging AI and semiconductor demand. Broadly our overweight to Brazil worked well and cancelled out the negative impact of our underweight to China.

Fund performance, and where do we go from here?

The Fund had an exceptionally bad year coinciding with an exceptionally positive year for the broader MSCI Emerging Markets Index. Our performance challenges for the year can be put into three buckets: 1) stock selection mistakes like Globant, where we were late to react to the imminent disruption to software service providers, 2) our significant overweight selection to India, where earnings multiples were stretched in September 2024 and earnings had tactical challenges amid a tightened credit environment and unfavourable weather disruptions to consumption/execution-heavy homebuilding/infrastructure stocks, 3) lack of new thematic opportunities, which historically has been core to the Fund's ability to deliver strong returns. Given our style, we could not have aggressively invested in Korea (memory names) and China, and our stock picking in Taiwan could have been much better. We aim to improve on the same in the coming year.

In 2025, approximately $60 billion flowed out of active EM funds while approximately $90 billion entered through passive funds.[2] This led to general pressure on the earnings multiples of compounder stocks (excluding AI tech), which were traditionally held by more active funds, while larger index names in general did better. A large part of EM outperformance on a sectoral basis can be explained by a rally in key index weights related to technology, including TSMC, Tencent, Alibaba, SK Hynix and Samsung Electronics. Stocks related to the AI supply chain in Taiwan (including materials stocks), banks (ex-India), and industrials (power and defence-linked stocks) in Korea have further added to the EM returns. Together, information technology, industrials and materials stocks that are thematically linked to AI accounted for a significant portion of the Fund's relative underperformance in 2025.

Is our country framework broken?

The Fund historically has focused on large secular growth markets where institutions are strong and capitalistic businesses thrive. Korea and China were the biggest drivers of index performance this year – countries where the Fund typically has an underweight position. We would like to highlight the recent ongoing investigations into Trip.com (in China) and Coupang (in Korea), where there is a socialistic approach to question these businesses' profitability as well as the way they conduct day-to-day operations. Trip.com corrected 20% in a day as the news came out. While China tech earnings continue to get revised down while narratives remain strong (even Alibaba's earnings are getting cut), the overall operating environment hasn't changed. We think many of the narratives driving China and Korea stocks are dilutive to earnings/return on capital employed (ROCE) over the medium term, at the least. We would like to remind readers that for stocks to consistently generate value, return on invested capital (ROIC) has to be greater than weighted average cost of capital, and must be sustained for long periods of time. This is precisely why India's (and the U.S.'s) returns over China and Korea have historically been substantially better over a longer-term period despite the latter countries' economies performing much better at an absolute gross domestic product level.

Portfolio Activity

During the quarter, we re-initiated a position in Tencent Holdings. We reduced our underweight allocation to China by adding Tencent given its significant representation in the MSCI China Index. While we expect dominant Chinese e-commerce and tech

1 Source: Morgan Stanley Investment Management. Data as of 31 December 2025.
2 Source: J.P. Morgan. Global Markets Strategy. EM Money Trail. Published on 16 January 2026.

companies to continue facing intense competition and capital inefficiency, we believe Tencent stands out as the only major platform with clearer visibility on monetizing AI use cases given its strong consumer interface. Specifically, AI integration is accelerating its advertising business and is expected to enhance gaming operations through cost optimization and faster development cycles. While we expect the broader MSCI China Index to gradually retrace gains from the past 15 months, we believe Tencent's differentiated AI monetization strategy positions it to deliver potential relative outperformance versus peers in a challenging market backdrop. We funded the trade by trimming our positions in ICICI Bank, KEI Industries and Bharti Airtel.

We trimmed our position in HDFC Bank and redeployed the capital to Cholamandalam Investment and Finance (Chola). With recent interest rate cuts in India and anticipation for more, we believe Chola will likely be a key beneficiary. We continue to believe that Chola remains one of the best-run vehicle financiers, with its foray into new segments, multiple tailwinds in the form of goods and services tax (GST)/income tax cuts and 8th Pay Commission payouts, and expected strong assets under management growth over the next few years.

We have been adding into fresh ideas such as True Corp (Thailand), a Thai telecom services provider. We believe True is well positioned with its solid ability to take average revenue per user hikes, operational efficiencies in a fixed-cost environment, ongoing cost-cutting measures, and reduced capital expenditure following the 5G rollout.

We initiated a position in Sabesp, Brazil's largest water and sanitation utility, serving approximately 60% of municipalities in São Paulo.[3] We expect the company to double its regulated asset base (RAB) over the next four years, supported by committed organic capital expenditure and improving operating expenditure efficiencies as assets mature. The regulator remains supportive of RAB expansion for value-accretive projects and is likely to provide additional opportunities within São Paulo.

We think the stock is also poised for rerating as Brazil's interest rates decline, reducing cost of equity, and could further benefit from a potential political regime change next year. Led by a CEO from Equatorial and a CFO from 3G Capital, we believe management is strong with disciplined capital allocation and a clear bidding strategy, which is critical for utilities.

We initiated a position in Banco Bradesco. After meeting with company management, we believe the bank's profitability can sharply turn around as 1) the CEO is focusing on reducing operational costs by cutting branches and cutting layers of fat accumulated from years of inefficient operations, and 2) industry credit growth is expected to accelerate as interest rates get cut and the political regime improves. We believe valuations are cheap, earnings expectations are still low and the macro environment is improving.

We trimmed our position in Coupang as the recent data breach and the associated political scrutiny have created an overhang that may weigh on sentiment in the near term. Coupang has not traditionally aligned itself with government objectives, and its recent refusal to participate in parliamentary hearings may increase regulatory and political risks in the near future. Additionally, we expect U.S. tech stocks to face pressure as the AI-driven rally unwinds, which could lead to collateral weakness in global growth-oriented tech names, including Coupang. Given these near-term headwinds, we believe it is prudent to reduce exposure and revisit the position once regulatory uncertainty and sentiment risks subside.

We exited our remaining position in Ambuja Cement due to weaker execution by the management team. The India cement market has yet to see expected pricing recovery or lasting reductions in operating expenses, both of which were expected to raise margins. The company has also faced challenges in leveraging group-level synergies, particularly in logistics and energy costs.

We added to other ideas within Brazil, including NU, XP and Localiza. We marginally trimmed our position in Raia Drogasil, taking some profits and right-sizing the position after its recent rally on third quarter 2025 results. We also right-sized MercadoLibre as concerns around local competition grow. We may reconsider the position if some of these concerns subside.

We also took profit and trimmed our existing position partly in Laurus Labs after its strong year-to-date performance.

We have implemented changes re-aligning our India and Brazil holdings and have reduced our underweight allocation to China. We feel that our portfolio is well positioned in our larger markets of India, Brazil, Taiwan and Mexico.

Strategy and Outlook

We remain committed to seeking to deliver strong returns to our investors by focusing on secular earnings compounding in specific pockets of EM while minimising regulatory and tail risks.

Our portfolio remains defensively positioned towards the "old world" of ROCEs and free cash flows largely centred around India and Brazil. By our measures, Brazil remains one of the cheapest markets on both price-to-earnings and dividend yields. We continue to find high quality businesses in Brazil at what we believe are very attractive valuations. We are positioning our portfolio for upcoming interest rate cuts and potential for a political change.

India's valuations have corrected in the past 12 months while earnings have bottomed out. We believe earnings growth should recover given tax cuts and monetary easing. Weather-related challenges, which impacted a significant part of consumption and our holdings (such as Varun Beverages), are expected to ease given the predicted El Nino weather phenomenon this year in India. Fiscal discipline remains a cornerstone of India's governance, and we believe that also argues for a reduction in equity risk premiums for India. We note Indian earnings have continued to be ahead of other large EM peers while the recent outperformance of other EM markets has been driven by multiple rerating.

On a fundamental basis, a large part of the EM rally excluding Taiwan has been driven by: 1) multiple rerating without much upgrade in earnings (such as China). The Hang Sang Tech Index 2025 earnings per share (EPS) estimates have been revised down by 28%

3 Source: Sabesp company data as of 30 September 2025.

over the last 12 months, with 2026 estimates revised 20% lower over the same period.[4] Or, 2) a cyclical bounce in earnings (such as memory stocks in Korea). In our previous newsletters, we have discussed in detail why we remain significant underweight to China. While we don't dispute the technical innovation in China, we continue to flag that competitive intensity remains high and entry barriers remain weak, which are a precursor to reap benefits of any innovation (free cash flow generation led by higher ROCE over a longer time period). We already see some of those challenges in the auto sector in China, which has been long perceived as a leader in electric vehicles (Xiaomi and BYD have corrected more than 30% from their recent highs).[5] And this appears to be a repeat of what we have already seen in solar, real estate, capital goods, quick service restaurants, cosmetics and several other sectors.

Similarly for Korea, where memory stocks and other AI-linked sectors have been rising meaningfully, we continue to believe many of these products remain commoditized in nature (and hence cyclical), eventually with limited pricing power with their customers. The narrative around strong AI demand (which has also propelled many stocks in Taiwan) remains centred around Open AI, where a capital expenditure commitment of $1.4 trillion has been made while its own revenues are only $13 billion.[6] While we don't doubt the revolutionary power of AI, we highlight the concerns around incrementally debt-fuelled capital expenditure as well as the circular nature of the demand among various AI players. We think the aggressive capital expenditure over recent years and adoption by real world consumers (whether corporates or individuals) are travelling on different tangents, and both need to eventually match to a respectable ROCE to sustain the recent run-up in valuations.

Overall, we continue to focus on finding what we consider to be high quality businesses across emerging markets at fair valuations while avoiding tail risks such as regulatory, key man and capital misallocation. In these days of exceptional volatility, valuations can get dislocated on both sides in very short time periods, providing good opportunities to both buy and sell stocks.

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

Fund Facts

Launch date	17 August 2012
Base currency	U.S. dollars
Benchmark	MSCI Emerging Markets (Net) Index

Calendar Year Returns (%)

Past performance is not a reliable indicator of future results.

	YTD	2025	2024	2023	2022	2021	2020	2019	2018	2017	2016
Class Z Shares	10.57	10.57	2.96	12.41	-33.10	2.91	58.88	26.14	-12.78	26.73	2.53
MSCI Emerging Markets (Net) Index	33.57	33.57	7.50	9.83	-20.09	-2.54	18.31	18.42	-14.57	37.28	11.19

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 shares. The sources for all performance and index data is Morgan Stanley Investment Management ('MSIM Ltd'). **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 fund may be impacted by movements in the exchange rates between the fund's currency and the currencies of the fund's investments.
- 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, available at www.morganstanleyinvestmentfunds.com. All data as of 31.12.2025 and subject to change daily.

4 Source: Bloomberg L.P. Data as of 31 December 2025.
5 Source: Bloomberg L.P.
6 Source: The Financial Times. Published on 7 November 2025.

Applications for shares in the Sub-Fund should not be made without first consulting the current Prospectus and the Key Information Document ("KID") or Key Investor Information Document ("KIID"), which are available in English and in the language of countries authorized for fund distribution and is available online at Morgan Stanley Investment Funds Webpages or free of charge from the Registered Office at European Bank and Business Centre, 6B route de Trèves, L-2633 Senningerberg, R.C.S. Luxemburg B 29 192.

The summary of investor rights is available in the aforementioned languages and website location under the General Literature section.

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The index is unmanaged and does not include any expenses, fees or sales charges. It is not possible to invest directly in an index.

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The **S&P 500® Index** 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.

The **MSCI All Country World Index (MSCI ACWI) - Net** is a free float-adjusted market-capitalization-weighted index designed to measure the equity market performance of developed and emerging markets. The term "free float" represents the portion of shares outstanding that are deemed to be available for purchase in the public equity markets by investors. Returns are calculated using the MSCI All Country World Index (gross dividends) prior to December 31, 2000 and the MSCI All Country World Index (net dividends) after December 31, 2000.

The **MSCI China Index** captures large and mid-cap representation across China A-shares, B-shares, H-shares, Red-chips and P-chips. It reflects the Mainland China and Hong Kong opportunity set from an international investor's perspective.

The **Hang Seng Tech Index** measures the performance of the 30 largest technology companies listed in Hong Kong that have high business exposure to technology themes.

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