A Sub-Fund of Morgan Stanley Investment Funds

Indian 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 January 2025, the Fund's Z shares returned -5.75% (net of fees)[1], while the benchmark returned -3.56%.

Indian equities experienced a soft patch, impacted by earnings misses, continued foreign selling and depreciating currency. The Fund underperformed the benchmark, affected by our negative stock selection. Our overweight allocation and stock selection in the financials sector contributed to returns. However, our stock selection and overweight allocation in the consumer discretionary and health care sectors detracted. Our stock selection within the industrials sector also detracted.

At the stock level, our zero-weight allocation to apparel retailer Trent contributed to returns. Although Trent reported EBITDA (earnings before interest, taxes, depreciation and amortization) growth of 34% year-on-year,[2] its share price consolidated as its valuation derated, and its earnings did not surprise to the upside. We expect this pause in the India growth story will likely persist in the short term but will likely benefit from the recently announced tax cuts, which should help the consumption story longer term.

Our overweight allocation to Cholamandalam Investment and Finance also contributed. The company reported a better-than-expected profit after tax for third quarter fiscal year 2025 on improved operating performance and flat credit costs quarter-on-quarter.

Our overweight allocation to KEC International, a global infrastructure engineering, procurement and construction major, detracted as its third quarter fiscal year 2025 results came in below expectations across its topline and profitability. This was attributed to weakness in the railways and civil segments despite strong transmission and distribution (T&D) order inflows. We expect KEC International to benefit from a robust order pipeline from domestic and internal T&D, particularly from Gulf Cooperation Council countries. The company announced new T&D orders of Rs 1,445 crores in late January.

Our overweight allocation to Zomato, a food delivery company, detracted as the shares tumbled after the company reported net income misses for the third quarter fiscal year 2025. While its food delivery business saw modest growth with improved margins, its quick commerce segment Blinkit incurred an EBIDTA loss due to growth investments and increased competition. The company noted a broad-based slowdown in demand, which started during the second half of November. While increased competition has led to an expected pause in margin expansion in quick commerce business, the company has assured that it has not seen any attrition of its core customers.

Market Review

The MSCI India Index (down -3.56%) underperformed the MSCI Emerging Markets Index (up 1.79%) in January in U.S. dollar terms. The S&P BSE Sensex (down 0.8%) outperformed the S&P BSE SmallCap Index (down 9.5%) and the S&P BSE Midcap Index (down 7.2%) in January, while the MSCI India Growth Index outperformed the MSCI India Value Index.

Total institutional flows were positive for the 31st month, running at $1.1 billion in January.[3] Foreign portfolio investors (FPI) turned sellers in January with outflows of $8.4 billion in the cash market and $0.5 billion in the debt market. FPI flows turned positive in the futures market with inflows of $0.5 billion. Domestic mutual funds continued to buy stocks, totalling $6.7 billion (up to 29 January).

In January, the rupee depreciated by -1.2% against the U.S. dollar and -0.8% against the euro.[4]

In January, oil prices rose by 4.8% month-on-month in rupee per barrel terms following a fall of 0.2% in the previous month.[4]

Portfolio Activity

We believe India is in a short cyclical slowdown and are hopeful it will bottom out in the first half of 2025. With that view, we took profit by trimming names that had benefited from the cyclical upturn in 2024. We exited our positions in Inox Wind and Premier Energies and trimmed our positions in Sai Life Sciences and One MobiKwik. While we like the supply and demand dynamics of solar cells manufacturing in India for next few years, we believe that Premier Energies is already well priced; hence, we exited the name. We rotated the capital toward relatively large-cap stocks and stocks with subdued performance over the past year such as Reliance

[1] Source: Morgan Stanley Investment Management Limited. Data as of 31 January 2025.
[2] Source: Trent company reports as of 6 February 2025.
[3] Source for all flows, GST and PMI data: Morgan Stanley – India Equity Strategy: January 2025, published 2 February 2025.
[4] Source: J.P. Morgan – India Equity Strategy, published 1 February 2025.

Industries and HDFC Bank. Our overall view remains that the current monetary cycle/credit cycle is likely to bottom out in the first half of the year, leading to credit growth and a consumption revival in the second half.

We initiated a position in Grasim Industries, a flagship company of the Aditya Birla Group, which started as a textiles manufacturer. The company has since evolved into a leading diversified player across cellulosic fibers, diversified chemicals, fashion yarn and fabrics production in India. It has also entered new growth categories such as decorative paints under the Birla Opus brand and a business-to-business online marketplace for building materials. Through its subsidiaries, it is also a prominent domestic cement producer, a leading diversified financial services firm and a clean energy solutions provider.

We also initiated a position in Dr. Agarwal's Health Care Limited, an eye clinic and hospital, through its initial public offering (IPO). Its eyecare services include the treatment of cataract, glaucoma, retinal detachment, macular hole, retinopathy prematurity, vitrectomy, dry eyes, Lasik and refractive surgery.

Strategy and Outlook

The recent incoming high-frequency indicators continued to show mixed performance. Within auto sales, two-wheeler retail sales moderated to 0.6% while passenger vehicles rose 2.6% on a year-on-year basis in January. Credit growth improved to 11.5% year-on-year as of 10 January versus 11.2% in December.[5]

January goods and services tax (GST) collections rose to 1.96 trillion rupees, growing at nine-month high of 12.3% year-on-year versus 7.3% in December. The manufacturing purchasing manager's index (PMI) edged up to a six-month high of 57.7 on the back of higher export orders while the services PMI fell to a 26-month low of 56.5 in January.[3]

The January headline consumer price index (CPI) further softened to a five-month low of 4.3% year-on-year in January versus 5.2% in December.[6] Food CPI slowed to 6% year-on-year in January from 8.4% in December, led by softening in vegetables, eggs, cereals and pulses prices. Core CPI (excluding food and fuel) ticked up to 4.1% year-on-year in January for the fourth consecutive month.

Despite a cash reserve ratio reduction of 50 basis points in December, system liquidity was tracking in deficit in December and January, and foreign exchange market intervention has further weighed on the interbank liquidity. This, in our view, has been weighing on the overall consumption revival, especially in discretionary consumption. While a rise in government discretionary expenditures in the last two months of the previous year was encouraging, some macro indicators continued to get pulled down by a sharp slowdown in GST tax collections and weakening bank deposits growth. Industrial activity on the other hand sequentially improved, driven by strengthening trends in engineering goods exports, infrastructure and road construction proxies. Consumption indicators pointed to improving rural consumption while the urban consumption indicators remained on the weaker side.

The economy is undergoing cyclical adjustments, with tight liquidity conditions leading to a slowdown in domestic consumption (following the withdrawal of the accommodative monetary policy stance since 2022). Additionally, the Reserve Bank's oversight on the financial sector has considerably reduced credit growth in the system. While the domestic growth and inflation outlook warrant monetary easing, the Reserve Bank faces a policy dilemma against external factors that are increasing pressure on the currency and the market intervention tightening liquidity conditions at the margin. This cyclical weakness, along with external uncertainty in terms of tariff-related announcements, has led to market outflows by foreign investors. In turn, this is helping clear out some excessive valuations that we have seen especially across the mid-cap space.

We continue to believe that the current fiscal consolidation path of the government leaves little fiscal room to support domestic consumption and that monetary policy will likely be the key catalyst for growth and earnings growth. While we feel monetary conditions will be on an easing trend in the near term, we are closely watching for impacts from external factors such as developments in U.S. economic growth and tariff announcements.

The cyclical slowdown is leading to pockets of earnings consolidation and near-term market correction, and we are taking this opportunity to trim richly valued stocks and further add to higher-conviction themes. While we continue to believe in long runway themes like power demand and indigenization, we have taken the opportunity to trim some of these exposures due to excessive valuations. We continue to favour cyclical financials where we expect credit costs and the cost of funds to peak in one to two quarters. We believe that fixed-rate book financials (both banks and non-banking financial companies) should benefit in the next two to three years in this cycle. Usually, easing in credit conditions has a delayed impact (about six to nine months) on pickup in lower-ticket discretionary spending and we continue to be well positioned for this inflection.

We will continue to be invested in structural capital expenditure themes (like power capital expenditure, renewables, import substitution and others). We are also on the lookout for total addressable market expansion themes in consumption.

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

Fund Facts

Launch date	30 November 2006
Base currency	U.S. dollars
Benchmark	MSCI India (Net) Index

3 Source for all flows, GST and PMI data: Morgan Stanley – India Equity Strategy: January 2025, published 2 February 2025.
5 Source: Morgan Stanley – India Economics: India Trendspotting, published 5 February 2025.
6 Source: Morgan Stanley – India Economics, published 12 February 2025.

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	-5.75	22.77	21.31	-9.84	32.47	8.82	1.98	-20.22	41.73	2.72	-0.29
MSCI India (Net) Index	-3.56	11.22	20.81	-7.95	26.23	15.55	7.58	-7.30	38.76	-1.43	-6.12

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.
- 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 31.01.2025 and subject to change daily.

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

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The **MSCI Emerging Markets Net Index** is a free float-adjusted market capitalization weighted index that is designed to measure equity market performance of 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. The MSCI Emerging Markets Index currently consists of 24 emerging-market country indices. The performance of the index is listed in U.S. dollars and assumes reinvestment of net dividends. The index does not include any expenses, fees or sales charges, which would lower performance.

The **S&P BSE SENSEX (S&P Bombay Stock Exchange Sensitive Index)** is a free-float market-weighted stock market index of 30 well-established and financially sound companies listed on Bombay Stock Exchange.

The **S&P BSE MidCap Index** measures the mid-cap segment of India’s stock market.

The **S&P BSE SmallCap Index** measures the small-cap segment of India’s stock market.

The **MSCI India Growth Index** captures large- and mid-cap securities exhibiting overall growth style characteristics in India, as defined by long-term forward earnings per share (EPS) growth rate, short-term forward EPS growth rate, current internal growth rate and long-term historical EPS growth trend and long-term historical sales per share growth trend.

The **MSCI India Value Index** captures large- and mid-cap Indian securities exhibiting overall value style characteristics, as defined by book value to price, 12-month forward earnings to price and dividend yield.

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