MORGAN STANLEY
Form 10-Q
August 02, 2013
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2013

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

Commission File Number 1-11758

(Exact Name of Registrant as specified in its charter)

Delaware	**1585 Broadway**	**36-3145972**	**(212) 761-4000**
(State or other jurisdiction of incorporation or organization)	**New York, NY 10036** (Address of principal executive offices, including zip code)	(I.R.S. Employer Identification No.)	(Registrant s telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer x Accelerated Filer ¨

Non-Accelerated Filer ¨ Smaller reporting company ¨
(Do not check if a smaller reporting company)
Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of July 31, 2013, there were 1,958,539,144 shares of the Registrant s Common Stock, par value $0.01 per share, outstanding.

Table of Contents

QUARTERLY REPORT ON FORM 10-Q

For the quarter ended June 30, 2013

Table of Contents		Page
Part I Financial Information		
Item 1.	Financial Statements (unaudited)	1
	Condensed Consolidated Statements of Financial Condition June 30, 2013 and December 31, 2012	1
	Condensed Consolidated Statements of Income Three and Six Months Ended June 30, 2013 and 2012	2
	Condensed Consolidated Statements of Comprehensive Income Three and Six Months Ended June 30, 2013 and 2012	3
	Condensed Consolidated Statements of Cash Flows Six Months Ended June 30, 2013 and 2012	4
	Condensed Consolidated Statements of Changes in Total Equity Six Months Ended June 30, 2013 and 2012	5
	Notes to Condensed Consolidated Financial Statements (unaudited)	7
	Report of Independent Registered Public Accounting Firm	99
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	100
	Introduction	100
	Executive Summary	101
	Business Segments	111
	Accounting Developments	128
	Other Matters	130
	Critical Accounting Policies	132
	Liquidity and Capital Resources	136
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	152
Item 4.	Controls and Procedures	167
Financial Data Supplement (unaudited)		168
Part II Other Information		
Item 1.	Legal Proceedings	174
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	178
Item 6.	Exhibits	178

Table of Contents

AVAILABLE INFORMATION

Morgan Stanley files annual, quarterly and current reports, proxy statements and other information with the U.S. Securities and Exchange Commission (the SEC). You may read and copy any document we file with the SEC at the SEC s public reference room at 100 F Street, NE, Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for information on the public reference room. The SEC maintains an internet site that contains annual, quarterly and current reports, proxy and information statements and other information that issuers (including Morgan Stanley) file electronically with the SEC. Morgan Stanley s electronic SEC filings are available to the public at the SEC s internet site, *www.sec.gov*.

Morgan Stanley s internet site is *www.morganstanley.com*. You can access Morgan Stanley s Investor Relations webpage at *www.morganstanley.com/about/ir*. Morgan Stanley makes available free of charge, on or through its Investor Relations webpage, its proxy statements, Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and any amendments to those reports filed or furnished pursuant to the Securities Exchange Act of 1934, as amended (the Exchange Act), as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC. Morgan Stanley also makes available, through its Investor Relations webpage, via a link to the SEC s internet site, statements of beneficial ownership of Morgan Stanley s equity securities filed by its directors, officers, 10% or greater shareholders and others under Section 16 of the Exchange Act.

Morgan Stanley has a Corporate Governance webpage. You can access information about Morgan Stanley s corporate governance at *www.morganstanley.com/about/company/governance*. Morgan Stanley posts the following on its Corporate Governance webpage:

- Amended and Restated Certificate of Incorporation;
- Amended and Restated Bylaws;
- Charters for its Audit Committee; Operations and Technology Committee; Compensation, Management Development and Succession Committee; Nominating and Governance Committee; and Risk Committee;
- Corporate Governance Policies;
- Policy Regarding Communication with the Board of Directors;
- Policy Regarding Director Candidates Recommended by Shareholders;
- Policy Regarding Corporate Political Contributions;
- Policy Regarding Shareholder Rights Plan;
- Code of Ethics and Business Conduct;
- Code of Conduct; and

Integrity Hotline information.

Morgan Stanley s Code of Ethics and Business Conduct applies to all directors, officers and employees, including its Chief Executive Officer, Chief Financial Officer and Deputy Chief Financial Officer. Morgan Stanley will post any amendments to the Code of Ethics and Business Conduct and any waivers that are required to be disclosed by the rules of either the SEC or the New York Stock Exchange LLC (NYSE) on its internet site. You can request a copy of these documents, excluding exhibits, at no cost, by contacting Investor Relations, 1585 Broadway, New York, NY 10036 (212-761-4000). The information on Morgan Stanley s internet site is not incorporated by reference into this report.

Table of Contents

Part I Financial Information.

Item 1. Financial Statements.

MORGAN STANLEY

Condensed Consolidated Statements of Financial Condition

(dollars in millions, except share data)

(unaudited)

	June 30, 2013	December 31, 2012
Assets		
Cash and due from banks ($380 and $526 at June 30, 2013 and December 31, 2012, respectively, related to consolidated variable interest entities generally not available to the Company)	$ 16,295	$ 20,878
Interest bearing deposits with banks	30,904	26,026
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	35,363	30,970
Trading assets, at fair value (approximately $145,191 and $147,348 were pledged to various parties at June 30, 2013 and December 31, 2012, respectively; $3,128 and $3,505 related to consolidated variable interest entities, generally not available to the Company at June 30, 2013 and December 31, 2012, respectively)	260,038	267,603
Securities available for sale, at fair value	42,858	39,869
Securities received as collateral, at fair value	14,749	14,278
Federal funds sold and securities purchased under agreements to resell (includes $869 and $621 at fair value at June 30, 2013 and December 31, 2012, respectively)	142,494	134,412
Securities borrowed	129,114	121,701
Customer and other receivables	64,473	64,288
Loans (net of allowances of $125 and $106 at June 30, 2013 and December 31, 2012, respectively)	34,571	29,046
Other investments	4,869	4,999
Premises, equipment and software costs (net of accumulated depreciation of $5,987 and $5,525 at June 30, 2013 and December 31, 2012, respectively) ($215 and $224 at June 30, 2013 and December 31, 2012, respectively, related to consolidated variable interest entities, generally not available to the Company)	5,966	5,946
Goodwill	6,600	6,650
Intangible assets (net of accumulated amortization of $1,420 and $1,250 at June 30, 2013 and December 31, 2012, respectively) (includes $9 and $7 at fair value at June 30, 2013 and December 31, 2012, respectively)	3,602	3,783
Other assets ($547 and $593 at June 30, 2013 and December 31, 2012, respectively, related to consolidated variable interest entities, generally not available to the Company)	10,795	10,511
Total assets	$ 802,691	$ 780,960
Liabilities		
Deposits (includes $1,425 and $1,485 at fair value at June 30, 2013 and December 31, 2012, respectively)	$ 81,514	$ 83,266
Commercial paper and other short-term borrowings (includes $1,590 and $725 at fair value at June 30, 2013 and December 31, 2012, respectively)	2,366	2,138
Trading liabilities, at fair value	128,085	120,122
Obligation to return securities received as collateral, at fair value	19,154	18,226
Securities sold under agreements to repurchase (includes $552 and $363 at fair value at June 30, 2013 and December 31, 2012, respectively)	133,582	122,674
Securities loaned	36,135	36,849
Other secured financings (includes $6,452 and $9,466 at fair value at June 30, 2013 and December 31, 2012, respectively) ($610 and $976 at June 30, 2013 and December 31, 2012, respectively, related to consolidated variable entities and are non-recourse to the Company)	13,671	15,727
Customer and other payables	145,555	127,722
Other liabilities and accrued expenses ($117 at both June 30, 2013 and December 31, 2012, related to consolidated variable interest entities and are non-recourse to the Company)	15,417	14,928
Long-term borrowings (includes $40,819 and $44,044 at fair value at June 30, 2013 and December 31, 2012, respectively)	161,098	169,571

	736,577	711,223
Commitments and contingent liabilities (see Note 12)		
Redeemable noncontrolling interests (see Notes 3 and 14)		4,309
Equity		
Morgan Stanley shareholders equity:		
Preferred stock	1,508	1,508
Common stock, $0.01 par value:		
Shares authorized: 3,500,000,000 at June 30, 2013 and December 31, 2012;		
Shares issued: 2,038,893,979 at June 30, 2013 and 2,038,893,979 at December 31, 2012;		
Shares outstanding: 1,959,326,270 at June 30, 2013 and 1,974,042,123 at December 31, 2012	20	20
Additional Paid-in capital	23,933	23,426
Retained earnings	41,455	39,912
Employee stock trust	1,821	2,932
Accumulated other comprehensive loss	(1,169)	(516)
Common stock held in treasury, at cost, $0.01 par value; 79,567,709 shares at June 30, 2013 and 64,851,856 shares at December 31, 2012	(2,566)	(2,241)
Common stock issued to employee trust	(1,821)	(2,932)
Total Morgan Stanley shareholders equity	63,181	62,109
Nonredeemable noncontrolling interests	2,933	3,319
Total equity	66,114	65,428
Total liabilities, redeemable noncontrolling interests and equity	$ 802,691	$ 780,960

See Notes to Condensed Consolidated Financial Statements.

1

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Income

(dollars in millions, except share and per share data)

(unaudited)

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Revenues:				
Investment banking	$ 1,303	$ 1,104	$ 2,527	$ 2,167
Trading	2,894	2,469	5,588	4,871
Investments	188	63	526	148
Commissions and fees	1,217	1,040	2,385	2,217
Asset management, distribution and administration fees	2,404	2,268	4,750	4,420
Other	293	158	496	262
Total non-interest revenues	8,299	7,102	16,272	14,085
Interest income	1,422	1,323	2,820	2,865
Interest expense	1,218	1,483	2,431	3,084
Net interest	204	(160)	389	(219)
Net revenues	8,503	6,942	16,661	13,866
Non-interest expenses:				
Compensation and benefits	4,105	3,631	8,321	8,061
Occupancy and equipment	377	378	756	766
Brokerage, clearing and exchange fees	456	405	884	808
Information processing and communications	470	487	918	946
Marketing and business development	163	155	297	301
Professional services	458	477	898	889
Other	699	472	1,230	956
Total non-interest expenses	6,728	6,005	13,304	12,727
Income from continuing operations before income taxes	1,775	937	3,357	1,139
Provision for income taxes	555	224	887	278
Income from continuing operations	1,220	713	2,470	861
Discontinued operations:				
Gain (loss) from discontinued operations	(42)	52	(71)	80
Provision for (benefit from) income taxes	(13)	15	(23)	57
Net gain (loss) from discontinued operations	(29)	37	(48)	23
Net income	$ 1,191	$ 750	$ 2,422	$ 884
Net income applicable to redeemable noncontrolling interests	100		222	
Net income applicable to non redeemable noncontrolling interests	111	159	258	387
Net income applicable to Morgan Stanley	$ 980	$ 591	$ 1,942	$ 497

Earnings applicable to Morgan Stanley common shareholders	$	803	$	564	$	1,739	$	446
Amounts applicable to Morgan Stanley:								
Income from continuing operations	$	1,009	$	562	$	1,990	$	483
Net gain (loss) from discontinued operations		(29)		29		(48)		14
Net income applicable to Morgan Stanley	$	980	$	591	$	1,942	$	497
Earnings per basic common share:								
Income from continuing operations	$	0.44	$	0.28	$	0.94	$	0.23
Net gain (loss) from discontinued operations		(0.02)		0.02		(0.03)		0.01
Earnings per basic common share	$	0.42	$	0.30	$	0.91	$	0.24
Earnings per diluted common share:								
Income from continuing operations	$	0.43	$	0.28	$	0.92	$	0.23
Net gain (loss) from discontinued operations		(0.02)		0.01		(0.03)		
Earnings per diluted common share	$	0.41	$	0.29	$	0.89	$	0.23
Dividends declared per common share	$	0.05	$	0.05	$	0.10	$	0.10
Average common shares outstanding:								
Basic		1,907,737,175		1,885,179,182		1,904,470,952		1,881,070,509
Diluted		1,951,362,736		1,911,709,377		1,945,813,411		1,907,107,639

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Comprehensive Income

(dollars in millions)

(unaudited)

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Net income	$ 1,191	$ 750	$ 2,422	$ 884
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments(1)	$ (201)	$ (151)	$ (446)	$ (131)
Amortization of cash flow hedges(2)	1	1	2	3
Change in net unrealized losses on securities available for sale(3)	(342)	41	(369)	22
Pension, postretirement and other related adjustments(4)	10	17	11	19
Total other comprehensive loss	$ (532)	$ (92)	$ (802)	$ (87)
Comprehensive income	$ 659	$ 658	$ 1,620	$ 797
Net income applicable to redeemable noncontrolling interests	100		222	
Net income applicable to non redeemable noncontrolling interests	111	159	258	387
Other comprehensive income applicable to redeemable noncontrolling interests				
Other comprehensive income (loss) applicable to nonredeemable noncontrolling interests	(57)	68	(149)	(24)
Comprehensive income applicable to Morgan Stanley	$ 505	$ 431	$ 1,289	$ 434

(1) Amounts are net of provision for income taxes of $135 million and $172 million for the quarters ended June 30, 2013 and 2012, respectively, and $300 million and $176 million for the six months ended June 30, 2013 and 2012, respectively.

(2) Amounts are net of provision for income taxes of $1 million and $1 million for the quarters ended June 30, 2013 and 2012, respectively, and $2 million and $2 million for the six months ended June 30, 2013 and 2012, respectively.

(3) Amounts are net of provision for (benefit from) income taxes of $(234) million and $30 million for the quarters ended June 30, 2013 and 2012, respectively, and $(253) million and $17 million for the six months ended June 30, 2013 and 2012, respectively.

(4) Amounts are net of provision for income taxes of $6 million and $8 million for the quarters ended June 30, 2013 and 2012, respectively, and $11 million and $10 million for the six months ended June 30, 2013 and 2012, respectively.

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Cash Flows

(dollars in millions)

(unaudited)

	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 2,422	$ 884
Adjustments to reconcile net income to net cash provided by operating activities:		
(Income) loss on equity method investees	(191)	20
Compensation payable in common stock and options	559	618
Depreciation and amortization	716	793
Gain on business dispositions	(30)	(108)
Gain on sale of securities available for sale	(38)	(23)
Impairment charges	112	33
Provision for credit losses on lending activities	63	62
Other non-cash adjustments to net income	13	(6)
Changes in assets and liabilities:		
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	(4,393)	36
Trading assets, net of Trading liabilities	12,075	38,656
Securities borrowed	(7,413)	(7,189)
Securities loaned	(714)	300
Customer and other receivables and other assets	(883)	(10,972)
Customer and other payables and other liabilities	13,278	5,310
Federal funds sold and securities purchased under agreements to resell	(8,082)	(17,833)
Securities sold under agreements to repurchase	10,908	6,885
Net cash provided by operating activities	18,402	17,466
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from (payments for):		
Premises, equipment and software costs	(583)	(436)
Business dispositions, net of cash disposed	530	1,536
Loans, net	(3,441)	(1,670)
Purchases of securities available for sale	(14,335)	(6,418)
Sales, maturities and redemptions of securities available for sale	11,040	5,439
Other investing activities	186	70
Net cash used for investing activities	(6,603)	(1,479)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net proceeds from (payments for):		
Commercial paper and other short-term borrowings	228	(855)
Noncontrolling interests	(540)	(178)
Other secured financings	(1,761)	(4,822)
Deposits	(1,752)	2,590
Proceeds from:		
Excess tax benefits associated with stock-based awards	13	42
Derivatives financing activities	459	241
Issuance of long-term borrowings	21,698	9,422
Payments for:		
Long-term borrowings	(22,958)	(26,445)
Derivatives financing activities	(498)	(113)
Repurchases of common stock for employee tax withholding	(314)	(191)

Purchase of additional stake in Morgan Stanley Smith Barney Holdings LLC	(4,725)	
Cash dividends	(239)	(230)
Net cash used for financing activities	(10,389)	(20,539)
Effect of exchange rate changes on cash and cash equivalents	(735)	(307)
Effect of cash and cash equivalents related to variable interest entities	(380)	(447)
Net increase (decrease) in cash and cash equivalents	295	(5,306)
Cash and cash equivalents, at beginning of period	46,904	47,312
Cash and cash equivalents, at end of period	$ 47,199	$ 42,006
Cash and cash equivalents include:		
Cash and due from banks	$ 16,295	$ 12,408
Interest bearing deposits with banks	30,904	29,598
Cash and cash equivalents, at end of period	$ 47,199	$ 42,006

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

Cash payments for interest were $2,177 million and $2,404 million for the six months ended June 30, 2013 and 2012, respectively.

Cash payments for income taxes were $537 million and $220 million for the six months ended June 30, 2013 and 2012, respectively.

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Changes in Total Equity

Six Months Ended June 30, 2013

(dollars in millions)

(unaudited)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Employee Stock Trust	Accumulated Other Comprehensive Income (Loss)	Common Stock Held in Treasury at Cost	Common Stock Issued to Employee Trust	Non-redeemable Non-controlling Interests	Total Equity
BALANCE AT DECEMBER 31, 2012	$ 1,508	$ 20	$ 23,426	$ 39,912	$ 2,932	$ (516)	$ (2,241)	$ (2,932)	$ 3,319	$ 65,428
Net income applicable to Morgan Stanley				1,942						1,942
Net income applicable to nonredeemable noncontrolling interests									258	258
Dividends				(248)						(248)
Shares issued under employee plans and related tax effects			507		(1,111)		(11)	1,111		496
Repurchases of common stock							(314)			(314)
Foreign currency translation adjustments						(297)			(149)	(446)
Net change in cash flow hedges						2				2
Change in net unrealized losses on securities available for sale						(369)				(369)
Pension, postretirement and other related adjustments						11				11
Morgan Stanley Smith Barney Holdings LLC redemption value adjustment				(151)						(151)
Other net decreases									(495)	(495)
BALANCE AT JUNE 30, 2013	$ 1,508	$ 20	$ 23,933	$ 41,455	$ 1,821	$ (1,169)	$ (2,566)	$ (1,821)	$ 2,933	$ 66,114

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Changes in Total Equity (Continued)

Six Months Ended June 30, 2012

(dollars in millions)

(unaudited)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Employee Stock Trust	Accumulated Other Comprehensive Income (Loss)	Common Stock Held in Treasury at Cost	Common Stock Issued to Employee Trust	Non-Redeemable Non-controlling Interests	Total Equity
BALANCE AT DECEMBER 31, 2011	$ 1,508	$ 20	$ 22,836	$ 40,341	$ 3,166	$ (157)	$ (2,499)	$ (3,166)	$ 8,029	$ 70,078
Net income applicable to Morgan Stanley				497						497
Net income applicable to nonredeemable noncontrolling interests									387	387
Dividends				(252)						(252)
Shares issued under employee plans and related tax effects			315		32		486	(32)		801
Repurchases of common stock							(191)			(191)
Foreign currency translation adjustments						(102)			(29)	(131)
Net change in cash flow hedges						3				3
Change in net unrealized gains on securities available for sale						22				22
Pension, postretirement and other related adjustments						14			5	19
Other net increases									404	404
BALANCE AT JUNE 30, 2012	$ 1,508	$ 20	$ 23,151	$ 40,586	$ 3,198	$ (220)	$ (2,204)	$ (3,198)	$ 8,796	$ 71,637

See Notes to Condensed Consolidated Financial Statements.

6

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Introduction and Basis of Presentation.

The Company. Morgan Stanley, a financial holding company, is a global financial services firm that maintains significant market positions in each of its business segments Institutional Securities, Wealth Management and Investment Management. The Company, through its subsidiaries and affiliates, provides a wide variety of products and services to a large and diversified group of clients and customers, including corporations, governments, financial institutions and individuals. Unless the context otherwise requires, the terms Morgan Stanley or the Company mean Morgan Stanley (the Parent) together with its consolidated subsidiaries.

Effective with the quarter ended June 30, 2013, the Global Wealth Management Group and Asset Management business segments were re-titled Wealth Management and Investment Management, respectively.

A summary of the activities of each of the Company s business segments is as follows:

Institutional Securities provides financial advisory and capital raising services, including advice on mergers and acquisitions, restructurings, real estate and project finance; corporate lending; sales, trading, financing and market-making activities in equity and fixed income securities and related products, including foreign exchange and commodities; and investment activities.

Wealth Management (formerly known as Global Wealth Management Group), provides brokerage and investment advisory services to individual investors and small-to-medium sized businesses and institutions covering various investment alternatives; financial and wealth planning services; annuity and other insurance products; credit and other lending products; cash management services; retirement services; and trust and fiduciary services and engages in fixed income trading, which primarily facilitates clients trading or investments in such securities.

Investment Management (formerly known as Asset Management) provides a broad array of investment strategies that span the risk/return spectrum across geographies, asset classes and public and private markets to a diverse group of clients across the institutional and intermediary channels as well as high net worth clients.

Discontinued Operations.

Quilter. On April 2, 2012, the Company completed the sale of Quilter & Co. Ltd. (Quilter), its retail wealth management business in the United Kingdom (U.K.). The results of Quilter are reported as discontinued operations within the Wealth Management business segment for all periods presented.

Saxon. On October 24, 2011, the Company announced that it had reached an agreement to sell Saxon, a provider of servicing and subservicing of residential mortgage loans, to Ocwen Financial Corporation. The transaction, which was restructured as a sale of Saxon s assets during the first quarter of 2012, was substantially completed in the second quarter of 2012. The results of Saxon are reported as discontinued operations within the Institutional Securities business segment for all periods presented.

Prior period amounts have been recast for discontinued operations. See Note 21 for additional information on discontinued operations.

Basis of Financial Information. The condensed consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (U.S.), which require the Company to make estimates and assumptions regarding the valuations of certain financial instruments, the valuation of goodwill and intangible assets, compensation, deferred tax assets, the outcome of litigation and tax matters, and other matters that affect the condensed consolidated financial statements and related disclosures. The Company believes that the estimates utilized in the preparation of the condensed consolidated financial statements are prudent and reasonable. Actual results could differ materially from these estimates.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Intercompany balances and transactions have been eliminated.

In the quarter ended March 31, 2013, the Company renamed Principal transactions Trading revenues as Trading revenues and Principal transactions Investments revenues as Investments revenues in the condensed consolidated statements of income, and Financial instruments owned as Trading assets, Financial instruments sold, not yet purchased as Trading liabilities, Receivables as Customer and other receivables Payables as Customer and other payables in the condensed consolidated statements of financial condition.

The condensed consolidated financial statements should be read in conjunction with the Company s consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2012 (the Form 10-K). The condensed consolidated financial statements reflect all adjustments of a normal recurring nature that are, in the opinion of management, necessary for the fair presentation of the results for the interim period. The results of operations for interim periods are not necessarily indicative of results for the entire year.

Consolidation. The condensed consolidated financial statements include the accounts of the Company, its wholly owned subsidiaries and other entities in which the Company has a controlling financial interest, including certain variable interest entities (VIE) (see Note 7). For consolidated subsidiaries that are less than wholly owned, the third-party holdings of equity interests are referred to as noncontrolling interests. The portion of net income attributable to noncontrolling interests for such subsidiaries is presented as either Net income (loss) applicable to redeemable noncontrolling interests or Net income (loss) applicable to nonredeemable noncontrolling interests in the condensed consolidated statements of income. The portion of the shareholders equity of such subsidiaries that is redeemable is presented as Redeemable noncontrolling interests outside of the equity section in the condensed consolidated statements of financial condition. The portion of the shareholders equity of such subsidiaries that is nonredeemable is presented as Nonredeemable noncontrolling interests, a component of total equity, in the condensed consolidated statements of financial condition.

For entities where (1) the total equity investment at risk is sufficient to enable the entity to finance its activities without additional support and (2) the equity holders bear the economic residual risks and returns of the entity and have the power to direct the activities of the entity that most significantly affect its economic performance, the Company consolidates those entities it controls either through a majority voting interest or otherwise. For VIEs (*i.e.*, entities that do not meet these criteria), the Company consolidates those entities where the Company has the power to make the decisions that most significantly affect the economic performance of the VIE and has the obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE, except for certain VIEs that are money market funds, investment companies or are entities qualifying for accounting purposes as investment companies. Generally, the Company consolidates those entities when it absorbs a majority of the expected losses or a majority of the expected residual returns, or both, of the entities.

For investments in entities in which the Company does not have a controlling financial interest but has significant influence over operating and financial decisions, the Company generally applies the equity method of accounting with net gains and losses recorded within Other revenues. Where the Company has elected to measure certain eligible investments at fair value in accordance with the fair value option, net gains and losses are recorded within Investments revenues (see Note 4).

Equity and partnership interests held by entities qualifying for accounting purposes as investment companies are carried at fair value.

The Company s significant regulated U.S. and international subsidiaries include Morgan Stanley & Co. LLC (MS&Co.), Morgan Stanley Smith Barney LLC (MSSB LLC), Morgan Stanley & Co. International plc

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(MSIP), Morgan Stanley MUFG Securities Co., Ltd. (MSMS), Morgan Stanley Bank, N.A. (MSBNA) and Morgan Stanley Private Bank, National Association (MSPBNA).

Income Statement Presentation. The Company, through its subsidiaries and affiliates, provides a wide variety of products and services to a large and diversified group of clients and customers, including corporations, governments, financial institutions and individuals. In connection with the delivery of the various products and services to clients, the Company manages its revenues and related expenses in the aggregate. As such, when assessing the performance of its businesses, primarily in its Institutional Securities business segment, the Company considers its trading, investment banking, commissions and fees and interest income, along with the associated interest expense, as one integrated activity.

2. Significant Accounting Policies.

For a detailed discussion about the Company s significant accounting policies, see Note 2 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K.

During the six months ended June 30, 2013, no updates were made to the Company s significant accounting policies.

Condensed Consolidated Statements of Cash Flows.

For purposes of the condensed consolidated statements of cash flows, cash and cash equivalents consist of Cash and due from banks and Interest bearing deposits with banks, which are highly liquid investments with original maturities of three months or less, held for investment purposes, and readily convertible to known amounts of cash.

In the six months ended June 30, 2012, the Company s significant non-cash activities included approximately $0.6 billion of net assets received from Citigroup, Inc. (Citi) related to Citi s required equity contribution in connection with the Morgan Stanley Smith Barney Holdings LLC (Wealth Management JV) platform integration (see Notes 3 and 14).

During the third quarter of 2012, the Company identified that activities related to certain loans had been reported as cash flows from operating activities that should have been presented as investing activities. The Company corrected the previously presented cash flows for these loans and in doing so, the condensed consolidated statements of cash flows for the six months ended June 30, 2012 has been adjusted to increase net cash flows from operating activities by $1.7 billion, with the corresponding decrease in net cash flows from investing activities. The Company has evaluated the effect of the incorrect presentation, both qualitatively and quantitatively, and concluded that it did not have a material impact on, nor require amendment of, any previously filed annual or quarterly consolidated financial statements.

Accounting Developments.

Disclosures about Offsetting Assets and Liabilities. In January 2013, the Financial Accounting Standards Board (the FASB) issued an accounting update that clarified the intended scope of the new balance sheet offsetting disclosures to derivatives, repurchase agreements, and securities lending transactions to the extent that they are either offset in the financial statements or subject to an enforceable master netting arrangement or similar agreement. These disclosure requirements became effective for the Company beginning on January 1, 2013. Since these amended principles require only additional disclosures concerning offsetting and related arrangements, adoption has not affected the Company s condensed consolidated statements of income or financial condition (see Notes 6 and 11).

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. In February 2013, the FASB issued an accounting update that created new disclosure requirements requiring entities to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under U.S. generally accepted accounting principles (GAAP) to be reclassified in its entirety to net income. The disclosure requirements became effective for the Company beginning on January 1, 2013. Since these amended principles require only additional disclosures concerning amounts reclassified out of accumulated other comprehensive income, adoption has not affected the Company s condensed consolidated statements of comprehensive income or notes to the condensed consolidated financial statements (see Note 14).

3. Morgan Stanley Smith Barney Holdings LLC.

On May 31, 2009, the Company and Citi consummated the combination of each institution s respective wealth management business. The combined businesses operated as the Wealth Management JV through June 28, 2013.

Prior to September 2012, the Company owned 51% and Citi owned 49% of the Wealth Management JV. On September 17, 2012, the Company purchased an additional 14% stake in the Wealth Management JV from Citi for $1.89 billion, increasing the Company s interest from 51% to 65%. In addition, in September 2012, the terms of the Wealth Management JV agreement regarding the purchase of the remaining 35% interest were amended, which resulted in a reclassification of approximately $4.3 billion from nonredeemable noncontrolling interests to redeemable noncontrolling interests during the third quarter of 2012. Prior to September 17, 2012, Citi s results related to its 49% interest were reported in net income (loss) applicable to nonredeemable noncontrolling interests in the condensed consolidated statements of income. Subsequent to the purchase of the additional 14% stake, Citi s results related to the 35% interest were reported in net income (loss) applicable to redeemable noncontrolling interests in the condensed consolidated statements of income. In connection with the Company s acquisition of the additional 14% stake in the Wealth Management JV and pursuant to an amended deposit sweep agreement between Citi and the Company, in October 2012 $5.4 billion of deposits held by Citi relating to customer accounts were transferred to the Company s depository institutions at no premium based on a valuation agreement reached between Citi and the Company, and as such were no longer swept to Citi.

In June 2013, the Company received all regulatory approvals to acquire the remaining 35% stake in the Wealth Management JV. On June 28, 2013, the Company purchased the remaining 35% interest for $4.725 billion, increasing the Company s interest from 65% to 100%. The Company recorded a negative adjustment to retained earnings of approximately $151 million (net of tax) to reflect the difference between the purchase price for the 35% interest in the Wealth Management JV and its carrying value. This adjustment negatively impacted the calculation of basic and diluted earnings per share for the quarter and six months ended June 30, 2013 (see Note 15). Concurrent with the acquisition of the remaining 35% stake in the Wealth Management JV, the deposit sweep agreement between Citi and the Company was terminated. As a result of the termination of the deposit sweep agreement, approximately $57 billion of deposits will no longer be swept to Citi but will instead be transferred to the Company s depository institutions on an agreed upon basis over the next 24 months (*i.e.*, through June 1, 2015) (see Note 22).

Additionally, in conjunction with the purchase of the remaining 35% interest, the Company redeemed all of the Class A Preferred Interests in the Wealth Management JV owned by Citi and its affiliates for approximately $2.028 billion and repaid to Citi $880 million in senior debt.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Fair Value Disclosures.

Fair Value Measurements.

A description of the valuation techniques applied to the Company s major categories of assets and liabilities measured at fair value on a recurring basis follows.

Trading Assets and Trading Liabilities.

U.S. Government and Agency Securities.

U.S. Treasury Securities. U.S. Treasury securities are valued using quoted market prices. Valuation adjustments are not applied. Accordingly, U.S. Treasury securities are generally categorized in Level 1 of the fair value hierarchy.

U.S. Agency Securities. U.S. agency securities are composed of three main categories consisting of agency-issued debt, agency mortgage pass-through pool securities and collateralized mortgage obligations. Non-callable agency-issued debt securities are generally valued using quoted market prices. Callable agency-issued debt securities are valued by benchmarking model-derived prices to quoted market prices and trade data for identical or comparable securities. The fair value of agency mortgage pass-through pool securities is model-driven based on spreads of the comparable To-be-announced (TBA) security. Collateralized mortgage obligations are valued using quoted market prices and trade data adjusted by subsequent changes in related indices for identical or comparable securities. Actively traded non-callable agency-issued debt securities are generally categorized in Level 1 of the fair value hierarchy. Callable agency-issued debt securities, agency mortgage pass-through pool securities and collateralized mortgage obligations are generally categorized in Level 2 of the fair value hierarchy.

Other Sovereign Government Obligations.

Foreign sovereign government obligations are valued using quoted prices in active markets when available. These bonds are generally categorized in Level 1 of the fair value hierarchy. If the market is less active or prices are dispersed, these bonds are categorized in Level 2 of the fair value hierarchy.

Corporate and Other Debt.

State and Municipal Securities. The fair value of state and municipal securities is determined using recently executed transactions, market price quotations and pricing models that factor in, where applicable, interest rates, bond or credit default swap spreads and volatility. These bonds are generally categorized in Level 2 of the fair value hierarchy.

Residential Mortgage-Backed Securities (RMBS), Commercial Mortgage-Backed Securities (CMBS) and other Asset-Backed Securities (ABS). RMBS, CMBS and other ABS may be valued based on price or spread data obtained from observed transactions or independent external parties such as vendors or brokers. When position-specific external price data are not observable, the fair value determination may require benchmarking to similar instruments and/or analyzing expected credit losses, default and recovery rates, and/or applying discounted cash flow techniques. In evaluating the fair value of each security, the Company considers security collateral-specific attributes, including payment priority, credit enhancement levels, type of collateral, delinquency rates and loss severity. In addition, for RMBS borrowers, Fair Isaac Corporation (FICO) scores and the level of documentation for the loan are also considered. Market standard models, such as Intex, Trepp or others, may be deployed to model the specific collateral composition and cash flow structure of each transaction. Key inputs to these models are market spreads, forecasted credit losses, default and prepayment rates for each asset category. Valuation

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

levels of RMBS and CMBS indices are also used as an additional data point for benchmarking purposes or to price outright index positions.

RMBS, CMBS and other ABS are generally categorized in Level 2 of the fair value hierarchy. If external prices or significant spread inputs are unobservable or if the comparability assessment involves significant subjectivity related to property type differences, cash flows, performance and other inputs, then RMBS, CMBS and other ABS are categorized in Level 3 of the fair value hierarchy.

Corporate Bonds. The fair value of corporate bonds is determined using recently executed transactions, market price quotations (where observable), bond spreads or credit default swap spreads obtained from independent external parties such as vendors and brokers adjusted for any basis difference between cash and derivative instruments. The spread data used are for the same maturity as the bond. If the spread data do not reference the issuer, then data that reference a comparable issuer are used. When position-specific external price data are not observable, fair value is determined based on either benchmarking to similar instruments or cash flow models with yield curves, bond or single-name credit default swap spreads and recovery rates as significant inputs. Corporate bonds are generally categorized in Level 2 of the fair value hierarchy; in instances where prices, spreads or any of the other aforementioned key inputs are unobservable, they are categorized in Level 3 of the fair value hierarchy.

Collateralized Debt Obligation (CDO). The Company holds cash CDOs that typically reference a tranche of an underlying synthetic portfolio of single name credit default swaps collateralized by corporate bonds (credit-linked notes) or cash portfolio of asset-backed securities (asset-backed CDOs). Credit correlation, a primary input used to determine the fair value of credit-linked notes, is usually unobservable and derived using a benchmarking technique. The other credit-linked note model inputs such as credit spreads, including collateral spreads, and interest rates are typically observable. Asset-backed CDOs are valued based on an evaluation of the market and model input parameters sourced from similar positions as indicated by primary and secondary market activity. Each asset-backed CDO position is evaluated independently taking into consideration available comparable market levels, underlying collateral performance and pricing, and deal structures, as well as liquidity. Cash CDOs are categorized in Level 2 of the fair value hierarchy when either the credit correlation input is insignificant or comparable market transactions are observable. In instances where the credit correlation input is deemed to be significant or comparable market transactions are unobservable, cash CDOs are categorized in Level 3 of the fair value hierarchy.

Corporate Loans and Lending Commitments. The fair value of corporate loans is determined using recently executed transactions, market price quotations (where observable), implied yields from comparable debt, and market observable credit default swap spread levels obtained from independent external parties such as vendors and brokers adjusted for any basis difference between cash and derivative instruments, along with proprietary valuation models and default recovery analysis where such transactions and quotations are unobservable. The fair value of contingent corporate lending commitments is determined by using executed transactions on comparable loans and the anticipated market price based on pricing indications from syndicate banks and customers. The valuation of loans and lending commitments also takes into account fee income that is considered an attribute of the contract. Corporate loans and lending commitments are categorized in Level 2 of the fair value hierarchy except in instances where prices or significant spread inputs are unobservable, in which case they are categorized in Level 3 of the fair value hierarchy.

Mortgage Loans. Mortgage loans are valued using observable prices based on transactional data or third-party pricing for identical or comparable instruments, when available. Where position-specific external prices are not observable, the Company estimates fair value based on benchmarking to prices and rates observed in the primary market for similar loan or borrower types or based on the present value of

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

expected future cash flows using its best estimates of the key assumptions, including forecasted credit losses, prepayment rates, forward yield curves and discount rates commensurate with the risks involved or a methodology that utilizes the capital structure and credit spreads of recent comparable securitization transactions. Mortgage loans valued based on observable market data for identical or comparable instruments are categorized in Level 2 of the fair value hierarchy. Where observable prices are not available, due to the subjectivity involved in the comparability assessment related to mortgage loan vintage, geographical concentration, prepayment speed and projected loss assumptions, mortgage loans are categorized in Level 3 of the fair value hierarchy. Mortgage loans are presented within Loans and lending commitments in the fair value hierarchy table.

Auction Rate Securities (ARS). The Company primarily holds investments in Student Loan Auction Rate Securities (SLARS) and Municipal Auction Rate Securities (MARS) with interest rates that are reset through periodic auctions. SLARS are ABS backed by pools of student loans. MARS are municipal bonds often wrapped by municipal bond insurance. ARS were historically traded and valued as floating rate notes, priced at par due to the auction mechanism. Beginning in fiscal 2008, uncertainties in the credit markets have resulted in auctions failing for certain types of ARS. Once the auctions failed, ARS could no longer be valued using observations of auction market prices. Accordingly, the fair value of ARS is determined using independent external market data where available and an internally developed methodology to discount for the lack of liquidity and non-performance risk.

Inputs that impact the valuation of SLARS are independent external market data, the underlying collateral types, level of seniority in the capital structure, amount of leverage in each structure, credit rating and liquidity considerations. Inputs that impact the valuation of MARS are recently executed transactions, the maximum rate, quality of underlying issuers/insurers and evidence of issuer calls/prepayment. ARS are generally categorized in Level 2 of the fair value hierarchy as the valuation technique relies on observable external data. SLARS and MARS are presented within Asset-backed securities and State and municipal securities, respectively, in the fair value hierarchy table.

Corporate Equities.

Exchange-Traded Equity Securities. Exchange-traded equity securities are generally valued based on quoted prices from the exchange. To the extent these securities are actively traded, valuation adjustments are not applied, and they are categorized in Level 1 of the fair value hierarchy; otherwise, they are categorized in Level 2 or Level 3 of the fair value hierarchy.

Unlisted Equity Securities. Unlisted equity securities are valued based on an assessment of each underlying security, considering rounds of financing and third-party transactions, discounted cash flow analyses and market-based information, including comparable company transactions, trading multiples and changes in market outlook, among other factors. These securities are generally categorized in Level 3 of the fair value hierarchy.

Fund Units. Listed fund units are generally marked to the exchange-traded price or net asset value (NAV) and are categorized in Level 1 of the fair value hierarchy if actively traded on an exchange or in Level 2 of the fair value hierarchy if trading is not active. Unlisted fund units are generally marked to NAV and categorized as Level 2; however, positions which are not redeemable at the measurement date or in the near future are categorized in Level 3 of the fair value hierarchy.

Derivative and Other Contracts.

Listed Derivative Contracts. Listed derivatives that are actively traded are valued based on quoted prices from the exchange and are categorized in Level 1 of the fair value hierarchy. Listed derivatives that

13

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

are not actively traded are valued using the same approaches as those applied to over-the-counter (OTC) derivatives; they are generally categorized in Level 2 of the fair value hierarchy.

OTC Derivative Contracts. OTC derivative contracts include forward, swap and option contracts related to interest rates, foreign currencies, credit standing of reference entities, equity prices or commodity prices.

Depending on the product and the terms of the transaction, the fair value of OTC derivative products can be either observed or modeled using a series of techniques and model inputs from comparable benchmarks, including closed-form analytic formulas, such as the Black-Scholes option-pricing model, and simulation models or a combination thereof. Many pricing models do not entail material subjectivity because the methodologies employed do not necessitate significant judgment, and the pricing inputs are observed from actively quoted markets, as is the case for generic interest rate swaps, certain option contracts and certain credit default swaps. In the case of more established derivative products, the pricing models used by the Company are widely accepted by the financial services industry. A substantial majority of OTC derivative products valued by the Company using pricing models fall into this category and are categorized in Level 2 of the fair value hierarchy.

Other derivative products, including complex products that have become illiquid, require more judgment in the implementation of the valuation technique applied due to the complexity of the valuation assumptions and the reduced observability of inputs. This includes certain types of interest rate derivatives with both volatility and correlation exposure and credit derivatives including credit default swaps on certain mortgage-backed or asset-backed securities, basket credit default swaps and CDO-squared positions (a CDO-squared position is a special purpose vehicle that issues interests, or tranches, that are backed by tranches issued by other CDOs) where direct trading activity or quotes are unobservable. These instruments involve significant unobservable inputs and are categorized in Level 3 of the fair value hierarchy.

Derivative interests in credit default swaps on certain mortgage-backed or asset-backed securities, for which observability of external price data is limited, are valued based on an evaluation of the market and model input parameters sourced from similar positions as indicated by primary and secondary market activity. Each position is evaluated independently taking into consideration available comparable market levels as well as cash-synthetic basis, or the underlying collateral performance and pricing, behavior of the tranche under various cumulative loss and prepayment scenarios, deal structures (*e.g.*, non-amortizing reference obligations, call features, etc.) and liquidity. While these factors may be supported by historical and actual external observations, the determination of their value as it relates to specific positions nevertheless requires significant judgment.

For basket credit default swaps and CDO-squared positions, the correlation input between reference credits is unobservable for each specific swap or position and is benchmarked to standardized proxy baskets for which correlation data are available. The other model inputs such as credit spread, interest rates and recovery rates are observable. In instances where the correlation input is deemed to be significant, these instruments are categorized in Level 3 of the fair value hierarchy; otherwise, these instruments are categorized in Level 2 of the fair value hierarchy.

The Company trades various derivative structures with commodity underlyings. Depending on the type of structure, the model inputs generally include interest rate yield curves, commodity underlier price curves, implied volatility of the underlying commodities and, in some cases, the implied correlation between these inputs. The fair value of these products is determined using executed trades and broker and consensus data to provide values for the aforementioned inputs. Where these inputs are unobservable, relationships to observable commodities and data points, based on historic and/or implied observations, are employed as a technique to estimate the model input values. Commodity derivatives are generally

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

categorized in Level 2 of the fair value hierarchy; in instances where significant inputs are unobservable, they are categorized in Level 3 of the fair value hierarchy.

For further information on derivative instruments and hedging activities, see Note 11.

Investments.

The Company s investments include direct investments in equity securities as well as investments in private equity funds, real estate funds and hedge funds, which include investments made in connection with certain employee deferred compensation plans. Direct investments are presented in the fair value hierarchy table as Principal investments and Other. Initially, the transaction price is generally considered by the Company as the exit price and is the Company s best estimate of fair value.

After initial recognition, in determining the fair value of non-exchange-traded internally and externally managed funds, the Company generally considers the NAV of the fund provided by the fund manager to be the best estimate of fair value. For non-exchange-traded investments either held directly or held within internally managed funds, fair value after initial recognition is based on an assessment of each underlying investment, considering rounds of financing and third-party transactions, discounted cash flow analyses and market-based information, including comparable company transactions, trading multiples and changes in market outlook, among other factors. Exchange-traded direct equity investments are generally valued based on quoted prices from the exchange.

Exchange-traded direct equity investments that are actively traded are categorized in Level 1 of the fair value hierarchy. Non-exchange-traded direct equity investments and investments in private equity and real estate funds are generally categorized in Level 3 of the fair value hierarchy. Investments in hedge funds that are redeemable at the measurement date or in the near future are categorized in Level 2 of the fair value hierarchy; otherwise, they are categorized in Level 3 of the fair value hierarchy.

Physical Commodities.

The Company trades various physical commodities, including crude oil and refined products, natural gas, base and precious metals, and agricultural products. Fair value for physical commodities is determined using observable inputs, including broker quotations and published indices. Physical commodities are categorized in Level 2 of the fair value hierarchy; in instances where significant inputs are unobservable, they are categorized in Level 3 of the fair value hierarchy.

Securities Available for Sale.

Securities available for sale are composed of U.S. government and agency securities (*e.g.*, U.S. Treasury securities, agency-issued debt, agency mortgage pass-through securities and collateralized mortgage obligations), CMBS, Federal Family Education Loan Program (FFELP) student loan asset-backed securities, auto loan asset-backed securities, corporate bonds and equity securities. Actively traded U.S. Treasury securities, non-callable agency-issued debt securities and equity securities are generally categorized in Level 1 of the fair value hierarchy. Callable agency-issued debt securities, agency mortgage pass-through securities, collateralized mortgage obligations, CMBS, FFELP student loan asset-backed securities, auto loan asset-backed securities and corporate bonds are generally categorized in Level 2 of the fair value hierarchy. For further information on securities available for sale, see Note 5.

Deposits.

Time Deposits. The fair value of certificates of deposit is determined using third-party quotations. These deposits are generally categorized in Level 2 of the fair value hierarchy.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Commercial Paper and Other Short-Term Borrowings/Long-Term Borrowings.

Structured Notes. The Company issues structured notes that have coupon or repayment terms linked to the performance of debt or equity securities, indices, currencies or commodities. Fair value of structured notes is determined using valuation models for the derivative and debt portions of the notes. These models incorporate observable inputs referencing identical or comparable securities, including prices to which the notes are linked, interest rate yield curves, option volatility and currency, commodity or equity prices. Independent, external and traded prices for the notes are considered as well. The impact of the Company s own credit spreads is also included based on the Company s observed secondary bond market spreads. Most structured notes are categorized in Level 2 of the fair value hierarchy.

Securities Purchased under Agreements to Resell and Securities Sold under Agreements to Repurchase.

The fair value of a reverse repurchase agreement or repurchase agreement is computed using a standard cash flow discounting methodology. The inputs to the valuation include contractual cash flows and collateral funding spreads, which are estimated using various benchmarks, interest rate yield curves and option volatilities. In instances where the unobservable inputs are deemed significant, reverse repurchase agreements and repurchase agreements are categorized in Level 3 of the fair value hierarchy; otherwise, they are categorized in Level 2 of the fair value hierarchy.

The following fair value hierarchy tables present information about the Company s assets and liabilities measured at fair value on a recurring basis at June 30, 2013 and December 31, 2012.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Assets and Liabilities Measured at Fair Value on a Recurring Basis at June 30, 2013.

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance at June 30, 2013
	(dollars in millions)				
Assets at Fair Value					
Trading assets:					
U.S. government and agency securities:					
U.S. Treasury securities	$ 25,543	$	$	$	$ 25,543
U.S. agency securities	1,694	23,321			25,015
Total U.S. government and agency securities	27,237	23,321			50,558
Other sovereign government obligations	25,894	7,632	4		33,530
Corporate and other debt:					
State and municipal securities		1,585			1,585
Residential mortgage-backed securities		3,500	19		3,519
Commercial mortgage-backed securities		1,536	181		1,717
Asset-backed securities		875	108		983
Corporate bonds		15,962	509		16,471
Collateralized debt obligations		403	1,333		1,736
Loans and lending commitments		8,988	5,243		14,231
Other debt		8,099	12		8,111
Total corporate and other debt		40,948	7,405		48,353
Corporate equities(1)	74,239	1,293	256		75,788
Derivative and other contracts:					
Interest rate contracts	3,159	590,334	2,980		596,473
Credit contracts		51,847	3,094		54,941
Foreign exchange contracts	27	59,958	125		60,110
Equity contracts	900	49,982	989		51,871
Commodity contracts	3,154	15,710	2,432		21,296
Other		189			189
Netting(2)	(5,645)	(670,281)	(6,697)	(63,496)	(746,119)
Total derivative and other contracts	1,595	97,739	2,923	(63,496)	38,761
Investments:					
Private equity funds			2,286		2,286
Real estate funds		6	1,422		1,428
Hedge funds		447	407		854
Principal investments	20	2	2,822		2,844
Other	181	141	385		707
Total investments	201	596	7,322		8,119
Physical commodities		4,929			4,929

Total trading assets	129,166	176,458	17,910	(63,496)	260,038
Securities available for sale	15,718	27,140			42,858
Securities received as collateral	14,674	75			14,749
Federal funds sold and securities purchased under agreements to resell		869			869
Intangible assets(3)			9		9
Total assets measured at fair value	$ 159,558	$ 204,542	$ 17,919	$ (63,496)	$ 318,523

17

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance at June 30, 2013
			(dollars in millions)		
Liabilities at Fair Value					
Deposits	$	$ 1,425	$	$	$ 1,425
Commercial paper and other short-term borrowings		1,590			1,590
Trading liabilities:					
U.S. government and agency securities:					
U.S. Treasury securities	19,741				19,741
U.S. agency securities	2,766	79			2,845
Total U.S. government and agency securities	22,507	79			22,586
Other sovereign government obligations	25,035	2,308			27,343
Corporate and other debt:					
State and municipal securities		36			36
Residential mortgage-backed securities			4		4
Corporate bonds		6,813	42		6,855
Collateralized debt obligations		16			16
Unfunded lending commitments		216	8		224
Other debt		246	11		257
Total corporate and other debt		7,327	65		7,392
Corporate equities(1)	28,256	792	16		29,064
Derivative and other contracts:					
Interest rate contracts	3,293	566,567	2,964		572,824
Credit contracts		49,712	2,409		52,121
Foreign exchange contracts	8	59,554	221		59,783
Equity contracts	598	54,666	2,273		57,537
Commodity contracts	3,776	15,234	1,651		20,661
Other		178	6		184
Netting(2)	(5,645)	(670,281)	(6,697)	(38,787)	(721,410)
Total derivative and other contracts	2,030	75,630	2,827	(38,787)	41,700
Total trading liabilities	77,828	86,136	2,908	(38,787)	128,085
Obligation to return securities received as collateral	19,062	92			19,154
Securities sold under agreements to repurchase		404	148		552
Other secured financings		6,196	256		6,452
Long-term borrowings		38,114	2,705		40,819
Total liabilities measured at fair value	$ 96,890	$ 133,957	$ 6,017	$ (38,787)	$ 198,077

(1) The Company holds or sells short for trading purposes equity securities issued by entities in diverse industries and of varying size.

(2) For positions with the same counterparty that cross over the levels of the fair value hierarchy, both counterparty netting and cash collateral netting are included in the column titled Counterparty and Cash Collateral Netting. For contracts with the same counterparty, counterparty netting among positions classified within the same level is included within that level. For further information on derivative instruments and hedging activities, see Note 11.

(3) Amount represents mortgage servicing rights (MSR) accounted for at fair value. See Note 7 for further information on MSRs.

Transfers Between Level 1 and Level 2 During the Quarter and Six Months Ended June 30, 2013.

For assets and liabilities that were transferred between Level 1 and Level 2 during the period, fair values are ascribed as if the assets or liabilities had been transferred as of the beginning of the period.

In the quarter and six months ended June 30, 2013, there were no material transfers between Level 1 and Level 2.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Assets and Liabilities Measured at Fair Value on a Recurring Basis at December 31, 2012.

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance at December 31, 2012
			(dollars in millions)		
Assets at Fair Value					
Trading assets:					
U.S. government and agency securities:					
U.S. Treasury securities	$ 24,662	$ 14	$	$	$ 24,676
U.S. agency securities	1,451	27,888			29,339
Total U.S. government and agency securities	26,113	27,902			54,015
Other sovereign government obligations	37,669	5,487	6		43,162
Corporate and other debt:					
State and municipal securities		1,558			1,558
Residential mortgage-backed securities		1,439	45		1,484
Commercial mortgage-backed securities		1,347	232		1,579
Asset-backed securities		915	109		1,024
Corporate bonds		18,403	660		19,063
Collateralized debt obligations		685	1,951		2,636
Loans and lending commitments		12,617	4,694		17,311
Other debt		4,457	45		4,502
Total corporate and other debt		41,421	7,736		49,157
Corporate equities(1)	68,072	1,067	288		69,427
Derivative and other contracts:					
Interest rate contracts	446	819,581	3,774		823,801
Credit contracts		63,234	5,033		68,267
Foreign exchange contracts	34	52,729	31		52,794
Equity contracts	760	37,074	766		38,600
Commodity contracts	4,082	14,256	2,308		20,646
Other		143			143
Netting(2)	(4,740)	(883,733)	(6,947)	(72,634)	(968,054)
Total derivative and other contracts	582	103,284	4,965	(72,634)	36,197
Investments:					
Private equity funds			2,179		2,179
Real estate funds		6	1,370		1,376
Hedge funds		382	552		934
Principal investments	185	83	2,833		3,101
Other	199	71	486		756
Total investments	384	542	7,420		8,346
Physical commodities		7,299			7,299
Total trading assets	132,820	187,002	20,415	(72,634)	267,603
Securities available for sale	14,466	25,403			39,869

Securities received as collateral	14,232	46			14,278
Federal funds sold and securities purchased under agreements to resell		621			621
Intangible assets(3)			7		7
Total assets measured at fair value	$ 161,518	$ 213,072	$ 20,422	$ (72,634)	$ 322,378

19

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance at December 31, 2012
			(dollars in millions)		
Liabilities at Fair Value					
Deposits	$	$ 1,485	$	$	$ 1,485
Commercial paper and other short-term borrowings		706	19		725
Trading liabilities:					
U.S. government and agency securities:					
U.S. Treasury securities	20,098	21			20,119
U.S. agency securities	1,394	107			1,501
Total U.S. government and agency securities	21,492	128			21,620
Other sovereign government obligations	27,583	2,031			29,614
Corporate and other debt:					
State and municipal securities		47			47
Residential mortgage-backed securities			4		4
Corporate bonds		3,942	177		4,119
Collateralized debt obligations		328			328
Unfunded lending commitments		305	46		351
Other debt		156	49		205
Total corporate and other debt		4,778	276		5,054
Corporate equities(1)	25,216	1,655	5		26,876
Derivative and other contracts:					
Interest rate contracts	533	789,715	3,856		794,104
Credit contracts		61,283	3,211		64,494
Foreign exchange contracts	2	56,021	390		56,413
Equity contracts	748	39,212	1,910		41,870
Commodity contracts	4,530	15,702	1,599		21,831
Other		54	7		61
Netting(2)	(4,740)	(883,733)	(6,947)	(46,395)	(941,815)
Total derivative and other contracts	1,073	78,254	4,026	(46,395)	36,958
Total trading liabilities	75,364	86,846	4,307	(46,395)	120,122
Obligation to return securities received as collateral	18,179	47			18,226
Securities sold under agreements to repurchase		212	151		363
Other secured financings		9,060	406		9,466
Long-term borrowings		41,255	2,789		44,044
Total liabilities measured at fair value	$ 93,543	$ 139,611	$ 7,672	$ (46,395)	$ 194,431

(1) The Company holds or sells short for trading purposes equity securities issued by entities in diverse industries and of varying size.
(2) For positions with the same counterparty that cross over the levels of the fair value hierarchy, both counterparty netting and cash collateral netting are included in the column titled Counterparty and Cash Collateral Netting. For contracts with the same counterparty, counterparty netting among positions classified within the same level is included within that level. For further information on derivative instruments and hedging activities, see Note 11.

(3) Amount represents MSRs accounted for at fair value. See Note 7 for further information on MSRs.

Transfers Between Level 1 and Level 2 During the Quarter Ended June 30, 2012.

Trading assets Derivative and other contracts and Trading liabilities Derivative and other contracts. During the quarter ended June 30, 2012, the Company reclassified approximately $1.5 billion of derivative assets and approximately $1.7 billion of derivative liabilities from Level 2 to Level 1 as these listed derivatives became actively traded and were valued based on quoted prices from the exchange. Also during the quarter ended June 30, 2012, the Company reclassified approximately $0.5 billion of derivative assets and approximately $0.7 billion of derivative liabilities from Level 1 to Level 2 as transactions in these contracts did not occur with sufficient frequency and volume to constitute an active market.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Transfers Between Level 1 and Level 2 During the Six Months Ended June 30, 2012.

Trading assets Derivative and other contracts and Trading liabilities Derivative and other contracts. During the six months ended June 30, 2012, the Company reclassified approximately $2.0 billion of derivative assets and approximately $1.8 billion of derivative liabilities from Level 2 to Level 1 as these listed derivatives became actively traded and were valued based on quoted prices from the exchange. Also during the six months ended June 30, 2012, the Company reclassified approximately $0.4 billion of derivative assets and approximately $0.4 billion of derivative liabilities from Level 1 to Level 2 as transactions in these contracts did not occur with sufficient frequency and volume to constitute an active market.

Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis.

The following tables present additional information about Level 3 assets and liabilities measured at fair value on a recurring basis for the quarters and six months ended June 30, 2013 and 2012, respectively. Level 3 instruments may be hedged with instruments classified in Level 1 and Level 2. As a result, the realized and unrealized gains (losses) for assets and liabilities within the Level 3 category presented in the tables below do not reflect the related realized and unrealized gains (losses) on hedging instruments that have been classified by the Company within the Level 1 and/or Level 2 categories.

Additionally, both observable and unobservable inputs may be used to determine the fair value of positions that the Company has classified within the Level 3 category. As a result, the unrealized gains (losses) during the period for assets and liabilities within the Level 3 category presented in the tables below may include changes in fair value during the period that were attributable to both observable (*e.g.*, changes in market interest rates) and unobservable (*e.g.*, changes in unobservable long-dated volatilities) inputs.

For assets and liabilities that were transferred into Level 3 during the period, gains (losses) are presented as if the assets or liabilities had been transferred into Level 3 at the beginning of the period; similarly, for assets and liabilities that were transferred out of Level 3 during the period, gains (losses) are presented as if the assets or liabilities had been transferred out at the beginning of the period.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Quarter Ended June 30, 2013.

	Beginning Balance at March 31, 2013	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at June 30, 2013	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at June 30, 2013(2)
	(dollars in millions)								
Assets at Fair Value									
Trading assets:									
Other sovereign government obligations	$ 3	$	$ 7	(6)	$	$	$	$ 4	$
Corporate and other debt:									
Residential mortgage-backed securities	19		15	(5)			(10)	19	(1)
Commercial mortgage-backed securities	174		26	(19)				181	21
Asset-backed securities	11	1	107	(11)				108	
Corporate bonds	888	(11)	183	(402)			(149)	509	2
Collateralized debt obligations	1,666	36	302	(596)		(87)	12	1,333	20
Loans and lending commitments	5,284	(55)	1,086	(190)		(850)	(32)	5,243	8
Other debt	1	7	4					12	7
Total corporate and other debt	8,043	(22)	1,723	(1,223)		(937)	(179)	7,405	57
Corporate equities	270	(24)	20	(13)			3	256	(12)
Net derivative and other contracts(3):									
Interest rate contracts	(22)	(43)	3		(24)	40	62	16	63
Credit contracts	1,403	(472)	130		(221)	(130)	(25)	685	(369)
Foreign exchange contracts	(235)	95				58	(14)	(96)	95
Equity contracts	(1,340)	18	7		(35)	(1)	67	(1,284)	(79)
Commodity contracts	703	81	26		(13)	(13)	(3)	781	58
Other	(3)	(2)				(1)		(6)	(2)
Total net derivative and other contracts	506	(323)	166		(293)	(47)	87	96	(234)
Investments:									
Private equity funds	2,291	104	20	(129)				2,286	97
Real estate funds	1,370	47	41	(36)				1,422	87
Hedge funds	545	(2)	10	(104)			(42)	407	(16)
Principal investments	2,855	(18)	60	(75)				2,822	82
Other	496	5	4	(30)			(90)	385	6
Total investments	7,557	136	135	(374)			(132)	7,322	256
Intangible assets	8	3				(2)		9	2
Liabilities at Fair Value									
Commercial paper and other short-term borrowings	$ 5	$	$	$	$	$ (2)	$ (3)	$	$

Trading liabilities:									
Corporate and other debt:									
Residential mortgage-backed securities	4							4	
Corporate bonds	424	4	(248)	36			(166)	42	(1)
Unfunded lending commitments	25	17						8	17
Other debt	11	1	(4)	2			3	11	
Total corporate and other debt	464	22	(252)	38			(163)	65	16
Corporate equities	4	3	(8)	17			6	16	2
Obligation to return securities									
Securities sold under agreements to repurchase	155	7						148	7
Other secured financings	275	16				(3)		256	16
Long-term borrowings	2,784	68			466	(457)	(20)	2,705	65

(1) Total realized and unrealized gains (losses) are primarily included in Trading in the condensed consolidated statements of income except for $136 million related to Trading assets Investments, which is included in Investments revenues.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(2) Amounts represent unrealized gains (losses) for the quarter ended June 30, 2013 related to assets and liabilities still outstanding at June 30, 2013.
(3) Net derivative and other contracts represent Trading assets Derivative and other contracts net of Trading liabilities Derivative and other contracts. For further information on derivative instruments and hedging activities, see Note 11.

Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Six Months Ended June 30, 2013.

	Beginning Balance at December 31, 2012	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at June 30, 2013	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at June 30, 2013(2)
	(dollars in millions)								
Assets at Fair Value									
Trading assets:									
Other sovereign government obligations	$ 6	$	$ 8	$ (8)	$	$	$ (2)	$ 4	$
Corporate and other debt:									
Residential mortgage-backed securities	45	27	16	(44)			(25)	19	10
Commercial mortgage-backed securities	232	17	25	(93)				181	30
Asset-backed securities	109	1	6	(8)				108	
Corporate bonds	660	2	193	(296)		(12)	(38)	509	(19)
Collateralized debt obligations	1,951	284	429	(1,314)		(15)	(2)	1,333	(54)
Loans and lending commitments	4,694	(55)	1,616	(294)		(1,050)	332	5,243	(16)
Other debt	45	(2)	20	(50)			(1)	12	(1)
Total corporate and other debt	7,736	274	2,305	(2,099)		(1,077)	266	7,405	(50)
Corporate equities	288	(9)	37	(41)			(19)	256	(24)
Net derivative and other contracts(3):									
Interest rate contracts	(82)	(193)	6		(30)	179	136	16	(76)
Credit contracts	1,822	(937)	169		(235)	(127)	(7)	685	(789)
Foreign exchange contracts	(359)	114				140	9	(96)	79
Equity contracts	(1,144)	48	74	(1)	(116)	(236)	91	(1,284)	(5)
Commodity contracts	709	46	36		(17)	9	(2)	781	38
Other	(7)	(4)				5		(6)	(4)
Total net derivative and other contracts	939	(926)	285	(1)	(398)	(30)	227	96	(757)
Investments:									
Private equity funds	2,179	218	88	(199)				2,286	194
Real estate funds	1,370	128	42	(119)			1	1,422	207
Hedge funds	552		38	(136)			(47)	407	(19)
Principal investments	2,833	45	95	(160)			9	2,822	143
Other	486	21	16	(47)			(91)	385	22
Total investments	7,420	412	279	(661)			(128)	7,322	547
Intangible assets	7	7				(5)		9	3

23

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Beginning Balance at December 31, 2012	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at June 30, 2013	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at June 30, 2013(2)
					(dollars in millions)				
Liabilities at Fair Value									
Commercial paper and other short-term borrowings	$ 19	$	$	$	$	$ (2)	$ (17)	$	$
Trading liabilities:									
Corporate and other debt:									
Residential mortgage-backed securities	4							4	
Corporate bonds	177	(7)	(437)	83			212	42	9
Unfunded lending commitments	46	38						8	38
Other debt	49	13	(33)	5			3	11	10
Total corporate and other debt	276	44	(470)	88			215	65	57
Corporate equities	5	5	(13)	29				16	5
Securities sold under agreements to repurchase	151	3						148	3
Other secured financings	406	29			14	(135)		256	21
Long-term borrowings	2,789	24			955	(361)	(654)	2,705	16

(1) Total realized and unrealized gains (losses) are primarily included in Trading in the condensed consolidated statements of income except for $412 million related to Trading assets Investments, which is included in Investments revenues.

(2) Amounts represent unrealized gains (losses) for the six months ended June 30, 2013 related to assets and liabilities still outstanding at June 30, 2013.

(3) Net derivative and other contracts represent Trading assets Derivative and other contracts net of Trading liabilities Derivative and other contracts. For further information on derivative instruments and hedging activities, see Note 11.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for Quarter Ended June 30, 2012.

	Beginning Balance at March 31, 2012	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at June 30, 2012	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at June 30, 2012(2)
					(dollars in millions)				
Assets at Fair Value									
Trading assets:									
U.S. agency securities	$ 23	$	$	$ (23)	$	$	$	$	$
Other sovereign government obligations	8		1	(1)			(7)	1	
Corporate and other debt:									
State and municipal securities	3	1		(1)				3	
Residential mortgage-backed securities	43	(6)	17	(33)			3	24	(23)
Commercial mortgage-backed securities	127	(3)	146	(12)			(2)	256	1
Asset-backed securities	3	(1)	8	(1)				9	(1)
Corporate bonds	899	(39)	277	(428)			36	745	(27)
Collateralized debt obligations	1,165	20	509	(241)			4	1,457	(10)
Loans and lending commitments	8,597	(126)	326	(1,320)		(580)	897	7,794	(173)
Other debt	57	(2)	14	(56)				13	(5)
Total corporate and other debt	10,894	(156)	1,297	(2,092)		(580)	938	10,301	(238)
Corporate equities	554	34	(14)	(45)			(47)	482	2
Net derivative and other contracts(3):									
Interest rate contracts	22	(35)	158		(235)	59	(141)	(172)	17
Credit contracts	4,381	340	19		(401)	(272)	(225)	3,842	181
Foreign exchange contracts	66	(103)				(187)		(224)	(147)
Equity contracts	(1,442)	218	31	(2)	(33)	15	40	(1,173)	213
Commodity contracts	803	142				(9)	1	937	89
Other	(23)					(4)		(27)	
Total net derivative and other contracts	3,807	562	208	(2)	(669)	(398)	(325)	3,183	353
Investments:									
Private equity funds	1,994	15	50	(54)				2,005	7
Real estate funds	1,338	12	30	(54)				1,326	10
Hedge funds	623	(23)	6	(25)			(48)	533	(23)
Principal investments	3,194	(9)	51	(80)			(109)	3,047	(22)
Other	527	23	19	(23)			(3)	543	21
Total investments	7,676	18	156	(236)			(160)	7,454	(7)
Intangible assets	99	(5)		(84)		(2)		8	(4)

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Beginning Balance at March 31, 2012	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at June 30, 2012	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at June 30, 2012(2)
	(dollars in millions)								
Liabilities at Fair Value									
Commercial paper and other short-term borrowings	$ 15	$	$	$	$	$ (13)	$	$ 2	$
Trading liabilities:									
Other sovereign government obligations	1		(1)						
Corporate and other debt:									
Residential mortgage-backed securities	61	57						4	57
Corporate bonds	193	32	(164)	139			(9)	127	59
Collateralized debt obligations			(1)	2				1	
Unfunded lending commitments	60	9						51	9
Other debt	33	16	(2)	48				63	16
Total corporate and other debt	347	114	(167)	189			(9)	246	141
Corporate equities	2	(27)	(13)	25			6	47	(26)
Securities sold under agreements to repurchase	186	1						185	1
Other secured financings	594	(4)			41	(152)	(17)	470	(4)
Long-term borrowings	2,143	(59)			315	(284)	(23)	2,210	(146)

(1) Total realized and unrealized gains (losses) are primarily included in Trading in the condensed consolidated statements of income except for $18 million related to Trading assets Investments, which is included in Investments revenues.

(2) Amounts represent unrealized gains (losses) for the quarter ended June 30, 2012 related to assets and liabilities still outstanding at June 30, 2012.

(3) Net derivative and other contracts represent Trading assets Derivative and other contracts net of Trading liabilities Derivative and other contracts. For further information on derivative instruments and hedging activities, see Note 11.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Six Months Ended June 30, 2012.

	Beginning Balance at December 31, 2011	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at June 30, 2012	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at June 30, 2012(2)
					(dollars in millions)				
Assets at Fair Value									
Trading assets:									
U.S. agency securities	$ 8	$	$	$ (7)	$	$	$ (1)	$	$
Other sovereign government obligations	119		1	(118)			(1)	1	
Corporate and other debt:									
State and municipal securities		1		(1)			3	3	1
Residential mortgage-backed securities	494	(27)	3	(265)			(181)	24	(61)
Commercial mortgage-backed securities	134	25	138	(37)		(1)	(3)	256	23
Asset-backed securities	31		8	(29)			(1)	9	(1)
Corporate bonds	675	6	331	(391)			124	745	(8)
Collateralized debt obligations	980	137	725	(335)			(50)	1,457	52
Loans and lending commitments	9,590	(168)	1,410	(2,269)		(695)	(74)	7,794	(312)
Other debt	128	(7)	32	(158)			18	13	(12)
Total corporate and other debt	12,032	(33)	2,647	(3,485)		(696)	(164)	10,301	(318)
Corporate equities	417	(13)	215	(149)			12	482	(20)
Net derivative and other contracts(3):									
Interest rate contracts	420	(28)	164		(240)	37	(525)	(172)	62
Credit contracts	5,814	(1,083)	81		(411)	(267)	(292)	3,842	(1,539)
Foreign exchange contracts	43	(40)				(207)	(20)	(224)	(102)
Equity contracts	(1,234)	117	211	(1)	(74)	(244)	52	(1,173)	102
Commodity contracts	570	320	5		(4)	34	12	937	338
Other	(1,090)	59				264	740	(27)	57
Total net derivative and other contracts	4,523	(655)	461	(1)	(729)	(383)	(33)	3,183	(1,082)
Investments:									
Private equity funds	1,936	15	143	(89)				2,005	(5)
Real estate funds	1,213	64	117	(68)				1,326	148
Hedge funds	696	(1)	24	(58)			(128)	533	1
Principal investments	2,937	24	230	(144)				3,047	(17)
Other	501	(12)	52	(24)			26	543	(18)
Total investments	7,283	90	566	(383)			(102)	7,454	109
Physical commodities	46					(46)			

Intangible assets	133	(39)	(84)	(2)	8	(8)

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Beginning Balance at December 31, 2011	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at June 30, 2012	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at June 30, 2012(2)
					(dollars in millions)				
Liabilities at Fair Value									
Commercial paper and other short-term borrowings	$ 2	$	$	$	$	$		$ 2	$
Trading liabilities:									
Other sovereign government obligations	8		(8)	1			(1)		
Corporate and other debt:									
Residential mortgage-backed securities	355	(4)	(355)					4	(4)
Corporate bonds	219	(25)	(203)	111			(25)	127	49
Collateralized debt obligations							1	1	
Unfunded lending commitments	85	34						51	34
Other debt	73	11	(1)	46		(55)	11	63	13
Total corporate and other debt	732	16	(559)	157		(55)	(13)	246	92
Corporate equities	1	(21)		27			(2)	47	(53)
Securities sold under agreements to repurchase	340	3					(152)	185	3
Other secured financings	570	(19)			52	(149)	(22)	470	(19)
Long-term borrowings	1,603	(190)			444	(102)	75	2,210	(214)

(1) Total realized and unrealized gains (losses) are primarily included in Trading in the condensed consolidated statements of income except for $90 million related to Trading assets Investments, which is included in Investments revenues.

(2) Amounts represent unrealized gains (losses) for the six months ended June 30, 2012 related to assets and liabilities still outstanding at June 30, 2012.

(3) Net derivative and other contracts represent Trading assets Derivative and other contracts net of Trading liabilities Derivative and other contracts. For further information on derivative instruments and hedging activities, see Note 11.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Quantitative Information about and Sensitivity of Significant Unobservable Inputs Used in Recurring Level 3 Fair Value Measurements at June 30, 2013 and December 31, 2012.

The disclosures below provide information on the valuation techniques, significant unobservable inputs and their ranges and averages for each major category of assets and liabilities measured at fair value on a recurring basis with a significant Level 3 balance. The level of aggregation and breadth of products cause the range of inputs to be wide and not evenly distributed across the inventory. Further, the range of unobservable inputs may differ across firms in the financial services industry because of diversity in the types of products included in each firm s inventory. The following disclosures also include qualitative information on the sensitivity of the fair value measurements to changes in the significant unobservable inputs.

At June 30, 2013.

	Balance at June 30, 2013 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s) / Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Averages(2)
Assets					
Trading assets:					
Corporate and other debt:					
Commercial mortgage-backed securities	$ 181	Comparable pricing	Comparable bond price / (A)	57 to 100 points	80 points
Asset-backed securities	108	Discounted cash flow	Discount rate / (C)	25%	25%
Corporate bonds	509	Comparable pricing	Comparable bond price / (A)	2 to 147 points	82 points
Collateralized debt obligations	1,333	Comparable pricing(6)	Comparable bond price / (A)	17 to 94 points	63 points
		Correlation model	Credit correlation / (B)	38 to 50%	47%
Loans and lending commitments	5,243	Corporate loan model	Credit spread / (C)	15 to 894 basis points	194 basis points
		Comparable pricing	Comparable bond price / (A)	80 to 120 points	101 points
		Margin loan model	Credit spread / (C)(D)	30 to 306 basis points	195 basis points
			Volatility skew / (C)(D)	-2 to 0%	-2%
		Option model	At the money volatility /(A)	31 to 42%	34%
		Comparable pricing(6)	Comparable loan price / (A)	24 to 101 points	86 points
Corporate equities(3)	256	Net asset value(6)	Discount to net asset value / (C)	0 to 50%	19%
		Comparable pricing	Comparable equity price / (A)	0 to 100%	43%
		Comparable pricing	Comparable price / (A)	8 to 100 points	58 points
		Market approach	EBITDA multiple / (A)	7 times	7 times
Net derivative and other contracts:					
Interest rate contracts	16	Option model	Interest rate volatility concentration liquidity multiple / (C)(D)	0 to 8 times	2 times
			Comparable bond price / (A)(D)	5 to 98 points	51 points / 51 points(4)
			Interest rate - Foreign exchange correlation / (A)(D)	2 to 63%	32% / 38%(4)
			Interest rate volatility skew / (A)(D)	25 to 55%	43% / 35%(4)
			Interest rate quanto correlation / (A)(D)	-53 to 33%	-5% / -9%(4)
			Interest rate curve correlation / (A)(D)	35 to 88%	67% / 70%(4)
			Inflation volatility / (A)(D)	77 to 83%	79% / 78%(4)
Credit contracts	685	Comparable pricing	Cash synthetic basis / (C)(D)	2 to 10 points	4 points
			Comparable bond price / (C)(D)	0 to 84 points	27 points
		Correlation model(6)	Credit correlation / (B)	34 to 90%	54%

Foreign exchange contracts(5)	(96)	Option model	Comparable bond price / (A)(D)	5 to 98 points	51 points / 51 points(4)
			Interest rate quanto correlation / (A)(D)	-53 to 33%	-5% / -9%(4)
			Interest rate - Credit spread correlation / (A)(D)	-59 to 47%	-5% / -3%(4)
			Interest rate curve correlation / (A)(D)	35 to 88%	67% / 70%(4)
			Interest rate - Foreign exchange correlation / (A)(D)	2 to 63%	32% / 38%(4)
			Interest rate volatility skew / (A)(D)	25 to 55%	43% / 35%(4)
			Interest rate curve / (A)(D)	0 to 2%	1% / 1%(4)

29

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Balance at June 30, 2013 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s) / Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Averages(2)
Equity contracts(5)	(1,284)	Option model	At the money volatility / (A)(D)	18 to 38 %	34%
			Volatility skew / (A)(D)	-1 to 1 %	-1%
			Equity - Equity correlation / (C)(D)	40 to 99%	71%
			Equity - Foreign exchange correlation / (C)(D)	-70 to 9%	-22%
			Equity - Interest rate correlation / (C)(D)	5 to 68%	38% /34%(4)
Commodity contracts	781	Option model	Forward power price / (C)(D)	$10 to $113 per Megawatt hour	$39 per Megawatt hour
			Commodity volatility / (A)(D)	12 to 58%	12%
			Cross commodity correlation / (C)(D)	43 to 98%	97%
Investments(3):					
Principal investments	2,822	Discounted cash flow	Implied weighted average cost of capital / (C)(D)	10 to 12%	10%
			Exit multiple / (A)(D)	7 to 10 times	9 times
		Discounted cash flow(6)	Capitalization rate / (C)(D)	6 to 9%	7%
			Equity discount rate / (C)(D)	10 to 35%	22%
		Market approach	EBITDA multiple / (A)	5 to 15 times	9 times
Other	385	Discounted cash flow	Implied weighted average cost of capital / (C)(D)	10 to 12%	10%
			Exit multiple / (A)(D)	5 to 7 times	6 times
		Market approach(6)	EBITDA multiple / (A)	7 to 8 times	8 times
Liabilities					
Trading liabilities:					
Securities sold under agreements to repurchase	$ 148	Discounted cash flow	Funding spread / (A)	157 basis points	157 basis points
Other secured financings	256	Comparable pricing(6)	Comparable bond price / (A)	96 to 100 points	96 points
		Discounted cash flow	Funding spread / (A)	157 basis points	157 basis points
Long-term borrowings	2,705	Option model	At the money volatility / (A)(D)	25 to 33%	28%
			Volatility skew / (A)(D)	-1 to 0%	-1%
			Equity - Equity correlation / (A)(D)	50 to 90%	73%
			Equity - Foreign exchange correlation / (A)(D)	-70 to 9%	-33%

EBITDA Earnings before interest, taxes, depreciation and amortization

(1) The ranges of significant unobservable inputs are represented in points, percentages, basis points, times or megawatt hours. Points are a percentage of par; for example, 100 points would be 100% of par. A basis point equals 1/100th of 1%; for example, 894 basis points would equal 8.94%.
(2) Amounts represent weighted averages except where simple averages and the median of the inputs are provided (see footnote 4 below). Weighted averages are calculated by weighting each input by the fair value of the respective financial instruments except for long-term borrowings and derivative instruments where inputs are weighted by risk.
(3) Investments in funds measured using an unadjusted NAV are excluded.
(4) The data structure of the significant unobservable inputs used in valuing Interest rate contracts, Foreign exchange contracts and certain Equity contracts may be in a multi-dimensional form, such as a curve or surface, with risk distributed across the structure. Therefore, a simple average and median, together with the range of data inputs, may be more appropriate measurements than a single point weighted average.
(5) Includes derivative contracts with multiple risks (*i.e.,* hybrid products).
(6) This is the predominant valuation technique for this major asset or liability class.

Sensitivity of the fair value to changes in the unobservable inputs:

(A) Significant increase (decrease) in the unobservable input in isolation would result in a significantly higher (lower) fair value measurement.
(B) Significant changes in credit correlation may result in a significantly higher or lower fair value measurement. Increasing (decreasing) correlation drives a redistribution of risk within the capital structure such that junior tranches become less (more) risky and senior tranches become more (less) risky.
(C) Significant increase (decrease) in the unobservable input in isolation would result in a significantly lower (higher) fair value measurement.
(D) There are no predictable relationships between the significant unobservable inputs.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

At December 31, 2012.

	Balance at December 31, 2012 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s) / Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Weighted Average
Assets					
Trading assets:					
Corporate and other debt:					
Commercial mortgage-backed securities	$ 232	Comparable pricing	Comparable bond price / (A)	46 to 100 points	76 points
Asset-backed securities	109	Discounted cash flow	Discount rate / (C)	21%	21%
Corporate bonds	660	Comparable pricing	Comparable bond price / (A)	0 to 143 points	24 points
Collateralized debt obligations	1,951	Comparable pricing	Comparable bond price / (A)	15 to 88 points	59 points
		Correlation model	Credit correlation / (B)	15 to 45%	40%
Loans and lending commitments	4,694	Corporate loan model	Credit spread / (C)	17 to 1,004 basis points	281 basis points
		Comparable pricing	Comparable bond price / (A)	80 to 120 points	104 points
		Comparable pricing	Comparable loan price / (A)	55 to 100 points	88 points
Corporate equities(2)	288	Net asset value	Discount to net asset value / (C)	0 to 37%	8%
		Comparable pricing	Discount to comparable equity price / (C)	0 to 27 points	14 points
		Market approach	EBITDA multiple / (A)	6 times	6 times
Net derivative and other contracts:					
Interest rate contracts	(82)	Option model	Interest rate volatility concentration liquidity multiple / (C)(D)	0 to 8 times	See(3)
			Comparable bond price / (A)(D)	5 to 98 points	
			Interest rate - Foreign exchange correlation / (A)(D)	2 to 63%	
			Interest rate volatility skew / (A)(D)	9 to 95%	
			Interest rate quanto correlation / (A)(D)	-53 to 33%	
			Interest rate curve correlation / (A)(D)	48 to 99%	
			Inflation volatility / (A)(D)	49 to 100%	
		Discounted cash flow	Forward commercial paper rate-LIBOR basis / (A)	-18 to 95 basis points	
Credit contracts	1,822	Comparable pricing	Cash synthetic basis / (C)	2 to 14 points	See(4)
			Comparable bond price / (C)	0 to 80 points	
		Correlation model	Credit correlation / (B)	14 to 94%	
Foreign exchange contracts(5)	(359)	Option model	Comparable bond price / (A)(D)	5 to 98 points	See(6)
			Interest rate quanto correlation / (A)(D)	-53 to 33%	
			Interest rate -Credit spread correlation / (A)(D)	-59 to 65%	
			Interest rate - Foreign exchange correlation / (A)(D)	2 to 63%	
			Interest rate volatility skew / (A)(D)	9 to 95%	
Equity contracts(5)	(1,144)	Option model	At the money volatility / (C)(D)	7 to 24%	See(7)
			Volatility skew / (C)(D)	-2 to 0%	
			Equity - Equity correlation / (C)(D)	40 to 96%	
			Equity - Foreign exchange correlation / (C)(D)	-70 to 38%	
			Equity - Interest rate correlation / (C)(D)	18 to 65%	
Commodity contracts	709	Option model	Forward power price / (C)(D)	$28 to $84 per Megawatt hour	
			Commodity volatility / (A)(D)	17 to 29%	

			Cross commodity correlation / (C)(D)	43 to 97%	
Investments(2):					
Principal investments	2,833	Discounted cash flow	Implied weighted average cost of capital / (C)(D)	8 to 15%	9%
			Exit multiple / (A)(D)	5 to 10 times	9 times
		Discounted cash flow	Capitalization rate / (C)(D)	6 to 10%	7%
			Equity discount rate / (C)(D)	15 to 35%	23%
		Market approach	EBITDA multiple / (A)	3 to 17 times	10 times

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Balance at December 31, 2012 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s) / Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Weighted Average
Other	486	Discounted cash flow	Implied weighted average cost of capital / (C)(D)	11%	11%
			Exit multiple / (A)(D)	6 times	6 times
		Market approach	EBITDA multiple / (A)	6 to 8 times	7 times
Liabilities					
Trading liabilities:					
Corporate and other debt:					
Corporate bonds	$ 177	Comparable pricing	Comparable bond price / (A)	0 to 150 points	50 points
Securities sold under agreements to repurchase	151	Discounted cash flow	Funding spread / (A)	110 to 184 basis points	166 basis points
Other secured financings	406	Comparable pricing	Comparable bond price / (A)	55 to 139 points	102 points
		Discounted cash flow	Funding spread / (A)	183 to 186 basis points	184 basis points
Long-term borrowings	2,789	Option model	At the money volatility / (A)(D)	20 to 24%	24%
			Volatility skew / (A)(D)	-1 to 0%	0%
			Equity - Equity correlation / (A)(D)	50 to 90%	77%
			Equity - Foreign exchange correlation / (A)(D)	-70 to 36%	-15%

LIBOR London Interbank Offered Rate

(1) The ranges of significant unobservable inputs are represented in points, percentages, basis points, times or megawatt hours. Points are a percentage of par; for example, 100 points would be 100% of par. A basis point equals 1/100th of 1%; for example, 1,004 basis points would equal 10.04%.
(2) Investments in funds measured using an unadjusted NAV are excluded.
(3) See Note 4 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K for a qualitative discussion of the wide unobservable input ranges for comparable bond prices, interest rate volatility skew, interest rate quanto correlation and forward commercial paper rate LIBOR basis.
(4) See Note 4 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K for a qualitative discussion of the wide unobservable input ranges for comparable bond prices and credit correlation.
(5) Includes derivative contracts with multiple risks (*i.e.*, hybrid products).
(6) See Note 4 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K for a qualitative discussion of the wide unobservable input ranges for comparable bond prices, interest rate quanto correlation, interest rate-credit spread correlation and interest rate volatility skew.
(7) See Note 4 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K for a qualitative discussion of the wide unobservable input range for equity-foreign exchange correlation.

Sensitivity of the fair value to changes in the unobservable inputs:

(A) Significant increase (decrease) in the unobservable input in isolation would result in a significantly higher (lower) fair value measurement.
(B) Significant changes in credit correlation may result in a significantly higher or lower fair value measurement. Increasing (decreasing) correlation drives a redistribution of risk within the capital structure such that junior tranches become less (more) risky and senior tranches become more (less) risky.
(C) Significant increase (decrease) in the unobservable input in isolation would result in a significantly lower (higher) fair value measurement.
(D) There are no predictable relationships between the significant unobservable inputs.

The following provides a description of significant unobservable inputs included in the June 30, 2013 and December 31, 2012 tables above for all major categories of assets and liabilities:

Comparable bond price a pricing input used when prices for the identical instrument are not available. Significant subjectivity may be involved when fair value is determined using pricing data available for comparable instruments. Valuation using comparable instruments can be done by calculating an implied yield (or spread over a liquid benchmark) from the price of a comparable bond, then adjusting that yield (or spread) to derive a value for the bond. The adjustment to yield (or spread) should account for relevant differences in the bonds such as maturity or credit quality. Alternatively, a price-to-price basis can be

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

assumed between the comparable instrument and bond being valued in order to establish the value of the bond. Additionally, as the probability of default increases for a given bond (*i.e.*, as the bond becomes more distressed), the valuation of that bond will increasingly reflect its expected recovery level assuming default. The decision to use price-to-price or yield/spread comparisons largely reflects trading market convention for the financial instruments in question. Price-to-price comparisons are primarily employed for CMBS, CDOs, mortgage loans and distressed corporate bonds. Implied yield (or spread over a liquid benchmark) is utilized predominately for non-distressed corporate bonds, loans and credit contracts.

Correlation a pricing input where the payoff is driven by more than one underlying risk. Correlation is a measure of the relationship between the movements of two variables (*i.e*., how the change in one variable influences a change in the other variable). Credit correlation, for example, is the factor that describes the relationship between the probability of individual entities to default on obligations and the joint probability of multiple entities to default on obligations.

Credit spread the difference in yield between different securities due to differences in credit quality. The credit spread reflects the additional net yield an investor can earn from a security with more credit risk relative to one with less credit risk. The credit spread of a particular security is often quoted in relation to the yield on a credit risk-free benchmark security or reference rate, typically either U.S. Treasury or LIBOR.

Volatility skew the measure of the difference in implied volatility for options with identical underliers and expiry dates but with different strikes. The implied volatility for an option with a strike price that is above or below the current price of an underlying asset will typically deviate from the implied volatility for an option with a strike price equal to the current price of that same underlying asset.

Volatility the measure of the variability in possible returns for an instrument given how much that instrument changes in value over time. Volatility is a pricing input for options and, generally, the lower the volatility, the less risky the option. The level of volatility used in the valuation of a particular option depends on a number of factors, including the nature of the risk underlying that option (*e.g.*, the volatility of a particular underlying equity security may be significantly different from that of a particular underlying commodity index), the tenor and the strike price of the option.

EBITDA multiple / Exit multiple is the Enterprise Value to EBITDA ratio, where the Enterprise Value is the aggregate value of equity and debt minus cash and cash equivalents. The EBITDA multiple reflects the value of the company in terms of its full-year EBITDA, whereas the exit multiple reflects the value of the company in terms of its full year expected EBITDA at exit. Either multiple allows comparison between companies from an operational perspective as the effect of capital structure, taxation and depreciation/amortization is excluded.

Forward commercial paper rate LIBOR basis the basis added to the LIBOR rate when the commercial paper yield is expressed as a spread over the LIBOR rate. The basis to LIBOR is dependent on a number of factors, including, but not limited to, collateralization of the commercial paper, credit rating of the issuer, and the supply of commercial paper. The basis may become negative, i.e., the return for highly-rated commercial paper, such as asset-backed commercial paper, may be less than LIBOR.

Cash synthetic basis the measure of the price differential between cash financial instruments (cash instruments) and their synthetic derivative-based equivalents (synthetic instruments). The range disclosed in the table above signifies the number of points by which the synthetic bond equivalent price is higher than the quoted price of the underlying cash bonds.

Implied weighted average cost of capital (WACC   ) the WACC implied by the current value of equity in a discounted cash flow model. The model assumes that the cash flow assumptions, including

33

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

projections, are fully reflected in the current equity value while the debt to equity ratio is held constant. The WACC theoretically represents the required rate of return to debt and equity investors, respectively.

Capitalization rate the ratio between net operating income produced by an asset and its market value at the projected disposition date.

Funding spread the difference between the general collateral rate (which refers to the rate applicable to a broad class of U.S. Treasury issuances) and the specific collateral rate (which refers to the rate applicable to a specific type of security pledged as collateral, such as a municipal bond). Repurchase agreements are discounted based on collateral curves. The curves are constructed as spreads over the corresponding overnight index swap (OIS)/ LIBOR curves, with the short end of the curve representing spreads over the corresponding OIS curves and the long end of the curve representing spreads over LIBOR.

Fair Value of Investments that Calculate Net Asset Value.

The Company s Investments measured at fair value were $8,119 million and $8,346 million at June 30, 2013 and December 31, 2012, respectively. The following table presents information solely about the Company s investments in private equity funds, real estate funds and hedge funds measured at fair value based on NAV at June 30, 2013 and December 31, 2012, respectively.

	At June 30, 2013		At December 31, 2012	
	Fair Value	Unfunded Commitment	Fair Value	Unfunded Commitment
	(dollars in millions)			
Private equity funds	$ 2,286	$ 594	$ 2,179	$ 644
Real estate funds	1,428	174	1,376	221
Hedge funds(1):				
Long-short equity hedge funds	486		475	
Fixed income/credit-related hedge funds	75		86	
Event-driven hedge funds	41		52	
Multi-strategy hedge funds	252	3	321	3
Total	$ 4,568	$ 771	$ 4,489	$ 868

(1) Fixed income/credit-related hedge funds, event-driven hedge funds, and multi-strategy hedge funds are redeemable at least on a six-month period basis primarily with a notice period of 90 days or less. At June 30, 2013, approximately 41% of the fair value amount of long-short equity hedge funds is redeemable at least quarterly, 39% is redeemable every six months and 20% of these funds have a redemption frequency of greater than six months. The notice period for long-short equity hedge funds at June 30, 2013 is primarily greater than six months. At December 31, 2012, approximately 36% of the fair value amount of long-short equity hedge funds is redeemable at least quarterly, 38% is redeemable every six months and 26% of these funds have a redemption frequency of greater than six months. The notice period for long-short equity hedge funds at December 31, 2012 is primarily greater than six months.

Private Equity Funds. Amount includes several private equity funds that pursue multiple strategies including leveraged buyouts, venture capital, infrastructure growth capital, distressed investments, and mezzanine capital. In addition, the funds may be structured with a focus on specific domestic or foreign geographic regions. These investments are generally not redeemable with the funds. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the fund. At June 30, 2013, it is estimated that 9% of the fair value of the funds will be liquidated in the next five years, another 60% of the fair value of the funds will be liquidated between five to 10 years and the remaining 31% of the fair value of the funds have a remaining life of greater than 10 years.

34

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Real Estate Funds. Amount includes several real estate funds that invest in real estate assets such as commercial office buildings, retail properties, multi-family residential properties, developments or hotels. In addition, the funds may be structured with a focus on specific geographic domestic or foreign regions. These investments are generally not redeemable with the funds. Distributions from each fund will be received as the underlying investments of the funds are liquidated. At June 30, 2013, it is estimated that 3% of the fair value of the funds will be liquidated within the next five years, another 52% of the fair value of the funds will be liquidated between five to 10 years and the remaining 45% of the fair value of the funds have a remaining life of greater than 10 years.

Hedge Funds. Investments in hedge funds may be subject to initial period lock-up restrictions or gates. A hedge fund lock-up provision is a provision that provides that, during a certain initial period, an investor may not make a withdrawal from the fund. The purpose of a gate is to restrict the level of redemptions that an investor in a particular hedge fund can demand on any redemption date.

Long-short Equity Hedge Funds. Amount includes investments in hedge funds that invest, long or short, in equities. Equity value and growth hedge funds purchase stocks perceived to be undervalued and sell stocks perceived to be overvalued. Investments representing approximately 7% of the fair value of the investments in this category cannot be redeemed currently because the investments include certain initial period lock-up restrictions. The remaining restriction period for these investments subject to lock-up restrictions was primarily two years or less at June 30, 2013. Investments representing approximately 6% of the fair value of the investments in long-short equity hedge funds cannot be redeemed currently because an exit restriction has been imposed by the hedge fund manager. The restriction period for these investments subject to an exit restriction was primarily less than one year at June 30, 2013.

Fixed Income/Credit-Related Hedge Funds. Amount includes investments in hedge funds that employ long-short, distressed or relative value strategies in order to benefit from investments in undervalued or overvalued securities that are primarily debt or credit related. At June 30, 2013, there were no restrictions on redemptions.

Event-Driven Hedge Funds. Amount includes investments in hedge funds that invest in event-driven situations such as mergers, hostile takeovers, reorganizations, or leveraged buyouts. This may involve the simultaneous purchase of stock in companies being acquired and the sale of stock in its acquirer, with the expectation to profit from the spread between the current market price and the ultimate purchase price of the target company. At June 30, 2013, there were no restrictions on redemptions.

Multi-strategy Hedge Funds. Amount includes investments in hedge funds that pursue multiple strategies to realize short- and long-term gains. Management of the hedge funds has the ability to overweight or underweight different strategies to best capitalize on current investment opportunities. At June 30, 2013, investments representing approximately 35% of the fair value of the investments in this category cannot be redeemed currently because the investments include certain initial period lock-up restrictions. The remaining restriction period for these investments subject to lock-up restrictions was primarily two years or less at June 30, 2013. Investments representing approximately 9% of the fair value of the investments in multi-strategy hedge funds cannot be redeemed currently because an exit restriction has been imposed by the hedge fund manager. The restriction period for these investments subject to an exit restriction was indefinite at June 30, 2013.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fair Value Option.

The Company elected the fair value option for certain eligible instruments that are risk managed on a fair value basis to mitigate income statement volatility caused by measurement basis differences between the elected instruments and their associated risk management transactions or to eliminate complexities of applying certain accounting models. The following tables present net gains (losses) due to changes in fair value for items measured at fair value pursuant to the fair value option election for the quarters and six months ended June 30, 2013 and 2012, respectively:

	Trading	Interest Income (Expense)	Gains (Losses) Included in Net Revenues
		(dollars in millions)	
Three Months Ended June 30, 2013			
Federal funds sold and securities purchased under agreements to resell	$ (2)	$ 2	$
Deposits	16	(16)	
Commercial paper and other short-term borrowings(1)	117	(1)	116
Securities sold under agreements to repurchase	9	(2)	7
Long-term borrowings(1)	1,116	(231)	885
Six Months Ended June 30, 2013			
Federal funds sold and securities purchased under agreements to resell	$ (1)	$ 3	$ 2
Deposits	30	(33)	(3)
Commercial paper and other short-term borrowings(1)	180	(2)	178
Securities sold under agreements to repurchase	5	(3)	2
Long-term borrowings(1)	1,207	(528)	679
Three Months Ended June 30, 2012			
Federal funds sold and securities purchased under agreements to resell	$ 12	$ 1	$ 13
Deposits	15	(22)	(7)
Commercial paper and other short-term borrowings(2)	211		211
Securities sold under agreements to repurchase	5	(1)	4
Long-term borrowings(2)	1,300	(325)	975
Six Months Ended June 30, 2012			
Federal funds sold and securities purchased under agreements to resell	$ 8	$ 2	$ 10
Deposits	25	(44)	(19)
Commercial paper and other short-term borrowings(2)	82		82
Securities sold under agreements to repurchase	3	(2)	1
Long-term borrowings(2)	(1,651)	(669)	(2,320)

(1) Of the total gains (losses) recorded in Trading for short-term and long-term borrowings for the quarter and six months ended June 30, 2013, $175 million and $(142) million, respectively, are attributable to changes in the credit quality of the Company, and the respective remainder is attributable to changes in foreign currency rates or interest rates or movements in the reference price or index for structured notes before the impact of related hedges.

(2) Of the total gains (losses) recorded in Trading for short-term and long-term borrowings for the quarter and six months ended June 30, 2012, $350 million and $(1,628) million, respectively, are attributable to changes in the credit quality of the Company, and the respective remainder is attributable to changes in foreign currency rates or interest rates or movements in the reference price or index for structured notes before the impact of related hedges.

In addition to the amounts in the above table, as discussed in Note 2 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K, all of the instruments within Trading assets or

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Trading liabilities are measured at fair value, either through the election of the fair value option or as required by other accounting guidance. The amounts in the above table are included within Net revenues and do not reflect gains or losses on related hedging instruments, if any.

The Company hedges the economics of market risk for short-term and long-term borrowings (*i.e.*, risks other than that related to the credit quality of the Company) as part of its overall trading strategy and manages the market risks embedded within the issuance by the related business unit as part of the business unit s portfolio. The gains and losses on related economic hedges are recorded in Trading and largely offset the gains and losses on short-term and long-term borrowings attributable to market risk.

At June 30, 2013 and December 31, 2012, a breakdown of the short-term and long-term borrowings by business unit responsible for risk-managing each borrowing is shown in the table below:

Business Unit	Short-term and Long-term Borrowings At June 30, 2013	At December 31, 2012
	(dollars in millions)	
Interest rates	$ 19,643	$ 23,330
Equity	19,387	17,326
Credit and foreign exchange	2,680	3,337
Commodities	699	776
Total	$ 42,409	$ 44,769

The following tables present information on the Company s short-term and long-term borrowings (primarily structured notes), loans and unfunded lending commitments for which the fair value option was elected.

Gains (Losses) due to Changes in Instrument-Specific Credit Risk.

	Three Months Ended June 30, 2013	2012	Six Months Ended June 30, 2013	2012
	(dollars in millions)			
Short-term and long-term borrowings(1)	$ 175	$ 350	$ (142)	$ (1,628)
Loans(2)	55	(119)	115	174
Unfunded lending commitments(3)	81	78	215	485

(1) The change in the fair value of short-term and long-term borrowings (primarily structured notes) includes an adjustment to reflect the change in credit quality of the Company based upon observations of the Company s secondary bond market spreads.
(2) Instrument-specific credit gains (losses) were determined by excluding the non-credit components of gains and losses, such as those due to changes in interest rates.
(3) Gains (losses) were generally determined based on the differential between estimated expected client yields and contractual yields at each respective period end.

37

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Net Difference between Contractual Principal Amount and Fair Value.

	Contractual Principal Amount Exceeds Fair Value	
	At June 30, 2013	At December 31, 2012
	(dollars in millions)	
Short-term and long-term borrowings(1)	$ (821)	$ (436)
Loans(2)	18,653	25,249
Loans 90 or more days past due and/or on non-accrual status(2)(3)	15,766	20,456

(1) These amounts do not include structured notes where the repayment of the initial principal amount fluctuates based on changes in the reference price or index.
(2) The majority of this difference between principal and fair value amounts emanates from the Company s distressed debt trading business, which purchases distressed debt at amounts well below par.
(3) The aggregate fair value of loans that were in non-accrual status, which includes all loans 90 or more days past due, was $1,523 million and $1,360 million at June 30, 2013 and December 31, 2012, respectively. The aggregate fair value of loans that were 90 or more days past due was $785 million and $840 million at June 30, 2013 and December 31, 2012, respectively.

The tables above exclude non-recourse debt from consolidated VIEs, liabilities related to failed sales of financial assets, pledged commodities and other liabilities that have specified assets attributable to them.

***Assets and Liabilities Measured at Fair Value on a Non-recurring Basis*.**

Certain assets were measured at fair value on a non-recurring basis and are not included in the tables above. These assets may include loans, other investments, premises, equipment and software costs, and intangible assets.

The following tables present, by caption on the condensed consolidated statements of financial condition, the fair value hierarchy for those assets measured at fair value on a non-recurring basis for which the Company recognized a non-recurring fair value adjustment for the quarters and six months ended June 30, 2013 and 2012, respectively.

Three and Six Months Ended June 30, 2013.

		Fair Value Measurements Using:				
	Carrying Value at June 30, 2013(1)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Gains (Losses) for the Three Months Ended June 30, 2013(2)	Total Gains (Losses) for the Six Months Ended June 30, 2013(2)
				(dollars in millions)		
Loans(3)	$ 1,511	$	$ 1,254	$ 257	$ (51)	$ (77)
Other investments(4)	64			64	(5)	(20)
Premises, equipment and software costs(4)					(6)	(6)

Intangible assets(4)	25				25		(8)		(9)
Total	$ 1,600	$	$	1,254	$ 346	$	(70)	$	(112)

(1) Carrying values relate only to those assets that had fair value adjustments during the quarter ended June 30, 2013. These amounts do not include assets that had fair value adjustments during the six months ended June 30, 2013, unless the assets also had a fair value adjustment during the quarter ended June 30, 2013.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(2) Losses are recorded within Other expenses in the condensed consolidated statements of income except for fair value adjustments related to Loans and losses related to Other investments, which are included in Other revenues.
(3) Non-recurring changes in fair value for loans held for investment were calculated based upon the fair value of the underlying collateral. The fair value of the collateral was determined using internal expected recovery models. The non-recurring change in fair value for mortgage loans held for sale is based upon a valuation model incorporating market observable inputs.
(4) Losses recorded were determined primarily using discounted cash flow models.

There were no liabilities measured at fair value on a non-recurring basis during the quarter and six months ended June 30, 2013.

Three and Six Months Ended June 30, 2012.

		Fair Value Measurements Using:				
	Carrying Value at June 30, 2012(1)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Gains (Losses) for the Three Months Ended June 30, 2012(2)	Total Gains (Losses) for the Six Months Ended June 30, 2012(2)
				(dollars in millions)		
Loans(3)	$ 762	$	$ 146	$ 616	$ (13)	$ (19)
Other investments(4)	86			86	(7)	(8)
Premises, equipment and software costs(4)	1			1		(2)
Intangible assets(4)					(2)	(4)
Total	$ 849	$	$ 146	$ 703	$ (22)	$ (33)

(1) Carrying values relate only to those assets that had fair value adjustments during the quarter ended June 30, 2012. These amounts do not include assets that had fair value adjustments during the six months ended June 30, 2012, unless the assets also had a fair value adjustment during the quarter ended June 30, 2012.
(2) Losses are recorded within Other expenses in the condensed consolidated statements of income except for fair value adjustments related to Loans and losses related to Other investments, which are included in Other revenues.
(3) Non-recurring changes in fair value for loans held for investment were calculated based upon the fair value of the underlying collateral. The fair value of the collateral was determined using internal expected recovery models. The non-recurring change in fair value for mortgage loans held for sale is based upon a valuation model incorporating market observable inputs.
(4) Losses recorded were determined primarily using discounted cash flow models.

In addition to the losses included in the table above, there was a pre-tax gain of approximately $51 million (related to Other assets) included in discontinued operations in the six months ended June 30, 2012 in connection with the disposition of Saxon (see Notes 1 and 21). This pre-tax gain was primarily due to the subsequent increase in the fair value of Saxon, which had incurred impairment losses of $98 million in the quarter ended December 31, 2011. The fair value of Saxon was determined based on the revised purchase price agreed upon with the buyer.

There were no liabilities measured at fair value on a non-recurring basis during the quarter and six months ended June 30, 2012.

Financial Instruments Not Measured at Fair Value.

The tables below present the carrying value, fair value and fair value hierarchy category of certain financial instruments that are not measured at fair value in the condensed consolidated statements of financial condition. The tables below exclude certain financial instruments such as equity method investments and all non-financial assets and liabilities such as the value of the long-term relationships with our deposit customers.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The carrying value of cash and cash equivalents, including Interest bearing deposits with banks, and other short-term financial instruments such as Federal funds sold and securities purchased under agreements to resell, Securities borrowed, Securities sold under agreements to repurchase, Securities loaned, certain Customer and other receivables and Customer and other payables arising in the ordinary course of business, Deposits, Commercial paper and other short-term borrowings and Other secured financings approximate fair value because of the relatively short period of time between their origination and expected maturity.

For longer-dated Federal funds sold and securities purchased under agreements to resell, Securities borrowed, Securities sold under agreements to repurchase, Securities loaned and Other secured financings, fair value is determined using a standard cash flow discounting methodology. The inputs to the valuation include contractual cash flows and collateral funding spreads, which are estimated using various benchmarks and interest rate yield curves.

For consumer and residential real estate loans where position-specific external price data are not observable, the fair value is based on the credit risks of the borrower using a probability of default and loss given default method, discounted at the estimated external cost of funding level. The fair value of corporate loans is determined using recently executed transactions, market price quotations (where observable), implied yields from comparable debt, and market observable credit default swap spread levels along with proprietary valuation models and default recovery analysis where such transactions and quotations are unobservable.

The fair value of long-term borrowings is generally determined based on transactional data or third party pricing for identical or comparable instruments, when available. Where position-specific external prices are not observable, fair value is determined based on current interest rates and credit spreads for debt instruments with similar terms and maturity.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Financial Instruments Not Measured at Fair Value at June 30, 2013 and December 31, 2012.

At June 30, 2013.

	At June 30, 2013		Fair Value Measurements Using:		
	Carrying Value	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
			(dollars in millions)		
Financial Assets:					
Cash and due from banks	$ 16,295	$ 16,295	$ 16,295	$	$
Interest bearing deposits with banks	30,904	30,904	30,904		
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	35,363	35,363	35,363		
Federal funds sold and securities purchased under agreements to resell	141,625	141,642		140,915	727
Securities borrowed	129,114	129,119		128,924	195
Customer and other receivables(1)	59,647	59,444		53,942	5,502
Loans(2)	34,571	34,797		7,458	27,339
Financial Liabilities:					
Deposits	$ 80,089	$ 80,089	$	$ 80,089	$
Commercial paper and other short-term borrowings	776	776		651	125
Securities sold under agreements to repurchase	133,030	132,996		123,861	9,135
Securities loaned	36,135	36,195		34,544	1,651
Other secured financings	7,219	7,236		4,453	2,783
Customer and other payables(1)	142,215	142,215		142,215	
Long-term borrowings	120,279	122,168		114,176	7,992

(1) Accrued interest, fees and dividend receivables and payables where carrying value approximates fair value have been excluded.
(2) Includes all loans measured at fair value on a non-recurring basis.

The fair value of the Company s unfunded lending commitments, primarily related to corporate lending in the Institutional Securities business segment, that are not carried at fair value at June 30, 2013 was $986 million, of which $706 million and $280 million would be categorized in Level 2 and Level 3 of the fair value hierarchy, respectively. The carrying value of these commitments, if fully funded, would be $68.6 billion.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

At December 31, 2012.

	At December 31, 2012		Fair Value Measurements Using:		
	Carrying Value	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
			(dollars in millions)		
Financial Assets:					
Cash and due from banks	$ 20,878	$ 20,878	$ 20,878	$	$
Interest bearing deposits with banks	26,026	26,026	26,026		
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	30,970	30,970	30,970		
Federal funds sold and securities purchased under agreements to resell	133,791	133,792		133,035	757
Securities borrowed	121,701	121,705		121,691	14
Customer and other receivables(1)	59,702	59,634		53,532	6,102
Loans(2)	29,046	27,263		5,307	21,956
Financial Liabilities:					
Deposits	$ 81,781	$ 81,781	$	$ 81,781	$
Commercial paper and other short-term borrowings	1,413	1,413		1,107	306
Securities sold under agreements to repurchase	122,311	122,389		111,722	10,667
Securities loaned	36,849	37,163		35,978	1,185
Other secured financings	6,261	6,276		3,649	2,627
Customer and other payables(1)	125,037	125,037		125,037	
Long-term borrowings	125,527	126,683		116,511	10,172

(1) Accrued interest, fees and dividend receivables and payables where carrying value approximates fair value have been excluded.
(2) Includes all loans measured at fair value on a non-recurring basis.

The fair value of the Company s unfunded lending commitments, primarily related to corporate lending in the Institutional Securities business segment, that are not carried at fair value at December 31, 2012 was $755 million, of which $543 million and $212 million would be categorized in Level 2 and Level 3 of the fair value hierarchy, respectively. The carrying value of these commitments, if fully funded, would be $50.0 billion.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

5. Securities Available for Sale.

The following tables present information about the Company s available for sale securities:

	At June 30, 2013				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Other-than-Temporary Impairment	Fair Value
	(dollars in millions)				
Debt securities available for sale:					
U.S. government and agency securities:					
U.S. Treasury securities	$ 15,772	$ 46	$ 110	$	$ 15,708
U.S. agency securities	14,364	30	166		14,228
Total U.S. government and agency securities	30,136	76	276		29,936
Corporate and other debt:					
Commercial mortgage-backed securities:					
Agency	2,426		64		2,362
Non-Agency	913		24		889
Auto loan asset-backed securities	2,056	1	7		2,050
Corporate bonds	3,679	2	67		3,614
Collateralized debt and loan obligations	1,087		8		1,079
FFELP student loan asset-backed securities(1)	2,911	14	7		2,918
Total Corporate and other debt	13,072	17	177		12,912
Total debt securities available for sale	43,208	93	453		42,848
Equity securities available for sale	15		5		10
Total	$ 43,223	$ 93	$ 458	$	$ 42,858

	At December 31, 2012				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Other-than-Temporary Impairment	Fair Value
	(dollars in millions)				
Debt securities available for sale:					
U.S. government and agency securities:					
U.S. Treasury securities	$ 14,351	$ 109	$ 2	$	$ 14,458
U.S. agency securities	15,330	122	3		15,449
Total U.S. government and agency securities	29,681	231	5		29,907
Corporate and other debt:					
Commercial mortgage-backed securities:					
Agency	2,197	6	4		2,199
Non-Agency	160				160

Auto loan asset-backed securities	1,993	4	1		1,996
Corporate bonds	2,891	13	3		2,901
FFELP student loan asset-backed securities(1)	2,675	23			2,698
Total Corporate and other debt	9,916	46	8		9,954
Total debt securities available for sale	39,597	277	13		39,861
Equity securities available for sale	15		7		8
Total	$ 39,612	$ 277	$ 20	$	$ 39,869

(1) Amounts are backed by a guarantee from the U.S. Department of Education of at least 95% of the principal balance and interest on such loans.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below present the fair value of investments in securities available for sale that are in an unrealized loss position:

At June 30, 2013	Less than 12 Months Fair Value	Less than 12 Months Gross Unrealized Losses	12 Months or Longer Fair Value	12 Months or Longer Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
	(dollars in millions)					
Debt securities available for sale:						
U.S. government and agency securities:						
U.S. Treasury securities	$ 6,428	$ 110	$	$	$ 6,428	$ 110
U.S. agency securities	7,108	166	8		7,116	166
Total U.S. government and agency securities	13,536	276	8		13,544	276
Corporate and other debt:						
Commercial mortgage-backed securities:						
Agency	2,362	64			2,362	64
Non-Agency	889	24			889	24
Auto loan asset-backed securities	1,288	7			1,288	7
Corporate bonds	3,080	67			3,080	67
Collateralized debt and loan obligations	1,079	8			1,079	8
FFELP student loan asset-backed securities	1,359	7			1,359	7
Total Corporate and other debt	10,057	177			10,057	177
Total debt securities available for sale	23,593	453	8		23,601	453
Equity securities available for sale			10	5	10	5
Total	$ 23,593	$ 453	$ 18	$ 5	$ 23,611	$ 458

At December 31, 2012	Less than 12 Months Fair Value	Less than 12 Months Gross Unrealized Losses	12 Months or Longer Fair Value	12 Months or Longer Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
	(dollars in millions)					
Debt securities available for sale:						
U.S. government and agency securities:						
U.S. Treasury securities	$ 1,012	$ 2	$	$	$ 1,012	$ 2
U.S. agency securities	1,534	3	27		1,561	3
Total U.S. government and agency securities	2,546	5	27		2,573	5
Corporate and other debt:						
Commercial mortgage-backed securities:						
Agency	1,057	4			1,057	4
Auto loan asset-backed securities	710	1			710	1
Corporate bonds	934	3			934	3

Total Corporate and other debt	2,701	8			2,701	8
Total debt securities available for sale	5,247	13	27		5,274	13
Equity securities available for sale	8	7			8	7
Total	$ 5,255	$ 20	$ 27	$	$ 5,282	$ 20

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Gross unrealized gains and losses are recorded in Accumulated other comprehensive income.

The unrealized losses reported above on debt securities available for sale are due to rising interest rates during the quarter ended June 30, 2013. The Company does not intend to sell these securities or expect to be required to sell these securities prior to recovery of the amortized cost basis. In addition, the Company does not expect the U.S. government and agency securities to experience a credit loss given the explicit and implicit guarantee provided by the U.S. government. The Company believes that the debt securities with an unrealized loss in Accumulated other comprehensive income were not other-than-temporarily impaired at June 30, 2013.

For equity securities available for sale in an unrealized loss position, the Company does not intend to sell these securities or expect to be required to sell these securities prior to the recovery of the amortized cost basis. The Company believes that the equity securities with an unrealized loss in Accumulated other comprehensive income were not other-than-temporarily impaired at June 30, 2013.

The following table presents the amortized cost and fair value of debt securities available for sale by contractual maturity dates at June 30, 2013.

At June 30, 2013	Amortized Cost	Fair Value (dollars in millions)	Annualized Average Yield
U.S. government and agency securities:			
U.S. Treasury securities:			
Due within 1 year	$ 449	$ 455	2.1%
After 1 year through 5 years	15,131	15,060	0.7%
After 5 years through 10 years	192	193	2.0%
Total	15,772	15,708	
U.S. agency securities:			
After 5 years through 10 years	2,061	2,053	1.1%
After 10 years	12,303	12,175	1.2%
Total	14,364	14,228	
Total U.S. government and agency securities	30,136	29,936	1.0%
Corporate and other debt:			
Commercial mortgage-backed securities:			
Agency:			
After 1 year through 5 years	542	533	0.9%
After 5 years through 10 years	555	544	0.9%
After 10 years	1,329	1,285	1.5%
Total	2,426	2,362	
Non-Agency:			
After 1 year through 5 years	116	113	1.1%
After 5 years through 10 years	38	37	0.8%
After 10 years	759	739	1.5%

Total	913	889	
Auto loan asset-backed securities:			
After 1 year through 5 years	1,933	1,929	0.7%
After 5 years through 10 years	123	121	0.7%
Total	2,056	2,050	

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

At June 30, 2013	Amortized Cost	Fair Value (dollars in millions)	Annualized Average Yield
Corporate bonds:			
Due within 1 year	208	208	0.5%
After 1 year through 5 years	2,735	2,697	1.2%
After 5 years through 10 years	736	709	2.1%
Total	3,679	3,614	
Collateralized debt and loan obligations:			
After 1 year through 5 years	50	50	1.7%
After 10 years	1,037	1,029	1.5%
Total	1,087	1,079	
FFELP student loan asset-backed securities:			
After 1 year through 5 years	110	110	0.7%
After 5 years through 10 years	474	476	1.0%
After 10 years	2,327	2,332	1.0%
Total	2,911	2,918	
Total Corporate and other debt	13,072	12,912	1.1%
Total debt securities available for sale	$ 43,208	$ 42,848	1.0%

See Note 7 for additional information on securities issued by VIEs, including U.S. agency mortgage-backed securities, auto loan asset-backed securities, FFELP student loan asset-backed securities and collateralized debt and loan obligations.

The following table presents information pertaining to sales of securities available for sale during the three and six months ended June 30, 2013 and 2012:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(dollars in millions)			
Gross realized gains	$ 35	$ 24	$ 41	$ 25
Gross realized losses	$ 1	$ 2	$ 3	$ 2

Gross realized gains and losses are recognized in Other revenues in the condensed consolidated statements of income.

6. Collateralized Transactions.

The Company enters into reverse repurchase agreements, repurchase agreements, securities borrowed and securities loaned transactions to, among other things, acquire securities to cover short positions and settle other securities obligations, to accommodate customers needs and to finance the Company s inventory positions. The Company manages credit exposure arising from such transactions by, in appropriate circumstances, entering into master netting agreements and collateral agreements with counterparties that provide the Company, in the event of a counterparty default (such as bankruptcy or a counterparty s failure to pay or perform), the right to net a counterparty s rights and obligations under such agreement and liquidate and setoff collateral against the net amount owed by the counterparty. The Company s policy is generally to take possession of securities purchased under agreements to resell and securities borrowed, and to receive securities and cash posted as collateral (with rights of rehypothecation), although in certain

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

cases the Company may agree for such collateral to be posted to a third party custodian under a tri-party arrangement that enables the Company to take control of such collateral in the event of a counterparty default. The Company also monitors the fair value of the underlying securities as compared with the related receivable or payable, including accrued interest, and, as necessary, requests additional collateral as provided under the applicable agreement to ensure such transactions are adequately collateralized. The following tables present information about the offsetting of these instruments and related collateral amounts. For information related to offsetting of derivatives, see Note 11.

	At June 30, 2013				
	Gross Amounts(1)	Amounts Offset in the Condensed Consolidated Statements of Financial Condition(2)	Net Amounts Presented in the Condensed Consolidated Statements of Financial Condition	Financial Instruments Not Offset in the Condensed Consolidated Statements of Financial Condition(3)	Net Exposure
			(dollars in millions)		
Assets					
Federal funds sold and securities purchased under agreements to resell	$ 224,457	$ (81,963)	$ 142,494	$ (134,752)	$ 7,742
Securities borrowed	135,398	(6,284)	129,114	(112,776)	16,338
Liabilities					
Securities sold under agreements to repurchase	$ 215,545	$ (81,963)	$ 133,582	$ (102,451)	$ 31,131
Securities loaned	42,419	(6,284)	36,135	(33,965)	2,170

(1) Amounts include $7.4 billion of Federal funds sold and securities purchased under agreements to resell, $13.2 billion of Securities borrowed, $29.6 billion of Securities sold under agreements to repurchase and $2.0 billion of Securities loaned which are either not subject to master netting agreements or collateral agreements or are subject to such agreements but the Company has not determined the agreements to be legally enforceable.
(2) Amounts relate to master netting agreements and collateral agreements which have been determined by the Company to be legally enforceable in the event of default and where certain other criteria are met in accordance with applicable offsetting accounting guidance.
(3) Amounts relate to master netting agreements and collateral agreements which have been determined by the Company to be legally enforceable in the event of default but where certain other criteria are not met in accordance with applicable offsetting accounting guidance.

	At December 31, 2012				
	Gross Amounts(1)	Amounts Offset in the Condensed Consolidated Statements of Financial Condition(2)	Net Amounts Presented in the Condensed Consolidated Statements of	Financial Instruments Not Offset in the Condensed Consolidated Statements	Net Exposure

			Financial Condition	of Financial Condition(3)	
			(dollars in millions)		
Assets					
Federal funds sold and securities purchased under agreements to resell	$ 203,448	$ (69,036)	$ 134,412	$ (126,303)	$ 8,109
Securities borrowed	127,002	(5,301)	121,701	(105,849)	15,852
Liabilities					
Securities sold under agreements to repurchase	$ 191,710	$ (69,036)	$ 122,674	$ (103,521)	$ 19,153
Securities loaned	42,150	(5,301)	36,849	(30,395)	6,454

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) Amounts include $7.4 billion of Federal funds sold and securities purchased under agreements to resell, $8.6 billion of Securities borrowed, $17.5 billion of Securities sold under agreements to repurchase and $0.6 billion of Securities loaned which are either not subject to master netting agreements or collateral agreements or are subject to such agreements but the Company has not determined the agreements to be legally enforceable.
(2) Amounts relate to master netting agreements and collateral agreements which have been determined by the Company to be legally enforceable in the event of default and where certain other criteria are met in accordance with applicable offsetting accounting guidance.
(3) Amounts relate to master netting agreements and collateral agreements which have been determined by the Company to be legally enforceable in the event of default but where certain other criteria are not met in accordance with applicable offsetting accounting guidance.

The Company also engages in securities financing transactions for customers through margin lending. Under these agreements and transactions, the Company either receives or provides collateral, including U.S. government and agency securities, other sovereign government obligations, corporate and other debt, and corporate equities. Customer receivables generated from margin lending activity are collateralized by customer-owned securities held by the Company. The Company monitors required margin levels and established credit limits daily and, pursuant to such guidelines, requires customers to deposit additional collateral, or reduce positions, when necessary. Margin loans are extended on a demand basis and are not committed facilities. Factors considered in the review of margin loans are the amount of the loan, the intended purpose, the degree of leverage being employed in the account, and overall evaluation of the portfolio to ensure proper diversification or, in the case of concentrated positions, appropriate liquidity of the underlying collateral or potential hedging strategies to reduce risk. Additionally, transactions relating to concentrated or restricted positions require a review of any legal impediments to liquidation of the underlying collateral. Underlying collateral for margin loans is reviewed with respect to the liquidity of the proposed collateral positions, valuation of securities, historic trading range, volatility analysis and an evaluation of industry concentrations. For these transactions, adherence to the Company s collateral policies significantly limits the Company s credit exposure in the event of customer default. The Company may request additional margin collateral from customers, if appropriate, and, if necessary, may sell securities that have not been paid for or purchase securities sold but not delivered from customers. At June 30, 2013 and December 31, 2012, there were approximately $21.3 billion and $24.0 billion, respectively, of customer margin loans outstanding.

Other secured financings include the liabilities related to transfers of financial assets that are accounted for as financings rather than sales, consolidated VIEs where the Company is deemed to be the primary beneficiary, and certain equity-linked notes and other secured borrowings. These liabilities are generally payable from the cash flows of the related assets accounted for as Trading assets (see Notes 7 and 10).

The Company pledges its trading assets to collateralize repurchase agreements and other securities financings. Pledged financial instruments that can be sold or repledged by the secured party are identified as Trading assets (pledged to various parties) in the condensed consolidated statements of financial condition. The carrying value and classification of Trading assets by the Company that have been loaned or pledged to counterparties where those counterparties do not have the right to sell or repledge the collateral were as follows:

	At June 30, 2013	At December 31, 2012
	(dollars in millions)	
Trading assets:		
U.S. government and agency securities	$ 9,350	$ 15,273
Other sovereign government obligations	4,001	3,278
Corporate and other debt	14,913	11,980
Corporate equities	9,788	26,377
Total	$ 38,052	$ 56,908

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company receives collateral in the form of securities in connection with reverse repurchase agreements, securities borrowed and derivative transactions, and customer margin loans. In many cases, the Company is permitted to sell or repledge these securities held as collateral and use the securities to secure repurchase agreements, to enter into securities lending and derivative transactions or for delivery to counterparties to cover short positions. The Company additionally receives securities as collateral in connection with certain securities-for-securities transactions in which the Company is the lender. In instances where the Company is permitted to sell or repledge these securities, the Company reports the fair value of the collateral received and the related obligation to return the collateral in the condensed consolidated statements of financial condition. At June 30, 2013 and December 31, 2012, the fair value of financial instruments received as collateral where the Company is permitted to sell or repledge the securities was $602 billion and $560 billion, respectively, and the fair value of the portion that had been sold or repledged was $443 billion and $397 billion, respectively.

At June 30, 2013 and December 31, 2012, cash and securities deposited with clearing organizations or segregated under federal and other regulations or requirements were as follows:

	At June 30, 2013	At December 31, 2013
	(dollars in millions)	
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	$ 35,363	$ 30,970
Securities(1)	14,555	13,424
Total	$ 49,918	$ 44,394

(1) Securities deposited with clearing organizations or segregated under federal and other regulations or requirements are sourced from Federal funds sold and securities purchased under agreements to resell and Trading assets in the condensed consolidated statements of financial condition.

7. Variable Interest Entities and Securitization Activities.

The Company is involved with various special purpose entities (SPE) in the normal course of business. In most cases, these entities are deemed to be VIEs.

The Company applies accounting guidance for consolidation of VIEs to certain entities in which equity investors do not have the characteristics of a controlling financial interest. Except for certain asset management entities, the primary beneficiary of a VIE is the party that both (1) has the power to direct the activities of a VIE that most significantly affect the VIE s economic performance and (2) has an obligation to absorb losses or the right to receive benefits that in either case could potentially be significant to the VIE. The Company consolidates entities of which it is the primary beneficiary.

The Company s variable interests in VIEs include debt and equity interests, commitments, guarantees, derivative instruments and certain fees. The Company s involvement with VIEs arises primarily from:

Interests purchased in connection with market-making activities, securities held in its available for sale portfolio and retained interests held as a result of securitization activities, including re-securitization transactions.

Guarantees issued and residual interests retained in connection with municipal bond securitizations.

Servicing of residential and commercial mortgage loans held by VIEs.

Loans made to and investments in VIEs that hold debt, equity, real estate or other assets.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Derivatives entered into with VIEs.

Structuring of credit-linked notes (CLN) or other asset-repackaged notes designed to meet the investment objectives of clients.

Other structured transactions designed to provide tax-efficient yields to the Company or its clients.

The Company determines whether it is the primary beneficiary of a VIE upon its initial involvement with the VIE and reassesses whether it is the primary beneficiary on an ongoing basis as long as it has any continuing involvement with the VIE. This determination is based upon an analysis of the design of the VIE, including the VIE s structure and activities, the power to make significant economic decisions held by the Company and by other parties, and the variable interests owned by the Company and other parties.

The power to make the most significant economic decisions may take a number of different forms in different types of VIEs. The Company considers servicing or collateral management decisions as representing the power to make the most significant economic decisions in transactions such as securitizations or CDOs. As a result, the Company does not consolidate securitizations or CDOs for which it does not act as the servicer or collateral manager unless it holds certain other rights to replace the servicer or collateral manager or to require the liquidation of the entity. If the Company serves as servicer or collateral manager, or has certain other rights described in the previous sentence, the Company analyzes the interests in the VIE that it holds and consolidates only those VIEs for which it holds a potentially significant interest of the VIE.

The structure of securitization vehicles and CDOs is driven by several parties, including loan seller(s) in securitization transactions, the collateral manager in a CDO, one or more rating agencies, a financial guarantor in some transactions and the underwriter(s) of the transactions, who serve to reflect specific investor demand. In addition, subordinate investors, such as the B-piece buyer (*i.e.,* investors in most subordinated bond classes) in commercial mortgage-backed securitizations or equity investors in CDOs, can influence whether specific loans are excluded from a CMBS transaction or investment criteria in a CDO.

For many transactions, such as re-securitization transactions, CLNs and other asset-repackaged notes, there are no significant economic decisions made on an ongoing basis. In these cases, the Company focuses its analysis on decisions made prior to the initial closing of the transaction and at the termination of the transaction. Based upon factors, which include an analysis of the nature of the assets, including whether the assets were issued in a transaction sponsored by the Company and the extent of the information available to the Company and to investors, the number, nature and involvement of investors, other rights held by the Company and investors, the standardization of the legal documentation and the level of the continuing involvement by the Company, including the amount and type of interests owned by the Company and by other investors, the Company concluded in most of these transactions that decisions made prior to the initial closing were shared between the Company and the initial investors. The Company focused its control decision on any right held by the Company or investors related to the termination of the VIE. Most re-securitization transactions, CLNs and other asset-repackaged notes have no such termination rights.

Except for consolidated VIEs included in other structured financings and managed real estate partnerships in the tables below, the Company accounts for the assets held by the entities primarily in Trading assets and the liabilities of the entities as Other secured financings in the condensed consolidated statements of financial condition. For consolidated VIEs included in other structured financings, the Company accounts for the assets held by the entities primarily in Premises, equipment and software costs, and Other assets in the condensed consolidated statements of financial condition. For consolidated VIEs included in managed real estate partnerships, the Company accounts for the assets held by the entities primarily in Trading assets in the condensed consolidated statements of financial condition. Except for consolidated VIEs included in other structured financings, the assets and liabilities are measured at fair value, with changes in fair value reflected in earnings.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The assets owned by many consolidated VIEs cannot be removed unilaterally by the Company and are not generally available to the Company. The related liabilities issued by many consolidated VIEs are non-recourse to the Company. In certain other consolidated VIEs, the Company has the unilateral right to remove assets or provides additional recourse through derivatives such as total return swaps, guarantees or other forms of involvement.

As part of the Company s Institutional Securities business segment s securitization and related activities, the Company has provided, or otherwise agreed to be responsible for, representations and warranties regarding certain assets transferred in securitization transactions sponsored by the Company (see Note 12).

The following tables present information at June 30, 2013 and December 31, 2012 about VIEs that the Company consolidates. Consolidated VIE assets and liabilities are presented after intercompany eliminations and include assets financed on a non-recourse basis:

	At June 30, 2013				
	Mortgage and Asset-Backed Securitizations	Collateralized Debt Obligations	Managed Real Estate Partnerships	Other Structured Financings	Other
	(dollars in millions)				
VIE assets	$ 753	$	$ 2,235	$ 1,226	$ 1,387
VIE liabilities	$ 448	$	$ 107	$ 65	$ 162

	At December 31, 2012				
	Mortgage and Asset-Backed Securitizations	Collateralized Debt Obligations	Managed Real Estate Partnerships	Other Structured Financings	Other
	(dollars in millions)				
VIE assets	$ 978	$ 52	$ 2,394	$ 983	$ 1,676
VIE liabilities	$ 646	$ 16	$ 83	$ 65	$ 313

In general, the Company s exposure to loss in consolidated VIEs is limited to losses that would be absorbed on the VIE s assets recognized in its financial statements, net of losses absorbed by third-party holders of the VIE s liabilities. At June 30, 2013 and December 31, 2012, managed real estate partnerships reflected nonredeemable noncontrolling interests in the Company s condensed consolidated financial statements of $1,679 million and $1,804 million, respectively. The Company also had additional maximum exposure to losses of approximately $62 million and $58 million at June 30, 2013 and December 31, 2012, respectively. This additional exposure related primarily to certain derivatives (*e.g.*, instead of purchasing senior securities, the Company has sold credit protection to synthetic CDOs through credit derivatives that are typically related to the most senior tranche of the CDO) and commitments, guarantees and other forms of involvement.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables present information about certain non-consolidated VIEs in which the Company had variable interests at June 30, 2013 and December 31, 2012. The tables include all VIEs in which the Company has determined that its maximum exposure to loss is greater than specific thresholds or meets certain other criteria. Most of the VIEs included in the tables below are sponsored by unrelated parties; the Company s involvement generally is the result of the Company s secondary market-making activities and securities held in its available for sale portfolio (see Note 5):

	At June 30, 2013				
	Mortgage and Asset-Backed Securitizations	Collateralized Debt Obligations	Municipal Tender Option Bonds	Other Structured Financings	Other
	(dollars in millions)				
VIE assets that the Company does not consolidate (unpaid principal balance)(1)	$ 279,227	$ 22,003	$ 3,247	$ 1,759	$ 9,631
Maximum exposure to loss:					
Debt and equity interests(2)	$ 22,707	$ 1,978	$ 79	$ 1,061	$ 2,788
Derivative and other contracts	119	24	1,999		231
Commitments, guarantees and other		278		661	539
Total maximum exposure to loss	$ 22,826	$ 2,280	$ 2,078	$ 1,722	$ 3,558
Carrying value of exposure to loss Assets:					
Debt and equity interests(2)	$ 22,707	$ 1,978	$ 79	$ 670	$ 2,788
Derivative and other contracts	119	5	4		83
Total carrying value of exposure to loss Assets	$ 22,826	$ 1,983	$ 83	$ 670	$ 2,871
Carrying value of exposure to loss Liabilities:					
Derivative and other contracts	$	$ 2	$	$	$ 54
Commitments, guarantees and other				10	
Total carrying value of exposure to loss Liabilities	$	$ 2	$	$ 10	$ 54

(1) Mortgage and asset-backed securitizations include VIE assets as follows: $26.9 billion of residential mortgages; $62.4 billion of commercial mortgages; $132.2 billion of U.S. agency collateralized mortgage obligations; and $57.7 billion of other consumer or commercial loans.

(2) Mortgage and asset-backed securitizations include VIE debt and equity interests as follows: $2.5 billion of residential mortgages; $1.6 billion of commercial mortgages; $13.7 billion of U.S. agency collateralized mortgage obligations; and $4.9 billion of other consumer or commercial loans.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	At December 31, 2012				
	Mortgage and Asset-Backed Securitizations	Collateralized Debt Obligations	Municipal Tender Option Bonds	Other Structured Financings	Other
	(dollars in millions)				
VIE assets that the Company does not consolidate (unpaid principal balance)(1)	$ 251,689	$ 13,178	$ 3,390	$ 1,811	$ 14,029
Maximum exposure to loss:					
Debt and equity interests(2)	$ 22,280	$ 1,173	$	$ 1,053	$ 3,387
Derivative and other contracts	154	51	2,158		562
Commitments, guarantees and other	66			679	384
Total maximum exposure to loss	$ 22,500	$ 1,224	$ 2,158	$ 1,732	$ 4,333
Carrying value of exposure to loss Assets:					
Debt and equity interests(2)	$ 22,280	$ 1,173	$	$ 663	$ 3,387
Derivative and other contracts	156	8	4		174
Total carrying value of exposure to loss Assets	$ 22,436	$ 1,181	$ 4	$ 663	$ 3,561
Carrying value of exposure to loss Liabilities:					
Derivative and other contracts	$ 11	$ 2	$	$	$ 172
Commitments, guarantees and other				12	
Total carrying value of exposure to loss Liabilities	$ 11	$ 2	$	$ 12	$ 172

(1) Mortgage and asset-backed securitizations include VIE assets as follows: $18.3 billion of residential mortgages; $53.8 billion of commercial mortgages; $126.3 billion of U.S. agency collateralized mortgage obligations; and $53.3 billion of other consumer or commercial loans.

(2) Mortgage and asset-backed securitizations include VIE debt and equity interests as follows: $1.0 billion of residential mortgages; $1.5 billion of commercial mortgages; $14.8 billion of U.S. agency collateralized mortgage obligations; and $5.0 billion of other consumer or commercial loans.

The Company s maximum exposure to loss often differs from the carrying value of the variable interests held by the Company. The maximum exposure to loss is dependent on the nature of the Company s variable interest in the VIEs and is limited to the notional amounts of certain liquidity facilities, other credit support, total return swaps, written put options, and the fair value of certain other derivatives and investments the Company has made in the VIEs. Liabilities issued by VIEs generally are non-recourse to the Company. Where notional amounts are utilized in quantifying maximum exposure related to derivatives, such amounts do not reflect fair value writedowns already recorded by the Company.

The Company s maximum exposure to loss does not include the offsetting benefit of any financial instruments that the Company may utilize to hedge these risks associated with the Company s variable interests. In addition, the Company s maximum exposure to loss is not reduced by the amount of collateral held as part of a transaction with the VIE or any party to the VIE directly against a specific exposure to loss.

Securitization transactions generally involve VIEs. Primarily as a result of its secondary market-making activities, the Company owned additional securities issued by securitization SPEs for which the maximum exposure to loss is less than specific thresholds. These additional securities totaled $4.5 billion at June 30, 2013. These securities were either retained in connection with transfers of assets by the Company, acquired in connection with secondary market-making activities or held in the Company s available for sale portfolio (see Note 5). Securities issued by

53

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

securitization SPEs consist of $1.7 billion of securities backed primarily by residential mortgage loans, $0.4 billion of securities backed by U.S. agency collateralized mortgage obligations, $1.0 billion of securities backed by commercial mortgage loans, $0.5 billion of securities backed by collateralized debt obligations or collateralized loan obligations and $0.9 billion backed by other consumer loans, such as credit card receivables, automobile loans and student loans. The Company s primary risk exposure is to the securities issued by the SPE owned by the Company, with the risk highest on the most subordinate class of beneficial interests. These securities generally are included in Trading assets Corporate and other debt or Securities available for sale and are measured at fair value (see Note 4). The Company does not provide additional support in these transactions through contractual facilities, such as liquidity facilities, guarantees or similar derivatives. The Company s maximum exposure to loss generally equals the fair value of the securities owned.

The Company s transactions with VIEs primarily include securitizations, municipal tender option bond trusts, credit protection purchased through CLNs, other structured financings, collateralized loan and debt obligations, equity-linked notes, managed real estate partnerships and asset management investment funds. The Company s continuing involvement in VIEs that it does not consolidate can include ownership of retained interests in Company-sponsored transactions, interests purchased in the secondary market (both for Company-sponsored transactions and transactions sponsored by third parties), derivatives with securitization SPEs (primarily interest rate derivatives in commercial mortgage and residential mortgage securitizations and credit derivatives in which the Company has purchased protection in synthetic CDOs), and as servicer in residential mortgage securitizations in the U.S. and Europe and commercial mortgage securitizations in Europe. Such activities are further described in Note 7 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K.

Transfers of Assets with Continuing Involvement.

The following tables present information at June 30, 2013 regarding transactions with SPEs in which the Company, acting as principal, transferred financial assets with continuing involvement and received sales treatment:

	At June 30, 2013			
	Residential Mortgage Loans	Commercial Mortgage Loans	U.S. Agency Collateralized Mortgage Obligations	Credit-Linked Notes and Other
	(dollars in millions)			
SPE assets (unpaid principal balance)(1)	$ 33,747	$ 53,754	$ 15,893	$ 12,870
Retained interests (fair value):				
Investment grade	$ 1	$ 55	$ 1,953	$
Non-investment grade	51	114		1,327
Total retained interests (fair value)	$ 52	$ 169	$ 1,953	$ 1,327
Interests purchased in the secondary market (fair value):				
Investment grade	$ 22	$ 67	$ 11	$ 361
Non-investment grade	80	25		61
Total interests purchased in the secondary market (fair value)	$ 102	$ 92	$ 11	$ 422
Derivative assets (fair value)	$	$ 776	$	$ 176
Derivative liabilities (fair value)	$ 2	$ 1	$	$ 189

(1) Amounts include assets transferred by unrelated transferors.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	At June 30, 2013 Level 1	Level 2	Level 3	Total
		(dollars in millions)		
Retained interests (fair value):				
Investment grade	$	$ 1,971	$ 38	$ 2,009
Non-investment grade		94	1,398	1,492
Total retained interests (fair value)	$	$ 2,065	$ 1,436	$ 3,501
Interests purchased in the secondary market (fair value):				
Investment grade	$	$ 438	$ 23	$ 461
Non-investment grade		145	21	166
Total interests purchased in the secondary market (fair value)	$	$ 583	$ 44	$ 627
Derivative assets (fair value)	$	$ 694	$ 258	$ 952
Derivative liabilities (fair value)	$	$ 172	$ 20	$ 192

The following tables present information at December 31, 2012 regarding transactions with SPEs in which the Company, acting as principal, transferred assets with continuing involvement and received sales treatment:

	At December 31, 2012 Residential Mortgage Loans	Commercial Mortgage Loans	U.S. Agency Collateralized Mortgage Obligations	Credit-Linked Notes and Other
		(dollars in millions)		
SPE assets (unpaid principal balance)(1)	$ 36,750	$ 70,824	$ 17,787	$ 14,701
Retained interests (fair value):				
Investment grade	$ 1	$ 77	$ 1,468	$
Non-investment grade	54	109		1,503
Total retained interests (fair value)	$ 55	$ 186	$ 1,468	$ 1,503
Interests purchased in the secondary market (fair value):				
Investment grade	$ 11	$ 124	$ 99	$ 389
Non-investment grade	113	34		31
Total interests purchased in the secondary market (fair value)	$ 124	$ 158	$ 99	$ 420
Derivative assets (fair value)	$ 2	$ 948	$	$ 177
Derivative liabilities (fair value)	$ 22	$	$	$ 303

(1) Amounts include assets transferred by unrelated transferors.

At December 31, 2012

	Level 1	Level 2	Level 3	Total
		(dollars in millions)		
Retained interests (fair value):				
Investment grade	$	$ 1,476	$ 70	$ 1,546
Non-investment grade		84	1,582	1,666
Total retained interests (fair value)	$	$ 1,560	$ 1,652	$ 3,212
Interests purchased in the secondary market (fair value):				
Investment grade	$	$ 617	$ 6	$ 623
Non-investment grade		139	39	178
Total interests purchased in the secondary market (fair value)	$	$ 756	$ 45	$ 801
Derivative assets (fair value)	$	$ 774	$ 353	$ 1,127
Derivative liabilities (fair value)	$	$ 295	$ 30	$ 325

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Transferred assets are carried at fair value prior to securitization, and any changes in fair value are recognized in the condensed consolidated statements of income. The Company may act as underwriter of the beneficial interests issued by securitization vehicles. Investment banking underwriting net revenues are recognized in connection with these transactions. The Company may retain interests in the securitized financial assets as one or more tranches of the securitization. These retained interests are included in the condensed consolidated statements of financial condition at fair value. Any changes in the fair value of such retained interests are recognized in the condensed consolidated statements of income.

Net gains on sales of assets in securitization transactions at the time of the sale were not material in the six months ended June 30, 2013 and 2012.

During the six months ended June 30, 2013 and 2012, the Company received proceeds from new securitization transactions of $13.0 billion and $9.2 billion, respectively. During the six months ended June 30, 2013 and 2012, the Company received proceeds from cash flows from retained interests in securitization transactions of $2.2 billion and $1.7 billion, respectively.

The Company has provided, or otherwise agreed to be responsible for, representations and warranties regarding certain assets transferred in securitization transactions sponsored by the Company (see Note 12).

Failed Sales.

In order to be treated as a sale of assets for accounting purposes, a transaction must meet all of the criteria stipulated in the accounting guidance for the transfer of financial assets. If the transfer fails to meet these criteria, that transfer of financial assets is treated as a failed sale. In such case for transfers to VIEs and securitizations, the Company continues to recognize the assets in Trading assets, and the Company recognizes the associated liabilities in Other secured financings in the condensed consolidated statements of financial condition.

The assets transferred to many unconsolidated VIEs in transactions accounted for as failed sales cannot be removed unilaterally by the Company and are not generally available to the Company. The related liabilities issued by many unconsolidated VIEs are non-recourse to the Company. In certain other failed sale transactions, the Company has the unilateral right to remove assets or provide additional recourse through derivatives such as total return swaps, guarantees or other forms of involvement.

The following table presents information about the carrying value (equal to fair value) of assets and liabilities resulting from transfers of financial assets treated by the Company as secured financings:

	At June 30, 2013 Carrying Value of		At December 31, 2012 Carrying Value of	
	Assets	Liabilities	Assets	Liabilities
	(dollars in millions)			
Credit-linked notes	$ 147	$ 141	$ 283	$ 222
Equity-linked transactions	35	31	422	405
Other	228	227	29	28

Mortgage Servicing Activities.

Mortgage Servicing Rights. The Company may retain servicing rights to certain mortgage loans that are sold. These transactions create an asset referred to as MSRs, which totaled approximately $9 million and $7 million at June 30, 2013 and December 31, 2012, respectively, and are included within Intangible assets and carried at fair value in the condensed consolidated statements of financial condition.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

SPE Mortgage Servicing Activities. The Company services residential mortgage loans in the U.S. and in Europe and commercial mortgage loans in Europe owned by SPEs, including SPEs sponsored by the Company and SPEs not sponsored by the Company. The Company generally holds retained interests in Company-sponsored SPEs. In some cases, as part of its market-making activities, the Company may own some beneficial interests issued by both Company-sponsored and non-Company sponsored SPEs.

The Company provides no credit support as part of its servicing activities. The Company is required to make servicing advances to the extent that it believes that such advances will be reimbursed. Reimbursement of servicing advances is a senior obligation of the SPE, senior to the most senior beneficial interests outstanding. Outstanding advances are included in Other assets and are recorded at cost, net of allowances. Advances at June 30, 2013 and December 31, 2012 totaled approximately $68 million and $49 million, respectively. There were no allowances at June 30, 2013 and December 31, 2012.

The following tables present information about the Company s mortgage servicing activities for SPEs to which the Company transferred loans at June 30, 2013 and December 31, 2012:

	At June 30, 2013		
	Residential Mortgage Unconsolidated SPEs	Residential Mortgage Consolidated SPEs	Commercial Mortgage Unconsolidated SPEs
	(dollars in millions)		
Assets serviced (unpaid principal balance)	$ 741	$ 863	$ 4,301
Amounts past due 90 days or greater (unpaid principal balance)(1)	$ 72	$ 48	$
Percentage of amounts past due 90 days or greater(1)	9.7%	5.5%	
Credit losses	$ 1	$ 3	$

(1) Amounts include loans that are at least 90 days contractually delinquent, loans for which the borrower has filed for bankruptcy, loans in foreclosure and real estate owned.

	At December 31, 2012		
	Residential Mortgage Unconsolidated SPEs	Residential Mortgage Consolidated SPEs	Commercial Mortgage Unconsolidated SPEs
	(dollars in millions)		
Assets serviced (unpaid principal balance)	$ 821	$ 1,141	$ 4,760
Amounts past due 90 days or greater (unpaid principal balance)(1)	$ 86	$ 43	$
Percentage of amounts past due 90 days or greater(1)	10.4%	3.8%	
Credit losses	$ 3	$ 2	$

(1) Amounts include loans that are at least 90 days contractually delinquent, loans for which the borrower has filed for bankruptcy, loans in foreclosure and real estate owned.

8. Financing Receivables and Allowance for Credit Losses.

Loans held for investment.

The Company s loans held for investment are recorded at amortized cost and classified as Loans in the condensed consolidated statements of financial condition.

57

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company s loans held for investment at June 30, 2013 and December 31, 2012 included the following:

	At June 30, 2013	At December 31, 2012
	(dollars in millions)	
Commercial and industrial	$ 11,170	$ 9,449
Consumer loans	9,452	7,618
Residential real estate loans	7,602	6,630
Wholesale real estate loans	863	326
Total loans held for investment, gross of allowance for loan losses	29,087	24,023
Allowance for loan losses	(125)	(106)
Total loans held for investment, net of allowance for loan losses	$ 28,962	$ 23,917

The above table does not include loans held for sale of $5,609 million and $5,129 million at June 30, 2013 and December 31, 2012, respectively.

The Company s Credit Risk Management Department evaluates new obligors before credit transactions are initially approved, and at least annually thereafter for consumer and industrial loans. For commercial loans, credit evaluations typically involve the evaluation of financial statements, assessment of leverage, liquidity, capital strength, asset composition and quality, market capitalization and access to capital markets, cash flow projections and debt service requirements, and the adequacy of collateral, if applicable. The Company s Credit Risk Management Department will also evaluate strategy, market position, industry dynamics, obligor s management and other factors that could affect the obligor s risk profile. For residential real estate and consumer loans, the initial credit evaluation includes, but is not limited to, review of the obligor s income, net worth, liquidity, collateral, loan-to-value ratio, and credit bureau information. Subsequent credit monitoring for residential real estate loans is performed at the portfolio level. Consumer loan collateral values are monitored on an ongoing basis.

Commercial and industrial loans of approximately $4 million and wholesale real estate loans of approximately $10 million were impaired at June 30, 2013. Approximately 99% of the Company s loan portfolio was current at June 30, 2013. Commercial and industrial loans of approximately $19 million and residential real estate loans of approximately $1 million were impaired at December 31, 2012. Approximately 99% of the Company s loan portfolio was current at December 31, 2012.

The Company assigned an internal grade of doubtful to certain commercial asset-backed and wholesale real estate loans totaling $11 million and $25 million at June 30, 2013 and December 31, 2012, respectively. Doubtful loans can be classified as current if the borrower is making payments in accordance with the loan agreement. The Company assigned an internal grade of pass to the majority of its remaining loan portfolio.

For a description of the Company s loan portfolio and credit quality indicators utilized in its credit monitoring process, see Note 8 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The table below summarizes information about the allowance for loan losses, loans by impairment methodology, the allowance for lending-related commitments and lending-related commitments by impairment methodology.

	Commercial and Industrial	Consumer	Residential Real Estate (dollars in millions)	Wholesale Real Estate	Total
Allowance for loan losses:					
Balance at December 31, 2012	$ 96	$ 3	$ 5	$ 2	$ 106
Gross charge-offs	(12)		(1)	(2)	(15)
Net charge-offs	(12)		(1)	(2)	(15)
Provision for loan losses(1)(4)	31	(2)		5	34
Balance at June 30, 2013	$ 115	$ 1	$ 4	$ 5	$ 125
Allowance for loan losses by impairment methodology:					
Collectively evaluated for impairment	$ 113	$ 1	$ 4	$ 4	$ 122
Individually evaluated for impairment	2			1	3
Total allowance for loan losses at June 30, 2013	$ 115	$ 1	$ 4	$ 5	$ 125
Loans evaluated by impairment methodology(2):					
Collectively evaluated for impairment	$ 11,154	$ 9,452	$ 7,594	$ 853	$ 29,053
Individually evaluated for impairment	16		8	10	34
Total loan evaluated at June 30, 2013	$ 11,170	$ 9,452	$ 7,602	$ 863	$ 29,087
Allowance for lending-related commitments:					
Balance at December 31, 2012	$ 90	$	$	$ 1	$ 91
Provision for lending-related commitments(3)(4)	29				29
Other	(10)				(10)
Balance at June 30, 2013	$ 109	$	$	$ 1	$ 110
Allowance for lending-related commitments by impairment methodology:					
Collectively evaluated for impairment	$ 109	$	$	$ 1	$ 110
Individually evaluated for impairment					
Total allowance for lending-related commitments at June 30, 2013	$ 109	$	$	$ 1	$ 110
Lending-related commitments evaluated by impairment methodology:					
Collectively evaluated for impairment	$ 52,245	$ 1,657	$ 2,093	$ 258	$ 56,253

Individually evaluated for impairment

Total lending-related commitments evaluated at June 30, 2013	$ 52,245	$ 1,657	$ 2,093	$ 258	$ 56,253

(1) The Company records charges to the provisions for loan losses within Other revenues.
(2) Balances are gross of the allowance and represent recorded investment in the loans.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(3) The Company records charges to the provisions for lending-related commitments within Other non-interest expenses.
(4) The Company s provision for loan losses and provision for lending-related commitments for the quarter ended June 30, 2013 were $7 million and $17 million, respectively.

	Commercial and Industrial	Consumer	Residential Real Estate (dollars in millions)	Wholesale Real Estate	Total
Allowance for loan losses:					
Balance at December 31, 2011	$ 14	$ 1	$ 1	$ 1	$ 17
Gross charge-offs	(2)				(2)
Gross recoveries				8	8
Net charge-offs	(2)			8	6
Provision for loan losses(1)(4)	53	5	3	(7)	54
Balance at June 30, 2012	$ 65	$ 6	$ 4	$ 2	$ 77
Allowance for loan losses by impairment methodology:					
Collectively evaluated for impairment	$ 94	$ 3	$ 5	$ 2	$ 104
Individually evaluated for impairment	2				2
Total allowance for loan losses at December 31, 2012	$ 96	$ 3	$ 5	$ 2	$ 106
Loans evaluated by impairment methodology(2):					
Collectively evaluated for impairment	$ 9,419	$ 7,618	$ 6,629	$ 326	$ 23,992
Individually evaluated for impairment	30		1		31
Total loan evaluated at December 31, 2012	$ 9,449	$ 7,618	$ 6,630	$ 326	$ 24,023
Allowance for lending-related commitments:					
Balance at December 31, 2011	$ 19	$ 3	$	$ 2	$ 24
Provision for lending-related commitments(3)(4)	9	(1)			8
Balance at June 30, 2012	$ 28	$ 2	$	$ 2	$ 32
Allowance for lending-related commitments by impairment methodology:					
Collectively evaluated for impairment	$ 86	$	$	$ 1	$ 87
Individually evaluated for impairment	4				4
Total allowance for lending-related commitments at December 31, 2012	$ 90	$	$	$ 1	$ 91
Lending-related commitments evaluated by impairment methodology:					
Collectively evaluated for impairment	$ 44,079	$ 1,406	$ 712	$ 101	$ 46,298
Individually evaluated for impairment	47				47

Total lending-related commitments evaluated at December 31, 2012	$ 44,126	$ 1,406	$ 712	$ 101	$ 46,345

(1) The Company records charges to the provisions for loan losses within Other revenues.
(2) Balances are gross of the allowance and represent recorded investment in the loans.
(3) The Company records charges to the provisions for lending-related commitments within Other non-interest expenses.
(4) The Company s provision for loan losses and provision for lending-related commitments for the quarter ended June 30, 2012 were $44 million and $12 million, respectively.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Employee Loans.

Employee loans are granted primarily in conjunction with a program established in the Wealth Management business segment to retain and recruit certain employees. These loans are recorded in Customer and other receivables in the condensed consolidated statements of financial condition. These loans are full recourse, generally require periodic payments and have repayment terms ranging from one to 12 years. The Company establishes a reserve for loan amounts it does not consider recoverable, which is recorded in Compensation and benefits expense. At June 30, 2013, the Company had $5,550 million of employee loans, net of an allowance of approximately $131 million. At December 31, 2012, the Company had $5,998 million of employee loans, net of an allowance of approximately $131 million.

The Company has also granted loans to other employees primarily in conjunction with certain after-tax leveraged investment arrangements. At June 30, 2013, the balance of these loans was $155 million, net of an allowance of approximately $103 million. At December 31, 2012, the balance of these loans was $172 million, net of an allowance of approximately $108 million. The Company establishes a reserve for non-recourse loan amounts not recoverable from employees, which is recorded in Other expense.

Collateralized Transactions.

In certain instances, the Company enters into reverse repurchase agreements and securities borrowed transactions to acquire securities to cover short positions, to settle other securities obligations and to accommodate customers needs. The Company also engages in securities financing transactions for customers through margin lending (see Note 6).

Servicing Advances.

As part of its servicing activities, the Company may make servicing advances to the extent that it believes that such advances will be reimbursed (see Note 7).

9. Goodwill and Net Intangible Assets.

The Company tests goodwill for impairment on an annual basis and on an interim basis when certain events or circumstances exist. The Company tests for impairment at the reporting unit level, which is generally at the level of or one level below its business segments. For both the annual and interim tests, the Company has the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If after assessing the totality of events or circumstances, the Company determines it is more likely than not that the fair value of a reporting unit is greater than its carrying amount, then performing the two-step impairment test is not required. However, if the Company concludes otherwise, then it is required to perform the first step of the two-step impairment test. Goodwill impairment is determined by comparing the estimated fair value of a reporting unit with its respective carrying value. If the estimated fair value exceeds the carrying value, goodwill at the reporting unit level is not deemed to be impaired. If the estimated fair value is below carrying value, however, further analysis is required to determine the amount of the impairment. Additionally, if the carrying value of a reporting unit is zero or a negative value and it is determined that it is more likely than not the goodwill is impaired, further analysis is required. The estimated fair values of the reporting units are derived based on valuation techniques the Company believes market participants would use for each of the reporting units.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The estimated fair values are generally determined utilizing methodologies that incorporate price-to-book and price-to-earnings multiples of certain comparable companies. The Company also utilizes a discounted cash flow methodology for certain reporting units.

The Company completed its annual goodwill impairment testing at July 1, 2012. The Company s testing did not indicate any goodwill impairment as each of the Company s reporting units with goodwill had a fair value that was substantially in excess of its carrying value. Adverse market or economic events could result in impairment charges in future periods. At December 31, 2012, each of the Company s reporting units with goodwill had a fair value that was substantially in excess of its carrying value.

Goodwill.

Changes in the carrying amount of the Company s goodwill, net of accumulated impairment losses for the six months ended June 30, 2013, were as follows:

	Institutional Securities(1)	Wealth Management(1)	Investment Management	Total
		(dollars in millions)		
Goodwill at December 31, 2012(2)	$ 337	$ 5,573	$ 740	$ 6,650
Foreign currency translation adjustments and other	(22)			(22)
Goodwill disposed of during the period(3)(4)	(17)	(11)		(28)
Goodwill at June 30, 2013(2)	$ 298	$ 5,562	$ 740	$ 6,600

(1) On January 1, 2013, the International Wealth Management business was transferred from the Wealth Management business segment to the Equity division within the Institutional Securities business segment. Accordingly, prior period amounts have been recast to reflect the International Wealth Management business as part of the Institutional Securities business segment.

(2) The amount of the Company s goodwill before accumulated impairments of $700 million, which included $673 million related to the Institutional Securities business segment and $27 million related to the Investment Management business segment, was $7,300 million and $7,350 million at June 30, 2013 and December 31, 2012, respectively.

(3) In 2011, the Company announced that it had reached an agreement with the employees of its in-house quantitative proprietary trading unit, Process Driven Trading (PDT), within the Institutional Securities business segment, whereby PDT employees will acquire certain assets from the Company and launch an independent advisory firm. This transaction closed on January 1, 2013.

(4) The Wealth Management business segment sold the U.K. operations of Global Stock Plan Services business to Computershare Limited. This transaction closed on May 31, 2013.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Net Intangible Assets.

Changes in the carrying amount of the Company s intangible assets for the six months ended June 30, 2013 were as follows:

	Institutional Securities	Wealth Management	Investment Management	Total
		(dollars in millions)		
Amortizable net intangible assets at December 31, 2012	$ 175	$ 3,600	$ 1	$ 3,776
Mortgage servicing rights (see Note 7)		7		7
Net intangible assets at December 31, 2012	$ 175	$ 3,607	$ 1	$ 3,783
Amortizable net intangible assets at December 31, 2012	$ 175	$ 3,600	$ 1	$ 3,776
Foreign currency translation adjustments and other	(4)			(4)
Amortization expense	(6)	(164)		(170)
Impairment losses(1)	(2)	(7)		(9)
Amortizable net intangible assets at June 30, 2013	163	3,429	1	3,593
Mortgage servicing rights (see Note 7)		9		9
Net intangible assets at June 30, 2013	$ 163	$ 3,438	$ 1	$ 3,602

(1) Impairment losses are recorded within Other expenses.

10. Long-Term Borrowings and Other Secured Financings.

The Company s long-term borrowings included the following components:

	At June 30, 2013	At December 31, 2012
	(dollars in millions)	
Senior debt	$ 148,763	$ 158,899
Subordinated debt	7,510	5,845
Junior subordinated debentures	4,825	4,827
Total	$ 161,098	$ 169,571

During the six months ended June 30, 2013, the Company issued and reissued notes with a principal amount of approximately $22 billion. This amount included the Company s issuances of $2.0 billion in 10 year subordinated debt on May 21, 2013, $3.7 billion in senior unsecured debt on April 25, 2013 and $4.5 billion in senior unsecured debt on February 25, 2013. During the six months ended June 30, 2013, approximately $23 billion in aggregate long-term borrowings matured or were retired.

The weighted average maturity of the Company s long-term borrowings, based upon stated maturity dates, was approximately 5.4 years and 5.3 years at June 30, 2013 and December 31, 2012, respectively.

Other Secured Financings.

Other secured financings include the liabilities related to transfers of financial assets that are accounted for as financings rather than sales, consolidated VIEs where the Company is deemed to be the primary beneficiary, pledged commodities, certain equity-linked notes and other secured borrowings. See Note 7 for further information on other secured financings related to VIEs and securitization activities.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company s other secured financings consisted of the following:

	At June 30, 2013	At December 31, 2012
	(dollars in millions)	
Secured financings with original maturities greater than one year	$ 9,824	$ 14,431
Secured financings with original maturities one year or less	3,448	641
Failed sales(1)	399	655
Total(2)	$ 13,671	$ 15,727

(1) For more information on failed sales, see Note 7.
(2) Amounts include $6,452 million and $9,466 million at fair value at June 30, 2013 and December 31, 2012, respectively.

11. Derivative Instruments and Hedging Activities.
The Company trades, makes markets and takes proprietary positions globally in listed futures, OTC swaps, forwards, options and other derivatives referencing, among other things, interest rates, currencies, investment grade and non-investment grade corporate credits, loans, bonds, U.S. and other sovereign securities, emerging market bonds and loans, credit indices, asset-backed security indices, property indices, mortgage-related and other asset-backed securities, and real estate loan products. The Company uses these instruments for trading, foreign currency exposure management and asset and liability management.

The Company manages its trading positions by employing a variety of risk mitigation strategies. These strategies include diversification of risk exposures and hedging. Hedging activities consist of the purchase or sale of positions in related securities and financial instruments, including a variety of derivative products (*e.g.*, futures, forwards, swaps and options). The Company manages the market risk associated with its trading activities on a Company-wide basis, on a worldwide trading division level and on an individual product basis.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In connection with its derivative activities, the Company generally enters into master netting agreements and collateral agreements with its counterparties. These agreements provide the Company with the right, in the event of a default by the counterparty (such as bankruptcy or a failure to pay or perform), to net a counterparty s rights and obligations under the agreement and to liquidate and setoff collateral against any net amount owed by the counterparty. However, in certain circumstances: the Company may not have such an agreement in place; the relevant insolvency regime (which is based on the type of counterparty entity and the jurisdiction of organization of the counterparty) may not support the enforceability of the agreement; or the Company may not have sought legal advice to support the enforceability of the agreement. In cases where the Company has not determined an agreement to be enforceable, the related amounts are not offset in the tabular disclosures. The Company s policy is generally to receive securities and cash posted as collateral (with rights of rehypothecation), irrespective of the enforceability determination regarding the master netting and collateral agreement. In certain cases the Company may agree for such collateral to be posted to a third party custodian under a control agreement that enables the Company to take control of such collateral in the event of a counterparty default. The enforceability of the master netting agreement is taken into account in the Company s risk management practices and application of counterparty credit limits. The following tables present information about the offsetting of derivative instruments and related collateral amounts. See information related to offsetting of certain collateralized transactions in Note 6.

	At June 30, 2013					
				Amounts Not Offset in the Condensed Consolidated Statements of Financial Condition(3)		
	Gross Amounts(1)	Amounts Offset in the Condensed Consolidated Statements of Financial Condition(2)	Net Amounts Presented in the Condensed Consolidated Statements of Financial Condition	Financial Instruments Collateral	Other Cash Collateral	Net Exposure
	(dollars in millions)					
Derivative assets						
Bilateral OTC	$ 486,776	$ (455,736)	$ 31,040	$ (7,335)	$ (107)	$ 23,598
Cleared OTC(4)	265,254	(264,443)	811			811
Exchange traded	32,850	(25,940)	6,910			6,910
Total derivative assets	$ 784,880	$ (746,119)	$ 38,761	$ (7,335)	$ (107)	$ 31,319
Derivative liabilities						
Bilateral OTC	$ 459,815	$ (429,459)	$ 30,356	$ (5,984)	$ (122)	$ 24,250
Cleared OTC(4)	267,009	(266,011)	998		(32)	966
Exchange traded	36,286	(25,940)	10,346	(2,525)		7,821
Total derivative liabilities	$ 763,110	$ (721,410)	$ 41,700	$ (8,509)	$ (154)	$ 33,037

(1) Amounts include $13.1 billion of derivative assets and $10.7 billion of derivative liabilities which are either not subject to master netting agreements or collateral agreements or are subject to such agreements but the Company has not determined the agreements to be legally enforceable. See also Fair Value and Notional of Derivative Instruments for additional disclosure about gross fair values and notionals for derivative instruments by risk type.
(2) Amounts relate to master netting agreements and collateral agreements which have been determined by the Company to be legally enforceable in the event of default and where certain other criteria are met in accordance with applicable offsetting accounting guidance.
(3) Amounts relate to master netting agreements and collateral agreements which have been determined by the Company to be legally enforceable in the event of default but where certain other criteria are not met in accordance with applicable offsetting accounting guidance.
(4) Includes OTC derivatives that are centrally cleared in accordance with certain regulatory requirements.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	At December 31, 2012					
				Amounts Not Offset in the Condensed Consolidated Statements of Financial Condition(3)		
	Gross Amounts(1)	Amounts Offset in the Condensed Consolidated Statements of Financial Condition(2)	Net Amounts Presented in the Condensed Consolidated Statements of Financial Condition	Financial Instruments Collateral	Other Cash Collateral	Net Exposure
	(dollars in millions)					
Derivative assets						
Bilateral OTC	$ 604,713	$ (573,844)	$ 30,869	$ (7,691)	$ (232)	$ 22,946
Cleared OTC(4)	375,233	(374,546)	687			687
Exchange traded	24,305	(19,664)	4,641			4,641
Total derivative assets	$ 1,004,251	$ (968,054)	$ 36,197	$ (7,691)	$ (232)	$ 28,274
Derivative Liabilities						
Bilateral OTC	$ 578,018	$ (547,285)	$ 30,733	$ (7,871)	$ (64)	$ 22,798
Cleared OTC(4)	374,960	(374,866)	94		(23)	71
Exchange traded	25,795	(19,664)	6,131	(1,028)		5,103
Total derivative liabilities	$ 978,773	$ (941,815)	$ 36,958	$ (8,899)	$ (87)	$ 27,972

(1) Amounts include $7.2 billion of derivative assets and $7.3 billion of derivative liabilities which are either not subject to master netting agreements or collateral agreements or are subject to such agreements but the Company has not determined the agreements to be legally enforceable. See also Fair Value and Notional of Derivative Instruments for additional disclosure about gross fair values and notionals for derivative instruments by risk type.

(2) Amounts relate to master netting agreements and collateral agreements which have been determined by the Company to be legally enforceable in the event of default and where certain other criteria are met in accordance with applicable offsetting accounting guidance.

(3) Amounts relate to master netting agreements and collateral agreements which have been determined by the Company to be legally enforceable in the event of default but where certain other criteria are not met in accordance with applicable offsetting accounting guidance.

(4) Includes OTC derivatives that are centrally cleared in accordance with certain regulatory requirements.

The Company incurs credit risk as a dealer in OTC derivatives. Credit risk with respect to derivative instruments arises from the failure of a counterparty to perform according to the terms of the contract. The Company s exposure to credit risk at any point in time is represented by the fair value of the derivative contracts reported as assets. The fair value of a derivative represents the amount at which the derivative could be exchanged in an orderly transaction between market participants and is further described in Note 2 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K and Note 4.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below present a summary by counterparty credit rating and remaining contract maturity of the fair value of OTC derivatives in a gain position at June 30, 2013 and December 31, 2012, respectively. Fair value is presented in the final column, net of collateral received (principally cash and U.S. government and agency securities):

OTC Derivative Products Trading Assets at June 30, 2013(1)

Credit Rating(2)	Years to Maturity: Less than 1	1-3	3-5	Over 5	Cross-Maturity and Cash Collateral Netting(3)	Net Exposure Post-Cash Collateral	Net Exposure Post-Collateral
	(dollars in millions)						
AAA	$ 428	$ 597	$ 1,429	$ 4,653	$ (4,570)	$ 2,537	$ 2,106
AA	3,311	1,846	1,976	9,579	(10,337)	6,375	4,417
A	10,049	9,456	11,120	23,417	(43,619)	10,423	8,858
BBB	3,216	3,665	3,176	15,686	(18,035)	7,708	6,040
Non-investment grade	2,270	2,823	1,298	3,241	(4,931)	4,701	2,988
Total	$ 19,274	$ 18,387	$ 18,999	$ 56,576	$ (81,492)	$ 31,744	$ 24,409

(1) Fair values shown represent the Company s net exposure to counterparties related to the Company s OTC derivative products. Amounts include centrally cleared OTC derivatives. The table does not include exchange-traded derivatives and the effect of any related hedges utilized by the Company.
(2) Obligor credit ratings are determined by the Company s Credit Risk Management Department.
(3) Amounts represent the netting of receivable balances with payable balances for the same counterparty across maturity categories. Receivable and payable balances with the same counterparty in the same maturity category are netted within such maturity category, where appropriate. Cash collateral received is netted on a counterparty basis, provided legal right of offset exists.

OTC Derivative Products Trading Assets at December 31, 2012(1)

Credit Rating(2)	Years to Maturity: Less than 1	1-3	3-5	Over 5	Cross-Maturity and Cash Collateral Netting(3)	Net Exposure Post-Cash Collateral	Net Exposure Post-Collateral
	(dollars in millions)						
AAA	$ 353	$ 551	$ 1,299	$ 6,121	$ (4,851)	$ 3,473	$ 3,088
AA	2,125	3,635	2,958	10,270	(12,761)	6,227	4,428
A	6,643	9,596	14,228	29,729	(50,722)	9,474	7,638
BBB	2,673	3,970	3,704	18,586	(21,713)	7,220	5,754
Non-investment grade	2,091	2,855	2,142	4,538	(6,696)	4,930	2,725
Total	$ 13,885	$ 20,607	$ 24,331	$ 69,244	$ (96,743)	$ 31,324	$ 23,633

(1) Fair values shown represent the Company s net exposure to counterparties related to the Company s OTC derivative products. Amounts include centrally cleared OTC derivatives. The table does not include exchange-traded derivatives and the effect of any related hedges utilized by the Company.
(2) Obligor credit ratings are determined by the Company s Credit Risk Management Department.
(3) Amounts represent the netting of receivable balances with payable balances for the same counterparty across maturity categories. Receivable and payable balances with the same counterparty in the same maturity category are netted within such maturity category, where appropriate. Cash collateral received is netted on a counterparty basis, provided legal right of offset exists.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Hedge Accounting.

The Company applies hedge accounting using various derivative financial instruments to hedge interest rate and foreign exchange risk arising from assets and liabilities not held at fair value as part of asset and liability management and foreign currency exposure management.

The Company s hedges are designated and qualify for accounting purposes as one of the following types of hedges: hedges of exposure to changes in fair value of assets and liabilities being hedged (fair value hedges) and hedges of net investments in foreign operations whose functional currency is different from the reporting currency of the parent company (net investment hedges).

For all hedges where hedge accounting is being applied, effectiveness testing and other procedures to ensure the ongoing validity of the hedges are performed at least monthly.

Fair Value Hedges Interest Rate Risk. The Company s designated fair value hedges consisted primarily of interest rate swaps designated as fair value hedges of changes in the benchmark interest rate of fixed rate senior long-term borrowings. The Company uses regression analysis to perform an ongoing prospective and retrospective assessment of the effectiveness of these hedging relationships (*i.e.*, the Company applies the long-haul method of hedge accounting). A hedging relationship is deemed effective if the fair values of the hedging instrument (derivative) and the hedged item (debt liability) change inversely within a range of 80% to 125%. The Company considers the impact of valuation adjustments related to the Company s own credit spreads and counterparty credit spreads to determine whether they would cause the hedging relationship to be ineffective.

For qualifying fair value hedges of benchmark interest rates, the changes in the fair value of the derivative and the changes in the fair value of the hedged liability provide offset of one another and, together with any resulting ineffectiveness, are recorded in Interest expense. When a derivative is de-designated as a hedge, any basis adjustment remaining on the hedged liability is amortized to Interest expense over the remaining life of the liability using the effective interest method.

Net Investment Hedges. The Company may utilize forward foreign exchange contracts to manage the currency exposure relating to its net investments in non-U.S. dollar functional currency operations. No hedge ineffectiveness is recognized in earnings since the notional amounts of the hedging instruments equal the portion of the investments being hedged and the currencies being exchanged are the functional currencies of the parent and investee. The gain or loss from revaluing hedges of net investments in foreign operations at the spot rate is deferred and reported within Accumulated other comprehensive income (loss) in Total Equity, net of tax effects. The forward points on the hedging instruments are recorded in Interest income.

The Company recognized an out of period pre-tax gain of approximately $300 million in the Institutional Securities business segment s Other sales and trading net revenues for the quarter ended June 30, 2012, related to the reversal of amounts recorded in cumulative other comprehensive income due to the incorrect application of hedge accounting on certain derivative contracts previously designated as net investment hedges of certain foreign, non-U.S. dollar denominated subsidiaries. This amount included a pre-tax gain of approximately $191 million related to the quarter ended March 31, 2012, with the remainder impacting prior periods. The Company evaluated the effects of the incorrect application of hedge accounting, both qualitatively and quantitatively, and concluded that it did not have a material impact on any prior annual or quarterly consolidated results. In addition, the Company recognized a partially offsetting pre-tax loss of approximately $224 million for the quarter ended June 30, 2012 resulting from fair value changes within the quarter of the related derivative positions not qualifying for net investment hedge accounting. Subsequent to the identification of the incorrect application of net investment hedge accounting, and during the quarter ended June 30, 2012, the Company appropriately redesignated the forward foreign exchange contracts and reapplied hedge accounting.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fair Value and Notional of Derivative Instruments. The following tables summarize the fair value of derivative instruments designated as accounting hedges and the fair value of derivative instruments not designated as accounting hedges by type of derivative contract and the platform on which these instruments are traded or cleared on a gross basis. Fair values of derivative contracts in an asset position are included in Trading assets and fair values of derivative contracts in a liability position are reflected in Trading liabilities in the condensed consolidated statements of financial condition (see Note 4):

	Derivative Assets At June 30, 2013							
	Fair Value				Notional			
	Bilateral OTC	Cleared OTC(2)	Exchange Traded	Total	Bilateral OTC	Cleared OTC(2)	Exchange Traded	Total
	(dollars in millions)							
Derivatives designated as hedging instruments:								
Interest rate contracts	$ 5,829	$ 149	$	$ 5,978	$ 63,071	$ 5,457	$	$ 68,528
Foreign exchange contracts	541			541	10,423	100		10,523
Total derivatives designated as hedging instruments	6,370	149		6,519	73,494	5,557		79,051
Derivatives not designated as hedges(1):								
Interest rate contracts	328,549	261,592	354	590,495	7,322,458	11,488,922	959,708	19,771,088
Credit contracts	51,546	3,395		54,941	1,562,941	228,753		1,791,694
Foreign exchange contracts	59,424	118	27	59,569	2,110,099	5,603	7,617	2,123,319
Equity contracts	24,174		27,697	51,871	314,370		461,446	775,816
Commodity contracts	16,524		4,772	21,296	203,156		174,677	377,833
Other	189			189	3,418			3,418
Total derivatives not designated as hedges	480,406	265,105	32,850	778,361	11,516,442	11,723,278	1,603,448	24,843,168
Total derivatives	$ 486,776	$ 265,254	$ 32,850	$ 784,880	$ 11,589,936	$ 11,728,835	$ 1,603,448	$ 24,922,219
Cash collateral netting	(59,341)	(1,424)		(60,765)				
Counterparty netting	(396,395)	(263,019)	(25,940)	(685,354)				
Total derivative assets	$ 31,040	$ 811	$ 6,910	$ 38,761	$ 11,589,936	$ 11,728,835	$ 1,603,448	$ 24,922,219

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Derivative Liabilities At June 30, 2013

	Fair Value				Notional			
	Bilateral OTC	Cleared OTC(2)	Exchange Traded	Total	Bilateral OTC	Cleared OTC(2)	Exchange Traded	Total
				(dollars in millions)				
Derivatives designated as hedging instruments:								
Interest rate contracts	$ 423	$ 449	$	$ 872	$ 3,004	$ 14,604	$	$ 17,608
Foreign exchange contracts	47	1		48	5,022	229		5,251
Total derivatives designated as hedging instruments	470	450		920	8,026	14,833		22,859
Derivatives not designated as hedges(1):								
Interest rate contracts	308,861	262,603	488	571,952	7,022,729	11,323,486	1,593,220	19,939,435
Credit contracts	48,247	3,874		52,121	1,436,811	223,801		1,660,612
Foreign exchange contracts	59,645	82	8	59,735	2,038,154	4,451	2,011	2,044,616
Equity contracts	27,059		30,478	57,537	320,717		456,502	777,219
Commodity contracts	15,349		5,312	20,661	185,304		147,719	333,023
Other	184			184	5,243			5,243
Total derivatives not designated as hedges	459,345	266,559	36,286	762,190	11,008,958	11,551,738	2,199,452	24,760,148
Total derivatives	$ 459,815	$ 267,009	$ 36,286	$ 763,110	$ 11,016,984	$ 11,566,571	$ 2,199,452	$ 24,783,007
Cash collateral netting	(33,064)	(2,992)		(36,056)				
Counterparty netting	(396,395)	(263,019)	(25,940)	(685,354)				
Total derivative liabilities	$ 30,356	$ 998	$ 10,346	$ 41,700	$ 11,016,984	$ 11,566,571	$ 2,199,452	$ 24,783,007

(1) Notional amounts include gross notionals related to open long and short futures contracts of $444 billion and $898 billion, respectively. The unsettled fair value on these futures contracts (excluded from the table above) of $505 million and $169 million is included in Customer and other receivables and Customer and other payables, respectively, on the condensed consolidated statements of financial condition.

(2) Includes OTC derivatives that are centrally cleared in accordance with certain regulatory requirements.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Derivative Assets At December 31, 2012							
	Fair Value				Notional			
	Bilateral OTC	Cleared OTC(2)	Exchange Traded	Total	Bilateral OTC	Cleared OTC(2)	Exchange Traded	Total
	(dollars in millions)							
Derivatives designated as hedging instruments:								
Interest rate contracts	$ 8,046	$ 301	$	$ 8,347	$ 66,916	$ 8,199	$	$ 75,115
Foreign exchange contracts	367			367	10,291			10,291
Total derivatives designated as hedging instruments	8,413	301		8,714	77,207	8,199		85,406
Derivatives not designated as hedges(1):								
Interest rate contracts	443,523	371,789	142	815,454	8,029,510	10,096,252	776,130	18,901,892
Credit contracts	65,168	3,099		68,267	1,734,907	197,879		1,932,786
Foreign exchange contracts	52,349	44	34	52,427	1,831,385	3,834	5,967	1,841,186
Equity contracts	19,916		18,684	38,600	258,484		329,216	587,700
Commodity contracts	15,201		5,445	20,646	164,842		176,714	341,556
Other	143			143	4,908			4,908
Total derivatives not designated as hedges	596,300	374,932	24,305	995,537	12,024,036	10,297,965	1,288,027	23,610,028
Total derivatives	$ 604,713	$ 375,233	$ 24,305	$ 1,004,251	$ 12,101,243	$ 10,306,164	$ 1,288,027	$ 23,695,434
Cash collateral netting	(68,024)	(1,224)		(69,248)				
Counterparty netting	(505,820)	(373,322)	(19,664)	(898,806)				
Total derivative assets	$ 30,869	$ 687	$ 4,641	$ 36,197	$ 12,101,243	$ 10,306,164	$ 1,288,027	$ 23,695,434

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Derivative Liabilities At December 31, 2012							
	Fair Value				Notional			
	Bilateral OTC	Cleared OTC(2)	Exchange Traded	Total	Bilateral OTC	Cleared OTC(2)	Exchange Traded	Total
	(dollars in millions)							
Derivatives designated as hedging instruments:								
Interest rate contracts	$ 167	$ 1	$	$ 168	$ 2,000	$ 660	$	$ 2,660
Foreign exchange contracts	319			319	17,156			17,156
Total derivatives designated as hedging instruments	486	1		487	19,156	660		19,816
Derivatives not designated as hedges(1):								
Interest rate contracts	422,864	370,856	216	793,936	7,726,241	9,945,979	1,994,947	19,667,167
Credit contracts	60,420	4,074		64,494	1,645,464	222,343		1,867,807
Foreign exchange contracts	56,062	29	3	56,094	1,878,597	3,473	4,003	1,886,073
Equity contracts	22,239		19,631	41,870	257,340		329,858	587,198
Commodity contracts	15,886		5,945	21,831	169,189		155,912	325,101
Other	61			61	5,161			5,161
Total derivatives not designated as hedges	577,532	374,959	25,795	978,286	11,681,992	10,171,795	2,484,720	24,338,507
Total derivatives	$ 578,018	$ 374,960	$ 25,795	$ 978,773	$ 11,701,148	$ 10,172,455	$ 2,484,720	$ 24,358,323
Cash collateral netting	(41,465)	(1,544)		(43,009)				
Counterparty netting	(505,820)	(373,322)	(19,664)	(898,806)				
Total derivative liabilities	$ 30,733	$ 94	$ 6,131	$ 36,958	$ 11,701,148	$ 10,172,455	$ 2,484,720	$ 24,358,323

(1) Notional amounts include gross notionals related to open long and short futures contracts of $368 billion and $1,476 billion, respectively. The unsettled fair value on these futures contracts (excluded from the table above) of $1,073 million and $24 million is included in Customer and other receivables and Customer and other payables, respectively, on the condensed consolidated statements of financial condition.

(2) Includes OTC derivatives that are centrally cleared in accordance with certain regulatory requirements.

The following tables summarize the gains or losses reported on derivative instruments designated and qualifying as accounting hedges for the quarters and six months ended June 30, 2013 and 2012, respectively.

Derivatives Designated as Fair Value Hedges.

The following table presents gains (losses) reported on derivative instruments and the related hedge item as well as the hedge ineffectiveness included in Interest expense in the condensed consolidated statements of income from interest rate contracts:

	Gains (Losses) Recognized			
	Three Months Ended June 30,		Six Months Ended June 30,	
Product Type	2013	2012	2013	2012
	(dollars in millions)			

Derivatives	$ (2,247)	$ 979	$ (3,119)	$ 432
Borrowings	2,629	(753)	3,791	(54)
Total	$ 382	$ 226	$ 672	$ 378

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Derivatives Designated as Net Investment Hedges.

Product Type	Gains Recognized in OCI (effective portion) Three Months Ended June 30, 2013	2012(1)	Six Months Ended June 30, 2013	2012(1)
	(dollars in millions)			
Foreign exchange contracts(2)	$ 230	$ 130	$ 539	$ 150
Total	$ 230	$ 130	$ 539	$ 150

(1) A gain of $193 million, net of tax, related to net investment hedges was reclassified from other comprehensive income into income during both the quarter and six months ended June 30, 2012. The amount primarily related to an out of period gain, net of tax, related to the reversal of amounts recorded in cumulative other comprehensive income due to the incorrect application of hedge accounting on certain derivative contracts (see above for further information).

(2) Losses of $36 million and $68 million were recognized in income related to amounts excluded from hedge effectiveness testing during the quarter and six months ended June 30, 2013, respectively. Losses of $63 million and $128 million were recognized in income related to amounts excluded from hedge effectiveness testing during the quarter and six months ended June 30, 2012, respectively.

The table below summarizes gains (losses) on derivative instruments not designated as accounting hedges for the quarters and six months ended June 30, 2013 and 2012, respectively:

Product Type	Gains (Losses) Recognized in Income(1)(2) Three Months Ended June 30, 2013	2012	Six Months Ended June 30, 2013	2012
	(dollars in millions)			
Interest rate contracts	$ (65)	$ (594)	$ 75	$ 961
Credit contracts	253	1,293	174	621
Foreign exchange contracts	1,485	(208)	2,036	427
Equity contracts	(301)	188	(3,361)	(628)
Commodity contracts	880	908	1,303	302
Other contracts	(42)	(32)	(44)	24
Total derivative instruments	$ 2,210	$ 1,555	$ 183	$ 1,707

(1) Gains (losses) on derivative contracts not designated as hedges are primarily included in Trading in the condensed consolidated statements of income.

(2) Gains (losses) associated with certain derivative contracts that have physically settled are excluded from the table above. Gains (losses) on these contracts are reflected with the associated cash instruments, which are also included in Trading in the condensed consolidated statements of income.

The Company also has certain embedded derivatives that have been bifurcated from the related structured borrowings. Such derivatives are classified in Long-term borrowings and had a net fair value of $59 million and $53 million at June 30, 2013 and December 31, 2012, respectively and a notional value of $2,143 million and $2,178 million at June 30, 2013 and December 31, 2012, respectively. The Company recognized gains of $2 million and losses of less than $1 million related to changes in the fair value of its bifurcated embedded derivatives for the quarter and six months ended June 30, 2013, respectively. The Company recognized losses of $13 million and $6 million related to changes in the fair value of its bifurcated embedded derivatives for the quarter and six months ended June 30, 2012, respectively.

At June 30, 2013 and December 31, 2012, the amount of payables associated with cash collateral received that was netted against derivative assets was $60.8 billion and $69.2 billion, respectively, and the amount of receivables in respect of cash collateral paid that was netted against derivative liabilities was $36.1 billion and

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

$43.0 billion, respectively. Cash collateral receivables and payables of $83 million and $50 million, respectively, at June 30, 2013 and $158 million and $34 million, respectively, at December 31, 2012, were not offset against certain contracts that did not meet the definition of a derivative.

Credit-Risk-Related Contingencies.

In connection with certain OTC trading agreements, the Company may be required to provide additional collateral or immediately settle any outstanding liability balances with certain counterparties in the event of a credit ratings downgrade. At June 30, 2013, the aggregate fair value of OTC derivative contracts that contain credit-risk-related contingent features that are in a net liability position totaled $25,020 million, for which the Company has posted collateral of $20,941 million, in the normal course of business. The long-term credit ratings on the Company by Moody s Investor Services, Inc. (Moody s) and Standard & Poor s Ratings Services (S&P) are currently at different levels (commonly referred to as split ratings). At June 30, 2013, the future potential collateral amounts, termination payments or other contractual amounts that could be called by counterparties in the event of a downgrade of the Company s long-term credit rating under various scenarios are: $334 million (Baa1 Moody s/BBB+ S&P) and $1,853 million (Baa2 Moody s/BBB S&P). Of these amounts, $1,646 million at June 30, 2013 related to bilateral arrangements between the Company and other parties where upon the downgrade of one party, the downgraded party must deliver collateral to the other party. These bilateral downgrade arrangements are a risk management tool used extensively by the Company as credit exposures are reduced if counterparties are downgraded.

Credit Derivatives and Other Credit Contracts.

The Company enters into credit derivatives, principally through credit default swaps, under which it receives or provides protection against the risk of default on a set of debt obligations issued by a specified reference entity or entities. A majority of the Company s counterparties are banks, broker-dealers, insurance and other financial institutions, and monoline insurers.

The tables below summarize the notional and fair value of protection sold and protection purchased through credit default swaps at June 30, 2013 and December 31, 2012:

	At June 30, 2013 Maximum Potential Payout/Notional			
	Protection Sold		Protection Purchased	
	Notional	Fair Value (Asset)/Liability	Notional	Fair Value (Asset)/Liability
	(dollars in millions)			
Single name credit default swaps	$ 961,737	$ (510)	$ 911,921	$ 412
Index and basket credit default swaps	547,491	4,326	442,342	(4,372)
Tranched index and basket credit default swaps	227,578	484	361,237	(3,160)
Total	$ 1,736,806	$ 4,300	$ 1,715,500	$ (7,120)

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	At December 31, 2012 Maximum Potential Payout/Notional			
	Protection Sold		Protection Purchased	
	Notional	Fair Value (Asset)/Liability	Notional	Fair Value (Asset)/Liability
	(dollars in millions)			
Single name credit default swaps	$ 1,069,474	$ 2,889	$ 1,029,543	$ (2,456)
Index and basket credit default swaps	551,630	5,664	454,800	(5,124)
Tranched index and basket credit default swaps	272,088	2,330	423,058	(7,076)
Total	$ 1,893,192	$ 10,883	$ 1,907,401	$ (14,656)

The table below summarizes the credit ratings and maturities of protection sold through credit default swaps and other credit contracts at June 30, 2013:

	Protection Sold Maximum Potential Payout/Notional Years to Maturity					Fair Value
Credit Ratings of the Reference Obligation	Less than 1	1-3	3-5	Over 5	Total	(Asset)/ Liability(1)(2)
	(dollars in millions)					
Single name credit default swaps:						
AAA	$ 1,724	$ 7,207	$ 16,735	$ 3,431	$ 29,097	$ (102)
AA	10,144	20,833	36,277	6,202	73,456	(498)
A	64,925	59,232	62,823	7,894	194,874	(2,297)
BBB	124,739	122,540	143,344	27,058	417,681	365
Non-investment grade	76,203	80,765	78,149	11,512	246,629	2,022
Total	277,735	290,577	337,328	56,097	961,737	(510)
Index and basket credit default swaps(3):						
AAA	24,815	49,440	52,666	2,458	129,379	(1,245)
AA	900	10,854	13,289	6,468	31,511	(43)
A	2,687	5,338	23,883	25	31,933	536
BBB	26,673	120,435	156,532	8,912	312,552	(1,028)
Non-investment grade	59,084	61,371	136,216	13,023	269,694	6,590
Total	114,159	247,438	382,586	30,886	775,069	4,810
Total credit default swaps sold	$ 391,894	$ 538,015	$ 719,914	$ 86,983	$ 1,736,806	$ 4,300
Other credit contracts(4)(5)	$ 354	$ 44	$ 137	$ 1,181	$ 1,716	$ (390)
Total credit derivatives and other credit contracts	$ 392,248	$ 538,059	$ 720,051	$ 88,164	$ 1,738,522	$ 3,910

(1) Fair value amounts are shown on a gross basis prior to cash collateral or counterparty netting.

(2) Fair value amounts of certain credit default swaps where the Company sold protection have an asset carrying value because credit spreads of the underlying reference entity or entities tightened during the terms of the contracts.
(3) Credit ratings are calculated internally.
(4) Other credit contracts include CLNs, CDOs and credit default swaps that are considered hybrid instruments.
(5) Fair value amount shown represents the fair value of the hybrid instruments.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The table below summarizes the credit ratings and maturities of protection sold through credit default swaps and other credit contracts at December 31, 2012:

Credit Ratings of the Reference Obligation	Protection Sold Maximum Potential Payout/Notional Years to Maturity (dollars in millions) Less than 1	1-3	3-5	Over 5	Total	Fair Value (Asset)/ Liability(1)(2)
Single name credit default swaps:						
AAA	$ 2,368	$ 6,592	$ 19,848	$ 5,767	$ 34,575	$ (204)
AA	10,984	16,804	34,280	7,193	69,261	(325)
A	66,635	72,796	67,285	10,760	217,476	(2,740)
BBB	124,662	145,462	142,714	34,396	447,234	(492)
Non-investment grade	91,743	98,515	92,143	18,527	300,928	6,650
Total	296,392	340,169	356,270	76,643	1,069,474	2,889
Index and basket credit default swaps(3):						
AAA	18,652	36,005	45,789	3,240	103,686	(1,377)
AA	1,255	9,479	12,026	8,343	31,103	(55)
A	2,684	5,423	5,440	125	13,672	(155)
BBB	27,720	105,870	143,562	29,101	306,253	(862)
Non-investment grade	97,389	86,703	153,858	31,054	369,004	10,443
Total	147,700	243,480	360,675	71,863	823,718	7,994
Total credit default swaps sold	$ 444,092	$ 583,649	$ 716,945	$ 148,506	$ 1,893,192	$ 10,883
Other credit contracts(4)(5)	$ 796	$ 125	$ 155	$ 1,323	$ 2,399	$ (745)
Total credit derivatives and other credit contracts	$ 444,888	$ 583,774	$ 717,100	$ 149,829	$ 1,895,591	$ 10,138

(1) Fair value amounts are shown on a gross basis prior to cash collateral or counterparty netting.
(2) Fair value amounts of certain credit default swaps where the Company sold protection have an asset carrying value because credit spreads of the underlying reference entity or entities tightened during the terms of the contracts.
(3) Credit ratings are calculated internally.
(4) Other credit contracts include CLNs, CDOs and credit default swaps that are considered hybrid instruments.
(5) Fair value amount shown represents the fair value of the hybrid instruments.

Single Name Credit Default Swaps. A credit default swap protects the buyer against the loss of principal on a bond or loan in case of a default by the issuer. The protection buyer pays a periodic premium (generally quarterly) over the life of the contract and is protected for the period. The Company in turn will have to perform under a credit default swap if a credit event as defined under the contract occurs. Typical credit events include bankruptcy, dissolution or insolvency of the referenced entity, failure to pay and restructuring of the obligations of the referenced entity. In order to provide an indication of the current payment status or performance risk of the credit default swaps, the external credit ratings of the underlying reference entity of the credit default swaps are disclosed.

Index and Basket Credit Default Swaps. Index and basket credit default swaps are credit default swaps that reference multiple names through underlying baskets or portfolios of single name credit default swaps. Generally, in the event of a default on one of the underlying names, the Company will have to pay a pro rata portion of the total notional amount of the credit default index or basket contract. In order to provide an

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

indication of the current payment status or performance risk of these credit default swaps, the weighted average external credit ratings of the underlying reference entities comprising the basket or index were calculated and disclosed.

The Company also enters into index and basket credit default swaps where the credit protection provided is based upon the application of tranching techniques. In tranched transactions, the credit risk of an index or basket is separated into various portions of the capital structure, with different levels of subordination. The most junior tranches cover initial defaults, and once losses exceed the notional of the tranche, they are passed on to the next most senior tranche in the capital structure.

When external credit ratings are not available, credit ratings were determined based upon an internal methodology.

Credit Protection Sold through CLNs and CDOs. The Company has invested in CLNs and CDOs, which are hybrid instruments containing embedded derivatives, in which credit protection has been sold to the issuer of the note. If there is a credit event of a reference entity underlying the instrument, the principal balance of the note may not be repaid in full to the Company.

Purchased Credit Protection with Identical Underlying Reference Obligations. For single name credit default swaps and non-tranched index and basket credit default swaps, the Company has purchased protection with a notional amount of approximately $1.3 trillion and $1.5 trillion at June 30, 2013 and December 31, 2012, respectively, compared with a notional amount of approximately $1.5 trillion and $1.6 trillion at June 30, 2013 and December 31, 2012, of credit protection sold with identical underlying reference obligations. In order to identify purchased protection with the same underlying reference obligations, the notional amount for individual reference obligations within non-tranched indices and baskets was determined on a pro rata basis and matched off against single name and non-tranched index and basket credit default swaps where credit protection was sold with identical underlying reference obligations.

The purchase of credit protection does not represent the sole manner in which the Company risk manages its exposure to credit derivatives. The Company manages its exposure to these derivative contracts through a variety of risk mitigation strategies, which include managing the credit and correlation risk across single name, non-tranched indices and baskets, tranched indices and baskets, and cash positions. Aggregate market risk limits have been established for credit derivatives, and market risk measures are routinely monitored against these limits. The Company may also recover amounts on the underlying reference obligation delivered to the Company under credit default swaps where credit protection was sold.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

12. Commitments, Guarantees and Contingencies.

Commitments.

The Company s commitments associated with outstanding letters of credit and other financial guarantees obtained to satisfy collateral requirements, investment activities, corporate lending and financing arrangements, mortgage lending and margin lending at June 30, 2013 are summarized below by period of expiration. Since commitments associated with these instruments may expire unused, the amounts shown do not necessarily reflect the actual future cash funding requirements:

	Years to Maturity				
	Less than 1	1-3	3-5	Over 5	Total at June 30, 2013
	(dollars in millions)				
Letters of credit and other financial guarantees obtained to satisfy collateral requirements	$ 953	$ 14	$	$ 1	$ 968
Investment activities	729	104	36	270	1,139
Primary lending commitments investment grade(1)	8,020	15,798	34,344	562	58,724
Primary lending commitments non-investment grade(1)	3,053	4,882	9,381	3,841	21,157
Secondary lending commitments(2)	38	31	20	21	110
Commitments for secured lending transactions	636	14	15		665
Forward starting reverse repurchase agreements and securities borrowing agreements(3)(4)	46,549				46,549
Commercial and residential mortgage-related commitments	2,088	30	332	283	2,733
Other commitments	2,237	350	153	111	2,851
Total	$ 64,303	$ 21,223	$ 44,281	$ 5,089	$ 134,896

(1) This amount includes $41.8 billion of investment grade and $9.5 billion of non-investment grade unfunded commitments accounted for as held for investment and $4.9 billion of investment grade and $7.4 billion of non-investment grade unfunded commitments accounted for as held for sale at June 30, 2013. The remainder of these lending commitments is carried at fair value.

(2) These commitments are recorded at fair value within Trading assets and Trading liabilities in the condensed consolidated statements of financial condition (see Note 4).

(3) The Company enters into forward starting reverse repurchase and securities borrowing agreements (agreements that have a trade date at or prior to June 30, 2013 and settle subsequent to period-end) that are primarily secured by collateral from U.S. government agency securities and other sovereign government obligations. These agreements primarily settle within three business days and of the total amount at June 30, 2013, $41.8 billion settled within three business days.

(4) The Company also has a contingent obligation to provide financing to a clearinghouse through which it clears certain transactions. The financing is required only upon the default of a clearinghouse member. The financing takes the form of a reverse repurchase facility, with a maximum amount of approximately $1.9 billion.

For further description of these commitments, refer to Note 13 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K.

The Company sponsors several non-consolidated investment funds for third-party investors where the Company typically acts as general partner of, and investment advisor to, these funds and typically commits to invest a minority of the capital of such funds, with subscribing third-party investors contributing the majority. The Company s employees, including its senior officers, as well as the Company s directors, may participate on the same terms and conditions as other investors in certain of these funds that the Company forms primarily for client investment, except that the Company may waive or lower applicable fees and charges for its employees. The Company has contractual capital commitments, guarantees, lending facilities and counterparty arrangements with respect to these investment funds.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Guarantees.

The table below summarizes certain information regarding the Company s obligations under guarantee arrangements at June 30, 2013:

Type of Guarantee	Maximum Potential Payout/Notional Years to Maturity Less than 1	1-3	3-5	Over 5	Total	Carrying Amount (Asset)/ Liability	Collateral/ Recourse
	(dollars in millions)						
Credit derivative contracts(1)	$ 391,894	$ 538,015	$ 719,914	$ 86,983	$ 1,736,806	$ 4,300	$
Other credit contracts	354	44	137	1,181	1,716	(390)	
Non-credit derivative contracts(1)	1,590,165	790,479	344,366	512,286	3,237,296	74,327	
Standby letters of credit and other financial guarantees issued(2)(3)	1,211	771	1,178	5,642	8,802	(206)	7,150
Market value guarantees		73	154	492	719	9	106
Liquidity facilities	2,206	148			2,354	(4)	3,327
Whole loan sales representations and warranties				23,873	23,873	80	
Securitization representations and warranties				69,907	69,907	64	
General partner guarantees	73	45	57	185	360	74	

(1) Carrying amounts of derivative contracts are shown on a gross basis prior to cash collateral or counterparty netting. For further information on derivative contracts, see Note 11.
(2) Approximately $2.0 billion of standby letters of credit are also reflected in the Commitments table above in primary and secondary lending commitments. Standby letters of credit are recorded at fair value within Trading assets or Trading liabilities in the condensed consolidated statements of financial condition.
(3) Amounts include guarantees issued by consolidated real estate funds sponsored by the Company of approximately $28.4 million. These guarantees relate to obligations of the fund s investee entities, including guarantees related to capital expenditures and principal and interest debt payments. Accrued losses under these guarantees of approximately $3.9 million are reflected as a reduction of the carrying value of the related fund investments, which are reflected in Trading assets on the condensed consolidated statement of financial condition.

For further description of these guarantees, refer to Note 13 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K.

The Company has obligations under certain guarantee arrangements, including contracts and indemnification agreements that contingently require a guarantor to make payments to the guaranteed party based on changes in an underlying measure (such as an interest or foreign exchange rate, security or commodity price, an index or the occurrence or non-occurrence of a specified event) related to an asset, liability or equity security of a guaranteed party. Also included as guarantees are contracts that contingently require the guarantor to make payments to the guaranteed party based on another entity s failure to perform under an agreement, as well as indirect guarantees of the indebtedness of others. The Company s use of guarantees is described below by type of guarantee:

Other Guarantees and Indemnities.

In the normal course of business, the Company provides guarantees and indemnifications in a variety of commercial transactions. These provisions generally are standard contractual terms. Certain of these guarantees and indemnifications are described below.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Trust Preferred Securities. The Company has established Morgan Stanley Capital Trusts for the limited purpose of issuing trust preferred securities to third parties and lending the proceeds to the Company in exchange for junior subordinated debentures. The Company has directly guaranteed the repayment of the trust preferred securities to the holders thereof to the extent that the Company has made payments to a Morgan Stanley Capital Trust on the junior subordinated debentures. In the event that the Company does not make payments to a Morgan Stanley Capital Trust, holders of such series of trust preferred securities would not be able to rely upon the guarantee for payment of those amounts. The Company has not recorded any liability in the condensed consolidated financial statements for these guarantees and believes that the occurrence of any events (*i.e.*, non-performance on the part of the paying agent) that would trigger payments under these contracts is remote. See Note 11 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K for details on the Company s junior subordinated debentures.

Indemnities. The Company provides standard indemnities to counterparties for certain contingent exposures and taxes, including U.S. and foreign withholding taxes, on interest and other payments made on derivatives, securities and stock lending transactions, certain annuity products and other financial arrangements. These indemnity payments could be required based on a change in the tax laws or change in interpretation of applicable tax rulings or a change in factual circumstances. Certain contracts contain provisions that enable the Company to terminate the agreement upon the occurrence of such events. The maximum potential amount of future payments that the Company could be required to make under these indemnifications cannot be estimated.

Exchange/Clearinghouse Member Guarantees. The Company is a member of various U.S. and non-U.S. exchanges and clearinghouses that trade and clear securities and/or derivative contracts. Associated with its membership, the Company may be required to pay a proportionate share of the financial obligations of another member who may default on its obligations to the exchange or the clearinghouse. While the rules governing different exchange or clearinghouse memberships vary, in general the Company s guarantee obligations would arise only if the exchange or clearinghouse had previously exhausted its resources. The maximum potential payout under these membership agreements cannot be estimated. The Company has not recorded any contingent liability in the condensed consolidated financial statements for these agreements and believes that any potential requirement to make payments under these agreements is remote.

Merger and Acquisition Guarantees. The Company may, from time to time, in its role as investment banking advisor be required to provide guarantees in connection with certain European merger and acquisition transactions. If required by the regulating authorities, the Company provides a guarantee that the acquirer in the merger and acquisition transaction has or will have sufficient funds to complete the transaction and would then be required to make the acquisition payments in the event the acquirer s funds are insufficient at the completion date of the transaction. These arrangements generally cover the time frame from the transaction offer date to its closing date and, therefore, are generally short term in nature. The maximum potential amount of future payments that the Company could be required to make cannot be estimated. The Company believes the likelihood of any payment by the Company under these arrangements is remote given the level of the Company s due diligence associated with its role as investment banking advisor.

In the ordinary course of business, the Company guarantees the debt and/or certain trading obligations (including obligations associated with derivatives, foreign exchange contracts and the settlement of physical commodities) of certain subsidiaries. These guarantees generally are entity or product specific and are required by investors or trading counterparties. The activities of the subsidiaries covered by these guarantees (including any related debt or trading obligations) are included in the Company s condensed consolidated financial statements.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Contingencies.

Legal. In the normal course of business, the Company has been named, from time to time, as a defendant in various legal actions, including arbitrations, class actions and other litigation, arising in connection with its activities as a global diversified financial services institution. Certain of the actual or threatened legal actions include claims for substantial compensatory and/or punitive damages or claims for indeterminate amounts of damages. In some cases, the entities that would otherwise be the primary defendants in such cases are bankrupt or are in financial distress. These actions have included, but are not limited to, residential mortgage and credit crisis related matters. Over the last several years, the level of litigation and investigatory activity focused on residential mortgage and credit crisis related matters has increased materially in the financial services industry. As a result, the Company expects that it may become the subject of increased claims for damages and other relief regarding residential mortgages and related securities in the future and, while the Company has identified below any individual proceedings where the Company believes a material loss to be reasonably possible and reasonably estimable, there can be no assurance that material losses will not be incurred from claims that have not yet been notified to the Company or are not yet determined to be probable or possible and reasonably estimable losses.

The Company is also involved, from time to time, in other reviews, investigations and proceedings (both formal and informal) by governmental and self-regulatory agencies regarding the Company s business and involving, among other matters, accounting and operational matters, certain of which may result in adverse judgments, settlements, fines, penalties, injunctions or other relief.

The Company contests liability and/or the amount of damages as appropriate in each pending matter. Where available information indicates that it is probable a liability had been incurred at the date of the condensed consolidated financial statements and the Company can reasonably estimate the amount of that loss, the Company accrues the estimated loss by a charge to income. In many proceedings, however, it is inherently difficult to determine whether any loss is probable or even possible or to estimate the amount of any loss. In addition, even where loss is possible or an exposure to loss exists in excess of the liability already accrued with respect to a previously recognized loss contingency, it is not always possible to reasonably estimate the size of the possible loss or range of loss.

For certain legal proceedings, the Company cannot reasonably estimate such losses, particularly for proceedings that are in their early stages of development or where plaintiffs seek substantial or indeterminate damages. Numerous issues may need to be resolved, including through potentially lengthy discovery and determination of important factual matters, determination of issues related to class certification and the calculation of damages, and by addressing novel or unsettled legal questions relevant to the proceedings in question, before a loss or additional loss or range of loss or additional loss can be reasonably estimated for any proceeding.

For certain other legal proceedings, the Company can estimate reasonably possible losses, additional losses, ranges of loss or ranges of additional loss in excess of amounts accrued, but does not believe, based on current knowledge and after consultation with counsel, that such losses will have a material adverse effect on the Company s condensed consolidated financial statements as a whole, other than the matters referred to in the following paragraphs.

On March 15, 2010, the Federal Home Loan Bank of San Francisco filed two complaints against the Company and other defendants in the Superior Court of the State of California. These actions are styled *Federal Home Loan Bank of San Francisco v. Credit Suisse Securities (USA) LLC, et al.*, and *Federal Home Loan Bank of San Francisco v. Deutsche Bank Securities Inc. et al.*, respectively. Amended complaints filed on June 10, 2010 allege that defendants made untrue statements and material omissions in connection with the sale to plaintiff of a number of mortgage pass-through certificates backed by securitization trusts containing residential mortgage

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

loans. The amount of certificates allegedly sold to plaintiff by the Company in these cases was approximately $704 million and $276 million, respectively. The complaints raise claims under both the federal securities laws and California law and seek, among other things, to rescind the plaintiff s purchase of such certificates. On July 29, 2011 and September 8, 2011, the court presiding over both actions sustained defendants demurrers with respect to claims brought under the Securities Act of 1933, as amended, and overruled defendants demurrers with respect to all other claims. At June 25, 2013, the current unpaid balance of the mortgage pass-through certificates at issue in these cases was approximately $345 million, and the certificates had incurred actual losses of approximately $2.8 million. Based on currently available information, the Company believes it could incur a loss for this action up to the difference between the $345 million unpaid balance of these certificates (plus any losses incurred) and their fair market value at the time of a judgment against the Company, plus pre- and post-judgment interest, fees and costs. The Company may be entitled to be indemnified for some of these losses and to an offset for interest received by the plaintiff prior to a judgment.

On July 9, 2010 and February 11, 2011, Cambridge Place Investment Management Inc. filed two separate complaints against the Company and other defendants in the Superior Court of the Commonwealth of Massachusetts, both styled *Cambridge Place Investment Management Inc. v. Morgan Stanley & Co., Inc., et al.* The complaints assert claims on behalf of certain clients of plaintiff s affiliates and allege that defendants made untrue statements and material omissions in the sale of a number of mortgage pass-through certificates backed by securitization trusts containing residential mortgage loans. The total amount of certificates allegedly issued by the Company or sold to plaintiff s affiliates clients by the Company in the two matters was approximately $263 million. Plaintiff filed amended complaints on October 14, 2011, which raise claims under the Massachusetts Uniform Securities Act and seek, among other things, to rescind the plaintiff s purchase of such certificates. On November 22, 2011, defendants filed a motion to dismiss the amended complaints. On March 12, 2012, the court denied defendants motion to dismiss with respect to plaintiff s standing to bring suit. Defendants sought interlocutory appeal from that decision on April 11, 2012. On April 26, 2012, defendants filed a second motion to dismiss for failure to state a claim upon which relief can be granted, which the court denied, in substantial part, on October 2, 2012. At June 25, 2013, the current unpaid balance of the mortgage pass-through certificates at issue in these cases was approximately $216 million, and the certificates had incurred actual losses of approximately $109 million. Based on currently available information, the Company believes it could incur a loss for these actions of up to the difference between the $216 million unpaid balance of these certificates (plus any losses incurred) and their fair market value at the time of a judgment against the Company, plus pre- and post-judgment interest, fees and costs. The Company may be entitled to be indemnified for some of these losses and to an offset for interest received by the plaintiff prior to a judgment.

On July 15, 2010, China Development Industrial Bank (CDIB) filed a complaint against the Company, styled *China Development Industrial Bank v. Morgan Stanley & Co. Incorporated et al.* and is pending in the Supreme Court of the State of New York, New York County (Supreme Court of NY). The complaint relates to a $275 million credit default swap referencing the super senior portion of the STACK 2006-1 CDO. The complaint asserts claims for common law fraud, fraudulent inducement and fraudulent concealment and alleges that the Company misrepresented the risks of the STACK 2006-1 CDO to CDIB, and that the Company knew that the assets backing the CDO were of poor quality when it entered into the credit default swap with CDIB. The complaint seeks compensatory damages related to the approximately $228 million that CDIB alleges it has already lost under the credit default swap, rescission of CDIB s obligation to pay an additional $12 million, punitive damages, equitable relief, fees and costs. On February 28, 2011, the court denied the Company s motion to dismiss the complaint. Based on currently available information, the Company believes it could incur a loss of up to approximately $240 million plus pre- and post-judgment interest, fees and costs.

On October 15, 2010, the Federal Home Loan Bank of Chicago filed a complaint against the Company and other defendants in the Circuit Court of the State of Illinois styled *Federal Home Loan Bank of Chicago v. Bank of*

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

America Funding Corporation et al. The complaint alleges that defendants made untrue statements and material omissions in the sale to plaintiff of a number of mortgage pass-through certificates backed by securitization trusts containing residential mortgage loans. The total amount of certificates allegedly sold to plaintiff by the Company in this action was approximately $203 million. The complaint raises claims under Illinois law and seeks, among other things, to rescind the plaintiff s purchase of such certificates. On March 24, 2011, the court granted plaintiff leave to file an amended complaint. The defendants motion to dismiss the amended complaint was denied on September 19, 2012. The Company filed its answer on December 21, 2012. At June 25, 2013, the current unpaid balance of the mortgage pass-through certificates at issue in this action was approximately $100 million and certain certificates had incurred actual losses of approximately $1 million. Based on currently available information, the Company believes it could incur a loss in this action up to the difference between the $100 million unpaid balance of these certificates (plus any losses incurred) and their fair market value at the time of a judgment against the Company, plus pre- and post-judgment interest, fees and costs. The Company may be entitled to be indemnified for some of these losses and to an offset for interest received by the plaintiff prior to a judgment.

On July 18, 2011, the Western and Southern Life Insurance Company and certain affiliated companies filed a complaint against the Company and other defendants in the Court of Common Pleas in Ohio, styled *Western and Southern Life Insurance Company, et al. v. Morgan Stanley Mortgage Capital Inc., et al.* An amended complaint was filed on April 2, 2012 and alleges that defendants made untrue statements and material omissions in the sale to plaintiffs of certain mortgage pass-through certificates backed by securitization trusts containing residential mortgage loans. The amount of the certificates allegedly sold to plaintiffs by the Company was approximately $153 million. The amended complaint raises claims under the Ohio Securities Act, federal securities laws, and common law and seeks, among other things, to rescind the plaintiffs purchases of such certificates. On May 21, 2012, the Company filed a motion to dismiss the amended complaint, which motion was denied on August 3, 2012. The court has set a trial date in May 2015. At June 25, 2013, the current unpaid balance of the mortgage pass-through certificates at issue in this action was approximately $121 million, and the certificates had incurred actual losses of approximately $1 million. Based on currently available information, the Company believes it could incur a loss in this action up to the difference between the $121 million unpaid balance of these certificates (plus any losses incurred) and their fair market value at the time of a judgment against the Company, plus post-judgment interest, fees and costs. The Company may be entitled to an offset for interest received by the plaintiff prior to a judgment.

On September 2, 2011, the Federal Housing Finance Agency (FHFA), as conservator for Fannie Mae and Freddie Mac, filed 17 complaints against numerous financial services companies, including the Company. A complaint against the Company and other defendants was filed in the Supreme Court of NY, styled *Federal Housing Finance Agency, as Conservator v. Morgan Stanley et al.* The complaint alleges that defendants made untrue statements and material omissions in connection with the sale to Fannie Mae and Freddie Mac of residential mortgage pass-through certificates with an original unpaid balance of approximately $11 billion. The complaint raises claims under federal and state securities laws and common law and seeks, among other things, rescission and compensatory and punitive damages. On September 26, 2011, defendants removed the action to the United States District Court for the Southern District of New York. On July 13, 2012, the Company filed a motion to dismiss the complaint, which motion was denied in large part on November 19, 2012. Trial is currently scheduled to begin in January 2015. At June 25, 2013, the current unpaid balance of the mortgage pass-through certificates at issue in this action was approximately $2.86 billion, and the certificates had incurred actual losses of approximately $59 million. Based on currently available information, the Company believes it could incur a loss in this action up to the difference between the $2.86 billion unpaid balance of these certificates (plus any losses incurred) and their fair market value at the time of a judgment against the Company, plus pre- and post-judgment interest, fees and costs. The Company may be entitled to be indemnified for some of these losses and to an offset for interest received by the plaintiff prior to a judgment.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

On April 25, 2012, Metropolitan Life Insurance Company and certain affiliates filed a complaint against the Company and certain affiliates in the Supreme Court of NY styled *Metropolitan Life Insurance Company, et al. v. Morgan Stanley, et al.* An amended complaint was filed on June 29, 2012 and alleges that defendants made untrue statements and material omissions in the sale to plaintiffs of certain mortgage pass-through certificates backed by securitization trusts containing residential mortgage loans. The total amount of certificates allegedly sponsored, underwritten and/or sold by the Company was approximately $758 million. The amended complaint raises common law claims of fraud, fraudulent inducement, and aiding and abetting fraud and seeks, among other things, rescission, compensatory and/or rescissionary damages, as well as punitive damages, associated with plaintiffs purchases of such certificates. On September 21, 2012, the Company filed a motion to dismiss the amended complaint, which was granted in part and denied in part on July 16, 2013. Following that decision, the total amount of certificates allegedly sponsored, underwritten and/or sold by the Company was approximately $656 million. At June 25, 2013, the current unpaid balance of the mortgage pass-through certificates remaining at issue in this case was approximately $369 million, and the certificates incurred actual losses of approximately $28.3 million. Based on currently available information, the Company believes it could incur a loss up to the difference between the $369 million unpaid balance of these certificates (plus any losses incurred) and their fair market value at the time of a judgment against the Company, plus pre- and post-judgment interest, fees and costs. The Company may be entitled to be indemnified for some of these losses and to an offset for interest received by the plaintiff prior to a judgment.

On April 25, 2012, The Prudential Insurance Company of America and certain affiliates filed a complaint against the Company and certain affiliates in the Superior Court of the State of New Jersey styled *The Prudential Insurance Company of America, et al. v. Morgan Stanley, et al.* The complaint alleges that defendants made untrue statements and material omissions in connection with the sale to plaintiffs of certain mortgage pass-through certificates backed by securitization trusts containing residential mortgage loans. The total amount of certificates allegedly sponsored, underwritten and/or sold by the Company is approximately $1 billion. The complaint raises claims under the New Jersey Uniform Securities Law, as well as common law claims of negligent misrepresentation, fraud and tortious interference with contract and seeks, among other things, compensatory damages, punitive damages, rescission and rescissionary damages associated with plaintiffs purchases of such certificates. On October 16, 2012, plaintiffs filed an amended complaint which, among other things, increases the total amount of the certificates at issue by approximately $80 million, adds causes of action for fraudulent inducement, equitable fraud, aiding and abetting fraud, and violations of the New Jersey RICO statute, and includes a claim for treble damages. On March 15, 2013, defendants motion to dismiss was denied. At June 25, 2013, the current unpaid balance of the mortgage pass-through certificates at issue in this action was approximately $674 million, and the certificates had not yet incurred actual losses. Based on currently available information, the Company believes it could incur a loss in this action up to the difference between the $674 million unpaid balance of these certificates (plus any losses incurred) and their fair market value at the time of a judgment against the Company, plus pre- and post-judgment interest, fees and costs. The Company may be entitled to be indemnified for some of these losses and to an offset for interest received by the plaintiff prior to a judgment.

13. Regulatory Requirements.

Morgan Stanley. The Company is a financial holding company under the Bank Holding Company Act of 1956, as amended, and is subject to the regulation and oversight of the Federal Reserve. The Federal Reserve establishes capital requirements for the Company, including well-capitalized standards, and evaluates the Company s compliance with such capital requirements. The Office of the Comptroller of the Currency establishes similar capital requirements and standards for Morgan Stanley Bank, N.A. and Morgan Stanley Private Bank, National Association.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company calculates its capital ratios and risk-weighted assets (RWAs) in accordance with the capital adequacy standards for financial holding companies adopted by the Federal Reserve. These standards are based upon a framework described in the International Convergence of Capital Measurement and Capital Standards, July 1988, as amended, also referred to as Basel I. In December 2007, the U.S. banking regulators published final regulation incorporating the Basel II Accord, which requires internationally active banking organizations, as well as certain of their U.S. bank subsidiaries, to implement Basel II standards over the next several years. In July 2010, the Company began reporting its capital adequacy standards on a parallel basis to its regulators under Basel I and Basel II as part of a phased implementation of Basel II.

In December 2010, the Basel Committee reached an agreement on Basel III. In July 2013, the U.S. banking regulators issued a final rule to implement many aspects of Basel III (the U.S. Basel III final rule). The U.S. Basel III final rule contains new capital standards that raise the capital requirements, strengthen counterparty credit risk capital requirements and replace the use of externally developed credit ratings with alternatives such as the Organisation for Economic Co-operation and Development s country risk classifications. The U.S. Basel III final rule also requires certain banking organizations, including the Company, to maintain both a capital conservation buffer and, if deployed, a countercyclical capital buffer, above the minimum risk-based capital ratios. Failure to maintain such buffers will result in restrictions on the banking organization s ability to make capital distributions and pay discretionary bonuses to executive officers. The U.S. Basel III final rule also subjects certain banking organizations, including the Company, to a minimum supplementary leverage ratio of 3%. The calibration of the supplementary leverage ratio is broadly similar to the December 2010 version of the Basel III leverage ratio and includes off-balance sheet exposures in the denominator. The Company will become subject to the U.S. Basel III final rule beginning on January 1, 2014. Certain requirements in the U.S. Basel III final rule, including the new capital buffers, will be phased in over several years.

In June 2011, the U.S. banking regulators published final regulations implementing a provision of the Dodd-Frank Act requiring that certain institutions supervised by the Federal Reserve, including the Company, be subject to minimum capital requirements that are not less than the generally applicable risk-based capital requirements. Currently, this minimum capital floor is based on Basel I. Beginning January 1, 2015, the U.S. Basel III final rule will replace the current Basel I-based capital floor with a standardized approach that, among other things, modifies the existing risk weights for certain types of asset classes and which is applicable to both minimum capital requirements and the sum of conservation and countercyclical capital buffers if deployed. On January 1, 2013, the U.S. banking regulators rules to implement the Basel Committee s market risk capital framework amendment, commonly referred to as Basel 2.5 , became effective, which increased the capital requirements for securitizations and correlation trading within the Company s trading book as well as incorporated add-ons for stressed VaR and incremental risk requirements (market risk capital framework amendment).

At June 30, 2013, the Company s capital levels calculated under Basel I, inclusive of the market risk capital framework amendment, were in excess of well-capitalized levels with ratios of Tier 1 capital to RWAs of 14.1% and total capital to RWAs of 14.9% (6% and 10% being well-capitalized for regulatory purposes, respectively). The Company s ratio of Tier 1 common capital to RWAs was 11.8% (5% under stressed conditions is the current minimum under the Federal Reserve s Comprehensive Capital Analysis and Review (CCAR) framework). Financial holding companies, including the Company, are subject to a Tier 1 leverage ratio defined by the Federal Reserve. Consistent with the Federal Reserve s definition, the Company calculated its Tier 1 leverage ratio as Tier 1 capital divided by adjusted average total assets (which reflects adjustments for disallowed goodwill, certain intangible assets, deferred tax assets and financial and non-financial equity investments). The adjusted average total assets are derived using weekly balances for the period. At June 30, 2013, the Company was in compliance with the Federal Reserve s Tier 1 leverage requirement, with a Tier 1 leverage ratio of 7.1% (5% is the current well-capitalized standard for regulatory purposes).

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table summarizes the capital measures for the Company:

	June 30, 2013		December 31, 2012	
	Balance	Ratio	Balance	Ratio
	(dollars in millions)			
Tier 1 common capital	$ 47,603	11.8%	$ 44,794	14.6%
Tier 1 capital	56,780	14.1%	54,360	17.7%
Total capital	59,987	14.9%	56,626	18.5%
RWAs	403,425		306,746	
Adjusted average total assets	804,932		769,495	
Tier 1 leverage		7.1%		7.1%

The Company s U.S. Bank Operating Subsidiaries. The Company s U.S. bank operating subsidiaries are subject to various regulatory capital requirements as administered by U.S. federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company s U.S. bank operating subsidiaries financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company s U.S. bank operating subsidiaries must meet specific capital guidelines that involve quantitative measures of the Company s U.S. bank operating subsidiaries assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices.

At June 30, 2013, the Company s U.S. bank operating subsidiaries met all capital adequacy requirements to which they are subject and exceeded all regulatory mandated and targeted minimum regulatory capital requirements to be well-capitalized. There are no conditions or events that management believes have changed the Company s U.S. bank operating subsidiaries category.

The table below sets forth the capital information for the Company s U.S. bank operating subsidiaries, which are U.S. depository institutions, calculated in a manner consistent with the guidelines described under Basel I, inclusive of the market risk capital framework amendment:

	June 30, 2013		December 31, 2012	
	Amount	Ratio	Amount	Ratio
	(dollars in millions)			
Total capital (to RWAs):				
MSBNA	$ 12,006	15.8%	$ 11,509	17.2%
MSPBNA	$ 1,736	26.5%	$ 1,673	28.8%
Tier 1 capital (to RWAs):				
MSBNA	$ 10,386	13.7%	$ 9,918	14.9%
MSPBNA	$ 1,729	26.4%	$ 1,665	28.7%
Tier 1 leverage:				
MSBNA	$ 10,386	13.1%	$ 9,918	13.3%
MSPBNA	$ 1,729	10.9%	$ 1,665	10.6%

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Under regulatory capital requirements adopted by the U.S. federal banking agencies, U.S. depository institutions, in order to be considered well-capitalized, must maintain a ratio of total capital to RWAs of 10%, a capital ratio of Tier 1 capital to RWAs of 6%, and a ratio of Tier 1 capital to average total assets (leverage ratio) of 5%. Each U.S. depository institution subsidiary of the Company must be well-capitalized in order for the Company to continue to qualify as a financial holding company and to continue to engage in the broadest range of financial activities permitted for financial holding companies. At June 30, 2013 and December 31, 2012, the Company s U.S. depository institutions maintained capital at levels in excess of the universally mandated well-capitalized levels. These subsidiary depository institutions maintain capital at levels sufficiently in excess of the well-capitalized requirements to address any additional capital needs and requirements identified by the federal banking regulators.

MS&Co. and Other Broker-Dealers. MS&Co. is a registered broker-dealer and registered futures commission merchant and, accordingly, is subject to the minimum net capital requirements of the U.S. Securities and Exchange Commission (the SEC), the Financial Industry Regulatory Authority, Inc. and the U.S. Commodity Futures Trading Commission (the CFTC). MS&Co. has consistently operated with capital in excess of its regulatory capital requirements. MS&Co s net capital and excess net capital decreased from December 31, 2012 due to regulatory capital deductions required for the composition of trading assets held at June 30, 2013. MS&Co. s net capital totaled $6,678 million and $7,820 million at June 30, 2013 and December 31, 2012, respectively, which exceeded the amount required by $5,237 million and $6,453 million, respectively. MS&Co. is required to hold tentative net capital in excess of $1 billion and net capital in excess of $500 million in accordance with the market and credit risk standards of Appendix E of SEC Rule 15c3-1. MS&Co. is also required to notify the SEC in the event that its tentative net capital is less than $5 billion. At June 30, 2013, MS&Co. had tentative net capital in excess of the minimum and the notification requirements.

MSSB LLC is a registered broker-dealer and registered futures commission merchant and, accordingly, is subject to the minimum net capital requirements of the SEC, the Financial Industry Regulatory Authority, Inc. and the CFTC. MSSB LLC has consistently operated with capital in excess of its regulatory capital requirements.

MSIP, a London-based broker-dealer subsidiary, is subject to the capital requirements of the Prudential Regulation Authority, and MSMS, a Tokyo-based broker-dealer subsidiary, is subject to the capital requirements of the Financial Services Agency. MSIP and MSMS have consistently operated in excess of their respective regulatory capital requirements.

Other Regulated Subsidiaries. Certain other U.S. and non-U.S. subsidiaries are subject to various securities, commodities and banking regulations, and capital adequacy requirements promulgated by the regulatory and exchange authorities of the countries in which they operate. These subsidiaries have consistently operated in excess of their local capital adequacy requirements.

Morgan Stanley Derivative Products Inc. (MSDP), a derivative products subsidiary rated A2 by Moody s and AAA by S&P, maintains certain operating restrictions that have been reviewed by Moody s and S&P. MSDP is operated such that creditors of the Company should not expect to have any claims on the assets of MSDP, unless and until the obligations to its own creditors are satisfied in full. Creditors of MSDP should not expect to have any claims on the assets of the Company or any of its affiliates, other than the respective assets of MSDP.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

14. Redeemable Noncontrolling Interests and Total Equity.
Redeemable Noncontrolling Interests.

Redeemable noncontrolling interests related to the Wealth Management JV (see Note 3). Changes in redeemable noncontrolling interests for the six months ended June 30, 2013 were as follows (dollars in millions):

Balance at December 31, 2012	$ 4,309
Net income applicable to redeemable noncontrolling interests	222
Distributions	(38)
Other	(11)
Carrying value of additional stake in Wealth Management JV purchased from Citi	(4,482)
Balance at June 30, 2013	$

Total Equity.

Morgan Stanley Shareholders Equity.

During the quarters and six months ended June 30, 2013 and 2012, the Company did not purchase any of its common stock as part of its share repurchase program. At June 30, 2013, the Company had approximately $1.6 billion remaining under its current share repurchase authorization. Share repurchases by the Company are subject to regulatory approval (see Note 22).

Accumulated Other Comprehensive Income (Loss).

The following table presents changes in Accumulated other comprehensive income (loss) by component, net of tax and net of noncontrolling interests, in the quarter ended June 30, 2013 (dollars in millions):

	Foreign Currency Translation Adjustments	Net Change in Cash Flow Hedges	Change in Net Unrealized Gains (Losses) on Securities Available for Sale	Pension, Postretirement and Other Related Adjustments	Total
Balance at March 31, 2013	$ (276)	$ (4)	$ 124	$ (538)	$ (694)
Other comprehensive income (loss) before reclassifications	(144)		(322)	5	(461)
Amounts reclassified from accumulated other comprehensive income (loss)		1	(20)	5	(14)
Net other comprehensive income (loss) during the period	(144)	1	(342)	10	(475)
Balance at June 30, 2013	$ (420)	$ (3)	$ (218)	$ (528)	$ (1,169)

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents changes in Accumulated other comprehensive income (loss) by component, net of tax and net of noncontrolling interests, in the six months ended June 30, 2013 (dollars in millions):

	Foreign Currency Translation Adjustments	Net Change in Cash Flow Hedges	Change in Net Unrealized Gains (Losses) on Securities Available for sale	Pension, Postretirement and Other Related Adjustments	Total
Balance at December 31, 2012	$ (123)	$ (5)	$ 151	$ (539)	$ (516)
Other comprehensive income (loss) before reclassifications	(297)		(347)	2	(642)
Amounts reclassified from accumulated other comprehensive income (loss)		2	(22)	9	(11)
Net other comprehensive income (loss) during the period	(297)	2	(369)	11	(653)
Balance at June 30, 2013	$ (420)	$ (3)	$ (218)	$ (528)	$ (1,169)

The Company had no significant reclassifications out of Accumulated other comprehensive income (loss) for the quarter and six months ended June 30, 2013.

Nonredeemable Noncontrolling Interests.

Changes in nonredeemable noncontrolling interests primarily resulted from distributions related to MSMS of $292 million and a real estate fund of $195 million in the six months ended June 30, 2013. Changes in nonredeemable noncontrolling interests in the six months ended June 30, 2012 primarily resulted from $622 million in net assets received from Citi related to Citi s required equity contribution in connection with the Wealth Management JV platform integration, partially offset by distributions related to MSMS of $151 million. See Note 20.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

15. Earnings per Common Share.

Basic earnings per common share (EPS) is computed by dividing earnings (loss) applicable to Morgan Stanley common shareholders by the weighted average number of common shares outstanding for the period. Common shares outstanding include common stock and vested restricted stock units (RSUs) where recipients have satisfied either the explicit vesting terms or retirement eligibility requirements. Diluted EPS reflects the assumed conversion of all dilutive securities. The Company calculates EPS using the two-class method and determines whether instruments granted in share-based payment transactions are participating securities (see Note 2 to the consolidated financial statements for the year ended December 31, 2012 in the Form 10-K). The following table presents the calculation of basic and diluted EPS (in millions, except for per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Basic EPS:				
Income from continuing operations	$ 1,220	$ 713	$ 2,470	$ 861
Net gain (loss) from discontinued operations	(29)	37	(48)	23
Net income	1,191	750	2,422	884
Net income applicable to redeemable noncontrolling interests	100		222	
Net income applicable to nonredeemable noncontrolling interests	111	159	258	387
Net income applicable to Morgan Stanley	980	591	1,942	497
Less: Preferred dividends (Series A Preferred Stock)	(11)	(11)	(22)	(22)
Less: Preferred dividends (Series C Preferred Stock)	(13)	(13)	(26)	(26)
Less: Wealth Management JV redemption value adjustment (see Note 3)	(151)		(151)	
Less: Allocation of (earnings) loss to participating RSUs(1):				
From continuing operations	(2)	(3)	(4)	(3)
Earnings applicable to Morgan Stanley common shareholders	$ 803	$ 564	$ 1,739	$ 446
Weighted average common shares outstanding	1,908	1,885	1,904	1,881
Earnings per basic common share:				
Income from continuing operations	$ 0.44	$ 0.28	$ 0.94	$ 0.23
Net gain (loss) from discontinued operations	(0.02)	0.02	(0.03)	0.01
Earnings per basic common share	$ 0.42	$ 0.30	$ 0.91	$ 0.24
Diluted EPS:				
Earnings applicable to Morgan Stanley common shareholders	$ 803	$ 564	$ 1,739	$ 446
Weighted average common shares outstanding	1,908	1,885	1,904	1,881
Effect of dilutive securities:				
Stock options and RSUs(1)	43	27	42	26
Weighted average common shares outstanding and common stock equivalents	1,951	1,912	1,946	1,907
Earnings per diluted common share:				
Income from continuing operations	$ 0.43	$ 0.28	$ 0.92	$ 0.23

Net gain (loss) from discontinued operations	(0.02)	0.01	(0.03)	
Earnings per diluted common share	$ 0.41	$ 0.29	$ 0.89	$ 0.23

(1) RSUs that are considered participating securities participate in all of the earnings of the Company in the computation of basic EPS, and, therefore, such RSUs are not included as incremental shares in the diluted calculation.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following securities were considered antidilutive and, therefore, were excluded from the computation of diluted EPS:

Number of Antidilutive Securities Outstanding at End of Period:	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
	(shares in millions)			
RSUs and performance-based stock units	4	32	4	13
Stock options	36	45	36	45
Total	40	77	40	58

16. Interest Income and Interest Expense.

Details of Interest income and Interest expense were as follows:

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
	(dollars in millions)			
Interest income(1):				
Trading assets(2)	$ 613	$ 662	$ 1,217	$ 1,453
Securities available for sale	110	76	206	162
Loans	278	139	522	257
Interest bearing deposits with banks	25	24	51	51
Federal funds sold and securities purchased under agreements to resell and Securities borrowed	66	46	158	159
Other	330	376	666	783
Total interest income	$ 1,422	$ 1,323	$ 2,820	$ 2,865
Interest expense(1):				
Deposits	$ 41	$ 45	$ 82	$ 90
Commercial paper and other short-term borrowings	5	11	14	24
Long-term debt	917	1,087	1,877	2,341
Securities sold under agreements to repurchase and Securities loaned	518	529	968	992
Other	(263)	(189)	(510)	(363)
Total interest expense	$ 1,218	$ 1,483	$ 2,431	$ 3,084
Net interest	$ 204	$ (160)	$ 389	$ (219)

(1) Interest income and expense are recorded within the condensed consolidated statements of income depending on the nature of the instrument and related market conventions. When interest is included as a component of the instrument s fair value, interest is included within Trading revenues or Investments revenues. Otherwise, it is included within Interest income or Interest expense.

(2) Interest expense on Trading liabilities is reported as a reduction to Interest income on Trading assets.

17. Employee Benefit Plans.

The Company sponsors various pension plans for the majority of its U.S. and non-U.S. employees. The Company provides certain other postretirement benefits, primarily health care and life insurance, to eligible U.S. employees. The Company also provides certain postemployment benefits to certain former employees or inactive employees prior to retirement.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The components of the Company s net periodic benefit expense for its pension and postretirement plans were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(dollars in millions)			
Service cost, benefits earned during the period	$ 7	$ 7	$ 14	$ 15
Interest cost on projected benefit obligation	39	41	78	82
Expected return on plan assets	(29)	(27)	(57)	(55)
Net amortization of prior service costs	(3)	(4)	(7)	(7)
Net amortization of actuarial loss	10	7	20	14
Net periodic benefit expense	$ 24	$ 24	$ 48	$ 49

18. Income Taxes.

The Company is under continuous examination by the Internal Revenue Service (the IRS) and other tax authorities in certain countries, such as Japan and the U.K., and in states in which the Company has significant business operations, such as New York. The Company is currently under review by the IRS Appeals Office for the remaining issues covering tax years 1999 2005. Also, the Company is currently at various levels of field examination with respect to audits with the IRS, as well as New York State and New York City, for tax years 2006 2008 and 2007 2009, respectively. During 2013, the Company expects to reach a conclusion with the U.K. tax authorities on substantially all issues through tax year 2010.

The Company believes that the resolution of tax matters will not have a material effect on the condensed consolidated statements of financial condition of the Company, although a resolution could have a material impact on the Company s condensed consolidated statements of income for a particular future period and on the Company s effective income tax rate for any period in which such resolution occurs. The Company has established a liability for unrecognized tax benefits that the Company believes is adequate in relation to the potential for additional assessments. Once established, the Company adjusts unrecognized tax benefits only when more information is available or when an event occurs necessitating a change.

It is reasonably possible that significant changes in the gross balance of unrecognized tax benefits may occur within the next 12 months. At this time, however, it is not possible to reasonably estimate the expected change to the total amount of unrecognized tax benefits and impact on the effective tax rate over the next 12 months.

The Company s effective tax rate from continuing operations for the six months ended June 30, 2013 included a discrete tax benefit of $81 million due to the retroactive effective date of the American Taxpayer Relief Act of 2012 (the Relief Act). The Relief Act that was enacted on January 2, 2013, among other things, extended with retroactive effect to January 1, 2012 a provision of U.S. tax law that defers the imposition of tax on certain active financial services income of certain foreign subsidiaries earned outside of the U.S. until such income is repatriated to the U.S. as a dividend. Additionally, the Company s effective tax rate from continuing operations for the six months ended June 30, 2013 included a discrete net tax benefit of $61 million associated with remeasurement of reserves and related interest based on new information regarding the status of certain tax authority examinations. Excluding these discrete tax benefits, the annual effective tax rate in the six months ended June 30, 2013 would have been 30.8%.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

19. Segment and Geographic Information.

Segment Information.

The Company structures its segments primarily based upon the nature of the financial products and services provided to customers and the Company s management organization. The Company provides a wide range of financial products and services to its customers in each of its business segments: Institutional Securities, Wealth Management and Investment Management. For further discussion of the Company s business segments, see Note 1.

Revenues and expenses directly associated with each respective segment are included in determining its operating results. Other revenues and expenses that are not directly attributable to a particular segment are allocated based upon the Company s allocation methodologies, generally based on each segment s respective net revenues, non-interest expenses or other relevant measures.

As a result of treating certain intersegment transactions as transactions with external parties, the Company includes an Intersegment Eliminations category to reconcile the business segment results to the Company s consolidated results. Intersegment Eliminations also reflect the effect of fees paid by the Institutional Securities business segment to the Wealth Management business segment related to the bank deposit program.

Selected financial information for the Company s segments is presented below:

Three Months Ended June 30, 2013	Institutional Securities	Wealth Management	Investment Management (dollars in millions)	Intersegment Eliminations	Total
Total non-interest revenues	$ 4,586	$ 3,085	$ 674	$ (46)	$ 8,299
Interest income	1,029	511	3	(121)	1,422
Interest expense	1,269	65	4	(120)	1,218
Net interest	(240)	446	(1)	(1)	204
Net revenues(1)	$ 4,346	$ 3,531	$ 673	$ (47)	$ 8,503
Income from continuing operations before income taxes	$ 960	$ 655	$ 160	$	$ 1,775
Provision for income taxes	288	229	38		555
Income from continuing operations	672	426	122		1,220
Discontinued operations(2):					
Gain (loss) from discontinued operations	(27)			(15)	(42)
Provision for (benefit from) income taxes	(9)			(4)	(13)
Net gain (loss) on discontinued operations	(18)			(11)	(29)
Net income (loss)	654	426	122	(11)	1,191
Net income applicable to redeemable noncontrolling interests		100			100
Net income applicable to nonredeemable noncontrolling interests	90		21		111
Net income (loss) applicable to Morgan Stanley	$ 564	$ 326	$ 101	$ (11)	$ 980

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Three Months Ended June 30, 2012	Institutional Securities(3)	Wealth Management(3)	Investment Management (dollars in millions)	Intersegment Eliminations	Total
Total non-interest revenues	$ 3,863	$ 2,816	$ 465	$ (42)	$ 7,102
Interest income	964	456	2	(99)	1,323
Interest expense	1,495	76	11	(99)	1,483
Net interest	(531)	380	(9)		(160)
Net revenues(1)	$ 3,332	$ 3,196	$ 456	$ (42)	$ 6,942
Income (loss) from continuing operations before income taxes	$ 488	$ 410	$ 43	$ (4)	$ 937
Provision for income taxes	69	149	6		224
Income (loss) from continuing operations	419	261	37	(4)	713
Discontinued operations(2):					
Gain (loss) from discontinued operations	(43)	91		4	52
Provision for (benefit from) income taxes	(15)	30			15
Net gain (loss) on discontinued operations	(28)	61		4	37
Net income	391	322	37		750
Net income applicable to nonredeemable noncontrolling interests	45	91	23		159
Net income applicable to Morgan Stanley	$ 346	$ 231	$ 14	$	$ 591

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Six Months Ended June 30, 2013	Institutional Securities	Wealth Management	Investment Management (dollars in millions)	Intersegment Eliminations	Total
Total non-interest revenues	$ 8,899	$ 6,142	$ 1,323	$ (92)	$ 16,272
Interest income	2,053	999	5	(237)	2,820
Interest expense	2,517	140	10	(236)	2,431
Net interest	(464)	859	(5)	(1)	389
Net revenues(1)	$ 8,435	$ 7,001	$ 1,318	$ (93)	$ 16,661
Income from continuing operations before income taxes	$ 1,758	$ 1,252	$ 347	$	$ 3,357
Provision for income taxes	348	449	90		887
Income from continuing operations	1,410	803	257		2,470
Discontinued operations(2):					
Gain (loss) from discontinued operations	(57)	(1)	1	(14)	(71)
Provision for (benefit from) income taxes	(20)			(3)	(23)
Net gain (loss) on discontinued operations	(37)	(1)	1	(11)	(48)
Net income (loss)	1,373	802	258	(11)	2,422
Net income applicable to redeemable noncontrolling interests	1	221			222
Net income applicable to nonredeemable noncontrolling interests	186		72		258
Net income (loss) applicable to Morgan Stanley	$ 1,186	$ 581	$ 186	$ (11)	$ 1,942

Six Months Ended June 30, 2012	Institutional Securities(3)	Wealth Management(3)	Investment Management (dollars in millions)	Intersegment Eliminations	Total
Total non-interest revenues	$ 7,449	$ 5,707	$ 1,006	$ (77)	$ 14,085
Interest income	2,141	914	5	(195)	2,865
Interest expense	3,123	134	22	(195)	3,084
Net interest	(982)	780	(17)		(219)
Net revenues(1)	$ 6,467	$ 6,487	$ 989	$ (77)	$ 13,866
Income (loss) from continuing operations before income taxes	$ 159	$ 813	$ 171	$ (4)	$ 1,139
Provision for (benefit from) income taxes	(37)	271	44		278
Income (loss) from continuing operations	196	542	127	(4)	861
Discontinued operations(2):					

Gain (loss) from discontinued operations		(18)		93		1		4		80
Provision for income taxes		26		31						57
Net gain (loss) on discontinued operations		(44)		62		1		4		23
Net income		152		604		128				884
Net income applicable to nonredeemable noncontrolling interests		124		175		88				387
Net income applicable to Morgan Stanley	$	28	$	429	$	40	$		$	497

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) In certain management fee arrangements, the Company is entitled to receive performance-based fees (also referred to as incentive fees) when the return on assets under management exceeds certain benchmark returns or other performance targets. In such arrangements, performance fee revenue is accrued (or reversed) quarterly based on measuring account fund performance to date versus the performance benchmark stated in the investment management agreement. The amount of performance-based fee revenue at risk of reversing if fund performance falls below stated investment management agreement benchmarks was approximately $335 million at June 30, 2013 and approximately $205 million at December 31, 2012 (see Note 2 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K).

(2) See Notes 1 and 21 for discussion of discontinued operations.

(3) On January 1, 2013, the International Wealth Management business was transferred from the Wealth Management business segment to the Equity division within the Institutional Securities business segment. Accordingly, prior period amounts have been recast to reflect the International Wealth Management business as part of the Institutional Securities business segment.

Total Assets(1)	Institutional Securities(2)	Wealth Management(2)	Investment Management	Total
		(dollars in millions)		
At June 30, 2013	$ 671,116	$ 124,319	$ 7,256	$ 802,691
At December 31, 2012	$ 648,049	$ 125,565	$ 7,346	$ 780,960

(1) Corporate assets have been fully allocated to the Company s business segments.

(2) Prior period amounts have been recast to reflect the transfer of the International Wealth Management business from the Wealth Management business segment to the Institutional Securities business segment.

Geographic Information.

The Company operates in both U.S. and non-U.S. markets. The Company s non-U.S. business activities are principally conducted and managed through European and Asian locations. The net revenues disclosed in the following table reflect the regional view of the Company s consolidated net revenues on a managed basis, based on the following methodology:

Institutional Securities: advisory and equity underwriting client location, debt underwriting revenue recording location, sales and trading trading desk location.

Wealth Management: wealth management representative coverage location.

Investment Management: client location, except for Merchant Banking and Real Estate Investing businesses, which are based on asset location.

Net Revenues	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
	(dollars in millions)			

Americas	$ 6,014	$ 5,104	$ 11,970	$ 9,888
Europe, Middle East and Africa	1,132	977	2,198	2,126
Asia	1,357	861	2,493	1,852
Net revenues	$ 8,503	$ 6,942	$ 16,661	$ 13,866

20. Equity Method Investments.

The Company has investments accounted for under the equity method of accounting (see Note 1) of $4,542 million and $4,682 million at June 30, 2013 and December 31, 2012, respectively, included in Other investments in the condensed consolidated statements of financial condition. Income from these investments were $127 million and $191 million for the quarter and six months ended June 30, 2013, respectively, and are included in Other revenues in the condensed consolidated statements of income. Income (losses) from these investments were $12 million and $(20) million for the quarter and six months ended June 30, 2012, respectively.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Japanese Securities Joint Venture.

The Company holds a 40% voting interest and Mitsubishi UFJ Financial Group, Inc. (MUFG) holds a 60% voting interest in Mitsubishi UFJ Morgan Stanley Securities Co., Ltd. (MUMSS), while the Company holds a 51% voting interest and MUFG holds a 49% voting interest in MSMS. The Company consolidates MSMS in its condensed consolidated financial statements and accounts for its interest in MUMSS as an equity method investment within the Institutional Securities business segment (see Note 14). During the quarters ended June 30, 2013 and 2012, the Company recorded income of $174 million and $54 million, respectively, and income of $299 million and $81 million in the six months ended June 30, 2013 and 2012, respectively, within Other revenues in the condensed consolidated statements of income, arising from the Company s 40% stake in MUMSS.

In June of 2013, MUMSS paid a dividend of approximately $287 million, of which the Company received approximately $115 million for its proportionate share of MUMSS.

21. Discontinued Operations.
See Note 1 for a discussion of the Company s discontinued operations.

The table below provides information regarding amounts included in discontinued operations:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(dollars in millions)			
Net revenues(1):				
Saxon	$	$ 1	$	$ 77
Quilter		132	(1)	163
Other	(9)	6	(18)	14
	$ (9)	$ 139	$ (19)	$ 254
Pre-tax gain (loss) on discontinued operations(1):				
Saxon	$ (19)	$ (40)	$ (39)	$ (15)
Quilter(2)		95	(1)	97
Other	(23)	(3)	(31)	(2)
	$ (42)	$ 52	$ (71)	$ 80

(1) Amounts included eliminations of intersegment activity.
(2) Amount for the quarter and six months ended June 30, 2012 included a pre-tax gain of approximately $108 million in connection with the sale of Quilter.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

22. Subsequent Events.

The Company has evaluated subsequent events for adjustment to or disclosure in the condensed consolidated financial statements through the date of this report and the Company has not identified any recordable or disclosable events, not otherwise reported in these condensed consolidated financial statements or the notes thereto, except for the following:

Common Dividend.

On July 18, 2013, the Company announced that its Board of Directors declared a quarterly dividend per common share of $0.05. The dividend is payable on August 15, 2013 to common shareholders of record on July 31, 2013.

Share Repurchases.

In July 2013, the Company received no objection from the Federal Reserve to repurchase up to $500 million of the Company s outstanding common stock under rules permitting annual capital distributions (12 Code of Federal Regulations 225.8, *Capital Planning*). Share repurchases will be made pursuant to the share repurchase program previously authorized by the Company s Board of Directors and will be exercised from time to time through March 31, 2014, at prices the Company deems appropriate subject to various factors, including the Company s capital position and market conditions. The share repurchases may be effected through open market purchases or privately negotiated transactions, including through Rule 10b5-1 plans, and may be suspended at any time (see Note 14 and Unregistered Sales of Equity Securities and Use of Proceeds in Part II, Item 2).

Wealth Management JV.

In July 2013, approximately $17 billion of deposits held by Citi relating to customer accounts were transferred to the Company s depository institutions (see Note 3).

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Morgan Stanley:

We have reviewed the accompanying condensed consolidated statement of financial condition of Morgan Stanley and subsidiaries (the Company) as of June 30, 2013, the related condensed consolidated statements of income and comprehensive income for the three-month and six-month periods ended June 30, 2013 and 2012, and the condensed consolidated statements of cash flows and changes in total equity for the six-month periods ended June 30, 2013 and 2012. These condensed consolidated financial statements are the responsibility of the management of the Company.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to such condensed consolidated financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statement of financial condition of the Company as of December 31, 2012, and the consolidated statements of income, comprehensive income, cash flows and changes in total equity for the year then ended (not presented herein) included in the Company s Annual Report on Form 10-K; and in our report dated February 26, 2013, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated statement of financial condition as of December 31, 2012 is fairly stated, in all material respects, in relation to the consolidated statement of financial condition from which it has been derived.

/s/ Deloitte & Touche LLP
New York, New York

August 2, 2013

Table of Contents

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.
Introduction.

Morgan Stanley, a financial holding company, is a global financial services firm that maintains significant market positions in each of its business segments Institutional Securities, Wealth Management and Investment Management. The Company, through its subsidiaries and affiliates, provides a wide variety of products and services to a large and diversified group of clients and customers, including corporations, governments, financial institutions and individuals. Unless the context otherwise requires, the terms Morgan Stanley or the Company mean Morgan Stanley (the Parent) together with its consolidated subsidiaries.

Effective with the quarter ended June 30, 2013, the Global Wealth Management Group and Asset Management business segments were re-titled Wealth Management and Investment Management, respectively.

A summary of the activities of each of the Company s business segments is as follows:

Institutional Securities provides financial advisory and capital-raising services, including advice on mergers and acquisitions, restructurings, real estate and project finance; corporate lending; sales, trading, financing and market-making activities in equity and fixed income securities and related products, including foreign exchange and commodities; and investment activities.

Wealth Management (formerly known as Global Wealth Management Group), provides brokerage and investment advisory services to individual investors and small-to-medium sized businesses and institutions covering various investment alternatives; financial and wealth planning services; annuity and other insurance products; credit and other lending products; cash management services; retirement services; and trust and fiduciary services and engages in fixed income trading, which primarily facilitates clients trading or investments in such securities.

Investment Management (formerly known as Asset Management) provides a broad array of investment strategies that span the risk/return spectrum across geographies, asset classes and public and private markets to a diverse group of clients across the institutional and intermediary channels as well as high net worth clients.

See Notes 1 and 21 to the condensed consolidated financial statements for a discussion of the Company s discontinued operations.

The results of operations in the past have been, and in the future may continue to be, materially affected by many factors, including the effect of economic and political conditions and geopolitical events; the effect of market conditions, particularly in the global equity, fixed income, credit and commodities markets, including corporate and mortgage (commercial and residential) lending and commercial real estate markets; the impact of current, pending and future legislation (including the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act)), regulation (including capital, leverage and liquidity requirements), and legal actions in the United States of America (U.S.) and worldwide; the level and volatility of equity, fixed income, and commodity prices and interest rates, currency values and other market indices; the availability and cost of both credit and capital as well as the credit ratings assigned to the Company s unsecured short-term and long-term debt; investor, consumer and business sentiment and confidence in the financial markets; the performance of the Company s acquisitions, joint ventures, strategic alliances or other strategic arrangements (including Mitsubishi UFJ Financial Group, Inc. (MUFG)); the Company s reputation; inflation, natural disasters and acts of war or terrorism; the actions and initiatives of current and potential competitors as well as governments, regulators and self-regulatory organizations; the effectiveness of the Company s risk management policies; and technological changes; or a combination of these or other factors. In addition, legislative, legal and regulatory developments related to the Company s businesses are likely to increase costs, thereby affecting results of operations. These factors also may have an adverse impact on the Company s ability to achieve its strategic objectives. For a further discussion of these and other important

Table of Contents

factors that could affect the Company s business, see Business Competition and Business Supervision and Regulation in Part I, Item 1, and Risk Factors in Part I, Item 1A of the Company s Annual Report on Form 10-K for the year ended December 31, 2012 (the Form 10-K), and Other Matters herein.

The discussion of the Company s results of operations below may contain forward-looking statements. These statements, which reflect management s beliefs and expectations, are subject to risks and uncertainties that may cause actual results to differ materially. For a discussion of the risks and uncertainties that may affect the Company s future results, please see Forward-Looking Statements immediately preceding Business Competition and Business Supervision and Regulation in Part I, Item 1, Risk Factors in Part I, Item 1A, and Executive Summary Significant Items in Part II, Item 7 of the Form 10-K and Other Matters herein.

Executive Summary.

Financial Information and Statistical Data (dollars in millions, except where noted and per share amounts).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net revenues:				
Institutional Securities(1)	$ 4,346	$ 3,332	$ 8,435	$ 6,467
Wealth Management(1)	3,531	3,196	7,001	6,487
Investment Management	673	456	1,318	989
Intersegment Eliminations	(47)	(42)	(93)	(77)
Consolidated net revenues	$ 8,503	$ 6,942	$ 16,661	$ 13,866
Net income	$ 1,191	$ 750	$ 2,422	$ 884
Net income applicable to redeemable noncontrolling interests(2)	100		222	
Net income applicable to nonredeemable noncontrolling interests(2)	111	159	258	387
Net income applicable to Morgan Stanley	$ 980	$ 591	$ 1,942	$ 497
Income from continuing operations applicable to Morgan Stanley:				
Institutional Securities(1)	$ 582	$ 374	$ 1,223	$ 72
Wealth Management(1)	326	178	582	376
Investment Management	101	14	185	39
Intersegment Eliminations		(4)		(4)
Income from continuing operations applicable to Morgan Stanley	$ 1,009	$ 562	$ 1,990	$ 483
Amounts applicable to Morgan Stanley:				
Income from continuing operations applicable to Morgan Stanley	$ 1,009	$ 562	$ 1,990	$ 483
Net gain (loss) from discontinued operations applicable to Morgan Stanley(3)	(29)	29	(48)	14
Net income applicable to Morgan Stanley	$ 980	$ 591	$ 1,942	$ 497
Earnings applicable to Morgan Stanley common shareholders	$ 803	$ 564	$ 1,739	$ 446
Earnings per basic common share:				
Income from continuing operations	$ 0.44	$ 0.28	$ 0.94	$ 0.23
Net gain (loss) from discontinued operations(3)	(0.02)	0.02	(0.03)	0.01
Earnings per basic common share(4)	$ 0.42	$ 0.30	$ 0.91	$ 0.24

Earnings per diluted common share:				
Income from continuing operations	$ 0.43	$ 0.28	$ 0.92	$ 0.23
Net gain (loss) from discontinued operations(3)	(0.02)	0.01	(0.03)	
Earnings per diluted common share(4)	$ 0.41	$ 0.29	$ 0.89	$ 0.23
Regional net revenues:				
Americas	$ 6,014	$ 5,104	$ 11,970	$ 9,888
Europe, Middle East and Africa	1,132	977	2,198	2,126
Asia	1,357	861	2,493	1,852
Net revenues	$ 8,503	$ 6,942	$ 16,661	$ 13,866

101

Table of Contents

Financial Information and Statistical Data (dollars in millions, except where noted and per share amounts) (Continued).

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Average common equity (dollars in billions):				
Institutional Securities	$ 38.3	$ 29.3	$ 39.2	$ 29.5
Wealth Management	13.3	13.3	13.3	13.3
Investment Management	2.8	2.5	2.8	2.5
Parent capital	7.1	16.3	5.9	15.7
Consolidated average common equity	$ 61.5	$ 61.4	$ 61.2	$ 61.0
Return on average common equity(5):				
Institutional Securities	5.9%	4.8%	6.0%	0.2%
Wealth Management	5.2%	5.2%	6.4%	5.6%
Investment Management	14.0%	2.1%	13.0%	3.0%
Consolidated	5.4%	3.5%	5.8%	1.4%
Book value per common share(6)	$ 31.48	$ 31.02	$ 31.48	$ 31.02
Tangible common equity(7)	$ 51,479	$ 54,765	$ 51,479	$ 54,765
Return on average tangible common equity from continuing operations(8)	6.3%	3.9%	6.7%	1.6%
Tangible book value per common share(9)	$ 26.27	$ 27.70	$ 26.27	$ 27.70
Effective income tax rate from continuing operations(10)	31.3%	23.9%	26.4%	24.4%
Worldwide employees at June 30, 2013 and 2012	55,610	58,627	55,610	58,627
Global liquidity reserve held by the bank and non-bank legal entities at June 30, 2013 and 2012 (dollars in billions)(11)	$ 181	$ 173	$ 181	$ 173
Average global liquidity reserve (dollars in billions)(11):				
Bank legal entities	$ 65	$ 63	$ 68	$ 63
Non-bank legal entities	119	113	118	114
Total average global liquidity reserve	$ 184	$ 176	$ 186	$ 177
Long-term borrowings at June 30, 2013 and 2012	$ 161,098	$ 167,828	$ 161,098	$ 167,828
Maturities of long-term borrowings outstanding at June 30, 2013 and 2012 (next 12 months)	$ 26,921	$ 25,356	$ 26,921	$ 25,356
Capital ratios at June 30, 2013 and 2012:				
Total capital ratio(12)	14.9%	18.4%	14.9%	18.4%
Tier 1 common capital ratio(12)	11.8%	13.6%	11.8%	13.6%
Tier 1 capital ratio(12)	14.1%	17.2%	14.1%	17.2%
Tier 1 leverage ratio(13)	7.1%	7.1%	7.1%	7.1%
Consolidated assets under management or supervision at June 30, 2013 and 2012 (dollars in billions)(14):				
Investment Management(15)	$ 347	$ 311	$ 347	$ 311
Wealth Management(1)(16)	625	511	625	511
Total	$ 972	$ 822	$ 972	$ 822

Table of Contents

Financial Information and Statistical Data (dollars in millions, except where noted and per share amounts) (Continued).

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Institutional Securities(1):				
Pre-tax profit margin(17)	22%	15%	21%	3%
Wealth Management(1)(16):				
Wealth Management representatives at June 30, 2013 and 2012(18)	16,321	16,478	16,321	16,478
Annualized revenues per representative (dollars in thousands)(19)	$ 866	$ 770	$ 858	$ 775
Assets by client segment at June 30, 2013 and 2012 (dollars in billions):				
$10 million or more	$ 604	$ 519	$ 604	$ 519
$1 million to $10 million	720	681	720	681
Subtotal $1 million or more	1,324	1,200	1,324	1,200
$100,000 to $1 million	410	391	410	391
Less than $100,000	44	44	44	44
Total client assets	$ 1,778	$ 1,635	$ 1,778	$ 1,635
Fee-based client assets as a percentage of total client assets(20)	35%	31%	35%	31%
Client assets per representative(21)	$ 109	$ 99	$ 109	$ 99
Fee-based client asset flows (dollars in billions)(22)	$ 10.0	$ 3.0	$ 25.3	$ 13.2
Bank deposits at June 30, 2013 and 2012 (dollars in billions)(23)	$ 127	$ 112	$ 127	$ 112
Retail locations at June 30, 2013 and 2012	676	722	676	722
Pre-tax profit margin(17)	19%	13%	18%	13%
Investment Management:				
Pre-tax profit margin(17)	24%	9%	26%	17%
Selected management financial measures, excluding DVA(24):				
Net revenues, excluding DVA(24)	$ 8,328	$ 6,592	$ 16,803	$ 15,494
Income from continuing operations applicable to Morgan Stanley, excluding DVA(24)	$ 898	$ 337	$ 2,080	$ 1,712
Income per diluted common share from continuing operations, excluding DVA(24)	$ 0.37	$ 0.16	$ 0.96	$ 0.87
Return on average common equity from continuing operations, excluding DVA(5)	4.6%	2.1%	6.0%	5.6%
Return on average tangible common equity from continuing operations, excluding DVA(8)	5.3%	2.3%	6.9%	6.3%

DVA Debt Valuation Adjustment represents the change in the fair value of certain of the Company s long-term and short-term borrowings resulting from the fluctuation in the Company s credit spreads and other credit factors.

(1) On January 1, 2013, the International Wealth Management business was transferred from the Wealth Management business segment to the Equity division within the Institutional Securities business segment. Accordingly, all results and statistical data have been recast for all periods to reflect the International Wealth Management business as part of the Institutional Securities business segment.
(2) See Notes 2, 3 and 15 to the consolidated financial statements for the year ended December 31, 2012 included in the Form 10-K and Notes 3 and 14 to the condensed consolidated financial statements for information on redeemable and nonredeemable noncontrolling interests.
(3) See Notes 1 and 21 to the condensed consolidated financial statements for information on discontinued operations.
(4) For the calculation of basic and diluted earnings per share (EPS), see Note 15 to the condensed consolidated financial statements.
(5) The calculation of each business segment s return on average common equity uses income from continuing operations applicable to Morgan Stanley less preferred dividends as a percentage of each business segment s average common equity. The return on average common equity from continuing operations is a non-generally accepted accounting principle (non-GAAP) financial measure that the Company considers to be a useful measure to the Company and investors to assess operating performance. The computation of average common equity for each business segment is determined using the Company s Required Capital framework (Required Capital Framework), an internal capital adequacy measure (see Liquidity and Capital Resources Regulatory Requirements Required

Table of Contents

Capital herein). The effective tax rates used in the computation of business segment return on average common equity were determined on a separate legal entity basis. To determine the return on average common equity from continuing operations, excluding the impact of DVA, also a non-GAAP financial measure, both the numerator and the denominator were adjusted to exclude the impact of DVA. The impact of DVA for the quarters ended June 30, 2013 and 2012 was 0.8% and 1.4%, and the impact of DVA for the six months ended June 30, 2013 and 2012 was (0.2)% and (4.2)%, respectively.

(6) Book value per common share equals common shareholders equity of $61,673 million at June 30, 2013 and $61,333 million at June 30, 2012 divided by common shares outstanding of 1,959 million at June 30, 2013 and 1,977 million at June 30, 2012.

(7) Tangible common equity is a non-GAAP financial measure that the Company considers to be a useful measure that the Company and investors use to assess capital adequacy. For a discussion of tangible common equity, see Liquidity and Capital Resources The Balance Sheet herein.

(8) Return on average tangible common equity from continuing operations is a non-GAAP financial measure that the Company considers to be a useful measure that the Company and investors use to assess capital adequacy. The calculation of return on average tangible common equity uses income from continuing operations applicable to Morgan Stanley less preferred dividends as a percentage of average tangible common equity. To determine the return on average tangible common equity from continuing operations, excluding the impact of DVA, also a non-GAAP financial measure, both the numerator and the denominator were adjusted to exclude the impact of DVA. The impact of DVA for the quarters ended June 30, 2013 and 2012 was 1.0% and 1.6%, and the impact of DVA for the six months ended June 30, 2013 and 2012 was (0.2)% and (4.7)%, respectively.

(9) Tangible book value per common share is a non-GAAP financial measure that the Company considers to be a useful measure that the Company and investors use to assess capital adequacy. Tangible book value per common share equals tangible common equity divided by period-end common shares outstanding.

(10) For a discussion of the effective income tax rate, see Overview of the Quarter Ended June 30, 2013 Financial Results and Significant Items Income Tax Items herein.

(11) For a discussion of global liquidity reserve, see Liquidity and Capital Resources Liquidity Risk Management Framework Global Liquidity Reserve herein.

(12) The Company calculates its Tier 1 capital ratio and risk-weighted assets (RWAs) in accordance with the capital adequacy standards for financial holding companies adopted by the Board of Governors of the Federal Reserve System (the Federal Reserve). These standards are based upon a framework described in the International Convergence of Capital Measurement and Capital Standards, July 1988, as amended, also referred to as Basel I. On January 1, 2013, the U.S. banking regulators rules to implement the Basel Committee on Banking Supervision s market risk capital framework amendment, commonly referred to as Basel 2.5 , became effective, which increased the capital requirements for securitizations and correlation trading within the Company s trading book, as well as incorporated add-ons for stressed Value-at-Risk (VaR) and incremental risk requirements (market risk capital framework amendment). The Company s Tier 1 capital ratio and RWAs for the current periods were calculated under this revised framework. The Company s Tier 1 capital ratio and RWAs for prior periods have not been recalculated under this revised framework. For a discussion of Total capital ratio, Tier 1 capital ratio and Tier 1 common capital ratio, see Liquidity and Capital Resources Regulatory Requirements herein.

(13) For a discussion of Tier 1 leverage ratio, see Liquidity and Capital Resources Regulatory Requirements herein.

(14) Revenues and expenses associated with these assets are included in the Company s Wealth Management and Investment Management business segments.

(15) Amounts exclude the Investment Management business segment s proportionate share of assets managed by entities in which it owns a minority stake.

(16) Prior-period amounts have been recast to exclude Quilter & Co. Ltd. (Quilter). See Notes 1 and 21 to the condensed consolidated financial statements for information on discontinued operations.

(17) Pre-tax profit margin is a non-GAAP financial measure that the Company considers to be a useful measure that the Company and investors use to assess operating performance. Percentages represent income from continuing operations before income taxes as a percentage of net revenues.

(18) For the quarters ended June 30, 2013 and 2012, global representatives for the Company are 16,705 and 16,934, which include approximately 384 and 456 representatives associated with the International Wealth Management business, the results of which are reported in the Institutional Securities business segment, respectively.

(19) Annualized revenues per representative for the quarters ended June 30, 2013 and 2012 equal Wealth Management business segment s annualized revenues divided by the average representative headcount for the quarters ended June 30, 2013 and 2012, respectively.

(20) Fee-based client assets represent the amount of assets in client accounts where the basis of payment for services is a fee calculated on those assets. Effective from the quarter ended March 31, 2013, client assets also include certain additional non-custodied assets as a result of the completion of the Morgan Stanley Wealth Management platform conversion.

(21) Client assets per representative equal total period-end client assets divided by period-end representative headcount.

(22) Beginning January 1, 2013, the Company enhanced its definition of fee-based asset flows. Fee-based asset flows have been recast for all periods to include dividends, interest and client fees, and to exclude cash management related activity.

(23) Approximately $70 billion and $58 billion of the bank deposit balances at June 30, 2013 and 2012, respectively, are held at Company-affiliated depositories with the remainder held at Citigroup Inc. (Citi) affiliated depositories. These deposit balances are held at certain of the Company s Federal Deposit Insurance Corporation (the FDIC) insured depository institutions for the benefit of the Company s clients through their accounts. For additional information regarding deposits, see Liquidity and Capital Resources Funding Management Deposits herein and Notes 3 and 22 to the condensed consolidated financial statements.

Table of Contents

(24) From time to time, the Company may disclose certain non-GAAP financial measures in the course of its earnings releases, earnings conference calls, financial presentations and otherwise. For these purposes, GAAP refers to generally accepted accounting principles in the U.S. The U.S. Securities and Exchange Commission defines a non-GAAP financial measure as a numerical measure of historical or future financial performance, financial positions, or cash flows that excludes or includes amounts or is subject to adjustments that effectively exclude, or include, amounts from the most directly comparable measure calculated and presented in accordance with GAAP. Non-GAAP financial measures disclosed by the Company are provided as additional information to investors in order to provide them with further transparency about, or an alternative method for assessing, our financial condition and operating results. These measures are not in accordance with, or a substitute for, GAAP, and may be different from or inconsistent with non-GAAP financial measures used by other companies. Whenever the Company refers to a non-GAAP financial measure, the Company will also generally present the most directly comparable financial measure calculated and presented in accordance with GAAP, along with a reconciliation of the differences between the non-GAAP financial measure and the GAAP financial measure.

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Reconciliation of Selected Management Financial Measures from a Non-GAAP to a GAAP Basis (dollars in millions, except per share amounts):				
Net revenues				
Net revenues Non-GAAP	$ 8,328	$ 6,592	$ 16,803	$ 15,494
Impact of DVA	175	350	(142)	(1,628)
Net revenues GAAP	$ 8,503	$ 6,942	$ 16,661	$ 13,866
Income (loss) from continuing operations applicable to Morgan Stanley				
Income applicable to Morgan Stanley Non-GAAP	$ 898	$ 337	$ 2,080	$ 1,712
Impact of DVA	111	225	(90)	(1,229)
Income (loss) applicable to Morgan Stanley GAAP	$ 1,009	$ 562	$ 1,990	$ 483
Earnings (loss) per diluted common share				
Income per diluted common share from continuing operations Non-GAAP	$ 0.37	$ 0.16	$ 0.96	$ 0.87
Impact of DVA	0.06	0.12	(0.04)	(0.64)
Income (loss) per diluted common share from continuing operations GAAP	$ 0.43	$ 0.28	$ 0.92	$ 0.23
Average diluted shares Non-GAAP (in millions)	1,951	1,912	1,946	1,907
Impact of DVA (in millions)				
Average diluted shares GAAP (in millions)	1,951	1,912	1,946	1,907

Table of Contents

Global Market and Economic Conditions.

During the six months ended June 30, 2013 global market and economic conditions improved modestly from 2012 year-end. The U.S. economy continued to grow moderately despite payroll and income tax increases that were implemented in January. Europe remained in recession, but market strains associated with the European financial crisis continued to ease after temporary concerns that were raised by election results in Italy and developments in Cyprus subsided. Despite these improvements, global market and economic conditions continued to be challenged by investor concerns about the scaling back of the U.S. monetary policy, the remaining European sovereign debt issues, the need to raise the U.S. federal debt ceiling and reduce government spending, and slowing economic growth in emerging markets.

In the U.S., major equity market indices ended the second quarter and the first six months of 2013 higher compared with the beginning of the quarter and the year, primarily due to improved investor confidence about the U.S. economy and dissipated concerns about the fiscal cliff (*i.e.*, the combination of expiring tax cuts and spending cuts on or after January 1, 2013). The U.S. economy continued its moderate growth pace in the first six months of 2013. A shrinking labor force helped push the unemployment rate down to 7.6% in June 2013 from 7.8% at 2012 year-end. Residential real estate markets strengthened, and home prices rose amid falling inventories across much of the country during the first six months of 2013, but investments in commercial real estate projects remained challenged. Consumer spending improved during the first six months of 2013 despite lower after-tax household income, but business investment spending growth moderated. Energy price volatility boosted consumer price inflation early in the year, but underlying inflation excluding food and energy slowed to near historical lows. The Federal Open Market Committee (FOMC) of the Federal Reserve kept key interest rates at historically low levels. At June 30, 2013, the federal funds target rate remained between 0.0% and 0.25% and the discount rate remained at 0.75%. In June 2013, the FOMC decided to continue purchasing U.S. Treasury securities and agency mortgage-backed securities until the job market improves substantially and also continued to anticipate that key interest rates will remain exceptionally low until the unemployment rate falls to 6.5% or lower, as long as medium-term inflation expectations remain below 2.5%. However, since the end of May 2013, concerns about the Federal Reserve s plan to scale back its stimulus plan later this year caused investors to sell off significant amounts of stocks and bonds, resulting in the rapid increase in interest rates. Addressing the recent market volatility, in July 2013, the chairman of the Federal Reserve reiterated that the U.S. economy continues to need a highly accommodative monetary policy.

In Europe, major equity market indices, except for FTSE 100 index in the United Kingdom, ended the second quarter of 2013 either higher or flat compared with the beginning of the quarter. At June 30, 2013, major European equity market indices were higher compared with the beginning of the year, primarily due to investors optimism about Europe s progress in addressing its sovereign debt issues. In the euro-area, the unemployment rate increased to a record 12.1% in June 2013 from 11.7% at 2012 year-end. At June 30, 2013, Bank of England s (BOE) benchmark interest rate was 0.5%, which was unchanged from December 31, 2012. To stimulate economic activity in Europe, in early May 2013 the European Central Bank lowered the benchmark interest rate from 0.75% to 0.5% and indicated it will keep open its special liquidity facilities until at least the middle of 2014. Euro-area manufacturing expanded in July 2013 for the first time in two years, led by Germany, signaling the euro-zone economy is emerging from recession.

Major equity market indices in Asia, except for the indices in China, ended the first quarter and the first six months of 2013 higher compared with the beginning of the year. Japan s economic activities started to pick up in the second quarter of 2013, primarily resulting from a series of economic stimulus packages announced by the Japanese government and the Bank of Japan in early 2013. Japan s benchmark interest rate remained within a range of zero to 0.1% in the first half of 2013. China s gross domestic product growth continued to slow during the first six months of 2013 as exports and domestic spending weakened, adding pressure on China to restructure its economy toward more sustainable growth driven by domestic consumption from reliance on exports and investments.

Table of Contents

Overview of the Quarter and Six Months Ended June 30, 2013 Financial Results.

Consolidated Results. The Company recorded net income applicable to Morgan Stanley of $980 million on net revenues of $8,503 million during the quarter ended June 30, 2013 (current quarter) compared with net income applicable to Morgan Stanley of $591 million on net revenues of $6,942 million during the quarter ended June 30, 2012 (prior year quarter).

Net revenues in the current quarter included positive revenues due to the impact of DVA of $175 million compared with positive revenues of $350 million in the prior year quarter. Non-interest expenses increased 12% to $6,728 million in the current quarter compared with $6,005 million in the prior year quarter. Compensation expenses increased 13% to $4,105 million in the current quarter compared with $3,631 million in the prior year quarter. Non-compensation expenses increased 10% to $2,623 million in the current quarter compared with $2,374 million in the prior year quarter.

Earnings per diluted common share (diluted EPS) and diluted EPS from continuing operations were $0.41 and $0.43 in the current quarter, respectively, compared with $0.29 and $0.28, respectively, in the prior year quarter. The EPS calculation for the current quarter included a negative adjustment of approximately $151 million, or $0.08 per diluted share, related to the previously announced purchase of the remaining interest in the Morgan Stanley Smith Barney Holdings LLC (Wealth Management JV), which was completed in June 2013.

Excluding the impact of DVA, net revenues were $8,328 million and diluted EPS from continuing operations were $0.37 per share in the current quarter, compared with $6,592 million and $0.16 per share, respectively, in the prior year quarter.

For the six months ended June 30, 2013, the Company recorded net income applicable to Morgan Stanley of $1,942 million on net revenues of $16,661 million, compared with net income applicable to Morgan Stanley of $497 million on net revenues of $13,866 million in the six months ended June 30, 2012. Non-interest expenses increased 5% to $13,304 million from the prior year period. Diluted EPS and diluted EPS from continuing operations were $0.89 and $0.92 in the six months ended June 30, 2013, compared with $0.23 and $0.23, respectively, in the prior year period.

The Company s effective tax rate from continuing operations was 31.3% and 23.9% for the quarters ended June 30, 2013 and 2012, respectively. The Company s effective tax rate from continuing operations was 26.4% and 24.4% for the six months ended June 30, 2013 and 2012, respectively. The results for the six months ended June 30, 2013 included a discrete net tax benefit of $142 million due to the retroactive effective date of the American Taxpayer Relief Act of 2012 (the Relief Act) and remeasurement of reserves and related interest based on new information regarding the status of certain tax authority examinations. Excluding these discrete net tax benefits, the annual effective tax rate for the six months ended June 30, 2013 would have been 30.7%. The increase in the effective tax rate is primarily reflective of the geographic mix of earnings. For further discussion of the discrete net tax benefit, see Executive Summary Significant Items Income Tax Items herein.

During the quarter ended June 30, 2012, the Company completed the sale of Quilter, its retail wealth management business in the U.K., resulting in a pre-tax gain of $108 million. In addition, the first phase of the asset sale of Saxon closed on April 2, 2012. The results of Quilter (reported in the Wealth Management business segment) and Saxon (reported in the Institutional Securities business segment) are presented as discontinued operations for all periods presented. Discontinued operations were a net gain (loss) of $(29) million and $37 million for the quarters ended June 30, 2013 and 2012, respectively, and a net gain (loss) of $(48) million and $23 million in the six months ended June 30, 2013 and 2012, respectively.

Institutional Securities. Income from continuing operations before taxes was $960 million in the current quarter compared with income from continuing operations before taxes of $488 million in the prior year quarter. Net revenues for the current quarter were $4,346 million compared with $3,332 million in the prior year quarter. The results in the current quarter included positive revenues due to the impact of DVA of $175 million compared with positive revenues of $350 million in the prior year quarter. Investment banking revenues for the current quarter increased 22% to $1,078 million from the prior year quarter, reflecting higher revenues from advisory transactions and equity and fixed income underwriting transactions. The following sales and trading net revenues results exclude the impact of DVA. The presentation of net revenues excluding the impact of DVA is a non-GAAP financial measure that the Company considers useful for the Company and investors to allow further comparability of period-to-period operating performance. See Business Segments Institutional Securities Sales and Trading Net Revenues for more information. Equity sales and trading net revenues, excluding the impact of DVA, of $1,806 million increased 44% from the prior year quarter, reflecting strong performance across all products and regions, with particular strength in derivatives. Excluding the impact of DVA, fixed income and commodities sales and trading net revenues were $1,153 million in the current quarter, an increase of 50% from the prior year quarter, reflecting the combination of higher revenues in foreign exchange products and commodities and that the prior year quarter was negatively impacted by period specific charges representing credit valuation allowances and other related adjustments (see Executive Summary Significant Items Rating Agency Downgrade herein). Other sales and trading net losses were $57 million in the current quarter compared with net losses of $12 million in the prior year quarter, primarily due to losses on economic hedges and other costs related to the Company s long-term debt and costs related to the amount of liquidity held (negative carry), partially offset by net gains associated with loans and lending commitments. Other revenues of $140 million were recognized in the current quarter compared with other revenues of $41 million in the prior year quarter. The results included income arising from the Company s 40% stake in Mitsubishi UFJ Morgan Stanley Securities Co., Ltd. (MUMSS) (see Executive Summary Significant Items Japanese Securities Joint Venture herein). Non-interest expenses increased 19% to $3,386 million in the current quarter, primarily due to both higher compensation and non-compensation expenses. Compensation and benefits expenses in the current quarter were $1,766 million compared with $1,506 million in the prior year quarter, due to higher net revenues. Non-compensation expenses were $1,620 million in the current quarter compared with $1,338 million in the prior year quarter reflecting increased litigation accruals and higher volume-driven expenses.

Wealth Management. Income from continuing operations before taxes was $655 million in the current quarter compared with $410 million in the prior year quarter. Net revenues were $3,531 million in the current quarter compared with $3,196 million in the prior year quarter. Transactional revenues, consisting of Commissions and fees, Trading and Investment banking increased 15% to $1,048 million from the prior year quarter. Trading revenues increased 18% to $223 million in the current quarter from the prior year quarter, primarily due to higher gains related to positions associated with certain employee deferred compensation plans and higher revenues from structured notes. Commissions and fees revenues increased 14% to $567 million in the current quarter from the prior year quarter, primarily due to higher equity and mutual fund activity. Investment banking revenues increased 16% to $258 million in the current quarter from the prior year quarter, primarily due to higher revenues from closed-end funds. Asset management, distribution and administration fees increased 4% to $1,896 million in the current quarter from the prior year quarter, primarily due to higher fee-based revenues, partially offset by lower revenues from the bank deposit program and managed futures. Net interest increased 17% to $446 million in the current quarter from the prior year quarter, primarily resulting from higher revenues from the bank deposit program, higher interest from securities based lending and higher interest on the available for sale portfolio, partially offset by lower customer margin receivables. Total client asset balances were $1,778 billion at June 30, 2013 and client assets in fee-based accounts were $629 billion, or 35% of total client assets. Fee-based client asset flows for the current quarter were $10 billion compared with $3 billion in the prior year quarter. Prior period amounts have been recast to reflect the transfer of the International Wealth Management business from the Wealth Management business segment to the Institutional Securities business segment and for the Company s enhanced definition of fee-based asset flows (see Business Segments herein). Compensation and benefit expenses increased 7% to $2,042 million in the current quarter from the prior year quarter, primarily due to higher compensable revenues. Non-compensation expenses decreased 5% to $834 million in the current quarter from the prior year quarter, partially driven by the absence of platform integration costs.

Investment Management. Income from continuing operations before taxes was $160 million in the current quarter compared with $43 million in the prior year quarter. Net revenues were $673 million in the current quarter compared with $456 million in the prior year quarter. The increase in net revenues reflected higher net

Table of Contents

gains predominantly within the Company s Merchant Banking investments, as well as higher gains within Traditional Asset Management and Real Estate Investing. Non-interest expenses were $513 million in the current quarter compared with $413 million in the prior year quarter. Compensation and benefits expenses increased 39% to $297 million in the current quarter, primarily due to higher net revenues. Non-compensation expenses increased 9% to $216 million in the current quarter, primarily due to higher brokerage and clearing expenses.

Significant Items.

Wealth Management JV. The Company completed the purchase of the remaining 35% interest in the Wealth Management JV from Citi on June 28, 2013 for the previously established price of $4.725 billion. The Company recorded a negative adjustment to retained earnings of approximately $151 million (net of tax) to reflect the difference between the purchase price for the 35% redeemable noncontrolling interest in the joint venture and its carrying value.

Litigation Accruals. During the quarter and six months ended June 30, 2013, the Company increased litigation accruals by approximately $199 million and $270 million, respectively, compared with increases of approximately $4 million and $21 million, during the quarter and six months ended June 30, 2012, respectively. Changes to litigation accruals are included in Other non-interest expenses in the condensed consolidated statements of income.

Available for Sale Securities. During the quarters ended June 30, 2013 and 2012, the available for sale portfolio held within the Wealth Management segment reported unrealized gains (losses) of $(342) million and $41 million, net of tax, respectively. During the six months ended June 30, 2013 and 2012, the Company reported unrealized gains (losses) of $(369) million and $22 million, net of tax, respectively, included in Accumulated other comprehensive income. These losses in 2013 were due to rising interest rates during the quarter ended June 30, 2013.

Severance Costs. In the quarter and six months ended June 30, 2013, the Company incurred severance costs of approximately $32 million and $164 million, respectively, and approximately $15 million and $153 million, in the quarter and six months ended June 30, 2012, respectively, associated with reduction in force events which are included in Compensation and benefits expenses in the condensed consolidated statements of income.

Corporate Lending. The Company recorded the following amounts primarily associated with loans and lending commitments within the Institutional Securities business segment (see Business Segments Institutional Securities herein):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(dollars in millions)			
Other sales and trading:				
Gains on loans and lending commitments and Net interest	$ 149	$ 38	$ 403	$ 823
Gains (losses) on hedges	(30)	91	(79)	(546)
Total Other sales and trading revenues	$ 119	$ 129	$ 324	$ 277
Other revenues:				
Provision for loan losses	$ 1	$ (44)	$ (27)	$ (52)
Losses on loans held for sale	(39)	(14)	(31)	(20)
Total Other revenues	$ (38)	$ (58)	$ (58)	$ (72)
Other expenses: Provision for unfunded commitments	(17)	(15)	(29)	(9)
Total	$ 64	$ 56	$ 237	$ 196

Income Tax Items. The Company s effective tax rate from continuing operations for the six months ended June 30, 2013 included a discrete tax benefit of $81 million due to the retroactive effective date of the Relief Act. The Relief Act that was enacted on January 2, 2013, among other things, extended with retroactive effect to

Table of Contents

January 1, 2012 a provision of U.S. tax law that defers the imposition of tax on certain active financial services income of certain foreign subsidiaries earned outside of the U.S. until such income is repatriated to the U.S. as a dividend. Additionally, the Company s effective tax rate from continuing operations for the six months ended June 30, 2013 included a discrete net tax benefit of $61 million associated with remeasurement of reserves and related interest based on new information regarding the status of certain tax authority examinations.

Japanese Securities Joint Venture. During the quarters ended June 30, 2013 and 2012, the Company recorded income of $174 million and $54 million, respectively, within Other revenues in the condensed consolidated statements of income, arising from the Company s 40% stake in MUMSS, and income of $299 million and $81 million for the six months ended June 30, 2013 and 2012, respectively. Net income applicable to nonredeemable noncontrolling interests associated with MUFG s interest in Morgan Stanley MUFG Securities Co., Ltd. (MSMS) was $82 million and $49 million for the quarters ended June 30, 2013 and 2012, respectively, and $172 million and $130 million for the six months ended June 30, 2013 and 2012, respectively (see Note 20 to the condensed consolidated financial statements).

Rating Agency Downgrade. On June 21, 2012, as a result of one rating agency s downgrade of the Company s long-term and short-term debt ratings, the amount of additional collateral requirements or other payments that could have been called by counterparties, exchanges or clearing organizations under the terms of certain over-the-counter (OTC) trading agreements and certain other agreements was approximately $6.3 billion, of which $2.9 billion was called and posted at June 30, 2012. Additionally, the Company incurred period specific charges of approximately $225 million representing credit valuation allowances, novations and other contractual adjustments in Trading revenues in the condensed consolidated statement of income in the quarter and six months ended June 30, 2012.

Table of Contents

Business Segments.

Substantially all of the Company s operating revenues and operating expenses are allocated to its business segments. Certain revenues and expenses have been allocated to each business segment, generally in proportion to its respective net revenues, non-interest expenses or other relevant measures.

Effective with the quarter ended June 30, 2013, the Global Wealth Management Group and Asset Management business segments were re-titled Wealth Management and Investment Management, respectively.

As a result of treating certain intersegment transactions as transactions with external parties, the Company includes an Intersegment Eliminations category to reconcile the business segment results to the Company s consolidated results. Intersegment Eliminations also reflect the effect of fees paid by the Institutional Securities business segment to the Wealth Management business segment related to the bank deposit program. The Company did not recognize any gains or losses from continuing operations before income taxes in Intersegment Elimination in the quarter and six months ended June 30, 2013. Losses from continuing operations before income taxes recorded in Intersegment Eliminations were $4 million in both the quarter and six months ended June 30, 2012.

On January 1, 2013, the International Wealth Management business was transferred from the Wealth Management business segment to the Equity division within the Institutional Securities business segment. Accordingly, all results and statistical data have been recast for all periods to reflect the International Wealth Management business as part of the Institutional Securities business segment.

Net Revenues.

Trading. Trading revenues include revenues from customers purchases and sales of financial instruments in which the Company acts as a market maker and gains and losses on the Company s related positions. Trading revenues include the realized gains and losses from sales of cash instruments and derivative settlements, unrealized gains and losses from ongoing fair value changes of the Company s positions related to market-making activities, and gains and losses related to investments associated with certain employee deferred compensation plans. In many markets, the realized and unrealized gains and losses from the purchase and sale transactions will include any spreads between bids and offers. Certain fees received on loans carried at fair value and dividends from equity securities are also recorded in this line item since they relate to market-making positions. Commissions received for purchasing and selling listed equity securities and options are recorded separately in the Commissions and fees line item. Other cash and derivative instruments typically do not have fees associated with them, and fees for related services would be recorded in Commissions and fees.

The Company often invests directly, as a principal, in investments or other financial instruments to economically hedge its obligations under its deferred compensation plans. Changes in value of such investments made by the Company are recorded in Trading revenues and Investments revenues. Expenses associated with the related deferred compensation plans are recorded in Compensation and benefits. Compensation expense is calculated based on the notional value of the award granted, adjusted for upward and downward changes in fair value of the referenced investment and is recognized ratably over the prescribed vesting period for the award. Generally, changes in compensation expense resulting from changes in fair value of the referenced investment will be offset by changes in fair value of investments made by the Company. However, there may be a timing difference between the immediate revenue recognition of gains and losses on the Company s investments and the deferred recognition of the related compensation expense over the vesting period.

As a market maker, the Company stands ready to buy, sell or otherwise transact with customers under a variety of market conditions and provide firm or indicative prices in response to customer requests. The Company s liquidity obligations can be explicit and obligatory in some cases, and in others, customers expect the Company to be willing to transact with them. In order to most effectively fulfill its market-making function, the Company

Table of Contents

engages in activities, across all of its trading businesses, that include, but are not limited to: (i) taking positions in anticipation of, and in response to, customer demand to buy or sell and depending on the liquidity of the relevant market and the size of the position holding those positions for a period of time; (ii) managing and assuming basis risk (risk associated with imperfect hedging) between customized customer risks and the standardized products available in the market to hedge those risks; (iii) building, maintaining and rebalancing inventory, through trades with other market participants, and engaging in accumulation activities to accommodate anticipated customer demand; (iv) trading in the market to remain current on pricing and trends; and (v) engaging in other activities to provide efficiency and liquidity for markets. Interest income and expense are also impacted by market-making activities as debt securities held by the Company earn interest and securities are loaned, borrowed, sold with agreement to repurchase and purchased with agreement to resell.

Investments. The Company s investments generally are held for long-term appreciation and generally are subject to significant sales restrictions. Estimates of the fair value of the investments may involve significant judgment and may fluctuate significantly over time in light of business, market, economic and financial conditions generally or in relation to specific transactions. In some cases, such investments are required or are a necessary part of offering other products. The revenues recorded are the result of realized gains and losses from sales and unrealized gains and losses from ongoing fair value changes of the Company s holdings as well as from investments associated with certain employee deferred compensation plans (as mentioned in the paragraph above). Typically, there are no fee revenues from these investments. The sales restrictions on the investments relate primarily to redemption and withdrawal restrictions on investments in real estate funds, hedge funds and private equity funds, which include investments made in connection with certain employee deferred compensation plans (see Note 4 to the condensed consolidated financial statements). Restrictions on interests in exchanges and clearinghouses generally include a requirement to hold those interests for the period of time that the Company is clearing trades on that exchange or clearinghouse. Additionally, there are certain investments related to assets held by consolidated real estate funds, which are primarily related to holders of noncontrolling interests.

Commissions and Fees. Commission and fee revenues primarily arise from agency transactions in listed and OTC equity securities, services related to sales and trading activities, and sales of mutual funds, futures, insurance products and options.

Asset Management, Distribution and Administration Fees. Asset management, distribution and administration fees include fees associated with the management and supervision of assets, account services and administration, performance-based fees relating to certain funds, separately managed accounts, shareholder servicing and the distribution of certain open-ended mutual funds.

Asset management, distribution and administration fees in the Wealth Management business segment also include revenues from individual investors electing a fee-based pricing arrangement and fees for investment management. Mutual fund distribution fees in the Wealth Management business segment are based on either the average daily fund net asset balances or average daily aggregate net fund sales and are affected by changes in the overall level and mix of assets under management or supervision.

Asset management fees in the Investment Management business segment arise from investment management services the Company provides to investment vehicles pursuant to various contractual arrangements. The Company receives fees primarily based upon mutual fund daily average net assets or based on monthly or quarterly invested equity for other vehicles. Performance-based fees in the Investment Management business segment are earned on certain funds as a percentage of appreciation earned by those funds and, in certain cases, are based upon the achievement of performance criteria. These fees are normally earned annually and are recognized on a monthly or quarterly basis.

Net Interest. Interest income and Interest expense are a function of the level and mix of total assets and liabilities, including trading assets and trading liabilities, securities available for sale, securities borrowed or purchased under agreements to resell, securities loaned or sold under agreements to repurchase, loans, deposits, commercial paper and other short-term borrowings, long-term borrowings, trading strategies, customer activity in the Company s prime brokerage business, and the prevailing level, term structure and volatility of interest rates. Certain Securities purchased under agreements to resell (reverse repurchase agreements) and Securities sold under agreements to repurchase (repurchase agreements) and Securities borrowed and Securities loaned transactions may be entered into with different customers using the same underlying securities, thereby generating a spread between the interest revenue on the reverse repurchase agreements or securities borrowed transactions and the interest expense on the repurchase agreements or securities loaned transactions.

Table of Contents

INSTITUTIONAL SECURITIES

INCOME STATEMENT INFORMATION

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012(1)	2013	2012(1)
	(dollars in millions)			
Revenues:				
Investment banking	$ 1,078	$ 884	$ 2,023	$ 1,735
Trading	2,598	2,287	5,012	4,362
Investments	51	46	193	(3)
Commissions and fees	650	544	1,259	1,150
Asset management, distribution and administration fees	69	61	135	113
Other	140	41	277	92
Total non-interest revenues	4,586	3,863	8,899	7,449
Interest income	1,029	964	2,053	2,141
Interest expense	1,269	1,495	2,517	3,123
Net interest	(240)	(531)	(464)	(982)
Net revenues	4,346	3,332	8,435	6,467
Compensation and benefits	1,766	1,506	3,658	3,709
Non-compensation expenses	1,620	1,338	3,019	2,599
Total non-interest expenses	3,386	2,844	6,677	6,308
Income from continuing operations before income taxes	960	488	1,758	159
Provision for (benefit from) income taxes	288	69		