Morgan Stanley

INVESTMENT MANAGEMENT

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Morgan Stanley Investment Funds

Global Balanced Fund

SOLUTIONS AND MULTI-ASSET | GLOBAL BALANCED RISK CONTROL TEAM | MONTHLY COMMENTARY | 31 MARCH 2019

Performance Review

In the one month period ending 31 March 2019, the Fund's Z shares returned 0.94% (net of fees)[1].

Equity markets continued to provide positive returns in March but traded more erratically compared with January and February due to growth concerns and on-going trade talks between the U.S. and China. The yields on both U.S. and German long-dated sovereign bonds fell sharply in March as the Federal Reserve (Fed) and the European Central Bank (ECB) took a dovish turn towards more accommodative monetary policy to encourage growth. Our allocations to U.S., Europe and Asia ex Japan equities and European corporate bonds were the top contributors to the portfolio's positive performance on the month.

Market Review

United States

The MSCI USA Index returned 1.81% in U.S. dollar terms (USD) and 3.27% in euro terms. The Institute for Supply Management (ISM) surveys of the U.S. manufacturing and services sectors continued to indicate expansionary conditions. But while the manufacturing index increased by more than expected, the services index came in lower than expected. The ISM Manufacturing PMI rose to 55.3 in March from 54.2 in February on stronger new orders, production and hiring. The ISM Non-Manufacturing index fell to 56.1 in March from February's 59.7 reading due to a slower expansion in new orders and production. Retail sales in February slipped 0.2% while the January number was revised upward to a 0.7% gain. Hiring rebounded in March after an unexpectedly weak February. The U.S. Labor Department said 196,000 jobs were added and the unemployment rate stayed at 3.8%. Wages grew by 3.2% over the 12 months ended March 2019. Core inflation, excluding food and energy, for March is up 2% year-on-year.

Europe

The MSCI Europe Index returned 2.03% in euro terms and 0.59% in USD terms. Manufacturing conditions deteriorated further in the eurozone. The IHS Markit Eurozone Manufacturing PMI for March was 47.5, dropping from February's 49.3. Weak global demand, trade/tariffs, Brexit and other political worries continued to dampen new orders, output and business confidence in the region. Business conditions in the services sector, however, showed further improvement. The IHS Markit Eurozone PMI Services Business Activity Index increased to 53.3 in March from 52.8 in February. Stronger new business volumes encouraged hiring and helped bolster business sentiment. Inflation weakened in March, according to Eurostat's flash estimate. The euro area annual inflation is expected to be 1.4%, below February's rate of 1.5%. The core inflation measure, which excludes food, energy, alcohol and tobacco, also declined in March to 0.8% from 1.0% in February. Separately, Eurostat reported that unemployment held steady in February at 7.8% for the euro area and 6.5% for the European Union.

Japan

The MSCI Japan Index returned -0.01% in yen terms and 1.99% in euro terms. Japan's manufacturers saw another month of contracting activity. After falling to 48.9 in February 2019, the first below-50 reading below since 2016, the Nikkei Japan Manufacturing PMI's rate of decline improved slightly to 49.2 in March. The services sector demonstrated resiliency amid stronger domestic demand and higher output as the Nikkei Japan Services PMI came in at 52.0 in March, down modestly from 52.3 in February. The Ministry of Economy, Trade and Industry said industrial production was "pausing" after an upturn in March snapped three months of declines. Production increased 1.4% month-on-month due to increased auto and auto parts production but remained down 1.0% year-on-year. Household spending grew by less than expected at 1.7% in real terms on the year in February after advancing 2.0% in January. Inflation remained subdued in February, as the core measure, excluding food and energy, increased 0.4% on the year. Unemployment stayed at two-decade lows, falling to 2.3% in February from 2.5% in January, Statistics Bureau data showed.

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1 Source: Morgan Stanley Investment Management Limited. Data as of 31 March 2019.

Portfolio Activity

We reduced equity exposure moderately in March as weak economic data reignited investors' concern over global growth. We maintain our view that a near-term recession is a low probability event. As a result, we continue to use the option strategy to gain equity exposures and provide downside protection given binary risks associated with events such as U.S.-China trade negotiation and Brexit. The effective equity exposure at the end of the month was 36.7%.

Strategy and Outlook

The recent inversion of the yield curve has further flamed fears about a forthcoming U.S. recession. While we acknowledge that yield curve inversion has historically been an accurate recession signal, we continue to view a near-term recession as a low probability scenario. Despite some deterioration in key leading indicators such as U.S. consumer and business confidence, they still remain far from levels indicating a recession. Furthermore, if the U.S. Congress reaches a bipartisan deal for infrastructure spending, this could provide the boost that keeps the U.S. from a recession. Moreover, the latest data out of China are showing signs that government stimulus measures may be working. The recent dovish pivot by both the Fed and the ECB has already translated into a meaningful loosening in global financial conditions. Assuming global growth bottoms in the second quarter of 2019, a pause in interest rate increases would likely be supportive of equity markets. We are cautious, however, as geopolitics and trade threats are dampening global economic momentum. Despite positive progress on U.S.-China trade talks, which is mostly priced in by investors, challenges remain around implementation and enforcement. Trade tension could also escalate between the U.S. and Europe should the U.S. decide to impose new tariffs on $11 billion of European Union products in addition to the auto tariff proposed last year. Given the magnitude of the year-to-date rally, U.S. equities, in particular the technology sector, are vulnerable to a correction should incoming data disappoint. As a result, we aim to be nimble in asset allocation and continue to use options to gain broader exposure. For fixed income assets, while short-term weakness in economic data and a dovish Fed may cause bond yields to drop, our view is that the return to owning longer-dated bonds relative to the risk remains unattractive. The flatness of the yield curve means that any evidence of renewed growth could lead to a sharp rebound in yields and negative returns for longer-dates bonds from current levels. We prefer emerging market debt instead, which is offering attractive yields and could benefit from a combination of falling inflation and weakening growth in some emerging market economies.

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

FUND FACTS

Launch date	Base currency
16 August 2016	Euro

12 Month Performance Periods to Latest Month End (%)

	MARCH '18 - MARCH '19	MARCH '17 - MARCH '18	MARCH '16 - MARCH '17	MARCH '15 - MARCH '16	MARCH '14 - MARCH '15
MS INVF Global Balanced Fund - Z Shares	3.64	-1.97	--	--	--

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

Share Class Z Risk and Reward Profile

Lower Risk **Higher Risk**

1 2 3 **4** 5 6 7

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 a range of assets with different levels of risk and the fund's simulated and/or realised return has experienced medium 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 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 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 funds 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.
- 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 March 2019 and subject to change daily.

INDEX INFORMATION

The **MSCI USA Index** is designed to measure the performance of the large and mid cap segments of the US market. With 631 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in the US.

The **MSCI Europe Index** is a free float-adjusted market capitalization index that is designed to measure developed market equity performance in Europe. 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. The performance of the Index is listed in U.S. dollars and assumes reinvestment of net dividends.

The **MSCI Japan Index** is a free-floated adjusted market capitalization weighted index that is designed to track the equity market performance of Japanese securities listed on the Tokyo Stock Exchange, Osaka Stock Exchange, JASDAQ and Nagoya Stock Exchange. The MSCI Japan Index is constructed based on the MSCI Global Investable Market Indices Methodology, targeting a free-float market capitalization coverage of 85%.

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