A Sub-Fund of Morgan Stanley Investment Funds

Global Brands Equity Income Fund

INTERNATIONAL 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 March 2025, the Fund's Z shares returned -1.96% (net of fees)[1], while the benchmark returned -4.45%.

For the first quarter overall, the portfolio's focus on earnings resilience and capital preservation shone through, with the portfolio delivering a positive absolute return of +1.78%, while the MSCI World Net Index delivered a negative absolute return, falling -1.79%. As a reminder, we expect the portfolio to deliver an asymmetric performance profile over the long term, offering attractive absolute long-term returns with reduced downside participation during challenging market environments.

As of 31 December 2024, the Fund had produced a distributed yield of +4.35% over the previous four quarters.

For the quarter, two of the three largest contributors to absolute performance were financials stocks, all driven by fundamentals following strong stock-specific updates: **Visa** (+63 basis points [bps]) performed well on the back of a good set of first quarter results, which saw the company raise full-year 2025 guidance, helped by strong growth in payments and the company's increasing breadth of products and services, while **AJ Gallagher** (+52 bps) returned a remarkable +22% in a falling market following a strong operating quarter, which saw the company beat earnings per share (EPS) estimates and reaffirm healthy organic growth guidance. The other notable contributor was **SAP** (+58 bps), which reported a good set of fourth quarter and full-year 2024 results and was an outlier within the broader global information technology (IT) sector, with the stock up +8% in the first quarter while the MSCI World IT sector fell -12%. After several painful years, the company is now benefiting from the sweet spot of clients' transition to the cloud, which is leading to accelerating growth and improving margins.

In terms of the largest absolute detractors during the quarter, **Microsoft** (-78 bps) and **Alphabet** (-47 bps) fell -11% and -18%, respectively, as investors appeared to question the sustainability of the Magnificent Seven's (Mag 7) dominance, given uncertainty regarding the payoff of higher capital expenditure being made by the artificial intelligence (AI) hyperscalers. In the case of Microsoft, we took advantage of the stock derating and added to our position, given the underlying fundamentals of the business appear robust. The other key detractor in the first quarter was **Constellation Brands** (-57 bps), which we sold in the quarter due to tariff implications.

In terms of the **relative performance** picture, stock selection and sector allocation were positive in both the month and quarter.

During the month, stock selection was helped by outperformance in IT, health care, financials and industrials, while for sector allocation, the benefit from the consumer staples overweight, along with some smaller positive allocation effects, offset the drag from the zero weight to energy.

For the first quarter overall, positive stock selection was primarily driven by our holdings within IT, where strong absolute performers such as SAP and Roper drove a sector-level return of -3% for the portfolio, significantly ahead of the -12% MSCI World IT sector return. In a reversal from previous quarters, relative IT performance was helped by the fact the portfolio doesn't own the more cyclical semiconductors and hardware subsectors, which suffered in the first quarter. Outperformance in financials and consumer discretionary was also notable: more than half of the portfolio's financials names delivered double digits in the first quarter, with the portfolio's sector-level return for financials double that of MSCI World (+12% versus the index sector's +6%), while consumer discretionary returns were flat against the index sector's 10% fall. In terms of sector allocation, the portfolio benefited from its overweight to consumer staples, health care and asset-light financials, as well as the consumer discretionary underweight, which more than outweighed the milder drag from not owning energy.

The overwrite (sales of index calls) contributed 4 bps to performance for the quarter. In the first quarter of 2025, swap performance has been slightly positive as expected given marginally negative world equity market performance over the quarter. Indeed, in January the equity markets had shown positive performance but it vanished in March with a higher level of volatility, which was beneficial for the Fund's short call overlay.

Market Review

A particularly volatile March rounded out a bumpy first quarter for global equity markets, with the MSCI World Net Index returning -4.5% in U.S. dollars (USD) in the month and -1.8% in the quarter (local currency returns of -5.0% in March and -2.7% in the quarter). Political uncertainty and concerns over a slowing U.S. economy defined market sentiment, although interestingly, the fall in equity markets in the first quarter appeared to be largely down to the high-profile AI plays – the Mag 7 – rather than widespread

[1] Source: Morgan Stanley Investment Management Limited. Data as of 31 March 2025.

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deterioration in other sectors. The IT and consumer discretionary sectors were down -9% and -8%, respectively, in the month and double digits in the first quarter (-12% and -10%, respectively), mainly due to Nvidia, Apple and Tesla, which each saw several hundred billion dollars wiped off their market capitalisations. The other Mag 7-exposed sector, communication services, delivered -7% in March and a slightly less severe -4% in the quarter, held back by Alphabet. Outside of these Mag 7-exposed sectors underperforming, there was little differentiation between defensive and cyclical sectors with all other sectors delivering positive returns. Energy and utilities led in the month (+5% and +3%, respectively) and quarter (+10% and 7%, respectively), while consumer staples, health care and financials were also ahead of the overall index in March and delivered positive quarterly returns (+5%-6%). Sector performance is shown in USD unless otherwise noted.

Turning to geographies, the rollout of the Trump administration's protectionist policies saw the greenback weaken against international currencies, with the U.S. the only major market to lag the MSCI World in March (-6%) and the first quarter (-5%), in USD terms. Major markets in continental Europe were strong, outperforming the overall index in the month and delivering double-digit USD returns in the quarter (+6%-12% local). Performance in Asia was more mixed: for the quarter overall, Singapore (+10% USD, 8% local) and Hong Kong (+4%, +5%) held up well despite tariff fears, while the appreciation of the yen saw weaker performance by Japan (0%, -5%).

Portfolio Activity

We initiated one new position in the quarter, **Oracle**, and made two final sales, **Constellation Brands** and **Pernod Ricard**.

Oracle is a software company with a semi-monopolistic position in the enterprise-grade relational database market and the second largest player in enterprise resource planning (ERP). These are mission critical applications characterised by predictable and sticky revenue streams, very high switching costs, and considerable pricing power. We believe the company's growth should be supported by its latest cloud offering, Oracle Cloud Infrastructure, which has the potential to be a successful niche offering in a large and growing market. A recent pullback in the share price provided us with the opportunity to initiate a position at an attractive mid-20s price-to-earnings (PE) multiple.[2]

We completed our exit from **Constellation Brands** in the first quarter. Our original investment thesis was predicated on the company's strong position in the fastest-growing segment of the U.S. beer market, namely premium international brands, which, historically, has been driving high single-digit sales and profit growth in its U.S. beer business. However, the recent introduction by the new U.S. administration of a 25% tariff on Mexican imports poses a material threat to the investment case, as we fear the company may struggle to offset tariffs through pricing given its main competitors are not exposed to the same protectionist measures. While Constellation is still expected to win market share over time, the increasingly complex tariff landscape, coupled with a recent earnings miss as a result of declining beer volumes, led to our decision to exit the position.

We also completed our exit from **Pernod Ricard** during the first quarter. The stock price has been depressed for several months due to weakness in two of its major markets, China and the U.S. During the quarter, the company announced that it expects the next fiscal year to be a "transition year" with modestly improving sales trends (assuming no further tariff impact). Our concern, however, is that the long-awaited post-COVID recovery has been consistently pushed out, and that the tariff environment could pose further headwinds. Following a cut to sales and marketing expense at its most recent earnings call, along with a downgrade to long-term organic growth guidance, we made the decision to exit the stock.

Over the first quarter, strong share price performance by the likes of **Abbott Laboratories, SAP, Visa** and **CME** saw us trim the positions and take profit. We recycled this capital by taking advantage of valuation opportunities, adding to **S&P Global,** which had derated from a peak +30x PE multiple,[2] **AJ Gallagher,** where there was upside to our price target, and **Booking Holdings,** which had derated over AI-related concerns despite robust operational performance. We also added to **Microsoft,** where we believed the market's focus on marginal disappointments around Azure growth (31% delivered versus 31.8% consensus)[3] was excessive, given the revenue outlook for the company remained strong, and **UnitedHealth**, which had derated on concerns over the regulatory landscape and media coverage of an investigation by the U.S. Department of Justice, which the company has commented relate to old investigations.

Strategy and Outlook

Life after the "Liberation Day" tariff announcement

Publishing an outlook in early April 2025 is a hostage to fortune, given the current fluid and fast-moving environment driven by the substantial uncertainties around the path of U.S. economic policy and its effects, not to mention the volatility of equity prices. We do not attempt to make any kind of definitive prediction about economic outcomes right now, but instead analyse what kind of outcomes are discounted in equity prices. We would argue that even after the circa 10% fall in the first two days after the "Liberation Day" tariff announcements, the markets are implicitly assuming that much of the tariff hikes will soon be reversed, before they have significant impacts on the U.S. economy.

Looking at the state of the markets before the "Liberation Day" tariff announcement, there had been much sound and fury about the slide in equity indexes in the first quarter, but the MSCI World Index finished down just 2%, and the S&P 500 only fell 4%. The first quarter drawdown was focused on the tech-plus sectors: information technology itself, communication services, dominated by Alphabet and Meta, and the consumer discretionary sector housing Amazon and Tesla. The other eight sectors in MSCI World were all up in the quarter, with a lack of significant performance differential between the defensive and cyclical sectors. We would argue

2 Source: FactSet.
3 Source: Microsoft Earnings Release FY25 Q2, published January 2025.

this implies the market was not pricing in major concerns about an economic slowdown, outside some select pockets of consumer discretionary such as airlines, hotels and the tariff-hit autos industry. This sanguine attitude was also shown in the market earnings forecasts for 2025 and 2026, which stayed roughly flat in the first quarter, admittedly helped at the margin by the weakening dollar, still booking in double-digit earnings growth for 2025 and 2026.

This resilience of the market ex-Mag 7 in the first quarter suggests investors were not yet focusing on the potential negative headwinds from tariffs but rather had continued to focus on the potential benefits to corporate profitability of the new administration policies, such as deregulation. As a result, the "Liberation Day" tariff announcement came as a shock. Multiple analysts[4] have suggested that the scale of the proposed tariffs, 20%-plus on leading trade partners, if they are indeed sustained, could reduce U.S. gross domestic product (GDP) growth by more than 1%, while adding up to a couple of points to inflation, not to mention cutting corporate profit margins. Such a stagflationary shock could also restrict the U.S. Federal Reserve's (Fed) ability to reduce interest rates, at a time when fiscal policy needs to be tight to start to deal with a deficit at 7% of GDP. While still relatively healthy before the tariff announcement, there were already some signs of the U.S. economy slowing down, while inflation was still above the Fed's 2% target. Aside from the mechanical impact of the tariffs, there is also the impact on both corporate and consumer confidence, both of which had already declined in March in anticipation of tariffs. Importantly, regardless of the end destination of this policy initiative, it is increasingly clear that the current administration has other populist priorities beyond large corporate profitability and the level of the S&P 500. Looking at the targets of the tariffs, major exporters to the U.S. face significant challenges, more likely to be a deflationary than an inflationary shock.

Even after the circa 10% drop in markets in the two days after the tariff announcement (up to the close on 4 April), markets look far from cheap by historical standards, with MSCI World on over 16x forward earnings and the S&P 500 still above 19x.[2] These multiples are on earnings still assumed to be rising double digits in each of the next two years, a pace we worried about even before the announcement. Both the multiple and earnings will be very vulnerable if the U.S. economy slows to sub-1% growth. This implies that even at its lowered level, the market seems to be pricing in sharp reductions in the tariff rates over the next few months, presumably on the back of successful negotiations with the likes of the EU and China. While not impossible, this tariff de-escalation is certainly not a given, particularly after China's retaliation.

As we explained in our recent Global Equity Observer article – The New Tariff Landscape – in terms of the potential impact of tariffs across our portfolio, we would split them between the direct effects and the more uncertain indirect effects from any retaliation or macroeconomic impacts. At the time of writing, given that our portfolio is skewed towards services rather than goods, we believe most of our companies should face limited direct impact from these U.S. tariffs, while local manufacturing, high gross margins, pricing power and recurring revenues should help dampen the extent of the impact for the goods producers.

It is possible that retaliation may spread beyond the goods sector, perhaps even with sanctions placed on U.S. technology giants by the EU — but again we believe their high gross margins, pricing power and recurring revenues should help mitigate the impacts on the portfolio. These same factors should also help the portfolio in the case that the tariffs trigger a significant slowdown and/or recession, given the portfolio companies' economics and the portfolio's history of earnings' robustness in tough economic times in the past. In addition, it also has limited exposure to the "Trough of Disillusionment" risk in AI. While the portfolio owns Microsoft and Alphabet, where we believe the adoption of GenAI can provide an extra driver of growth on top of the ongoing transition to cloud, it does not own the other five of the Mag 7. Being in the "not owning" business has been a significant tailwind to the portfolio's strong relative performance so far this year. If markets are indeed not reflecting a sustained high tariff environment and the sharp economic slowdown it implies, then not owning could continue to be a positive as the year progresses.

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

Fund Facts

Launch date	29 April 2016
Base currency	U.S. dollars
Benchmark	MSCI World Net Index

Calendar Year Returns (%)

Past performance is not a reliable indicator of future results.

	YTD	2024	2023	2022	2021	2020	2019	2018	2017	2016	2015
Class Z Shares	1.78	7.80	13.32	-16.18	19.64	11.99	25.55	-3.07	22.60	--	--
MSCI World Net Index	-1.79	18.67	23.79	-18.14	21.82	15.90	27.67	-8.71	22.40	--	--

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.**

[2] Source: FactSet.
[4] For instance, Goldman Sachs, UBS, Deutsche Bank, Yale Budget Laboratory.

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 value of financial derivative instruments are highly sensitive and may result in losses in excess of the amount invested by the Sub-Fund.
- 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.
- 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.
- The derivative strategy aims to increase the income paid to investors, but there is potential for the fund to suffer losses.
- 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 31.03.2025 and subject to change daily.

Applications for shares in the 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.

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