

# Shareholder Q&A on MS INVF Anti-Dilution Measures

FEBRUARY 2018

Morgan Stanley Investment Funds (“MS INVF”) operates a ‘partial swing pricing’ policy. It aims to protect shareholders from the impact of dilution which occurs as a result of other investors’ subscription and redemption activity.

## Why does MS INVF need to Implement Anti-Dilution Measures?

As investors enter or exit a fund, the portfolio manager will purchase and sell securities. This activity incurs trading costs such as brokerage fees, transaction charges and taxes, which are charged to the fund and are borne by all existing shareholders, rather than the investor who has just traded. This problem is magnified when the fund is valued each day using the Net Asset Value (NAV) per share. This is because the price at which investors buy and sell shares is based on the last traded price of the underlying securities at the valuation point, which does not reflect trading costs resulting from investment subscriptions and redemptions. This is known as dilution and can negatively impact returns for existing shareholders of the fund.

## What is Swing Pricing?

Swing pricing aims to address the dilution effect outlined above by ‘adjusting’ the NAV of a fund either up or down to better reflect trading costs incurred as a result of net subscriptions and redemptions on a particular day.

MS INVF has adopted a partial swing pricing policy in order to protect existing shareholders from the value of their shares being diluted. This approach is accepted as the industry standard across Luxembourg domiciled funds as published in ‘The Association of the Luxembourg Fund Industry (“ALFI”) 2011 best practice brochure.’

A ‘Partial Swing Pricing’ policy considers that small amounts of shareholder activity will not trigger material trading costs and can be covered with existing cash balances held within a fund. If subscriptions or redemptions on a dealing day cause the net shareholder activity to exceed a defined threshold—the ‘Swing Threshold’, the NAV per share of all share classes within the fund will be ‘swung’ up or down by a defined percentage—the ‘Swing Factor’, to compensate for this.

## Swing Pricing in Practice

Below are 3 hypothetical scenarios of how swing pricing operates in practice.

For the purpose of the examples, the assumption is that the NAV per share is \$100 and the swing factor is 100 basis points (bps).

1. Net subscriptions/redemptions do not exceed the swing threshold
  - There is no adjustment made to the NAV
  - A NAV per share of \$100 is published
2. Net shareholder activity has resulted in net inflows that exceed the swing threshold
  - The NAV per share is swung upwards by 100bps
  - A NAV per share of \$101 is published

Shareholders trading in the fund, including those redeeming, receive a NAV of \$101. Investors subscribing to the fund receive fewer shares, compensating existing shareholders for dilution resulting from significant inflows.

**3. Net shareholder activity has resulted in net outflows that exceed the swing threshold**

- The NAV per share is swung down by 100bps
- A NAV per share of \$99 is published

Shareholders trading in the fund, including those subscribing, receive a NAV of \$99. Investors redeeming from the fund receive a lower price per share, compensating existing shareholders for dilution resulting from significant outflows.

		CLIENT IMPACT		
		NET INFLOWS EXCEED THRESHOLD	NET FLOWS DO NOT EXCEED THRESHOLD	NET OUTFLOWS EXCEED THRESHOLD
		NAV Adjusted Upwards	NAV Remains Constant	NAV Adjusted Downwards
CLIENT ACTIVITY	Subscribing	Pay \$101	Pay \$100	Pay \$99
	Holding	No Dilution Impact	No Impact	No Dilution Impact
	Redeeming	Receive \$101	Receive \$100	Receive \$99

**How is the Swing Threshold and Swing Factor Determined?**

The swing threshold and swing factor for each MS INVF sub-fund is established as a percentage of total assets of the fund and is reviewed and determined by Morgan Stanley Investment Management’s Anti-Dilution Subcommittee.

The swing threshold is reviewed on at least a quarterly basis with the primary objective being to protect existing shareholders whilst minimising NAV volatility. By taking into account factors such as, but not limited to, fund size, liquidity of holdings, fund cash management policy, and client composition, the swing threshold is set at a level that will not be triggered by shareholder activity for which the dilution impact would be considered immaterial to existing shareholders.

The swing factor is calculated and updated on a monthly basis or as frequently as market conditions require per market best practice and will take account of bid/offer spreads of the underlying securities, asset class, associated transaction costs, taxes and market conditions.

**How is Performance Impacted by Swing Pricing?**

Swing pricing aims to protect the overall performance of the fund. When the swing threshold of a particular sub-fund is breached, the price will be swung for all share classes of that sub-fund and an adjusted NAV will be stated. This NAV will be used in all measures of performance and for accounting purposes.

Swing pricing may increase the variability of the fund’s returns causing the fund to appear more volatile than in practice, however, this should not be interpreted as an increase in the inherent level of portfolio risk. The percentage by which the NAV is swung is an estimate of trading costs incurred and will therefore improve the fund’s performance in the long-term.

**Is Swing Pricing Just Another Charge for Investors?**

No. Swing pricing is a widely used mechanism designed solely for the protection of ongoing investors within a fund, to reduce the impact of trading costs incurred by other investors entering or exiting the fund. A swung price includes a best estimation of these trading costs, so that they are rightfully allocated to those investors that generated them.

**Does MS INVF Publish the Swing Threshold for its Sub-Funds?**

In line with industry practice, MS INVF will not disclose the swing thresholds applicable to each of its sub-funds in order to protect its shareholders from investors who may intend to trade just below the threshold in order to avoid the price being swung.

### **Does MS INV F Publish the Swing Factors Applied to its Sub-Funds?**

MS INV F does not publish swing factors calculated for each of its funds; however, this will not exceed 2% of the Net Asset Value of the fund on the relevant dealing day.

#### **PROSPECTIVE/EXISTING CLIENTS**

The swing factor is not published for any funds; however, prospectuses will confirm upper limit swing factors. Upon request, MS INV F provides clients with the following summary statistics relating to the most recent rolling 12 month period: swing factor high, swing factor low, and number of times the NAV has been swung. Prospective clients may need to sign an NDA.

#### **POST SUBSCRIPTION/REDEMPTION**

The swing factor is not published for any funds; however, MS INV F will confirm upon request if an investor received a swung price post full redemption and the factor that was applied to their transaction. In the case of a subscription or partial redemption, MS INV F will confirm, upon request, 30 days post trade date the following:

- if an investor received a swung price,
- whether the fund swung to bid or offer,
- and the factor that was applied to the transaction.

### **Who Can I Contact if I have a Question about Swing Pricing?**

Please contact [Client.Service.Administration.Luxembourg@morganstanley.com](mailto:Client.Service.Administration.Luxembourg@morganstanley.com)

**IMPORTANT INFORMATION**

**EMEA: This marketing communication has been issued by Morgan Stanley Investment Management Limited ("MSIM"). Authorised and regulated by the Financial Conduct Authority. Registered in England No. 1981121. Registered Office: 25 Cabot Square, Canary Wharf, London E14 4QA.**

This document contains information relating to the sub-fund ("Fund") of Morgan Stanley Investment Funds, a Luxembourg domiciled Société d'Investissement à Capital Variable. Morgan Stanley Investment Funds (the "Company") is registered in the Grand Duchy of Luxembourg as an undertaking for collective investment pursuant to Part 1 of the Law of 17th December 2010, as amended. The Company is an Undertaking for Collective Investment in Transferable Securities ("UCITS").

Applications for shares in the Fund should not be made without first consulting the current Prospectus, Key Investor Information Document ("KIID"), Annual Report and Semi-Annual Report ("Offering Documents"), or other documents available in your local jurisdiction which is available free of charge from the Registered Office: European Bank and Business Centre, 6B route de Trèves, L-2633 Senningerberg, R.C.S. Luxemburg B 29 192. In addition, all Italian investors should refer to the 'Extended Application Form', and all Hong Kong investors should refer to the 'Additional Information for Hong Kong Investors' section, outlined within the Prospectus. Copies of the Prospectus, KIID, the Articles of Incorporation and the annual and semi-annual reports, in German, and further information can be obtained free of charge from the representative in Switzerland. The representative in Switzerland is Carnegie Fund Services S.A., 11, rue du Général-Dufour, 1204 Geneva. The paying agent in Switzerland is Banque Cantonale de Genève, 17, quai de l'Île, 1204 Geneva. The document has been prepared solely for informational purposes and does not constitute an offer or a recommendation to buy or sell any particular security or to adopt any specific investment strategy.

Any index referred to herein is the intellectual property (including registered trademarks) of the applicable licensor. Any product based on an index is in no way sponsored, endorsed, sold or promoted by the applicable licensor and it shall not have any liability with respect thereto.

All investments involve risks, including the possible loss of principal. The material contained herein has not been based on a consideration of any individual client circumstances and is not investment advice, nor should it be construed in any way as tax, accounting, legal or regulatory advice. To that end, investors should seek independent legal and financial advice, including advice as to tax consequences, before making any investment decision.

**The information contained in this communication is not a research recommendation or 'investment research' and is classified as a 'Marketing Communication' in accordance with the applicable European or Swiss regulation. This means that this marketing communication (a) has not been prepared in accordance with legal requirements designed to promote the independence of investment research (b) is not subject to any prohibition on dealing ahead of the dissemination of investment research.**

MSIM has not authorised financial intermediaries to use and to distribute this document, unless such use and distribution is made in accordance with applicable law and regulation. MSIM shall not be liable for, and accepts no liability for, the use or misuse of this document by any such financial intermediary. If you are a distributor of the Morgan Stanley Investment Funds, some or all of the funds or shares in individual funds may be available for distribution. Please refer to your sub-distribution agreement for these details before forwarding fund information to your clients.

The whole or any part of this work may not be reproduced, copied or transmitted or any of its contents disclosed to third parties without MSIM's express written consent.

All information contained herein is proprietary and is protected under copyright law.

This document may be translated into other languages. Where such a translation is made this English version remains definitive. If there are any discrepancies between the English version and any version of this document in another language, the English version shall prevail.