What is currency risk?
When investors invest in assets that are denominated in currencies other than their local currency, changes in exchange rates will affect the value of their investment. When investing in collective investment schemes currency risk can arise in two forms:

Net Asset Value (NAV) Currency Risk – This arises from changes in exchange rates between an investor’s local currency and the base currency of the sub-fund in which they are invested.

Portfolio Currency Risk – This arises from changes in exchange rates between a sub-fund’s base currency and the currencies in which the sub-fund’s underlying assets are denominated. Where a sub-fund’s portfolio is invested solely in assets denominated in the sub-fund’s base currency, there is very little Portfolio Currency Risk, for example Morgan Stanley Investment Funds Japanese Equity Fund.

What is currency hedging?
Currency hedging is a technique that is used to reduce the impact of changes in exchange rates, on your investment.

How does the hedging work?
Currency hedging is offered for different sub-funds across the Morgan Stanley Investment Funds umbrella through separate share classes. In addition to their share of the sub-fund’s underlying assets and liabilities, these share classes also hold currency hedge positions.

Gains/losses will arise on the valuation of these currency hedge positions on each business day and are attributable to the currency hedged share classes and therefore included in the performance of these share classes only. These gains/losses are designed to offset the gains/losses arising from changes in foreign currency exchange rates.

Currency hedging involves the use of derivatives. For an explanation of how derivatives are used in the sub-funds under the Morgan Stanley Investment Funds umbrella, please refer to the Prospectus.

What types of currency hedging are available?
Morgan Stanley Investment Funds offer two types of currency hedging: NAV Hedging; and Portfolio Hedging.

The different types of currency hedging are distinguished by the following suffixes to the share class name:

<table>
<thead>
<tr>
<th>Hedging Type</th>
<th>Suffix</th>
</tr>
</thead>
<tbody>
<tr>
<td>NAV Hedging</td>
<td>H</td>
</tr>
<tr>
<td>Portfolio Hedging</td>
<td>H1</td>
</tr>
</tbody>
</table>

(eg. AH, ZH)

Why are there different types of currency hedging?
The different types of currency hedged share classes will result in differing currency exposures, as such they will be suitable for investors with differing currency requirements.

NAV Hedged Share Classes hedge the sub-fund’s base currency to the requested currency without taking into account the currency exposure of the underlying portfolio. As a result, the impact of a change in the exchange rates between the base currency and the hedge currency is reduced, however the investor still retains the risk of changes in the exchange rate between the base currency and the portfolio’s underlying currencies.
NAV Hedged Share Classes may be suitable for investors who:

• Are looking to reduce the impact of changes in exchange rates between their local currency and the base currency of the sub-fund

**Portfolio Hedged Share Classes** hedge the sub-fund’s different underlying currencies to the hedged currency. As a result, the impact of a change in the exchange rates between the underlying portfolio’s currencies and the requested currency is reduced.

Portfolio Hedged Share Classes may be suitable for investors who:

• Are looking to reduce the underlying currency exposure of the sub-fund

**How should the currency hedged share classes behave relative to unhedged share classes?**

It should be noted that currency hedging may decrease or increase a share class’ performance compared to that of an unhedged share class. In particular currency hedging may substantially limit currency hedged share classes from benefitting if the currency of the currency hedged share class falls against a sub-fund’s base currency or the portfolio’s currencies.

Consequently, non-hedged share classes can profit from currency movements, and investors in currency-hedged share classes may miss out on additional gains in these circumstances.

**NAV Hedged Share Classes**

NAV Hedged Share Classes aim to replicate the performance of the unhedged share class in the sub-fund’s base currency. However, due to imperfections in the hedging process the relative performances will not exactly match. The main reasons for this are:

• Interest rate differentials – this arises where interest rates differ between currencies, meaning that an investor would earn more by holding one currency than the other.

• Costs – there are additional costs incurred in the administration and execution of hedged share classes which are not borne by unhedged share classes.

• Hedge position mismatch – As the value of assets and exchange rates are constantly changing the hedge position will not always exactly match the underlying assets.

• Unrealised gains/losses – Open hedge positions carry an unrealized gain or loss, which do not exist in unhedged share classes, as a result the underlying assets are slightly different and therefore will not generate the same returns.

• Timing differences – Hedge positions cannot always be implemented at the same time that the sub-fund is valued, as a result the exchange rates at which currency positions are opened and closed may differ to the rates used to value the portfolio.

The NAV hedging process has no impact on the management of underlying assets in the sub-funds offering NAV hedged share classes because it is the NAV of the relevant share class which is hedged, not the underlying assets.

**Example**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>16.6%</td>
<td>8.7%</td>
<td>8.3%</td>
</tr>
<tr>
<td>2011</td>
<td>10.2%</td>
<td>6.8%</td>
<td>7.0%</td>
</tr>
<tr>
<td>2012</td>
<td>15.8%</td>
<td>18.0%</td>
<td>17.4%</td>
</tr>
<tr>
<td>2013</td>
<td>-13.1%</td>
<td>-9.5%</td>
<td>-9.7%</td>
</tr>
</tbody>
</table>

**Portfolio Hedged Share Classes**

Portfolio Hedged Share Classes aim to reduce underlying currency exposure, so they will generate different levels of performance to the sub-fund’s unhedged share classes due to the different currency hedge positions. These currency hedge positions will also suffer from the imperfections listed above for NAV Hedged Share Classes, as a result there will be some residual currency exposure.

In addition, where a sub-fund’s investment manager uses ‘active’ currency positions to try to generate additional returns, Portfolio Hedged Share Classes will negate these positions and therefore investors in these share classes will not benefit from the gains associated with these positions.

**How is the hedging monitored?**

The hedge positions are monitored daily to ensure they remain within a tolerance threshold. If the hedging positions move outside the tolerance threshold the hedges are adjusted on the same day.

**Are there any additional fees that will be incurred by the hedged share classes?**

Hedged share classes incur an additional 0.05% charge per annum. This covers the additional cost of the hedging.
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Applications for shares in Morgan Stanley Investment Funds 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 are available free of charge from our Registered Office: European Bank and Business Centre, 6B route de Trèves, L-2633 Senningerberg, R.C.S. Luxembourg 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.

Swiss investors are advised that the Prospectus, the Key Investor Information Document (KIID), the Articles of Incorporation of the Company, the audited Annual Reports and the unaudited Semi-Annual Reports may be obtained free of charge from the Swiss representative. Morgan Stanley & Co. International plc, London, Zurich Branch, Bahnhofstrasse 92, 8001 Zurich, is the Swiss representative of the Company and RBC Investor Services Bank S.A., Esch-sur-Alzette, Zurich Branch, Badenerstrasse 567, 8048 Zurich, is the Swiss paying agent.

For cash management purposes the Fund may invest in shares in the Liquidity Funds of Morgan Stanley Liquidity Funds.

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