Morgan Stanley Institutional Fund

Global Franchise Portfolio

INTERNATIONAL EQUITY TEAM

Performance Review

In the quarter period ending June 30, 2024, the Portfolio's I shares returned -2.00% (net of fees)[1], while the benchmark returned 2.63%.

For the second quarter overall, the portfolio's underperformance was due to both stock selection and sector allocation. In terms of stock selection, outperformance in information technology (IT) was the main positive, but was more than offset by weakness in financials, consumer discretionary, consumer staples and health care. Within sector allocation, the lack of energy holdings was the primary drag, although the overweight to consumer staples and underweight to communication services also hurt performance.

Market Review

Global equity markets were milder in the second quarter, with the MSCI World Index returning +2.6% in U.S. dollars (USD) and +3.0% in local currency, although for the year-to-date the index has returned a very healthy +12% in USD. IT (+11%) and communication services (+8%) continued their mighty year-to-date performance (+25% and +22%, respectively). However, it is perhaps more meaningful to look at returns at the subsector/stock level. IT strength was underpinned by semiconductors (+19%) and hardware (+17%) in the second quarter, largely thanks to Nvidia (+37%) and Apple (+23%), respectively, while for communication services Alphabet (+21%) has been the key return driver. The portfolio's key defensive sectors – consumer staples and health care (both 0%) – just avoided finishing in the red, while materials (-3%) came in last. Geography-wise, the U.S. (+4%) outperformed the index in the quarter. Singapore (+9% USD and local) was the strongest performing major market, followed by the U.K. (+4% USD and local) and Switzerland (+3% USD and local). Barring Hong Kong (+1% USD and local), all other major markets were in the red. France (-8% USD, -7% local) was the weakest constituent.

Outlook

Nvidious Position

Global equity markets are back to high multiples on high earnings, with the MSCI World Index at 18.5x forward earnings, and those earnings meant to rise 12% in 2025 despite already record margins.[2] The market seems to be dominated by the twin beliefs in the invulnerability of the U.S. economy and the massive impact of generative artificial intelligence (GenAI). The confidence in the U.S. economy is understandable given that there has been no economic recession for 15 years, barring the special case of COVID in 2020, and the GenAI excitement fits with the history of potentially transformative technologies, from railways to the internet. This is not the easiest environment for an investment philosophy that looks to back proven and established winners, with earnings that are resilient in tough economic times. When risk is "on" and the market is fixated on exponential growth curves, rating stocks on their "AI-ness", a portfolio of businesses designed for long-term compounding at reasonable valuations is not in fashion. But what if the prevailing orthodoxy is wrong or starts to unravel?

While the companies we own generally continue to compound and include good potential second-wave beneficiaries of AI, where they control proprietary data and strong market positions, they are not experiencing the rocketing valuations seen by those first-wave AI "winners". This narrative is not a surprise to those who invested through the internet bubble of the late 1990s. In recent years quality has become more conflated with growth, and many quality managers are unabashed in claiming current market winners as quality trophies. The disconnect persists long enough to test the steeliest resolve, to force conversations about whether semiconductors still display cyclical characteristics, and for the conversation to turn to a $3 trillion-plus topic: Nvidia's position.

Even with its recent pullback, Forbes' "hottest stock of the decade" (June 2024)[3] — valued at more than 20x sales and above 40x price-to-earnings (P/E)2 — has growth rates more akin to a startup, with earnings expectations having increased a staggering five times versus where they were just two years ago. Nvidia holds a 90%-95% market share in data centre GPUs (graphics processing units), has EBIT (earnings before interest and taxes) margins of 60%+ and has single-handedly produced the equivalent of 80% of the

1 Source: Morgan Stanley Investment Management. Data as of June 30, 2024. Performance for other share classes will vary.
2 Source: FactSet, as at June 30, 2024.
3 Source: Forbes, June 13, 2024, "The World's Largest Semiconductor Companies 2024"

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market capitalisation rise of the dot-com bubble.3 The current valuation assumes two things: that there will be massive commercial applications of GenAI and that Nvidia's dominance will continue.

GenAI does indeed have enormous potential in multiple areas, from coding to customer relations to image generation and beyond, and we do expect some data-rich constituents of our portfolios to benefit. However, so far at least, most businesses, which are the potential end users, have been experimenting with GenAI rather than betting heavily as they are struggling to find clear-cut use cases. There is a stark contrast between the forecasts of close to a trillion dollars of annual GenAI capital expenditures in a few years, and the mere $500 million of GenAI-related revenue that Accenture, the world's leading IT services company, has reported over the past year.

The other threat will come if any of Nvidia's four largest customers (Microsoft, Amazon, Alphabet and Meta) succeed in their efforts to design a better priced alternative to the H100 or its next generation follow-up chips Blackwell (2025) and Rubin (2026). Economics undergraduate principles spring to mind: abnormal profits first attract abnormal speculation and then abnormal competition. Moreover, there's an inherent cyclicality of demand for capital expenditure beneficiaries — whatever today's trend might be — as shown by the history of massive 50%-90% drawdowns in Nvidia's otherwise very successful history, in 2002, 2008, 2018 and 2022.[2]

For the avoidance of doubt, we are not making a bear case for Nvidia here; there is plenty of potential upside. It is just that there is plenty of potential downside as well, and the market seems more focused on the former at present. It is this very wide range of outcomes that excludes us from owning Nvidia. Our strategies do embrace change and evolve significantly over time – our flagship global strategy's consumer staples weight has gone from over 60% to under 20% over the last decade, and information technology is now over a quarter of the portfolio, even excluding the stocks that the Global Industry Classification Standard, known as GICS, moved into other sectors last year. However, we continue to look for the same characteristics since our strategy launched – strong intangible assets delivering high returns and pricing power, recurring revenues and decent, resilient growth, all at a reasonable valuation. We have also reflected on some important lessons, most notably in consumer staples and health care. We shall aim to be less patient where larger holdings underdeliver on earnings while overdelivering on negative surprises, even if their valuations appear to be supportive. Also, we recognize we need to be more wary of transformational acquisitions, especially if they may be covering up existing problems in the core business.

While recent relative performance has been challenging, our experienced team sees good prospects for our portfolio holdings. Our portfolio composition has continued to evolve, from companies with powerful strongholds in dental care and pain-relief medication to medtech for burgeoning women's health services, innovative life sciences that support medical discovery, digital music, leading data companies set to benefit from AI and the enterprise staples of our era – cloud-based software as a service, data, payments and insurance broking. We believe these should deliver a portfolio offering resilient revenue growth and faster earnings growth at a reasonable valuation, with a free cash flow yield close to that of the market, offering a history of double-digit compounding achieved over the last quarter of a century.

The current index composition and economic sailing conditions have made it challenging to deliver strong relative performance. We remain steadfast in following our quality process and our focus on valuation and fundamentals. We believe our focus on absolute compounding has worked in the past and will continue to work in the future. The backdrop of high expectations generally in the market and high expectations specifically for direct GenAI plays (and increasingly one exceptional company) make us nervous about the prospects for the market. There are only two ways of losing money in equities: the earnings go away or the multiple goes away. Our "double fussy" philosophy — owning resilient earnings at reasonable valuations — should help mitigate both risks, while providing decent compounding.

Fund Facts

Inception Date	November 28, 2001
Minimum Initial Investment ($)*	A Shares - 1,000
	I Shares - 1,000,000
Benchmark	MSCI World Net Index
Class I expense ratio	**Gross 0.92 %**
	Net 0.92 %
Class A expense ratio	**Gross 1.17 %**
	Net 1.17 %

Where the net expense ratio is lower than the gross expense ratio, certain fees have been waived and/or expenses reimbursed. These waivers and/or reimbursements will continue for at least one year from the date of the applicable fund's current

[2] Source: FactSet, as at June 30, 2024.
* Share class availability may vary by platform. For more information, please visit the specified fund page on the website.

prospectus (unless otherwise noted in the applicable prospectus) or until such time as the fund's Board of Directors acts to discontinue all or a portion of such waivers and/or reimbursements. Absent such waivers and/or reimbursements, returns would have been lower. Expenses are based on the fund's current prospectus, in effect as of the date of this commentary. For information on the applicable fund's current fees and expenses, please see the fund's current prospectus.

Performance (%)

As of June 30, 2024	MTD	QTD	YTD	1 YR	3 YR	5 YR	10 YR
Class I Shares at NAV	1.49	-2.00	2.85	7.11	3.24	7.92	9.40
Class A Shares at NAV	1.48	-2.05	2.72	6.86	2.99	7.67	9.12
Class A Shares (With Max 5.25% Sales Charge)	-3.86	-7.18	-2.66	1.26	1.15	6.51	8.53
MSCI World Net Index	2.03	2.63	11.75	20.19	6.86	11.78	9.16

Performance data quoted represents past performance, which is no guarantee of future results, and current performance may be lower or higher than the figures shown. For the most recent month end performance figures, please visit morganstanley.com/im. Investment returns and principal value will fluctuate and fund shares, when redeemed, may be worth more or less than their original cost.

Returns are net of fees and assume the reinvestment of all dividends and income. They are compared to an unmanaged market index. Returns for less than one year are cumulative (not annualized). Performance for one year or more is based on average annual total returns. The returns are reported for Class I and A shares. Performance for other share classes will vary.

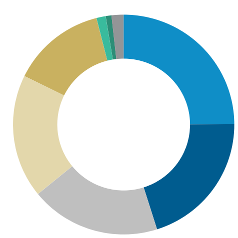
Please keep in mind that high double-digit returns are highly unusual and cannot be sustained. Investors should also be aware that these returns were primarily achieved during favorable market conditions.

Top Holdings (% of Total Net Assets)

	FUND	INDEX
Microsoft Corp	8.71	4.77
SAP SE	6.69	0.32
Visa Inc	5.78	0.63
Accenture Plc	5.01	0.29
Intercontinental Exchange Inc	4.40	0.12
RELX PLC	4.06	0.13
UnitedHealth Group Inc	3.75	0.71
Thermo Fisher Scientific Inc	3.46	0.32
Becton, Dickinson & Co.	3.36	0.10
Aon plc	3.27	0.09
Total	**48.49**	--

Effective June 30, 2023, the investment team updated the investment criteria to allow for greater flexibility regarding the need for companies in the Portfolio to pay a dividend. While a steady dividend can help underpin shareholder returns, in some cases, using capital for acquisitions and/or steady share buybacks may offer a reasonable alternative to returning capital to shareholders.

Sector Allocation (% of Total Net Assets)^



	FUND	INDEX
Information Technology	24.88	25.95
Financials	20.13	14.84
Consumer Staples	18.93	6.32
Health Care	18.11	11.77
Industrials	13.72	10.68
Consumer Discretionary	1.35	10.17
Communication Services	0.86	7.80
Energy	--	4.27
Materials	--	3.65
Real Estate	--	2.11
Utilities	--	2.44
Cash	1.74	--

^ May not sum to 100% due to rounding.

INDEX INFORMATION

The **MSCI World Net Index** is a free float adjusted market capitalization weighted index that is designed to measure the global equity market performance of developed 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 performance of the Index is listed in U.S. dollars and assumes reinvestment of net dividends.

The Index is unmanaged and do not include any expenses, fees or sales charges. It is not possible to invest directly in an Index. Any index referred to herein is the intellectual property (including registered trademarks) of the applicable licensor.

RISK CONSIDERATIONS

There is no assurance that a portfolio will achieve its investment objective. Portfolios are subject to market risk, which is the possibility that the market value of securities owned by the portfolio will decline.Portfolios are subject to market risk, which is the possibility that the market value of securities owned by the portfolio will decline and that the value of portfolio shares may therefore be less than what you paid for them. Market values can change daily due to economic and other events (e.g. natural disasters, health crises, terrorism, conflicts and social unrest) that affect markets, countries, companies or governments. It is difficult to predict the timing, duration, and potential adverse effects (e.g. portfolio liquidity) of events.Accordingly, you can lose money investing in this portfolio. Please be aware that this strategy may be subject to certain additional risks.**ESG strategies** that incorporate impact investing and/or Environmental, Social and Governance (ESG) factors could result in relative investment performance deviating from other strategies or broad market benchmarks, depending on whether such sectors or investments are in or out of favor in the market. As a result, there is no assurance ESG strategies could result in more favorable investment performance. Changes in the worldwide economy, consumer spending, competition, demographics and consumer preferences, government regulation and economic conditions may adversely affect **global franchise companies** and may negatively impact the strategy to a greater extent than if the strategy's assets were invested in a wider variety of companies. In general, **equity securities'** values also fluctuate in response to activities specific to a company. Stocks of **small-capitalization companies** carry special risks, such as limited product lines, markets and financial resources, and greater market volatility than securities of larger, more established companies. Investments in **foreign markets** entail special risks such as currency, political, economic, and market risks. The risks of investing in **emerging market** countries are greater than the risks generally associated with investments in foreign developed countries. **Non-diversified portfolios** often invest in a more limited number of issuers. As such, changes in the financial condition or market value of a single issuer may cause greater volatility. **Illiquid securities** may be more difficult to sell and value than publicly traded securities (liquidity risk). **Derivative instruments** may disproportionately increase losses and have a significant impact on performance. They also may be subject to counterparty, liquidity, valuation, correlation and market risks.

IMPORTANT INFORMATION

The views and opinions and/or analysis expressed are those of the investment team as of the date of preparation of this material and are subject to change at any time without notice due to market or economic conditions and may not necessarily come to pass. Furthermore, the views will not be updated or otherwise revised to reflect information that subsequently becomes available or circumstances existing, or changes occurring, after the date of publication. The views expressed do not reflect the opinions of all investment personnel at Morgan Stanley Investment Management (MSIM) and its subsidiaries and affiliates (collectively "the Firm"), and may not be reflected in all the strategies and products that the Firm offers.

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Please consider the investment objective, risks, charges and expenses of the fund carefully before investing. The prospectus contains this and other information about the fund. To obtain a prospectus (which includes the applicable fund's current fees and expenses, if different from those in effect as of the date of this commentary), download one at morganstanley.com/im or call 1-800-548-7786. Please read the prospectus carefully before investing.

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