

INVESTMENT MANAGEMENT

Morgan Stanley Investment Funds

Emerging Markets Corporate Debt Fund

FIXED INCOME | GLOBAL FIXED INCOME TEAM | MONTHLY FUND ANALYSIS | 31 August 2020

Commentary

MARKET REVIEW

EM corporate debt returned 0.90% in the month, as measured by the JP Morgan CEMBI Broad Diversified Index. Returns predominantly came from high yield companies as they were less affected by rising U.S. Treasury yields given their shorter duration profile than investment grade companies. From a regional perspective, corporate debt in Latin America (Costa Rica, the Dominican Republic, Argentina, Chile, Trinidad & Tobago, Peru and Brazil) and the Middle East (Jordan, Iraq, Oman, the U.A.E., Kuwait and Qatar) outperformed the broader index, while those in Europe (Kazakhstan, Czech Republic, Latvia and Turkey) and Asia (Thailand, Taiwan, the Philippines, China and Korea) lagged.

STRATEGY REVIEW

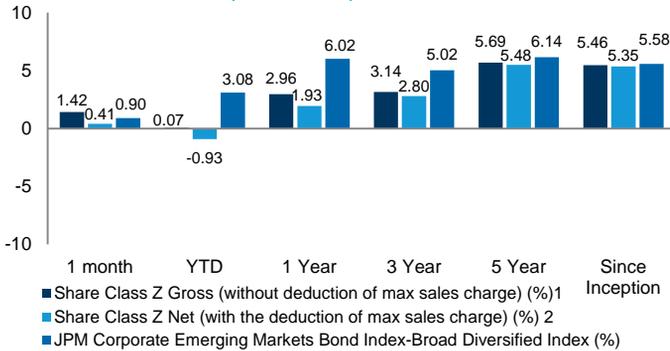
During the month, contribution to relative performance came from security selection in India, China and Turkey, as well as in the oil & gas, metals & mining and real estate sectors. Contribution to relative performance also came from overweight positions in the U.A.E., Ukraine and China, as well as in the real estate and consumer sectors. Underweight to financials and positioning in industrials contributed to performance too. Conversely, security selection in Argentina, Hong Kong and Chile, as well as in infrastructure detracted from relative performance. Performance detraction also came from underweight to Qatar, Turkey and Morocco, as well as in utilities and pulp & paper.

MAIN STRATEGY CHANGES IN THE MONTH

During the month, we increased exposure in India, Qatar, Chile and South Africa, while reducing exposure to the U.A.E. and Turkey. From a sector perspective, the underweight exposure to financials was decreased, while the underweight exposure to utilities was increased.

Source: Morgan Stanley Investment Management. As of 31st August 2020.

Investment Performance (% net of fees) in USD - Z Class Shares



12 Month Performance

Periods to Latest Month Aug '20- Aug '19- Aug '18- Aug '17- Aug '16- Aug '15- End (%)^{1,2}

	Aug '20- Aug '19	Aug '19- Aug '18	Aug '18- Aug '17	Aug '17- Aug '16	Aug '16- Aug '15
Class Z Gross (without deduction of max sales charge) ¹	2.96	10.26	-3.34	8.14	11.15
Class Z Net (with the deduction of max sales charge) ²	1.93	9.13	-4.30	7.04	10.01

¹ Figure shown assumes reinvestment of all distributions and deduction of fund level costs, but does not reflect the deduction of any sales charge applicable at investor level.

² Figure shown assumes reinvestment of all distributions and deduction of fund level costs, and includes the deduction of the maximum sales charge applicable at investor level that may be taken out of your money before it is invested.

*Example: An investor wishes to purchase shares of USD 100. At the maximum sales charge of 5.75% the investor has to expend USD 106.10. The sales charge is only incurred upon subscription.

The index is JP Morgan CEMBI Broad Diversified Index. 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.

Source: Morgan Stanley Investment Management. As of 31st August 2020.

Sector Allocation

	Portfolio (%)	Index (%)	Active (%)
Real Estate	11.26	5.81	5.46
Consumer	12.47	10.12	2.36
Transport	2.12	0.52	1.60
Other	0.81	0.00	0.81
Industrial	7.37	7.17	0.20
Infrastructure	1.76	1.78	-0.02
Diversified	2.09	2.23	-0.13
Metals & Mining	5.25	5.88	-0.63
Pulp & Paper	0.51	1.28	-0.77
Oil & Gas	12.28	13.15	-0.86
Financials	29.50	30.37	-0.87
Technology, Media & Telecommunications	6.81	10.11	-3.30
Utilities	7.77	11.60	-3.84

Regional Allocation

	Portfolio (%)	Index (%)	Active (%)
Latin America	27.06	26.39	0.67
Supranational	0.50	0.00	0.50
United States	0.43	0.00	0.43
Asia	39.52	39.10	0.43
Europe	9.55	10.35	-0.81
Middle East & Africa	22.93	24.17	-1.23
Total	100.00	100.00	-

Top Country Overweights

	Portfolio (%)	Index (%)	Active (%)
China	10.83	7.54	3.29
UAE	5.90	4.03	1.87
Nigeria	2.56	1.03	1.53
Colombia	5.38	3.93	1.45
Indonesia	4.20	2.91	1.29

Top Country Underweights

	Portfolio (%)	Index (%)	Active (%)
Qatar	1.08	3.18	-2.10
Hong Kong	3.05	4.66	-1.61
Russia	2.85	4.42	-1.57
South Korea	3.03	4.10	-1.07
Thailand	2.15	3.07	-0.92

Top 10 Issuers

Issuer Name	Portfolio (%)
PETROBRAS GLOBAL FINANCE BV	2.11
SAUDI ARABIAN OIL CO	2.05
TEVA PHARMACEUTICAL FINANCE NETHERLANDS III BV	1.79
LLPL CAPITAL PTE. LTD.	1.51
ECOPETROL SA	1.44
PROSUS NV	1.20
PARKWAY PANTAI LTD	1.11
UNITED OVERSEAS BANK LTD	1.04
SANDS CHINA LTD	1.01
MAF GLOBAL SECURITIES LTD	0.96

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Views expressed herein are the opinions of the Team and are subject to change based on market and economic conditions. These views are not necessarily representative of Morgan Stanley Investment Management (MSIM) or the firm as a whole.

Investment Approach

- Long-term mind-set that is focused on identifying companies that exhibit unique features, such as
 - Market leaders in a given EM country/sector and/or are positioned to benefit from EM's growing middle class
 - Developing into global market leaders with defensible market niches
 - Special situations where we have a strong view of the company's prospects
- Process integrates bottom-up security selection with top-down macroeconomic, sovereign, and sector analysis
- Our dedicated credit team engage in ongoing in-depth analysis, utilising proprietary fundamental research, which is a cornerstone of our rigorous credit investment process
- Analysts are able to cover the entire sector (investment-grade and high-yield) to provide a full view of industry fundamentals
- Risk management is integrated into our entire investment process

Risk Considerations

- 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.
- 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.

Definitions

Alpha is the excess return or value added (positive or negative) of the portfolio's return relative to the return of the benchmark. **Average maturity** represents the weighted average maturity for all bonds held in the portfolio. A bond's **Average price** is calculated by adding its face value to the price paid for it and dividing the sum by two. The average price is sometimes used in determining a bond's yield to maturity where the average price replaces the purchase price in the yield to maturity calculation. **Beta** is a measure of the relative volatility of a security or portfolio to the market's upward or downward movements. A beta greater than 1.0 identifies an issue or fund that will move more than the market, while a beta less than 1.0 identifies an issue or fund that will move less than the market. The beta of the market is always equal to 1. **Current yield** is a measure that looks at the current price of a bond instead of its face value and represents the return an investor would expect if he or she purchased the bond and held it for a year. Calculated by dividing the Annual Cash Inflows / Market Price. **Effective**

Portfolio Characteristics

Characteristics	Portfolio	Index
Average Price	102.59	103.64
Average Coupon	5.56	5.04
Number of Holdings	229	1,663
Yield to Maturity	5.26	4.25
Current Yield	5.60	4.87
Spread Duration	5.31	4.85
Effective Duration	4.92	4.72
Average Maturity	6.78	6.70
Beta ¹	1.29	1.00
Average S&P Rating	BB	BBB-
Average Moody's Rating	Ba1	Baa3

³ Beta calculation is based on trailing 12 months.

Fund Characteristics Summary

Benchmark	• JPM Corporate Emerging Markets Bond Index-Broad Diversified Index
Fund Launch	• March 2011
Investment Universe (Alpha Source)	• Debt securities of Emerging market corporate issuers (sovereign non-brady, corporate bonds, quasi sovereign)
Size of Universe	• Approximately \$800bn USD
Denominated in	• U.S. dollar, and to a lesser extent, non U.S. or EM local currencies
Effective Duration	• In the range of 5.0 – 5.5 years
Yield to Maturity	• Typically 5 – 6%
Average Credit Quality (Moody's/S&P/Fitch)	• Typically: BB – BBB
Expected Tracking Error	• 150 to 250 bps
Principal Portfolio Managers*	• Warren Mar, Eric Baurmeister, Sahil Tandon and Budi Suharto

*Managers may change from time to time without notice.

Duration is a measure of the sensitivity of the price (the value of principal) of a fixed-income investment to a change in interest rates. Duration is expressed as a number of years. Rising interest rates mean falling bond prices, while declining interest rates mean rising bond prices. **Fundamental research** is the analysis of overall economic, industry and company metrics. **NAV** is the Net Asset Value per share of the Fund (NAV), which represents the value of the assets of a fund less its liabilities. **Number of holdings** is the total number of securities that make up a portfolio. **Spread Duration** is a measurement of the spread of a fixed-income security rate and the risk-free rate of return. **Tracking error** is the standard deviation of the difference between the returns of an investment and its benchmark. **Yield to maturity (YTM)** measures the annual return on interest-bearing securities. In this it is assumed that they will be held to maturity. This metric includes both the coupon payments received during the term of the security and the repayment of the capital on maturity.

Themes and Investment Ideas

Market	Segment	Sub-segment	Risk considerations
Credit spectrum	HY Bias	<p>IG: Favour 5-10 year BBB, hybrid bank capital securities and corporate perps.</p> <p>HY: Focus on 3-5 year B and BB segment where refinancing risks are considered low and balance sheets strong enough to withstand the sharp drawdown and deterioration in growth outlook.</p>	<p>COVID-19: Growth outlook and shape of recovery. Success/failure of re-opening strategies. Individual government responses and implications for private sector credit. Role and willingness of multilateral lenders (such as the IMF) to support weaker EM countries. Ratings and default risks and extent to which current valuations price in uncertainty. Portfolio flows, supply technical and market access for HY issuers. Other: Escalation in geopolitical tensions around the world but particularly those between the US/China (around trade and Hong Kong). Upcoming US elections and implications for US domestic and foreign policy.</p>
Region / Country	UW Asia	<p>OW: China (Real Estate), Indonesia (M&M, Real Estate), Malaysia (Consumer), Indonesia (Real Estate, Transport), Malaysia (Oil and Gas, Consumer). MW: India (Industrial, Infrastructure, Utilities).</p> <p>UW: Hong Kong, Macau, Taiwan, Vietnam.</p>	<p>China Macro (outlook for the CNY/growth) and structural reform as the country emerges from COVID-19. India and Indonesia's fiscal space to address fallout from COVID-19. Over and above COVID-related risks, US-China relations/trade, and rising regional tensions between China and India, India and Pakistan.</p>
	OW LatAm	<p>OW: Colombia (Utilities, Oil and Gas); Brazil (Transport, Oil and Gas, Industrial), Panama (Financials, TMT).</p> <p>UW: Chile (on valuations), Mexico (on macro-deterioration), Argentina (on sovereign restructuring).</p>	<p>Brazil's ability to handle COVID-19, which has and will continue to delay much needed economic reform. Mexico's deteriorating macro outlook as government pursues austerity despite COVID-19 drag. Argentina sovereign debt restructuring and implications for the corporate sector. Demand technicals and influence of crossover flows.</p>
	MW Europe	<p>Focus on idiosyncratic stories: OW: single names: Georgia, Latvia, Ukraine, Moldova. MW: Turkey (Banks/Blue-chip corps). UW: Russia (Valuations and geopolitics).</p>	<p>Uncertainty over energy prices -- Dispute between OPEC+ member states combined with demand shock; US/Russia relations and ongoing sanctions risk. Turkey (structural reform; Central Bank independence, tightening financial conditions and implications for wholesale funding).</p>
	UW M.E & OW Africa	<p>Focus: Nigeria and Tanzania (banks and TMT), UAE (Real Estate, Financials, Utilities).</p>	<p>Demand shock to energy. Pace of oil price recovery for countries most exposed. Geopolitics across the Middle East (Saudi/GCC/Qatar).</p>
Industry / Sector	OW Real Estate	<p>Focus: China (China – high quality HY, Indonesia – developers with recurrent income streams).</p>	<p>China property, pick up in refi risk vs. broader monetary policy response, loosening financial conditions.</p>
	OW Consumer	<p>Focus: Healthcare, Food and Beverage and Protein</p>	<p>Resilience of key sectors should the recovery in growth stall or fall backwards on a second outbreak.</p>
	OW Transport, Utilities & TMT	<p>Focus: Ports, infrastructure/engineering (UAE), green energy (India). TMT broadly.</p>	<p>Pace of the economic recovery and regulatory reform. Focus on sectors and companies where we have higher cash flow visibility.</p>
	OW Industrials	<p>Focus: Basic materials (chemicals/fertilizers).</p>	<p>Pace of the economic recovery and China demand.</p>
	UW Financials, Infrastructure, O&G, M&M, P&P	<p>Focus: Financials: Hybrid capital securities from ME (UAE), LatAm (Brazil, Mexico) and Asia (Korea, Thailand). Ports (UAE) and integrated O&G SOEs in Colombia, Russia, and Indonesia.</p>	<p>Slower growth recovery and impact on banks' asset quality. Vulnerability of non-bank financial institutions particularly in India and Mexico. Continuing price weakness in energy and commodity prices.</p>

Source: MSIM. The views, opinions, forecasts and estimates expressed are those of the portfolio management team. They may not necessarily come to pass, are subject to change based on market, economic and other conditions, and do not necessarily represent those of the Firm. All information is provided for informational purposes and should not be deemed as a recommendation to buy or sell securities in the sectors or jurisdictions mentioned. **OW = Overweight, MW = Market Weight, UW = Underweight.** As of July 13, 2020.

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