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MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

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Report and financial statements

31 December 2018

MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

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MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

STRATEGIC REPORT

The Directors present their Strategic report for Morgan Stanley Investment Management (ACD) Limited (the "Company") for the year ended 31 December 2018.

INTRODUCTION

The principal activity of the Company is the provision of authorised corporate director services to United Kingdom ("UK") authorised open-ended investment companies ("OEICs") and to act as the management company for the undertakings for collective investments in transferable securities ("UCITS") and alternative investment funds ("AIF").

There have not been any significant changes in the Company's principal activity in the year under review. As described in note 25, in relation to the Morgan Stanley Group's preparation for the UK withdrawal from the European Union ("EU"), on 1 January 2019 MSIM Fund Management (Ireland) Limited, another Morgan Stanley Group undertaking, was appointed to the role of UCITS management company by Morgan Stanley Investment Funds and Morgan Stanley Liquidity Funds, and to the role of Alternative Investment Fund Manager ("AIFM") by Galaxy Fund and Alpha Plus Funds plc.

Following this appointment, the Company no longer acts as management company for these funds, but continues to provide authorised corporate director services to UK authorised OEICs, being the Morgan Stanley Funds (UK).

The Company is authorised and regulated by the Financial Conduct Authority ("FCA").

The Company's ultimate parent undertaking and controlling entity is Morgan Stanley, which, together with the Company and Morgan Stanley's other subsidiary undertakings, form the "Morgan Stanley Group".

BUSINESS REVIEW

Global market and economic conditions

Global economic growth was strong at 3.7% in 2018. Global growth was strong at 4.0% in the first half of the year before slowing to 3.6% in the second half. Growth accelerated in the United States ("US") at 2.9% for the year as a whole. However, in the rest of the world, growth weakened considerably, particularly in the second half. A combination of lingering trade tensions, a slowdown in China and its spillovers, and a backdrop of tighter US Federal Reserve policy, even as global growth began to soften and the associated tightening of financial conditions weighed on sentiment and economic activity. Global growth was also held back by slower growth in the Euro area and Japan, which in turn were weighed down by factors such as a switch in emission standards in Germany and natural disasters in Japan. In terms of policy, the US Federal Reserve continued to hike interest rates by a further 100bps and continued its balance sheet normalisation process. In Europe, the European Central Bank ("ECB") halved the size of its quantitative easing ("QE") program to monthly purchases of €15bn after September, and ended the QE program after December. Policymakers in China intensified its easing measures by cutting taxes and boosting infrastructure spending as labour market pressures began to build. Since November, the US Federal Reserve has begun to signal policy flexibility in response to a deteriorating growth outlook. Other major central banks have also begun to guide for a more dovish policy outlook in early 2019 following the weaker than expected growth momentum in the fourth quarter of 2018.

UK withdrawal from the EU

On 23 June 2016, the UK electorate voted to leave the EU. On 29 March 2017, the UK invoked Article 50 of the Lisbon Treaty which triggered a two-year period, subject to extension (which would need the unanimous approval of the EU Member States), during which the UK government negotiated a form of withdrawal agreement with the EU.

BUSINESS REVIEW (CONTINUED)

UK withdrawal from the EU (continued)

On 22 March 2019, the UK and the other EU Member States agreed to an extension of the two-year period to 22 May 2019, (if the UK Parliament approved the withdrawal agreement by 29 March 2019) or 12 April 2019 (if it did not). On 11 April 2019, the UK and the other EU Member States agreed to a further extension to 31 October 2019 (or, if the Withdrawal Agreement is ratified by both parties before this date, until the first day of the following month). This further extension ceases to apply on 31 May 2019 in the event that the UK has not held elections to the European Parliament in accordance with applicable EU law and has not ratified the Withdrawal Agreement by 22 May 2019. Absent any further changes to this time schedule, the UK is expected to leave the EU by 31 October 2019 at the latest.

The proposed withdrawal agreement includes a transition period until December 2020 and provides that the UK will leave the EU single market and will seek a phased period of implementation for a new UK-EU relationship that may include the legal and regulatory framework applicable to financial institutions with significant operations in Europe, such as Morgan Stanley.

It is difficult to predict the future of the UK's relationship with the EU, the uncertainty of which may increase the volatility in the global financial markets in the short- and medium-term and may negatively disrupt regional and global financial markets. Additionally, depending on the outcome, such uncertainty may adversely affect the manner in which the Morgan Stanley Group operates certain businesses in Europe.

The withdrawal agreement has been rejected by the UK Parliament on 15 January 2019 and on two subsequent occasions. As a result, the terms and conditions of the anticipated withdrawal from the EU remain uncertain. Discussions are ongoing within the UK Parliament on the negotiated withdrawal agreement and the alternatives to it, and between the UK Government and the EU.

The ongoing political uncertainty in relation to the proposed withdrawal agreement in the UK means there is a risk that these arrangements may not be ready for implementation by 31 October 2019 or that there will be no transition period. Potential effects of the UK exit from the EU and potential mitigation actions may vary considerably depending on the timing of withdrawal, the nature of any transition, implementation or successor arrangements, and the future trading arrangements between the UK and the EU.

If the withdrawal agreement (or any alternative agreement) is not agreed and as a result no transition period applies, Morgan Stanley's UK licensed entities may be unable to rely on EU passporting rights to provide services in a number of EU jurisdictions from the date the UK leaves the EU, absent further regulatory relief. Even if a transition period is agreed, Morgan Stanley's UK licensed entities may lose their rights to provide services in a number of EU jurisdictions after such transition period unless the new UK-EU relationship provides for such rights.

The Morgan Stanley Group is continuing to prepare its European operations to be able to do business with its clients in the EU regardless of whether or not a withdrawal or transition agreement is reached. Changes are being made to European operations in an effort to ensure that the Morgan Stanley Group can continue to provide cross-border investment management services in EU member states without the need for separate regulatory authorisations in each member state through the use of EU passporting arrangements, which allow for such cross-border activity. In the event that its UK licenced entities are unable to rely on EU passporting rights to provide services, the Morgan Stanley Group will adjust its operations in Europe to be able to carry out activities from within the EU.

These changes include establishment of a new management company in Ireland, MSIM Fund Management (Ireland) Limited ("MSIM FM"), authorised under both the Undertakings for Collective Investment in Transferable Securities Directive and the Alternative Investment Fund Managers Directive. Since 1 January 2019 this entity has acted as management company to the majority of Morgan Stanley's European domiciled funds. In addition an Irish domiciled investment firm, Morgan Stanley Investment Management (Ireland) Limited ("MSIM Ireland"), has been established to provide distribution and separately managed account services to clients where required. Both entities will operate a network of European branches to facilitate provision of services as necessary. MSIM FM established a branch in Luxembourg on 1 January 2019.

STRATEGIC REPORT

BUSINESS REVIEW (CONTINUED)

UK withdrawal from the EU (continued)

The Morgan Stanley Group is continuing to build out the capabilities of these entities, including engagement with clients and local regulators. The Morgan Stanley Group also expects to continue to add personnel to certain existing offices in the EU.

As part of the Morgan Stanley Group's Brexit planning to achieve the strategy mentioned above, the Company has made certain structural changes. On 4 July 2018, the Company transferred its investment in MSIM FM to Morgan Stanley International Limited ("MSI"), the Company's ultimate UK parent undertaking.

As a result of the political uncertainty described above, it is currently unclear what the final post-Brexit structure of European operations will be for the Morgan Stanley Group overall. Given the potential negative disruption to regional and global financial markets, and depending on the extent to which Morgan Stanley may be required to make material changes to European operations beyond those currently planned or executed, results of Morgan Stanley's operations and business prospects could be negatively affected.

In relation to the Company specifically, as described above and in note 25, on 1 January 2019 MSIM FM was appointed to the role of UCITS management company by Morgan Stanley Investment Funds and Morgan Stanley Liquidity Funds (both of which are Luxembourg domiciled funds), and to the role of AIFM by Galaxy Fund (a Luxembourg domiciled fund) and Alpha Plus Funds plc (an Irish domiciled fund). These roles were previously held by the Company. The Company continues to provide authorised corporate director services to the UK authorised OEICs, being the Morgan Stanley Funds (UK) and is expected to remain profitable in respect of the provision of these services.

Key performance indicators

The Board of Directors monitors the results of the Company by reference to a range of performance and risk based metrics, including, but not limited to, the following:

Assets under management

AUM contracted with the Company increased from $95.3 billion to $95.9 billion from 31 December 2017 to 31 December 2018.

Profitability metrics

Return on assets: The Company's return on assets (profit for the year as a percentage of total assets at the end of the financial year) was 3.5% (2017: 3.5%).

Capital

Solvency Ratio: The Company's capital surplus over and above the FCA requirements (as per IPRU 11) was $20.1 million (2017: $15.7 million), giving rise to a solvency ratio of 275% (2017: 229%).

Overview of 2018 Financial Results

The statement of comprehensive income for the year is set out on page 16. The profit after tax for the financial year was $3,989,000 compared to profit after tax of $3,754,000 in 2017.

Fee and commission income increased by $134,920,000 compared to the prior year driven by higher average assets under management ("AUM"). Other expenses have increased by $134,978,000 primarily due to higher Management charges from other Morgan Stanley Group undertakings relating to other services driven by increased sub-delegation expenses as a result of higher average AUM.

The statement of financial position is set out on page 18 of the financial statements. Total assets increased by $6,552,000 to $112,615,000 at 31 December 2018. There was an increase in trade receivables of $10,839,000 compared to the prior year, recognised in 'Trade and other receivables'. This was offset by a decrease in amounts due from other Morgan Stanley Group undertakings of $5,454,000 within 'Loans and advances' and 'Trade and other receivables'.

BUSINESS REVIEW (CONTINUED)

Overview of 2018 Financial Results (continued)

Total liabilities increased by $2,563,000 to $77,006,000 at 31 December 2018 primarily driven by a $3,456,000 increase in trade payables, offset by a $1,122,000 decrease in amounts due to other Morgan Stanley Group undertakings, both of which are recognised in 'Trade and other payables'.

The risk management section below sets out the Company's and the Morgan Stanley Group's policies for the management of liquidity and cash flow risk and other significant business risks.

Risk management

Risk is an inherent part of the Company's business activity. The Company seeks to identify, assess, monitor and manage each of the various types of risk involved in its business activities, in accordance with defined policies and procedures. The Company is an agency business that manages money on behalf of its clients and has a fiduciary responsibility to those clients. The Company has developed its own risk management policy framework, which leverages the risk management policies and procedures of the Morgan Stanley Group where appropriate. The risk management policy framework includes escalation to the Company's Board of Directors and to appropriate senior management of the Company, as well as oversight through a dedicated Risk Committee of non-executive directors that reports to the Board of MSI, the Company's ultimate UK parent undertaking, and the Europe, Middle East and Africa ("EMEA") Investment Management risk management committee that reports to the Company's Board of Directors. .

Where risk is specific to that of an agency business, it is captured in specific risk management policies for the investment management business. The Board is responsible for ensuring that there are adequate risk management policies and procedures in place consistent with the risk profile of the Company. These policies and procedures are designed to ensure that all applicable risks of the Company can be identified, monitored and managed at all times. The Chief Executive Officer ("CEO") of the Board apportions the primary responsibility for internal controls and risks to the Chief Risk Officer ("CRO").

The Board and the CRO are supported in performing these responsibilities by the internal Risk Management Committees, which are responsible for:

- overseeing the risk management framework to ensure compliance with risk regulation; and
- establishing policies and procedures to measure, monitor and manage material risks of the Company's business activities.

The Board is satisfied that the risk management function is appropriately separated from the operating units, including the portfolio management function.

The Company uses a combination of direct monitoring from its own risk management systems and management information from the delegated portfolio manager to identify, measure, manage and monitor all risks relevant to its business activities.

Risk management policies are updated at least on an annual basis to ensure that they reflect best practice and any regulatory changes.

Set out below is an overview of the Company's policies for the management of financial risk and other significant business risks. More detailed qualitative and quantitative disclosures about the Company's management of and exposure to financial risks are included in note 20 to the financial statements.

BUSINESS REVIEW (CONTINUED)

Risk management (continued)

Operational risk

Operational risk refers to the risk of loss, or of damage to the Company's reputation, resulting from inadequate or failed processes, from human factors or from external events (e.g. fraud, theft, legal and compliance risks, cyber attacks or damage to physical assets). Operational risk relates to the following risk event categories as defined by Basel Capital Standards: internal fraud; external fraud; employment practices and workplace safety; clients, products and business practices; business disruption and system failure; damage to physical assets; and execution, delivery and process management. The Company may incur operational risk across the full scope of its business activities, including revenue-generating activities (e.g. investment management) and support and control group (e.g. information technology). Legal and compliance risk is included in the scope of operational risk and is discussed below under "Legal, regulatory and compliance risk".

Clients, products and business practices is defined as losses or other impacts arising from an unintentional or negligent failure to meet a professional obligation to specific clients (including fiduciary and suitability requirements), or from the nature or design of a product. For the Company, this also encapsulates the risk associated with lack of management oversight and control. Robust risk management policies, governance and controls ensure that this risk remains very low.

The Company has adopted the Morgan Stanley Group's Operational Risk Policies and Procedures and established an operational risk framework to identify, measure, monitor and control risk in the context of an approved risk tolerance appetite, set by the Board.

The Operational Risk Team - an independent team within the business - provides oversight of operational risk management framework and is responsible for implementing the framework, and promoting awareness, education and best practices.

The Company - through its Operational risk framework - has applied the policies and procedures to monitor and analyse internal and external operational risk events, business environment and internal control factors and to perform risk control self assessments and scenario analysis. The collected data elements are incorporated in the operational risk capital model which encompasses both quantitative and qualitative elements.

Operational risk dashboards are presented to the Company's Management Committee on a periodic basis and the Operational Risk Team works with the business units and control groups to identify and assess risks and to create action plans to mitigate risk.

Conduct risk

Conduct risk is defined within the Morgan Stanley International Limited Group ("MSI Group"), of which the Company is a part, as the risk of an adverse impact on clients, markets or Morgan Stanley's reputation as a consequence of the conduct of Morgan Stanley and/ or its employees. Conduct includes both intentional and unintentional behaviours.

The MSI Group has an approved Conduct Risk Management Policy. The Policy covers the two main strands of Morgan Stanley's Conduct Risk management:

- Managing the risk posed by the MSI Group's business activity, for example risks posed by the MSI Group strategy or risks created in the execution of that strategy; and
- Managing the risk that employees of the MSI Group pose, for example risks arising from poor culture or failure to consider Morgan Stanley's values when conducting duties.

BUSINESS REVIEW (CONTINUED)

Risk management (continued)

Operational risk (continued)

Conduct risk (continued)

The policy sets out four statements outlining what the MSI Group must do to manage Conduct Risk:

- **Identification and Assessment**: Business and Support units must identify and assess the Conduct Risks which arise from their current or planned strategies and activities.
- **Management**: Internal controls and processes must be implemented to manage Conduct Risks identified. Reasonable steps must be taken to ensure effectiveness.
- **Incidents**: Areas must identify and record Conduct Risk Incidents ("CRIs").
- **Escalation & Reporting**: Processes must be established to report risks and incidents, ensuring prompt escalation and appropriate notification.

Furthermore, the policy sets out key roles and responsibilities and a framework identifying key functions and processes for the good management of Conduct Risk. The framework also sets out various key support and governance mechanisms, such as the production of key metrics and management information, and the establishment of a Conduct Risk Committee to oversee the management of Conduct Risk and the implementation of the framework.

Legal, regulatory and compliance risk

Legal, regulatory and compliance risk includes the risk of legal or regulatory sanctions, material financial loss; including fines, penalties, judgements, damages and/ or settlements or loss to reputation which the Company may suffer as a result of a failure to comply with laws, regulations, rules, related self-regulatory organisation standards and codes of conduct applicable to the Company's business activities. This risk also includes contractual and commercial risk, such as the risk that a counterparty's performance obligations will be unenforceable. It also includes compliance with Anti-Money Laundering, anti-corruption and terrorist financing rules and regulations. The Company is generally subject to extensive regulation in the different jurisdictions in which it conducts its business.

The Company, principally through the Morgan Stanley Group's Legal and Compliance Division, has established procedures based on legal and regulatory requirements on a worldwide basis that are designed to facilitate compliance with applicable statutory and regulatory requirements and to require that the Company's policies relating to business conduct, ethics and practices are followed globally. The Company has also established procedures that are designed to facilitate compliance with regulatory rules that apply to the Company's investment management activities, such as those contained within the UCITS Directives, and contractual investment guidelines that may be agreed with clients.

In addition, the Company has established procedures to mitigate the risk that a counterparty's performance obligations will be unenforceable, including consideration of counterparty legal authority and capacity, adequacy of legal documentation, the permissibility of a transaction under applicable law and whether applicable bankruptcy or insolvency laws limit or alter contractual remedies. The heightened legal and regulatory focus on the financial services and banking industries globally continues to present a business challenge for the Company.

Cyber and information security risk management

As a general matter, the financial services industry faces increased global regulatory focus regarding cyber and information security risk management practices. Many aspects of the businesses are subject to cybersecurity legal and regulatory requirements enacted by U.S. federal and state governments and other non-U.S. jurisdictions in Europe and Asia. These laws are aimed at codifying basic cybersecurity protections and mandating data breach notification requirements.

BUSINESS REVIEW (CONTINUED)

Risk management (continued)

Operational risk (continued)

Cyber and information security risk management (continued)

The Company maintains a program that oversees cyber and information security risks and is designed to address regulatory requirements. Cybersecurity and information security policies, procedures and technologies are designed to protect the Company's information assets against unauthorised disclosure, modification or misuse. These policies cover a broad range of areas, including: identification of internal and external threats, access control, data security, protective controls, detection of malicious or unauthorized activity, incident response and recovery planning.

Certain of the Company's businesses are also subject to privacy and data protection information security legal requirements concerning the use and protection of certain customer information. For example, the General Data Protection Regulation ("GDPR") became effective in the EU on 25 May 2018 as a replacement for the EU Data Protection Directive. The GDPR imposes mandatory breach notification obligations, including significant fines for noncompliance, enhanced governance and accountability requirements and has extraterritorial impact. In addition, other jurisdictions have adopted or are proposing GDPR or similar standards, such as Australia, Singapore, Japan, Columbia, Argentina, India, Turkey, Hong Kong and Switzerland.

Market risk

Market risk refers to the risk that a change in the level of one or more market prices, rates, indices, implied volatilities, correlations or other market factors, such as market liquidity, will result in losses for a position or portfolio.

Market risk management policies and procedures for the Company are in place to ensure that investment strategies are in line with investment objectives, which are set out at a product and strategy level. The Company is not directly exposed to the market risk of funds managed, as it does not normally hold any equity interest in these funds. The policies and procedures are consistent with those of the Morgan Stanley Group and include escalation to the Company's Board of Directors and appropriate senior management personnel.

Credit risk

Credit risk refers to the risk of loss arising when a borrower, counterparty or issuer does not meet its financial obligations to the Company. The Company primarily incurs credit risk exposure through its investment management activities to third party debtors, other Morgan Stanley Group undertakings and credit institutions where the Company holds operating or surplus cash.

The Company follows the Morgan Stanley Investment Management Counterparty Risk Policy (the "Policy") which sets forth the broad principles that serve as the foundation for managing counterparty risk for all investment management business globally. The objective of the Policy is to avoid or mitigate risk of loss arising from the default or inability of a counterparty to meet its financial obligations.

Liquidity risk

Liquidity risk refers to the risk that the Company will be unable to finance its operations in a timely manner due to difficulty in liquidating its assets. Liquidity risk also encompasses the Company's ability (or perceived ability) to meet its financial obligations without experiencing significant business disruption, and the associated funding risks triggered by the market or idiosyncratic stress events that may negatively affect the Company's liquidity.

STRATEGIC REPORT

BUSINESS REVIEW (CONTINUED)

Risk management (continued)

Liquidity risk (continued)

The primary goal of the Morgan Stanley Group's liquidity risk management framework is to ensure that the Morgan Stanley Group, including the Company, has access to adequate funding across a wide range of market conditions and time horizons. The framework is designed to enable the Morgan Stanley Group to fulfil its financial obligations and support the execution of the Company's business strategies. The framework is further described in note 20.

Culture, values and conduct of employees

All employees of the Morgan Stanley Group are accountable for conducting themselves in accordance with the Morgan Stanley Group's core values *Putting Clients First, Doing the Right Thing, Leading with Exceptional Ideas,* and *Giving Back*. The Morgan Stanley Group is committed to reinforcing and confirming adherence to the core values through our governance framework, tone from the top, management oversight, risk management and controls, and a three lines of defence structure (business, control functions such as Risk Management and Compliance, and Internal Audit).

The Morgan Stanley Group's Board is responsible for overseeing the Morgan Stanley Group's practices and procedures relating to culture, values and conduct, as set forth in the Morgan Stanley Group's Corporate Governance Policies. The Morgan Stanley Group's Culture, Values and Conduct Committee is the senior management committee that oversees the Firm-wide culture, values and conduct program. A fundamental building block of this program is the Morgan Stanley Group's Code of Conduct (the "Code") which establishes standards for employee conduct that further reinforce the Morgan Stanley Group's commitment to integrity and ethical conduct. Every new hire and every employee annually must attest to their understanding of and adherence to the Code of Conduct. The Morgan Stanley UK Group's Conduct Risk Management Policy also sets out a consistent framework for managing Conduct Risk (i.e. the risk arising from misconduct by employees or contingent workers) and Conduct Risk incidents.

The annual employee performance evaluation process includes an evaluation of employee conduct related to risk management practices and the Morgan Stanley Group's expectations. The Morgan Stanley Group also has several mutually reinforcing processes to identify employee conduct that may have an impact on employment status, current year compensation and/ or prior year compensation. For example, the Global Incentive Compensation Discretion Policy sets forth standards for managers when making annual compensation decisions and specifically requires managers to consider whether their employees effectively managed and/ or supervised risk control practices during the performance year. Management committees from control functions periodically meet to discuss employees whose conduct does not meet the Firm's standards. These results are incorporated in the employees' performance evaluation, which links to compensation and promotion decisions.

The Morgan Stanley Group's clawback and cancellation provisions, which permit recovery of deferred incentive compensation and cover a broad scope of employee conduct, including any act or omission (including with respect to direct supervisory responsibilities) that constitutes a breach of obligation to the Morgan Stanley Group or causes a restatement of the Morgan Stanley Group's financial results, constitutes a violation of the Morgan Stanley Group's global risk management principles, policies and standards, or causes a loss of revenue associated with a position on which the employee was paid and the employee operated outside of internal control policies.

Liquidity and capital resource management

The Company is an agency business that manages money on behalf of its clients and has a fiduciary responsibility to those clients. As a result, the Company is not required to finance its activities through the global capital markets.

STRATEGIC REPORT

BUSINESS REVIEW (CONTINUED)

Liquidity and capital resource management (continued)

The Company continues to actively manage its capital and liquidity position to ensure adequate resources are available to support its activities, to enable it to withstand market stresses and to meet regulatory stress testing requirements proposed by its regulators globally.

The Company views capital as an important source of financial strength. It manages and monitors its capital in line with established policies and procedures and in compliance with local regulatory requirements.

In line with the Morgan Stanley Group's capital management policies, the Company manages its capital position based upon among other things, business opportunities, risks, capital availability and rates of return together with internal capital policies and regulatory requirements and, therefore, in the future may expand or contract its capital base to address the changing needs of its businesses.

Morgan Stanley Investment Management Limited ("MSIM"), the Company's immediate parent undertaking, and the Company (together the "MSIM Group") conduct an Internal Capital Adequacy Assessment Process ("ICAAP") at least annually in order to meet obligations under the fourth EU Capital Requirements Directive and EU Capital Requirements Regulation ("CRR"), collectively known as "CRD IV" which the FCA review through its Supervisory Review and Evaluation Process ("SREP").

MSIM Group capital is managed to ensure capital requirements assessed through the ICAAP and SREP are met. Internal capital minima are set to ensure the MSIM Group has sufficient capital to meet its regulatory requirements at all times.

See note 23 for further details on the Company's capital management.

OTHER REGULATORY MATTERS

Resolution and recovery planning

Both the Morgan Stanley Group and the MSI Group, of which the Company is a part, prepare, on an annual basis, a recovery plan which identifies mitigation tools available to both groups in times of severe stress.

The Morgan Stanley Group has developed a resolution plan in accordance with the requirements of Section 165(d) of Title I of the Dodd-Frank Wall Street Reform and Consumer Protection Act and its implementing regulations adopted by the Federal Reserve Board and the Federal Deposit Insurance Corporation. The resolution plan presents the Firm's strategy for resolution of the Firm upon material financial distress or failure in a severely adverse macroeconomic environment.

The EU Bank Recovery and Resolution Directive ("BRRD") has established a recovery and resolution framework for EU credit institutions and investment firms. The MSI Group produces information required by the UK Resolution Authority in the form of a resolution pack and ad hoc regulatory submissions, as necessary under BRRD and UK regulatory requirements.

European Financial Regulation Reform

In November 2016, the European Commission published a comprehensive regulatory reform package which aims to continue the reforms that the EU implemented in the wake of the financial crisis. The proposals seek to amend the existing prudential regime implemented through the Capital Requirements Directive and the Capital Requirements Regulation (CRD IV and CRR) with the amendments to those regulations known as CRD5 and CRR2, the BRRD and the Single Resolution Mechanism ("SRM").

These legislative proposals continue to be discussed and negotiated; therefore it is not possible to anticipate their final content or time of application.

OTHER REGULATORY MATTERS (CONTINUED)

Finalising Basel III Reforms

On 7 December 2017, the Basel Committee released the final part of its Basel III reform package. The key amendments provide updates to the standardized measures for calculating capital requirements and include a risk-weighted asset ("RWA") floor calculated as 72.5% of total standardized RWA. These proposals will need to be transposed into national/ EU law; however the timing of this is still uncertain.

Prudential regime for Investment firms

On 20 December 2017, the EU Commission published a proposal for the overhaul of the prudential regime for EU investment firms. The proposed changes are covered in a new Directive and Regulation which set out a revised prudential framework, as well as proposed amendments to CRD IV.

These legislative proposals continue to be discussed and negotiated; therefore it is not possible to anticipate their final content or time of application, noting also the uncertainty on the terms and timing of the UK's potential withdrawal from the EU.

Regulatory requirements upon withdrawal from the EU

The Company is currently subject to EU regulatory requirements based on the implementation of EU directives by the UK and through EU regulations that apply directly. As a result of the UK's decision to leave the EU (Brexit), there is uncertainty around what EU regulatory requirements will continue to apply in the UK. EU regulatory requirements in effect at the withdrawal date may continue to apply to the Company directly. Alternatively, the UK may implement equivalent standards for a period of time, including introducing equivalent standards for evolving regulation being introduced by the EU, that would apply to the Company. This may include additional proposals made by the Basel Committee in its Basel III reform package.

GOING CONCERN

Retaining sufficient liquidity and capital to withstand market pressures remains central to the Morgan Stanley Group's and the Company's strategy. In particular, the Company's capital and liquidity is deemed sufficient to exceed regulatory minimums under both a normal and stressed market environment for the foreseeable future. Additionally, the Company has access to further Morgan Stanley Group capital and liquidity.

Taking the above factors into consideration, the Directors believe it is reasonable to assume that the Company will have access to adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

Approved by the Board and signed on its behalf by

D. Hosie
Director
17 April 2019

MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

DIRECTORS' REPORT

The Directors present their report and financial statements (which comprise the statement of comprehensive income, the statement of changes in equity, the statement of financial position, and the related notes, 1 to 25) for the Company for the year ended 31 December 2018.

RESULTS AND DIVIDENDS

The profit for the year, after tax, was $3,989,000 (2017: $3,754,000).

During the year, no dividends were paid or proposed (2017: $nil).

REGULATION, RISK MANAGEMENT AND FUTURE DEVELOPMENTS

Information regarding regulation, risk management and future developments has been included in the Strategic report.

PILLAR 3 DISCLOSURES

The regulatory disclosures made in order to comply with the EU Directive and Regulation implementing the Basel capital framework ("the Pillar 3 disclosures") are available on the Morgan Stanley website (see note 23 for further details).

COUNTRY-BY-COUNTRY REPORTING

The disclosures made in order to comply with the Capital Requirements (Country-by-Country Reporting) Regulations 2018 in respect of the year ended 31 December 2018 will be made available on the Morgan Stanley website (see note 23 for further details).

DIRECTORS

The following Directors held office throughout the year and to the date of approval of this report (except where otherwise shown):

E Cowhey	(appointed 14 March 2018)
D J Hosie	
A J Mack (Chairman)	
R O'Healai	
A C Onslow	(resigned 31 December 2018)

DIRECTORS' AND OFFICERS' LIABILITY INSURANCE

Directors' and Officers' Liability Insurance is taken out by Morgan Stanley, the Company's ultimate parent undertaking, for the benefit of the Directors and Officers of the Company.

DIRECTORS' INDEMNITY

Qualifying third party indemnity provisions (as defined in section 234 of the Companies Act 2006) were in force during the year and up to and including the date of the Directors' report for the benefit of the Directors of the Company.

AUDIT COMMITTEE

MSI, the Company's ultimate UK parent undertaking, has an Audit Committee which assists the Boards of MSI, the Company and other MSI regulated subsidiary undertakings in meeting their responsibilities in ensuring an effective system of internal control and compliance, and in meeting their external financial reporting obligations. The Audit Committee meets regularly and reports to the MSI Board on a quarterly basis.

EVENTS AFTER THE REPORTING DATE

In relation to the Morgan Stanley Group's preparation for the UK withdrawal from the EU, on 1 January 2019 MSIM Fund Management (Ireland) Limited, another Morgan Stanley Group undertaking, was appointed to the role of UCITS management company by Morgan Stanley Investment Funds and Morgan Stanley Liquidity Funds, and to the role of AIFM by Galaxy Fund and Alpha Plus Funds plc.

MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

DIRECTORS' REPORT

EVENTS AFTER THE REPORTING DATE (CONTINUED)

Following this appointment, the Company no longer acts as management company for these funds, but continues to provide authorised corporate director services to UK authorised OEICs, being the Morgan Stanley Funds (UK).

AUDITOR

Deloitte LLP have expressed their willingness to continue in office as auditor of the Company and, under Sections 485 to 488 of the Companies Act 2006, will be deemed to be re-appointed.

Statement as to disclosure of information to the auditor

Each of the persons who are Directors of the Company at the date when this report is approved confirms that:

- so far as each of the Directors is aware, there is no relevant audit information (being information needed by the Company's auditor in connection with preparing their report) of which the Company's auditor is unaware; and
- each of the Directors has taken all the steps that he/ she ought to have taken as a Director to make himself/ herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

DIRECTORS' RESPONSIBILITIES STATEMENT

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with UK Generally Accepted Accounting Practice (UK Accounting Standards and applicable law), including Financial Reporting Standard 101 '*Reduced Disclosure Framework*' ("FRS 101"). Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable United Kingdom Accounting Standards, including FRS 101, have been followed; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Approved by the Board and signed on its behalf by

D Hosie

Director – D. Hosie

17 April 2019

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

Opinion

In our opinion the financial statements of Morgan Stanley Investment Management (ACD) Limited (the "Company"):

- give a true and fair view of the state of the Company's affairs as at 31 December 2018 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice including Financial Reporting Standard 101 "Reduced Disclosure Framework"; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:

- the statement of comprehensive income;
- the statement of changes in equity;
- the statement of financial position; and
- the related notes 1 to 25.

The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the "FRC's") Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters where:

- the Directors' use of the going concern basis of accounting in preparation of the financial statements is not appropriate; or
- the Directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of these matters.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

Other information

The Directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in respect of these matters.

Responsibilities of Directors

As explained more fully in the Directors' responsibilities statement, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic report or the Directors' report.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

Matters on which we are required to report by exception

Under the Companies Act 2006 we are required to report in respect of the following matters if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Andrew Partridge (Senior statutory auditor)

For and on behalf of Deloitte LLP

Statutory Auditor

Glasgow, United Kingdom

17 April 2019

MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

STATEMENT OF COMPREHENSIVE INCOME
Year ended 31 December 2018

	Note	2018 $'000	2017 $'000
Fee and commission income	5	848,381	713,461
Other revenue	6	-	54
Total non-interest revenues		848,381	713,515
Interest income		1,542	951
Interest expense		(1,036)	(773)
Net interest income	7	506	178
Non-interest expense			
Other expense	8	(843,977)	(708,999)
PROFIT BEFORE TAXATION		4,910	4,694
Income tax expense	9	(921)	(940)
PROFIT AND TOTAL COMPREHENSIVE INCOME FOR THE YEAR		3,989	3,754

All operations were continuing in the current and prior year.

The notes on pages 19 to 41 form an integral part of the financial statements.

MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

STATEMENT OF CHANGES IN EQUITY
Year ended 31 December 2018

	Share capital $'000	Currency translation reserve $'000	Retained earnings $'000	Total equity $'000
Balance at 1 January 2017	13,404	(156)	14,618	27,866
Profit and total comprehensive income for the year	-	-	3,754	3,754
Balance at 31 December 2017	13,404	(156)	18,372	31,620
Profit and total comprehensive income for the year	-	-	3,989	3,989
Balance at 31 December 2018	13,404	(156)	22,361	35,609

The notes on pages 19 to 41 form an integral part of the financial statements.

MORGAN STANLEY INVESTMENT MANAGEMENT (ACD) LIMITED

Registered number: 4250833

STATEMENT OF FINANCIAL POSITION
As at 31 December 2018

	Note	2018 $'000	2017 $'000
ASSETS			
Cash and short-term deposits	11	8,783	7,693
Loans and advances	12	548	5,006
Trade and other receivables	13	103,207	93,364
Prepayments and accrued income		77	-
Investments in subsidiaries	14	-	-
TOTAL ASSETS		112,615	106,063
LIABILITIES AND EQUITY			
Trade and other payables	16	74,365	71,955
Current tax liabilities		1,796	1,987
Accruals and deferred income		845	501
TOTAL LIABILITIES		77,006	74,443
Share capital	17	13,404	13,404
Currency translation reserve	17	(156)	(156)
Retained earnings		22,361	18,372
TOTAL EQUITY		35,609	31,620
TOTAL LIABILITIES AND EQUITY		112,615	106,063

These financial statements were approved by the Board and authorised for issue on 17 April 2019.

Signed on behalf of the Board

D Hosie

Director - D. Hosie

The notes on pages 19 to 41 form an integral part of the financial statements.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2018

1. CORPORATE INFORMATION

The Company is incorporated and domiciled in England and Wales, United Kingdom at the following registered address 25 Cabot Square, Canary Wharf, London, England, E14 4QA. The Company is a private company and is limited by shares. The registered number of the Company is 4250833.

The Company's immediate parent undertaking is Morgan Stanley Investment Management Limited, which has its registered office at 25 Cabot Square, Canary Wharf, London, England, E14 4QA, and is registered in England and Wales. Copies of its financial statements can be obtained from the Registrar of Companies for England and Wales, Companies House, Crown Way, Cardiff CF14 3UZ.

The Company's ultimate parent undertaking and controlling entity and the smallest and largest group of which the Company is a member and for which group financial statements are prepared is Morgan Stanley which, together with the Company and Morgan Stanley's other subsidiary undertakings, form the Morgan Stanley Group. Morgan Stanley has its registered office c/o The Corporation Trust Company, The Corporation Trust Center, 1209 Orange Street, Wilmington, DE 19801, United States of America and is incorporated in the state of Delaware, in the United States of America. Copies of its financial statements can be obtained from www.morganstanley.com/investorrelations

2. BASIS OF PREPARATION

The Company is not required to prepare consolidated financial statements by virtue of the exemption under section 401 of the Companies Act 2006. The results of the Company are included within the financial statements of Morgan Stanley which has prepared consolidated financial statements for the year ended 31 December 2018, has its registered office c/o The Corporation Trust Company, The Corporation Trust Center, 1209 Orange Street, Wilmington, DE 19801, United States of America and is incorporated in the state of Delaware, in the United States of America. The financial statements therefore present information about the Company as an individual entity and not about its group.

Statement of compliance

The financial statements are prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 101.

The Company meets the definition of a qualifying entity and is a Financial institution as defined in Financial Reporting Standard 100 '*Application of Financial Reporting Requirements*' ("FRS 100"). The Company has taken advantage of the disclosure exemptions available under FRS 101 in relation to share-based payments, fair value measurement (as applicable to assets and liabilities other than financial instruments), revenue from contracts with customers, presentation of comparative information in respect of certain assets and shares outstanding, presentation of a cash-flow statement, accounting standards not yet effective and related party transactions.

Where relevant, equivalent disclosures have been provided in the group accounts of Morgan Stanley, in which the Company is consolidated. Copies of Morgan Stanley's accounts can be obtained as detailed at note 1.

2. BASIS OF PREPARATION (CONTINUED)

New standards and interpretations adopted during the year

The following, standards and amendments to standards relevant to the Company's operations were adopted during the year. Except where otherwise stated, these standards and amendments to standards did not have a material impact on the Company's financial statements.

International Financial Reporting Standards ("IFRS") 9 '*Financial instruments*' ("IFRS 9") was issued by the International Accounting Standards Board ("IASB") in November 2009, reissued in October 2010, amended in November 2013, and revised and reissued by the IASB in July 2014. IFRS 9 is applicable retrospectively, except where otherwise prescribed by transitional provisions of the standard, and is effective for accounting periods beginning on or after 1 January 2018. The standard was endorsed by the EU in November 2016.

The main aspects of IFRS 9 which impact the Company are its requirements relating to:

- Classification and measurement of financial assets

  The classification and measurement of financial assets is determined based upon how these financial assets are managed and their contractual cash flow characteristics.

- Impairment of financial instruments

  The impairment requirements are based on expected credit losses ("ECL") and apply to financial assets measured at amortised cost.

The Company has completed a project to implement IFRS 9. As part of this project, the Company performed an evaluation of its business models and a review of the contractual terms of financial assets. There was no impact on the classification and measurement of the Company's financial assets and liabilities.

As a result of the implementation of the ECL impairment approach there was no impact to the retained earnings of the Company as at 1 January 2018.

The Company has updated the presentation of its primary statements on transition to IFRS 9 to provide more relevant information to the users of the financial statements. The comparative period has been re-presented to align to the new format in the annual financial statements.

Note 3 Summary of Significant Accounting Policies provides the new accounting policies under IFRS 9 applicable from 1 January 2018, alongside the accounting policies applicable to 31 December 2017 under International Accounting Standards ("IAS") 39 '*Financial instruments: Recognition and Measurement*' ("IAS 39").

To reflect the differences between IFRS 9 and IAS 39, IFRS 7 '*Financial Instruments: Disclosures*' ("IFRS 7") was updated by the IASB and the Company adopted the updated IFRS 7 for the year beginning 1 January 2018. The updated requirements include transition disclosures shown in note 4, in addition to qualitative and quantitative information about the ECL as set out in note 20.

IFRS 15 '*Revenue from Contracts with Customers*' ("IFRS 15") was issued by the IASB in May 2014 for retrospective application in accounting periods beginning on or after 1 January 2018. In addition, amendments relating to clarifications to IFRS 15 were issued by the IASB in April 2016 requiring application in accounting periods beginning on or after 1 January 2018. The standard and amendments were endorsed by the EU in October 2016. Refer to note 4 for further information.

Amendments to FRS 100 and FRS 101 '*Triennial review 2017 amendments*' were issued by the Financial Reporting Council in December 2017 for application in accounting periods beginning on or after 1 January 2019. The Company has early adopted all these amendments from 1 January 2018.

There were no other standards or amendments to standards relevant to the Company's operations which were adopted during the year.

2. BASIS OF PREPARATION (CONTINUED)

Basis of measurement

The financial statements of the Company are prepared under the historical cost basis, except for certain financial instruments that have been measured at fair value as explained in the accounting policies below, and in accordance with applicable United Kingdom Accounting Standards, including FRS 101, and UK company law.

Critical accounting judgements and sources of estimation uncertainty

In preparing the financial statements, the Company considers judgements and estimates that affect the application of accounting policies and reported amounts.

Critical accounting judgements are key decisions made by management in the application of the Company's accounting policies, other than those involving estimations, which have the most significant effects on the amounts recognised in the financial statements. Critical accounting estimates represent assumptions and estimations made by management that have a significant risk of resulting in a material adjustment to the carrying amount of assets and liabilities within the next financial year.

The critical judgement in applying the Company's accounting policies is the consolidation of structured entities. The Company determines whether it controls, and therefore should consolidate a structured entity upon its initial involvement and reassess on an ongoing basis for as long as it has any continuing involvement with the structured entity. See note 15.

There were no critical sources of estimation uncertainty that have a significant risk of resulting in a material adjustment to the carrying amount of assets and liabilities within the next financial year.

The Company evaluates the critical accounting judgements and accounting estimates on an ongoing basis and believes that these are reasonable.

The going concern assumption

The Company's business activities, together with the factors likely to affect its future development, performance and position, are reflected in the Business Review section of the Strategic report on pages 1 to 8. In addition, the notes to the financial statements include the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments; and its exposures to credit risk and liquidity risk.

As set out in the Strategic report, retaining sufficient liquidity and capital to withstand market pressures remains central to the Morgan Stanley Group's and the Company's strategy.

Taking the above factors into consideration, the Directors believe it is reasonable to assume that the Company will have access to adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Functional currency

Items included in the financial statements are measured and presented in US dollars, the currency of the primary economic environment in which the Company operates.

All currency amounts in the financial statements and Strategic and Directors' reports are rounded to the nearest thousand US dollars.

b. Foreign currencies

All monetary assets and liabilities denominated in currencies other than US dollars are translated into US dollars at the rates ruling at the reporting date. Transactions and non-monetary assets and liabilities denominated in currencies other than US dollars are recorded at the rates prevailing at the dates of the transactions. All translation differences are taken through the statement of comprehensive income and are presented in 'Other revenue' or 'Other expense'.

c. Financial instruments

i) Investments in subsidiaries

Subsidiaries are entities over which the Company has control. The Company controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

In certain cases, the Company may exercise control over another entity on behalf of investors or other parties. In such cases it is necessary, as part of the assessment of whether it should consolidate the entity, for the Company to determine whether it exercises such control primarily as an agent for the other investors or whether it does so primarily as principal on its own behalf. In making such a determination, Management will consider all relevant factors, including in particular:

- The scope of the Company's decision-making authority over the investee;
- The rights, including removal rights, held by other parties;
- The remuneration to which the Company is entitled;
- The significance of the Company's exposure to variability of returns from its interests in the entity.

ii) Financial assets and financial liabilities at amortised cost

Applicable from 1 January 2018

Financial assets are recognised at amortised cost when the Company's business model objective is to collect the contractual cash flows of the assets and where these cash flows are solely payments of principal and interest ("SPPI") on the principal amount outstanding until maturity. Such assets are recognised when the Company becomes a party to the contractual provisions of the instrument. The instruments are initially measured at fair value (see note 3(d) below) and subsequently measured at amortised cost less ECL allowance. Interest is recognised in the statement of comprehensive income in 'Interest income', using the effective interest rate ("EIR") method as described below. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. Transaction costs that are directly attributable to the acquisition of the financial asset are added to the fair value on initial recognition. ECL and reversals thereof are recognised in the statement of comprehensive income in 'Net impairment loss on financial instruments'.

Financial assets at amortised cost include cash and short-term deposits, trade and other receivables and loans and advances.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

c. Financial instruments (continued)

ii) Financial assets and financial liabilities at amortised cost (continued)

Applicable until 31 December 2017

Financial assets classified as loans and receivables were recognised when the Company became a party to contractual provisions of the instrument. They were initially measured at fair value (see note 3(d) below) and subsequently measured at amortised cost less allowance for impairment. Interest was recognised in the statement of comprehensive income in 'Interest income', using the EIR method as described below. Transaction costs that were directly attributable to the acquisition of the financial asset were added to the fair value on initial recognition. Impairment losses and reversals of impairment losses on financial assets classified as loans and receivables were recognised in the statement of comprehensive income in 'Other expense'.

Financial assets classified as loans and receivables included cash and short-term deposits, trade receivables, loans and advances and other receivables.

Applicable until 31 December 2017 and from 1 January 2018

Financial liabilities are recognised when the Company becomes a party to the contractual provisions of the instrument and are initially measured at fair value (see note 3(d) below) and subsequently measured at amortised cost. Interest is recognised in the statement of comprehensive income in 'Interest expense' using the EIR method as described below. Transaction costs that are directly attributable to the issue of a financial liability are deducted from the fair value on initial recognition.

The EIR method is a method of calculating the amortised cost of a financial instrument (or a group of financial instruments) and of allocating the interest income or interest expense over the expected life of the financial instrument. The EIR is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial instrument (or, where appropriate a shorter period) to the carrying amount of the financial instrument. The EIR is established on initial recognition of the financial instrument. The calculation of the EIR includes all fees and commissions paid or received, transaction costs, and discounts or premiums that are an integral part of the EIR.

Financial liabilities classified at amortised cost include trade and other payables.

d. Fair value

Fair value measurement

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e. the "exit price") in an orderly transaction between market participants at the measurement date.

For all financial instruments, the carrying amount is considered to be a reasonable approximation of fair value, due to the short term nature of these assets and liabilities.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

e. Derecognition of financial assets and liabilities

The Company derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risk and rewards of ownership of the asset.

If the asset has been transferred, and the Company neither transfers nor retains substantially all of the risks and rewards of the asset, then the Company determines whether it has retained control of the asset.

If the Company has retained control of the asset, it shall continue to recognise the financial asset to the extent of its continuing involvement in the financial asset. If the Company has not retained control of the asset, it derecognises the asset and separately recognises any rights or obligation created or retained in the transfer.

Upon derecognition of a financial asset, the difference between the previous carrying amount and the sum of any consideration received is recognised in the statement of comprehensive income within 'Net gains/ (losses) on derecognition of financial assets measured at amortised cost'.

The Company derecognises financial liabilities when the Company's obligations are discharged or cancelled or when they expire.

f. Impairment of financial instruments

Applicable from 1 January 2018

The Company recognises loss allowances for ECL for financial assets measured at amortised cost.

Measurement of ECL

For financial assets, ECL are the present value of cash shortfalls (i.e. the difference between contractual and expected cash flows) over the expected life of the financial instrument, discounted at the asset's EIR.

The Company applies a three stage approach to measuring ECL based on the change in credit risk since initial recognition:

- Stage 1: if the credit risk of the financial instrument at the reporting date has not increased significantly since initial recognition then the loss allowance is calculated as the lifetime cash shortfalls that will result if a default occurs in the next 12 months, weighted by the probability of that default occurring.
- Stage 2: if there has been a significant increase in credit risk ("SICR") since initial recognition, the loss allowance is calculated as the ECL over the remaining life of the financial instrument. If it is subsequently determined that there has no longer been a SICR since initial recognition, then the loss allowance reverts to reflecting 12 month expected losses.
- Stage 3: if there has been a SICR since initial recognition and the financial instrument is deemed credit-impaired (see below for definition of credit-impaired), the loss allowance is calculated as the ECL over the remaining life of the financial instrument. If it is subsequently determined that there has no longer been a SICR since initial recognition, then the loss allowance reverts to reflecting 12 month expected losses

The Company's accounting policy is to not use the 'low' credit risk practical expedient. As a result, the Company monitors all financial instruments which do not have a significant financing component that are subject to impairment for SICR, with the exception of trade receivables for which a lifetime ECL is always calculated.

Where there is a history of no credit losses, and where this is expected to persist into the future for structural or other reasons, such as credit enhancements, it may be determined that the ECL for a financial instrument is de minimis (highly immaterial) and recognition of the ECL may not be necessary.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Impairment of financial instruments (continued)

Measurement of ECL (continued)

The Company measures ECL on an individual asset basis and has no purchased or originated credit-impaired financial assets.

Presentation of ECL

ECL is recognised in the statement of comprehensive income within 'Net impairment loss on financial instruments'. ECL on financial assets measured at amortised cost are presented as an ECL allowance, reducing the net carrying amount on the face of the statement of financial position.

Applicable until 31 December 2017

At each reporting date, an assessment was made as to whether there was any objective evidence of impairment in the value of a financial asset classified as loans and receivables. Impairment losses were recognised if an event had occurred which would have had an adverse impact on the expected future cash flows of an asset and the expected impact could be reliably estimated.

Impairment losses on loans and receivables were measured as the difference between the carrying amount of the loans and receivables and the present value of estimated cash flows discounted at the asset's original EIR. Such impairment losses were recognised in the statement of comprehensive income within 'Other expense' and were recognised against the carrying amount of the impaired asset on the statement of financial position. Interest on the impaired asset continued to be accrued on the reduced carrying amount based on the original EIR of the asset.

For all other financial assets, if in a subsequent year, the amount of the estimated impairment loss decreased because of an event occurring after the impairment was recognised, the previously recognised impairment loss was reversed as described for the relevant categories of financial asset in note 3(c). Any reversal was limited to the extent that the value of the asset would not exceed the original amortised cost of the asset had no impairment occurred.

g. Revenue recognition and contract assets and liabilities

Fees and commissions classified within 'Fee and commission income' in the statement of comprehensive income include investment management, distribution, administration and performance fees. These are generally recognised when services are performed and the fees become known, except for performance fees as noted below.

- Investment management fees are primarily based on pre-determined percentages of the market value of AUM.
- Distribution fees are received on certain funds managed by the Company and are primarily priced at pre-determined percentages, dependent on share class.
- Administration fees are received on certain funds managed by the Company to reimburse any costs, charges, fees and expenses incurred in relation to the administration of the funds. These are primarily priced at pre-determined fixed percentages.
- Performance fees are received from certain investment products. These are earned upon exceeding specified relative and/ or absolute investment return thresholds. From 1 January 2018, performance fees are recognised only when the performance obligation is satisfied, upon completion of the measurement period, which varies by product or account, and could be monthly, quarterly, annually or longer. Until 31 December 2017, performance fees were recognised throughout the measurement period based on estimated performance relative to investment return thresholds.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

g. Revenue recognition and contract assets and liabilities (continued)

Other items

Receivables from contracts with customers are recognised within 'Trade and other receivables' in the statement of financial position when the underlying performance obligations have been satisfied and the Company has the right per the contract to bill the customer. Contract assets are recognised when the Company has satisfied its performance obligations and customer payment is conditional, and are presented within 'Prepayments and accrued income'. Contract liabilities are recognised when the Company has collected payment from a customer based on the terms of the contract, but the underlying performance obligations are not yet satisfied, and are presented within 'Accruals and deferred income'.

Incremental costs to obtain the contract are expensed as incurred if the contract duration is one year or less. Revenues are not discounted when payment is expected within one year.

h. Cash and cash equivalents

Cash and cash equivalents comprise cash and demand deposits with banks, net of outstanding bank overdrafts.

i. Income tax

The tax expense represents the sum of the tax currently payable.

The tax currently payable is calculated based on taxable profit for the year. Taxable profit may differ from profit before taxation as reported in the statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the reporting date. Current tax is charged or credited in the statement of comprehensive income, except when it relates to items charged or credited directly to other comprehensive income or equity, in which case the current tax is also recorded within other comprehensive income or equity respectively.

Current tax assets are offset against current tax liabilities when there is a legally enforceable right to set off current tax assets against current tax liabilities and the Company intends to settle its current tax assets and current tax liabilities on a net basis or to realise the asset and settle the liability simultaneously.

4. TRANSITION TO IFRS 9 AND IFRS 15

As discussed at note 2, the Company adopted two new standards from 1 January 2018, IFRS 9 and IFRS 15. There was no cumulative adjustment to retained earnings at the date of adoption of either standard.

IFRS 9

The Company had no impairment provisions under IAS 39 at 31 December 2017 and has no ECL impairment allowance as at 1 January 2018 (see note 2 *New standards and interpretations adopted during the year)*.

There was no remeasurement of the Company's financial assets or financial liabilities following the adoption of the new measurement categories in accordance with the Company's updated accounting policies on the classification of financial instruments under IFRS 9 as set out in note 3(c).

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Company's financial assets and financial liabilities.

	Note	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount under IAS 39	New carrying amount under IFRS 9
				$'000	$'000
Financial assets					
Cash and short-term deposits		Loans and receivables	Financial assets at amortised cost	7,693	7,693
Loans and advances	a	Loans and receivables	Financial assets at amortised cost	5,006	5,006
Trade and other receivables		Loans and receivables	Financial assets at amortised cost	93,364	93,364
Total financial assets				106,063	106,063

	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount under IAS 39	New carrying amount under IFRS 9
			$'000	$'000
Financial liabilities				
Trade and other payables	Financial liabilities at amortised cost	Financial liabilities at amortised cost	71,955	71,955
Total financial liabilities			71,955	71,955

a. Loans and advances to customers are classified as financial assets at amortised cost where they are in a held to collect business model and their contractual terms are SPPI.

IFRS 15

At 1 January 2018, the Company adopted IFRS 15, in accordance with the transition provisions therein. The Company has applied the provisions of IFRS 15 retrospectively only to contracts that were not completed as at 1 January 2018, the date of initial application. Prior periods have not been restated. No cumulative gain or loss was recorded as of 1 January 2018 on assessment of the timing of the recognition of revenues.

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Year ended 31 December 2018

5. FEE AND COMMISSION INCOME

	2018 $'000	2017 $'000
Investment management fees	692,611	566,108
Distribution fees	67,697	70,171
Administration fees	88,073	77,180
Performance fees	-	2
	848,381	713,461
Of which, revenue from contracts with customers	848,381	713,461

The increase in fee and commission income is driven by increased average AUM compared to the prior year.

Revenue from contracts with customers

'Revenue from contracts with customers' was introduced by IFRS 15, for which comparative periods have not been restated.

As at 31 December 2018 there are $nil (2017: $nil) contract assets and liabilities from contracts with customers.

6. OTHER REVENUE

	2018 $'000	2017 $'000
Net foreign exchange gains	-	54
	-	54

Other income for the year ending December 2017 relates to foreign exchange income. Foreign exchange loss has been disclosed in other expense (note 8) for the year ending December 2018.

7. INTEREST INCOME AND INTEREST EXPENSE

'Interest income' represents total interest generated from financial assets at amortised cost whilst 'Interest expense' represents total interest arising on financial liabilities at amortised cost. All interest income and expense is calculated using the EIR method (see accounting policy 3(c)(ii)).

No gains or losses have been recognised in respect of financial assets and liabilities at amortised cost other than those disclosed as 'Interest income', 'Interest expense' and foreign exchange differences as disclosed in 'Other revenue' (note 6) or 'Other expense' (note 8).

8. OTHER EXPENSE

	2018 $'000	2017 $'000
Administration expense	28,943	29,451
Net foreign exchange losses	20	-
Management charges from other Morgan Stanley Group undertakings relating to Directors	299	297
Management charges from other Morgan Stanley Group undertakings relating to other services	814,659	679,231
Auditor's remuneration:		
Fees payable to the Company's auditor and its associates for the audit of the Company's annual financial statements	19	20
Fees payable to the Company's auditor and its associates for other assurance services to the Company	37	-
	843,977	708,999

The Company employed no staff during the year (2017: nil).

Certain fees payable to the Company's auditor and its associates for other assurance services in relation to the audit of client assets and client money have been borne by another Morgan Stanley Group undertaking in the current and prior year.

The amount of remuneration received by Directors in respect of their qualifying services to the Company is disclosed in the Related party disclosures note (note 24).

9. INCOME TAX EXPENSE

Analysis of expense in the year

	2018 $'000	2017 $'000
Current tax expense		
UK corporation tax at 19% (2017: 19.25%)		
- Current year	921	940
Total current tax	921	940
Income tax expense	921	940

Finance (No.2) Act 2015 enacted a reduction in the UK corporation tax rate to 19% with effect from 1 April 2017. Finance Act 2016 enacted a further reduction in the UK corporation tax rate to 17% with effect from 1 April 2020 which will impact the current tax charge in future periods.

9. INCOME TAX EXPENSE (CONTINUED)

Reconciliation of effective tax rate

The current year income tax expense is lower (2017: higher) than that resulting from applying the average standard rate of corporation tax in the UK for the year of 19% (2017: 19.25%). The main differences are explained below:

	2018 $'000	2017 $'000
Profit before taxation	4,910	4,694
Income tax using the average standard rate of corporation tax in the UK of 19.00% (2017: 19.25%)	933	903
Impact on tax of:		
Expenses not (taxable)/ deductible for tax purposes	(12)	24
Currency translation on tax	-	13
Total income tax expense in the statement of comprehensive income	921	940

10. FINANCIAL ASSETS AND FINANCIAL LIABILITIES BY MEASUREMENT CATEGORY

All financial assets and financial liabilities are measured at amortised cost.

11. CASH AND SHORT-TERM DEPOSITS

Included in 'Cash and short-term deposits' is an amount of $152,452 (2017: $20,522) which represents segregated client money, held in accordance with the FCA's Client Money Rules.

12. LOANS AND ADVANCES

	2018 $'000	2017 $'000
Amounts due from other Morgan Stanley Group undertakings	548	5,006

13. TRADE AND OTHER RECEIVABLES

	2018 $'000	2017 $'000
Trade and other receivables		
Trade receivables	94,598	-
Other receivables		
Amounts due from other Morgan Stanley Group undertakings	8,609	-
	103,207	-
Loans and receivables		
Trade receivables	-	83,759
Other receivables		
Amounts due from other Morgan Stanley Group undertakings	-	9,605
	103,207	93,364

14. INVESTMENT IN SUBSIDIARIES

On the 5 December 2017, the Company incorporated and subscribed to 1 ordinary share of €1 par value in a new Irish limited liability company, MSIM Fund Management (Ireland) Limited.

On 4 July 2018, the Company sold 1 ordinary share of €1 par value held in MSIM Fund Management (Ireland) Limited to MSI, recognising no gain or loss on disposal.

Details of all investments in subsidiaries (including indirect subsidiaries) of the Company at 31 December 2018 and 31 December 2017 are as follows, details of which are shown below:

Name of Company	Address of undertaking's registered office	Type of shares held	Proportion of shares held		Proportion of voting rights held		Nature of business
			2018	2017	2018	2017	
MSIM Fund Management (Ireland) Limited	The Observatory, 7-11, Sir John Rogerson's Quay, Dublin 2, Ireland	Ordinary	0%	100%	0%	100%	Investment Management

15. INTERESTS IN STRUCTURED ENTITIES

The Company is involved with various special purpose entities in the normal course of business. In most cases, these entities are considered to be structured entities.

A structured entity is an entity that has been designed such that voting or similar rights are not the dominant factor in deciding who controls the entity. The party that consolidates the structured entity is the investor that controls the structured entity. An investor controls a structured entity when it is exposed, or has the rights, to variable returns from its involvement with the structured entity and has the ability to affect those returns through its power over the structured entity.

The Company has interests in structured entities in the form of fee and commissions income from investment management funds (OEICs, UCITS and AIFs). The Company does not normally hold any equity interest in these funds. Where equity interests are held, they are held by another Morgan Stanley Group undertaking.

The Company determines whether it controls, and therefore should consolidate, a structured entity upon its initial involvement with the structured entity and reassesses whether it should be consolidated on an ongoing basis as long as it has any continuing involvement with the structured entity. This determination is based upon an analysis of the design of the structured entity, including the structured entity's structure and activities; assessment of the significance of the powers to make economic decisions which are held by the Company and its related parties and whether such powers may be used to affect its investor returns; and consideration of the significance of direct and indirect interests in the structured entity which are held by the Company and its related parties.

The power to make the most significant economic decisions may take a number of different forms. In fund structures, the power to appoint or direct the fund manager is generally the most significant power.

15. INTERESTS IN STRUCTURED ENTITIES (CONTINUED)

Sponsored unconsolidated structured entities

The Company considers itself the sponsor of certain non-consolidated structured entities where it has been involved in the establishment of a structured entity and where the Company acts as the management company or the authorized corporate director of the entity. The Company sub-delegates the investment management services to other Morgan Stanley Group undertakings.

The table below shows income received from sponsored entities. Income is reported under 'Fee and commission income' in the statement of comprehensive income.

	Investment management funds *(1)* $'000
31 December 2018	
Income from sponsored entity	848,381
31 December 2017	
Income from sponsored entity	713,461

(1) This income is passed to other Morgan Stanley Group undertakings (after deducting relevant expenses) as the Company sub-delegates the investment management services to those undertakings.

During the current and prior years no assets transferred to those sponsored entities.

16. TRADE AND OTHER PAYABLES

	2018 $'000	2017 $'000
Trade payables	23,196	19,741
Other payables		
Amounts due to other Morgan Stanley Group undertakings	51,092	52,214
Other amounts payable	77	-
	74,365	71,955

17. EQUITY

Ordinary share capital

	Ordinary shares of $1 each Number	Ordinary shares of $1 each $'000	Ordinary shares of £1 each Number	Ordinary shares of £1 each $'000	Total ordinary shares $'000
Allotted and fully paid					
At 1 January 2018 and 31 December 2018	13,000,000	13,000	244,000	404	13,404

The holders of both the £1 and the $1 ordinary shares are entitled to receive dividends as declared from time to time and are entitled, on a show of hands, to one vote and, on a poll, one vote per share at meetings of the shareholders of the Company. All shares rank equally with regard to the Company's residual assets.

All ordinary shares are recorded at the rates of exchange ruling at the date the shares were paid up.

17. EQUITY (CONTINUED)

Reserves

Currency translation reserve

The 'Currency translation reserve' of $156,000 loss (2017: $156,000 loss) comprises all foreign exchange differences arising from the translation of historical comparative information from Pounds Sterling to US Dollars as a result of a change in the Company's functional currency from Pounds Sterling to US Dollars with effect from 1 January 2014.

18. EXPECTED MATURITY OF ASSETS AND LIABILITIES

The table below shows an analysis of assets and liabilities analysed according to when they are expected to be recovered, realised or settled.

At 31 December 2018	Less than or equal to twelve months $'000	More than twelve months $'000	Total $'000
ASSETS			
Cash and short-term deposits	8,783	-	8,783
Loans and advances	548	-	548
Trade and other receivables	103,207	-	103,207
Prepayments and accrued income	77	-	77
	112,615	-	112,615
LIABILITIES			
Trade and other payables	74,365	-	74,365
Current tax liabilities	1,796	-	1,796
Accruals and deferred income	845	-	845
	77,006	-	77,006

At 31 December 2017	Less than or equal to twelve months $'000	More than twelve months $'000	Total $'000
ASSETS			
Cash and short-term deposits	7,693	-	7,693
Loans and advances	5,006	-	5,006
Trade and other receivables	83,759	9,605	93,364
	96,458	9,605	106,063
LIABILITIES			
Trade and other payables	54,726	17,229	71,955
Current tax liabilities	1,987	-	1,987
Accruals and deferred income	501	-	501
	57,214	17,229	74,443

19. SEGMENT REPORTING

The Company has only one class of business as described in the Strategic report and operates in one geographic market, EMEA.

20. FINANCIAL RISK MANAGEMENT

Risk management procedures

Risk is an inherent part of the Company's business activity. The Company seeks to identify, assess, monitor and manage each of the various types of risk involved in its business activities in accordance with defined policies and procedures. The Company has developed its own risk management policy framework, which is consistent with and leverages the risk management policies and procedures of the Morgan Stanley Group and which include escalation to the Company's Board of Directors and to appropriate senior management personnel of the Company.

The Company's management of operational risk, deemed to be a material risk of the Company's business activity, is included in the Business Review section of the Strategic Report on pages 1 to 9. Other risks faced by the Company resulting from its financing and investment activities are set out below and are not deemed to be material risks.

Credit risk

Credit risk refers to the risk of loss arising when a borrower, counterparty or issuer does not meet its financial obligations to the Company. The Company primarily incurs credit risk exposure to institutions through its Investment Management business.

The Company's credit risk management policies and procedures establish the framework for ensuring transparency of material credit risks and escalation of risk concentrations to appropriate senior management.

The Company may incur credit risk exposure through its investment management activities to third party debtors, other Morgan Stanley Group undertakings and credit institutions where the Company holds surplus or operating cash. Due to the nature of the activities and the following controls in place to mitigate the risk, the credit exposure to the Company is not considered to be material.

Monitoring and Control

In order to help protect the Company from credit losses, the Morgan Stanley Group's Risk Management Department establishes policies and procedures in line with firm-wide practices to evaluate, monitor and control credit risk exposure.

Examples of risk mitigation include, but are not limited to, the following:

- Cash and short-term deposits are placed with highly-rated approved banks to mitigate the risk of loss.
- Trade receivables comprise amounts due from investment management funds and segregated managed accounts. In the case of investment management funds, following issuance of an invoice, the amounts receivable may be settled from the AUM of the fund, which serves as a credit enhancement given the receivables rank senior to the issued fund units. In the case of segregated managed accounts, the Company, having followed credit risk management procedures is satisfied that the credit risk is minimal.
- Loans and advances and other receivables primarily comprise amounts due from other Morgan Stanley Group undertakings, where both the Company and the other Morgan Stanley Group undertakings are wholly-owned subsidiaries of the same ultimate parent entity, Morgan Stanley. As a result of the implicit support that would be provided by Morgan Stanley, the Company is considered exposed to the credit risk of Morgan Stanley, except where the Company transacts with other Morgan Stanley Group undertakings that have a higher credit rating to that of Morgan Stanley.

20. FINANCIAL RISK MANAGEMENT (CONTINUED)

Credit risk (continued)

All exposures are monitored on an on-going basis.

In addition, the Policy sets forth the broad principles for the management of Counterparty Risk for the Company. The following standards are incorporated into the Policy:

a. Approval and monitoring

The Company mitigates Counterparty Risk by adopting procedures that limit transactions with the potential for material loss to approved counterparties. In addition, the Company conducts reviews of the counterparties' financial condition and monitors current exposure on an on-going basis. The counterparty risk of the Company is not deemed to be material.

b. Trading with approved counterparties

As a standard of practice, the Company will transact only with approved counterparties. The Morgan Stanley Group's Risk Management Department approves extensions of credit, evaluates the creditworthiness of the Company's obligors on a regular basis, and ensures that credit exposure is actively monitored and managed. The evaluation of obligors includes an assessment of the probability that an obligor will default on its financial obligations and any subsequent losses that may occur when an obligor defaults.

The Company also reviews its credit exposure and risk to types of customers. At 31 December 2018, the Company's largest credit exposure was to financial institutions.

Exposure to credit risk

The maximum exposure to credit risk ("gross credit exposure") of the Company as at 31 December 2018 is disclosed below, based on the carrying amounts of the financial assets the Company believes are subject to credit risk.

The Company does not have any significant exposure arising from items not recognised on the statement of financial position.

The Company does not hold financial assets considered to be credit-impaired.

Exposure to credit risk by product

2018

	Gross credit exposure [1] $'000
Subject to ECL:	
Cash and short-term deposits	8,783
Loans and advances	548
Trade and other receivables	103,207
	112,538

(1) The carrying amount recognised in the statement of financial position best represents the Company's maximum exposure to credit risk.

20. FINANCIAL RISK MANAGEMENT (CONTINUED)

Credit risk (continued)

Maximum exposure to credit risk for 2017 is presented as follows:

2017

	Gross credit exposure (1) $'000
Cash and short-term deposits	7,693
Loans and advances	5,006
Trade and other receivables	93,364
	106,063

(1) The carrying amount recognised in the statement of financial position best represents the Company's maximum exposure to credit risk

Expected credit loss measurement

As explained in note 3(f), in order to assess whether an instrument is subject to a 12 month ECL or to a lifetime ECL, and therefore its appropriate staging, the Company determines whether there has been a SICR for the instrument since initial recognition.

When making this assessment, the Company considers both quantitative and qualitative information and analysis based on the Company's historical experience and expert credit risk assessment, including forward-looking information.

At 31 December 2018, the Company has determined that the ECL for its financial instruments is not material, reflecting their short term nature and/ or the benefit of other credit mitigants.

Exposure to credit risk by internal rating grades

Internal credit ratings are derived using methodologies generally consistent with those used by external agencies.

The following table provides an analysis of the credit risk exposure by ECL stage per class of recognised financial instrument subject to ECL, based on the following internal credit rating grades:

Investment grade:	internal grades AAA - BBB
Non-investment grade:	internal grades BB - CCC
Default:	internal grades D

20. FINANCIAL RISK MANAGEMENT (CONTINUED)

Credit risk (continued)

Exposure to credit risk by internal rating grades (continued)

	ECL Staging	
	Stage 1 12-month ECL $'000	Stage 2 Lifetime ECL $'000
Cash and short-term deposits:		
Credit grade		
Investment grade	8,783	-
Loans and advances:		
Credit grade		
Investment grade	548	-
Trade and other receivables [(1)]:		
Credit grade		
Investment grade		
Trade receivables	-	94,598
Other receivables	8,609	-
Carrying amount	17,940	94,598

(1) There are no trade receivables at stage 1, as the Company's accounting policy is to measure lifetime credit losses on trade receivables under the simplified approach. ECL on trade receivables included at stage 2 are estimated to be close to zero, reflecting their short term nature and other credit mitigants.

- *Ageing analysis*

Class	Less than 30 days past due $'000	More than 30 days but less than 60 days past due $'000	More than 60 days but less than 90 days past due $'000	More than 90 days but less than 180 days past due $'000	More than 180 days but less than 1 year past due $'000	More than 1 year past due $'000	Total $'000
31 December 2018							
Trade and other receivables:							
Trade receivables	5,308	5,401	5,132	2,543	-	17	18,401
31 December 2017							
Trade and other receivables:							
Trade receivables	4,570	3,707	2,418	16	8	-	10,719

There are no concerns surrounding recoverability of the above aged balances. No amounts that were previously past due were written off in the current year. As at the date of approval of the financial statements the balance of receivables past due as at 31 December 2018 was reduced to $39,000.

20. FINANCIAL RISK MANAGEMENT (CONTINUED)

Credit risk (continued)

Exposure to credit risk by internal rating grades (continued)

The main considerations for assessing whether there has been a SICR include whether there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Company assesses each individually significant asset on an individual basis. Items considered include the sustainability of the counterparty's business plan, the counterparty's ability to improve performance once a financial difficulty has arisen and the timing of expected cash flows.

Liquidity risk

Liquidity risk refers to the risk that the Company will be unable to finance its operations in a timely manner due to difficulty in liquidating its assets. Liquidity risk also encompasses the Company's ability (or perceived ability) to meet its financial obligations without experiencing significant business disruption, and the associated funding risks triggered by the market or idiosyncratic stress events that may negatively affect the Company's liquidity.

The Morgan Stanley Group's Liquidity Risk Management Framework is critical to helping ensure that the Company maintains sufficient liquidity reserves and durable funding sources to meet its daily obligations and to withstand unanticipated stress events.

The primary goal of the Company's liquidity risk and funding management framework is to ensure that the Company has access to adequate funding across a wide range of market conditions and time horizons. The framework is designed to enable the Company to fulfil its financial obligations and support the execution of its business strategies.

The Required Liquidity Framework establishes the amount of liquidity the Company must hold in both normal and stressed environments to ensure that its financial condition and overall soundness is not adversely affected by an inability (or perceived inability) to meet its financial obligations in a timely manner.

The Company uses Liquidity Stress Tests to model external and intercompany liquidity flows across multiple scenarios and a range of time horizons. These scenarios contain various combinations of idiosyncratic and systemic stress events of different severity and duration. The methodology, implementation, production and analysis of the Company's Liquidity Stress Tests are important components of the Required Liquidity Framework. Additionally based on Liquidity Stress Tests appropriate thresholds have been set and approved by the Board of Directors to ensure sufficient liquidity is available for the business at all times.

At 31 December 2018 and 31 December 2017, the Company maintained sufficient liquidity to meet current and contingent funding obligations as modelled in its Liquidity Stress Tests.

The Company holds its own Liquidity Reserve which is composed of diversified cash.

Balance sheet management

In managing both the Morgan Stanley Group's and the Company's funding risk the composition and size of the entire balance sheet, not just financial liabilities, is monitored and evaluated. The liquid nature of marketable securities and short-term receivables arising principally from sales and trading activities in the Institutional Securities business provides the Morgan Stanley Group and the Company with flexibility in managing the composition and size of its balance sheet.

Maturity analysis

The financial assets and financial liabilities of the Company are expected to be recovered, realised or settled on demand, with the exception of those shown at note 18 which have a maturity of greater than one year but less than 5 years as at 31 December 2018 and 31 December 2017.

20. FINANCIAL RISK MANAGEMENT (CONTINUED)

Market risk

Market risk is defined by IFRS 7 '*Financial instruments – Disclosures*' ("IFRS 7") as the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices.

Sound market risk management is an integral part of the Company's culture. The Company is responsible for ensuring that market risk exposures are well-managed and monitored. The Company also ensures transparency of material market risks, monitors compliance with established limits, and escalates risk concentrations to appropriate senior management.

The Company is managed within the Morgan Stanley Group's global framework. The market risk management policies and procedures of the Company include performing risk analyses and reporting material risks identified to appropriate senior management of the Company.

The Company is not directly exposed to the market risk of funds managed, as it does not normally hold any equity interest in these funds.

The Company is exposed to the following types of market risk under the definition above: interest rate risk and currency risk.

Interest rate risk

Interest rate risk is defined by IFRS 7 as the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company is primarily exposed to interest rate risk under this definition as a result of loans held at amortised cost.

The application of a parallel shift in interest rates of 50 basis points increase or decrease to these positions, would result in a net gain or loss of approximately $245,000 (2017: $195,000).

Currency risk

The Company has foreign currency exposure on its assets and liabilities in currencies other than US dollars, which primarily arise from revenue and expenses denominated in currencies other than US dollars. It actively manages this foreign currency exposure by hedging with other Morgan Stanley Group undertakings. The residual currency risk for the Company from this activity is not material.

The majority of this foreign currency risk has been hedged by other members of the Morgan Stanley Group, primarily Morgan Stanley, by utilising spot and forward foreign currency exchange contracts.

21. ASSETS AND LIABILITIES MEASURED AT FAIR VALUE

As disclosed in note 2 Statement of Compliance, the Company is exempt from certain disclosure requirements of IFRS 13 *'Fair value measurement'* ("IFRS 13") to the extent that they apply to assets and liabilities other than financial instruments. As such the disclosure included in this note relates only to financial instruments.

None of the Company's financial instruments are measured at fair value in the current or prior year.

22. ASSETS AND LIABILITIES NOT MEASURED AT FAIR VALUE

As disclosed in note 2 Statement of Compliance, the Company is exempt from certain disclosure requirements of IFRS 13 to the extent that they apply to assets and liabilities other than financial instruments. As such the disclosure included in this note relates only to financial instruments.

For all financial instruments, the carrying amount is considered to be a reasonable approximation of fair value due to the short term nature of these assets and liabilities.

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23. CAPITAL MANAGEMENT

The capital managed by the Company broadly includes share capital and reserves. In order to maintain or adjust its capital structure, the Company may adjust the amount of dividends paid, return capital to its shareholder or issue new shares. Details of its managed capital are set out in the table below. This does not represent the Company's capital measured in accordance with regulatory requirements.

	2018 $'000	2017 $'000
Ordinary share capital	13,404	13,404
Reserves	22,205	18,216
	35,609	31,620

The Company complied with all of its regulatory capital requirements during the year.

Pillar 3 disclosures and Country-by-Country Reporting

The Company is included in the MSI Group Pillar 3 disclosures which allow investors and other market participants to understand capital adequacy, particular risk exposures and risk management processes of individual firms required by the EU implementation of Basel capital standards. The Pillar 3 disclosures for the MSI Group can be found at www.morganstanley.com/investorrelations.

24. RELATED PARTY DISCLOSURES

Key management compensation

Directors' remuneration

The Company paid no remuneration to its Directors during the current or prior year. The charges in respect of Directors' qualifying services to the Company have been borne by another Morgan Stanley Group undertaking. The amount of remuneration received by Directors in respect of their qualifying services to the Company is disclosed below:

	2018 $'000	2017 $'000
Total remuneration of all Directors:		
Aggregate remuneration	824	718
Long term incentive schemes	31	14
Company contributions to pension schemes	12	13
	867	745
Disclosures in respect of the highest paid Director:		
Aggregate remuneration	234	272
Long term incentive schemes	14	8
Company contributions to pension schemes	4	6
	252	286

Directors' remuneration has been calculated as the sum of cash, bonuses, and benefits in kind.

24. RELATED PARTY DISCLOSURES (CONTINUED)

Key management compensation (continued)

Directors' remuneration (continued)

All Directors who are employees of the Morgan Stanley Group are eligible for shares and share options of the parent company, Morgan Stanley, awarded under the Morgan Stanley Group's equity-based long term incentive schemes. In accordance with Schedule 5 paragraph 1(3)(a) of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, the above disclosures include neither the value of shares awarded, nor the gains made on exercise of share options. During the year three Directors received restricted stock unit awards in respect of qualifying services (2017: three), including the highest paid Director in both 2017 and 2018.

The value of assets (other than shares or share options) awarded under other long term incentive schemes has been included in the above disclosures when the awards vest, which is generally within three years from the date of the award.

The Morgan Stanley Group operates a defined contribution pension scheme, the Morgan Stanley UK Group Pension Plan. There are two Directors to whom retirement benefits are accruing under this defined contribution scheme (2017: three). One Director has benefits accruing under a non-UK defined contribution scheme (2017: none).

The Company has not provided any loans or other credit advances to its Directors during the year (2017: $nil).

25. EVENTS AFTER THE REPORTING PERIOD

In relation to the Morgan Stanley Group's preparation for the UK withdrawal from the EU, on 1 January 2019 MSIM Fund Management (Ireland) Limited, another Morgan Stanley Group undertaking, was appointed to the role of UCITS management company by Morgan Stanley Investment Funds and Morgan Stanley Liquidity Funds (both of which are Luxembourg domiciled funds), and to the role of AIFM by Galaxy Fund (a Luxembourg domiciled fund) and Alpha Plus Funds plc (a Republic of Ireland domiciled fund).

Following this appointment, the Company no longer acts as management company for these funds, but continues to provide authorised corporate director services to UK authorised OEICs, being the Morgan Stanley Funds (UK).

As a result, AUM contracted with the Company decreased from $95.9 billion to $2.0 billion.