Morgan Stanley

INVESTMENT MANAGEMENT

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Morgan Stanley Investment Funds

US Dollar Short Duration High Yield Bond Fund

GLOBAL FIXED INCOME | GLOBAL FIXED INCOME TEAM | MONTHLY COMMENTARY | 30 APRIL 2019

Performance Review

In the one month period ending 30 April 2019, the Fund's Z shares returned 1.27% (net of fees)[1], while the benchmark returned 0.92%.

Over the month, overweight positioning to capital goods, specifically building materials and diversified manufacturing, contributed positively to performance. Overweight positioning to exploration & production was also additive. An underweight to technology detracted slightly from performance.

Market Review

Market Review

In April, investor confidence continued to rally as markets continued to fare well and volatility declined. U.S. Treasury yields widened across the curve and investors took on more risk, particularly as U.S. gross domestic product (GDP) numbers beat expectations and surprised the markets. Globally, economic data was satisfactory as the 'Goldilocks' conditions returned. Yields also widened across Europe, Japan and New Zealand. The U.S. dollar marginally strengthened against other developed markets' currencies overall.

Following the European Union granting an extension to the Article 50 negotiation period until the end of October, there have been few new significant Brexit developments. The Tory government continues to negotiate with the opposition Labour party so as to achieve a cross-party agreement. However, achieving a deal remains elusive and, even if one is reached, it would be difficult to find a majority in Parliament in favor of such a deal.

In the eurozone, economic data was mixed, although euro area GDP growth saw its strongest reading in three quarters. The European Central Bank (ECB) met in the middle of the month and kept rates on hold, as expected, and pushed back expectations of a rate hike to 'the end of 2019'. ECB President Mario Draghi stated that the bank is ready to utilize 'all available instruments' if the economic landscape deteriorates further in the eurozone. Draghi reiterated that the balance of risks to the eurozone remains 'tilted to the downside', citing Brexit and trade issues as two specific risks plaguing the eurozone.

In the U.S., U.S.-China trade talks looked as if they were 'in the final laps', but recent news suggests that all is not well. President Trump tweeted that tariffs may in fact go up as China has backpedaled on previously agreed points. Two other areas that remain in contention are around whether the U.S. will lift current tariffs and how the U.S. will enforce Beijing's 'trade abuses'. We will just have to wait and see.

U.S High Yield

The U.S. high yield market continued to rally in April, and the index produced total returns of +1.42%. Year-to-date, the index has returned +8.78%. Spreads tightened 34 basis points (bps) to end the month at 380 bps, while yields decreased by 31 bps to 6.12%. On a year-to-date basis, spreads tightened 161 bps and yields decreased 183 bps.

From a ratings perspective, lower quality bonds outperformed. On a year-to-date basis, CCC rated bonds have returned 9.32%, while B rated credits are up 8.88% and BBs are up 8.40%.

All sectors were up last month. The worst performing were aerospace/defense (+0.35%), health insurance (+0.41%) and other financial (+0.47%). The best performing were supermarkets (+3.40%), retailers (+3.26%) and oil field services (+2.77%).

New issuance continues to underwhelm, as $17.6 billion was priced in April. Gross and net issuance, totalling $83.5 billion and $27.5 billion, respectively, in 2019, are down -11% and -10%, respectively, year-over-year. Default activity picked up in April, with

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1 Source: Morgan Stanley Investment Management Limited. Data as of 30 April 2019.

six companies defaulting on $8.1 billion in bonds and loans. However, the default rate continues to track below long-term historical averages.

High yield mutual funds and exchange-traded funds experienced month-to-date inflows of $2.8 billion and year-to-date inflows of $13.3 billion, according to Lipper. Meanwhile, loan funds had outflows of $2.9 billion for the month.

Portfolio Activity

We remain focused on middle market-sized credits and continue to be overweight transports and building materials. We remain underweight communications, a sector that tends to have the lowest coupon and longest duration capital structures.

Strategy and Outlook

Easy monetary policy, economic data that is both not too hot nor too cold, decent corporate earnings and strong demand for credit are all supportive for the markets looking forward. While we find credit relatively attractive given this rather benign macro backdrop for the year, further tightening will require risk sentiment to remain high and volatility to remain low. While the backdrop is broadly supportive, valuations are no longer as cheap. We believe the bulk of capital gains are behind us, and our base case is for the asset class to generate the majority of future excess returns from carry as opposed to aggressive spread tightening.

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

FUND FACTS

Launch date	Base currency	Index
04 December 2014	U.S. dollars	Bloomberg Barclays US High Yield 1-5 Year Cash Pay 2% Issuer Capped Index

12 Month Performance Periods to Latest Month End (%)

	APRIL '18 - APRIL '19	APRIL '17 - APRIL '18	APRIL '16 - APRIL '17	APRIL '15 - APRIL '16	APRIL '14 - APRIL '15
MS INVF US Dollar Short Duration High Yield Bond Fund - Z Shares	6.28	5.64	13.73	-1.65	--
Bloomberg Barclays US High Yield 1-5 Year Cash Pay 2% Issuer Capped Index	5.68	4.03	13.36	-2.17	--

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 fixed income securities 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.
- 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 30 April 2019 and subject to change daily.

INDEX INFORMATION

Bloomberg Barclays US High Yield 1-5 Year Cash Pay 2% Issuer Capped Index: is an issuer-constrained version of the Bloomberg Barclays US Corporate High-Yield Index that measures the market of USD denominated, noninvestment-grade, fixed-rate, taxable corporate bonds. The index follows the same rules as the uncapped index but only includes issues with a 1-5 year maturity and limits the exposure of each issuer to 2% of the total market value and redistributes any excess market value index-wide on a pro-rata basis.

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