Registered number: 04798688

Registered office:
20 Bank Street
Canary Wharf
London E14 4AD
United Kingdom

MORGAN STANLEY GAMMA INVESTMENTS

Report and financial statements

31 December 2019

MORGAN STANLEY GAMMA INVESTMENTS

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MORGAN STANLEY GAMMA INVESTMENTS

STRATEGIC REPORT

The Directors present their Strategic report for Morgan Stanley Gamma Investments (the "Company") for the year ended 31 December 2019.

PRINCIPAL ACTIVITY

The principal activity of the Company is to enter into financing transactions and investments, and its main transaction is a financing arrangement with a third party which is scheduled to generate income until 2033.

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". The Company's immediate controlling undertaking is MS Lion LLC.

There have not been any significant changes in the Company's principal activity in the year under review and no significant change in the Company's principal activity is expected.

BUSINESS REVIEW

Overview of 2019

The Company's statement of comprehensive income is set out on page 10. The Company made a profit after tax, of £417,000, compared to a profit after tax, in the prior year of £510,000. The decrease in profit after tax is primarily attributable to a decrease in net interest income of £39,000 relating to balances to and from external parties and other Morgan Stanley group undertakings and a net loss on investment in subsidiary in the current year of £52,000.

The Company's statement of financial position is set out on page 12. Total assets at the end of the year were £219,040,000, a decrease of £8,813,000 from the prior year. The decrease in total assets is primarily due to a decrease in financial assets due from external counterparties and other Morgan Stanley Group undertakings of £8,975,000 and impairment in investments in subsidiaries of £52,000. Total liabilities at the end of the year were £189,830,000, a decrease of £9,230,000 from its prior year. The decrease in total liabilities is primarily due to a decrease in amounts due to external counterparties and other Morgan Stanley group undertakings of £7,027,000 and a decrease in current tax liabilities of £2,204,000.

The performance of the Company is included in the results of the Morgan Stanley Group. The Company's Directors believe that providing further performance indicators for the Company itself would not enhance an understanding of the development, performance or position of the business of the Company.

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.

Emergence of COVID-19

The coronavirus disease (COVID-19) pandemic has, and will likely continue to, severely impact global economic conditions, resulting in substantial volatility in the global financial markets, increased unemployment, and operational challenges such as the temporary closure of businesses, sheltering-in-place directives and increased remote work protocols. Governments and central banks around the world have reacted to the economic crisis caused by the pandemic by implementing stimulus and liquidity programs and cutting interest rates, though it is unclear whether these or future actions will be successful in countering the economic disruption. If the pandemic is prolonged or the actions of governments and central banks are unsuccessful, the adverse impact on the global economy will deepen, and the future results of operations and financial condition of Morgan Stanley will be adversely affected.

MORGAN STANLEY GAMMA INVESTMENTS

STRATEGIC REPORT

BUSINESS REVIEW (CONTINUED)

Emergence of COVID-19 (continued)

Since the emergence of the pandemic each business segment of Morgan Stanley and the business of the Company has been impacted and such impact will likely be greater in the future if conditions persist (e.g., decline and volatility of asset prices, reduction in interest rates, widening of credit spreads, credit deterioration, market volatility and reduced investment banking advisory activity). Operationally, although Morgan Stanley have initiated a work remotely protocol and restricted business travel and have not experienced any significant loss of operational capability, if significant portions of Morgan Stanley's workforce, including key personnel, are unable to work effectively because of illness, government actions, or other restrictions in connection with the pandemic, the business impact of the pandemic could be exacerbated.

While the emergence of the COVID-19 (coronavirus) pandemic has negatively impacted the results of Morgan Stanley, the extent to which it, and the related global economic crisis, affects the businesses, the results of operations and financial condition, as well as the regulatory capital and liquidity ratios of Morgan Stanley, will depend on future developments that are highly uncertain and cannot be predicted, including the scope and duration of the pandemic and any recovery period, future actions taken by governmental authorities, central banks and other third parties in response to the pandemic, and the effects on our customers, counterparties, employees and third-party service providers. Morgan Stanley and the Company continue to use their Risk Management framework, including Stress testing, to understand the attendant uncertainties and their potential impact on our operations, liquidity and capital. Morgan Stanley is maintaining an active dialogue with all its relevant global regulators during this period.

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 has developed its own risk management policy framework, which leverages the risk management policies and procedures of the Morgan Stanley Group. The risk management policy framework includes escalation to appropriate senior management of the Company.

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 19 to the financial statements.

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.

The Company manages the market risk associated with its trading activities at both a trading division and an individual product level, and includes consideration of market risk at the legal entity level.

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.

Market risk management policies and procedures for the Company are consistent with those of the Morgan Stanley Group and include escalation to the 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.

MORGAN STANLEY GAMMA INVESTMENTS

STRATEGIC REPORT

BUSINESS REVIEW (CONTINUED)

Risk management (continued)

Credit risk (continued)

Credit risk management policies and procedures for the Company are consistent with those of the Morgan Stanley Group and include escalation to appropriate senior management personnel.

Credit risk exposure is managed on a global basis and in consideration of each significant legal entity within the Morgan Stanley Group. The credit risk management policies and procedures establish the framework for identifying, measuring, monitoring and controlling credit risk whilst ensuring transparency of material credit risks and compliance with established limits and escalating risk concentrations to appropriate senior management.

Liquidity risk

Liquidity risk refers to the risk that the Company will be unable to finance its operations due to a loss of access to the capital markets or difficulty in liquidating its assets. Liquidity risk encompasses the Company's ability (or perceived ability) to meet its financial obligations without experiencing significant business disruption or reputational damage that may threaten its viability as a going concern as well as associated funding risks triggered by the market or idiosyncratic stress events that may cause unexpected changes in funding needs or an inability to raise new funding. Generally, the Company incurs liquidity and funding risk as a result of its trading, investing and client facilitation activities.

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 19.

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.

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. Legal, regulatory and compliance risk is discussed below under "Legal, regulatory and compliance risk".

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 our business activities. This risk also includes contractual and commercial risk, such as the risk that 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, 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.

STRATEGIC REPORT

BUSINESS REVIEW (CONTINUED)

Risk management (continued)

Legal, regulatory and compliance risk (continued)

In addition, the Company has established procedures to mitigate the risk that 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 presents a continuing business challenge for the Company.

Going concern

Business risks associated with the uncertain market and economic conditions are being actively monitored and managed by the Morgan Stanley Group and Company. Retaining sufficient capital and liquidity to withstand these market pressures remains central to the Morgan Stanley Group and Company's strategy. The existing and potential effects of COVID-19 (coronavirus) on the business of the Morgan Stanley Group and Company have been considered as part of the going concern analysis, including impact on operational capacity, access to liquidity and capital, contractual obligations. The Company has access to further Morgan Stanley capital and liquidity as required.

Although the Company has net current liabilities payable within the next 12 months, the Company is performing in line with expectations and the net liabilities payable within the next 12 months are due to amounts owing to fellow Morgan Stanley Group undertakings, the demand for repayment of which is wholly within the control of the Morgan Stanley Group. In addition, the Company's ultimate parent undertaking and controlling entity, Morgan Stanley, intends to provide financial support to the Company to meet its obligations.

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 reports and financial statements.

Section 172(1) statement

The Directors are aware of their responsibilities to promote the success of the Company in accordance with s172 of the Companies Act 2006. When making decisions, Directors have regard to the interests of stakeholders relevant to the Company as well as the need to maintain a reputation for high standards of business conduct and the long term consequences of decisions. They also fulfil their responsibilities through the application of Morgan Stanley Group policies and practices, underpinned by Morgan Stanley's five core values of: do the right thing, put clients first, lead with exceptional ideas, commit to diversity and inclusion and give back.

Approved by the Board on 07 October 2020 and signed on its behalf by

DocuSigned by:
573CF73A7AAB435...
S T Merry
Director
08 October 2020

MORGAN STANLEY GAMMA INVESTMENTS

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 24) for the Company for the year ended 31 December 2019.

RESULTS AND DIVIDENDS

The profit for the year after tax was £417,000 (2018: £510,000).

During the year, dividends of £10,110,000 (2018: £10,593,000) were charged as interest expense out of which dividends of £8,893,000 (2018: £8,917,000) were paid to the holders of the Class A1-A86 preference shares. In addition, dividends of £71,000 (2018: £70,000) were charged as an interest expense out of which dividends of £60,000 (2018: £56,000) were paid to the holders of the Class B preference shares. Further capital repayments in aggregate of £10,606,000 (2018: £10,582,000) were made to the holders of the Classes A30, A31, A32 and A33 (2018: A26, A27, A28 and A29) preference shares.

RISK MANAGEMENT AND FUTURE DEVELOPMENTS

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

DIRECTORS

The following Directors held office throughout the year and to the date of approval of this report:

E T Laino
S I Merry
C A Villar

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 and its subsidiary undertakings.

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 and its subsidiary undertakings.

EVENTS AFTER THE REPORTING DATE

Pursuant to the Company's Articles of Association, on 13 March 2020 the Company paid dividends of £2,296,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares. On 15 June 2020 the Company paid dividends of £2,248,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares. On 15 September 2020 the Company paid dividends of £2,223,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares.

In addition, pursuant to the Company's Articles of Association, on 13 March 2020 the Company repaid capital of £2,578,000 in respect of the Company's Class A34 preference shares. On 15 June 2020 the Company repaid capital of £2,627,000 in respect of the Company's Class A35 preference shares. On 15 September 2020 the Company repaid capital of £2,652,000 in respect of the Company's Class A36 preference shares.

On 15 June 2020 by passing a Special Resolution, the ordinary share capital of the Company was reduced by £6,125,000 by reducing the par value of the Company's 24,500,002 issued £1.00 ordinary shares to £0.75 each (the "**Capital Reduction**").

MORGAN STANLEY GAMMA INVESTMENTS

DIRECTORS' REPORT

EVENTS AFTER THE REPORTING DATE (CONTINUED)

Since the balance sheet date, the coronavirus disease (COVID-19) pandemic has, and will likely continue to, severely impact global economic conditions, resulting in substantial volatility in the global financial markets and operational challenges. The extent of the impact is highly uncertain and cannot be predicted and could adversely affect the future operations and financial condition of Morgan Stanley and the Company.

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 United Kingdom Generally Accepted Accounting Practice ("UK GAAP") (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 on 07 October 2020 and signed on its behalf by

S T Merry
Director
08 October 2020

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MORGAN STANLEY GAMMA INVESTMENTS

Report on the audit of the financial statements

Opinion

In our opinion the financial statements of Morgan Stanley Gamma Investments (the 'Company'):

- give a true and fair view of the state of the company's affairs as at 31 December 2019 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 24.

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" (UK GAAP).

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 GAMMA INVESTMENTS (CONTINUED)

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.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MORGAN STANLEY GAMMA INVESTMENTS (CONTINUED)

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.

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.

P Cawley

Paul Cowley, C.A. (Senior Statutory Auditor)

For and on behalf of Deloitte LLP

Statutory Auditor

Glasgow, United Kingdom

08 October 2020

MORGAN STANLEY GAMMA INVESTMENTS

STATEMENT OF COMPREHENSIVE INCOME
Year ended 31 December 2019

	Note	2019 £'000	2018 £'000
Net trading expense		(111)	(112)
Interest income	4	10,811	11,299
Interest expense	4	(10,221)	(10,670)
Net interest income		590	629
Net loss on investment in subsidiary	5	(52)	-
Other expense	6	(10)	(8)
PROFIT BEFORE TAXATION		417	509
Income tax expense	7	-	1
PROFIT AND TOTAL COMPREHENSIVE INCOME FOR THE YEAR		417	510

All results were derived from continuing operations.

The notes on pages 13 to 43 form an integral part of the financial statements.

MORGAN STANLEY GAMMA INVESTMENTS

STATEMENT OF CHANGES IN EQUITY
Year ended 31 December 2019

	Share capital £'000	Retained earnings £'000	Total equity £'000
Balance at 1 January 2018	24,500	3,783	28,283
Profit and total comprehensive income for the year	-	510	510
Balance at 31 December 2018	24,500	4,293	28,793
Profit and total comprehensive income for the year	-	417	417
Balance at 31 December 2019	24,500	4,710	29,210

The notes on pages 13 to 43 form an integral part of the financial statements.

MORGAN STANLEY GAMMA INVESTMENTS

Registered number: 04798688

STATEMENT OF FINANCIAL POSITION
As at 31 December 2019

	Note	2019 £'000	2018 £'000
ASSETS			
Cash and short-term deposits		321	109
Trading financial assets	9	42	41
Loans and advances	10	217,560	226,470
Other receivables	11	69	133
Investments in subsidiaries	12	1,048	1,100
TOTAL ASSETS		219,040	227,853
LIABILITIES			
Trading financial liabilities	9	47	46
Other payables	13	2,408	58
Debt and other borrowings	14	187,375	196,752
Current tax liabilities		-	2,204
TOTAL LIABILITIES		189,830	199,060
EQUITY			
Share capital	15	24,500	24,500
Retained earnings		4,710	4,293
Equity attributable to owners of the Company		29,210	28,793
TOTAL EQUITY		29,210	28,793
TOTAL LIABILITIES AND EQUITY		219,040	227,853

These financial statements were approved by the Board on 07 October 2020 and authorised for issue on 08 October 2020.

Signed on behalf of the Board

DocuSigned by:

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S I Merry

Director

The notes on pages 13 to 43 form an integral part of the financial statements.

1. CORPORATE INFORMATION

The Company is incorporated and domiciled in England and Wales, United Kingdom ("UK"), at the following registered address: 20 Bank Street, Canary Wharf, London, E14 4AD, UK. The Company is a private unlimited company having share capital. The registered number of the Company is 04798688.

Details of the parent and ultimate parent of the group are disclosed in the Related party disclosures note 23 to these financial statements.

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 2019, has its registered office at c/o The Corporation Trust Company, 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

These financial statements are prepared in accordance with UK GAAP (UK 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'*. The Company has taken advantage of the disclosure exemptions available under FRS 101 in relation to fair value measurement as applicable to assets and liabilities other than financial instruments and 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 23.

New standards and interpretations adopted during the year

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

As part of the 2015-2017 Annual Improvements Cycle published in December 2017, the IASB made amendments to the following standards that are relevant to the Company's operations: IAS 12 *'Income Taxes'*, for application in accounting periods beginning on or after 1 January 2019.

IFRIC 23 '*Uncertainty over Income Tax Treatments*' was issued by the IASB in June 2017 for application in accounting periods beginning on or after 1 January 2019. The interpretation was endorsed by the EU in October 2018.

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

New standards and interpretations not yet adopted

At the date of authorisation of these financial statements, the following amendments to standards and interpretations relevant to the Company's operations were issued by the IASB but not mandatory for accounting periods beginning 1 January 2019. Except where otherwise stated, the Company does not expect that the adoption of the following amendments to standards and interpretations will have a material impact on the Company's financial statements.

2. BASIS OF PREPARATION (CONTINUED)

New standards and interpretations not yet adopted (continued)

Amendments to IAS 1 'Presentation of Financial Statements' and IAS 8 'Accounting Policies, Changes in Accounting Estimates and Errors': Definition of Material were issued by the IASB in October 2018, for application in accounting periods beginning on or after 1 January 2020. The amendments were endorsed by the EU in December 2019.

An amendment to IAS 1 'Presentation of Financial Statements': Classification of Liabilities as Current or Non-current was issued by the IASB in January 2020, for application in accounting periods beginning on or after 1 January 2022.

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 key sources of estimation uncertainty

No critical accounting judgements have been made in the process of applying the Company's accounting policies that have had a significant effect on the amounts recognised in the financial statements. There are no key sources of estimation uncertainty in the reporting period that may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities in the next financial year.

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 4. 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.

Specifically, the existing and potential effects of COVID-19 (coronavirus) on the operational capacity of the business, access to liquidity and capital, contractual obligations have been considered on page 1 and 2. The notes to the Company's financial statements include details of its financial instruments and provide further information, not included in the Strategic report, on its credit risk and liquidity risk.

Although the Company has net liabilities payable within the next 12 months, the Company is performing in line with expectations and the net liabilities payable within the next 12 months are due to amounts owing to fellow Morgan Stanley Group undertakings, the demand for repayment of which is wholly supported by the Morgan Stanley Group.

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 a period of at least 12 months from the date of approval of the financial statements. 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 Pounds Sterling, 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 Pounds Sterling.

b. Foreign currencies

All monetary assets and liabilities denominated in currencies other than Pounds Sterling are translated into Pounds Sterling at the rates ruling at the reporting date. Transactions and non-monetary assets and liabilities denominated in currencies other than Pounds Sterling are recorded at the rates prevailing at the dates of the transactions. All translation differences are taken through the statement of comprehensive income except where noted in 3(c) below.

c. Financial instruments

i) Financial instruments mandatorily at fair value through profit and loss

Trading financial instruments

Trading financial instruments including all derivatives are initially recorded on trade date at fair value (see note 3(d) below). All subsequent changes in fair value, foreign exchange differences and unrealised interest are reflected in the statement of comprehensive income in 'Net trading income'.

For all trading financial instruments, transaction costs are excluded from the initial fair value measurement of the financial instrument. These costs are recognised in the statement of comprehensive income.

ii) 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.

Investments in subsidiaries are stated at cost, less provision for any impairment (see note 3(f) below). Dividends, impairment losses and reversals of impairment losses are recognised in the statement of comprehensive income. Dividends from investments which would be classified as financial liabilities by the investee are classified as interest and recognised in the statement of comprehensive income in 'Interest income'.

iii) Financial assets and financial liabilities at amortised cost

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

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 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 expected credit losses ("ECL") allowance. Interest is recognised in the statement of comprehensive income in 'Interest income', using the EIR method as described below. 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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

c. Financial instruments (continued)

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

Financial liabilities classified at amortised cost include other payables and certain debt and other borrowings.

Financial liabilities are classified as being subsequently measured at amortised cost, except where they are held for trading or are designated as measured at FVPL. They 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 the 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.

Preference shares

The redeemable preference shares issued by the Company are classified as financial liabilities at amortised cost in accordance with the substance of the contractual arrangement. Dividends on these redeemable preference shares are recognised in the statement of comprehensive income in 'Interest expense' using the EIR method.

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.

Fair value is a market-based measure considered from the perspective of a market participant rather than an entity-specific measure. Therefore, even when market assumptions are not readily available, assumptions are set to reflect those that the Company believes market participants would use in pricing the asset or liability at the measurement date.

Where the Company manages a group of financial assets and financial liabilities on the basis of its net exposure to either market risks or credit risk, the Company measures the fair value of that group of financial instruments consistently with how market participants would price the net risk exposure at the measurement date.

In determining fair value, the Company uses various valuation approaches and establishes a hierarchy for inputs used in measuring fair value that requires the most observable inputs be used when available.

Observable inputs are inputs that market participants would use in pricing the asset or liability that were developed based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect assumptions the Company believes other market participants would use in pricing the asset or liability, that are developed based on the best information available in the circumstances.

The fair value hierarchy is broken down into three levels based on the observability of inputs as follows, with Level 1 being the highest and level 3 being the lowest level:

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

d. Fair value (continued)

Fair value measurement (continued)

- Level 1 – Quoted prices (unadjusted) in an active market for identical assets or liabilities

  Valuations based on quoted prices in active markets that the Morgan Stanley Group has the ability to access for identical assets or liabilities. Valuation adjustments, block discounts and discounts for equity-specific restrictions that would not transfer to market participants are not applied to Level 1 instruments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgement.

- Level 2 – Valuation techniques using observable inputs

  Valuations based on one or more quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

- Level 3 – Valuation techniques with significant unobservable inputs

  Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The availability of observable inputs can vary from product to product and is affected by a wide variety of factors, including the type of product, whether the product is new and not yet established in the marketplace, the liquidity of markets and other characteristics particular to the product. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgement. Accordingly, the degree of judgement exercised by the Company in determining fair value is greatest for instruments categorised in Level 3 of the fair value hierarchy.

The Company considers prices and inputs that are current as of the measurement date, including during periods of market dislocation. In periods of market dislocation, the observability of prices and inputs may be reduced for many instruments. This condition could cause an instrument to be reclassified from Level 1 to Level 2 or from Level 2 to Level 3 of the fair value hierarchy.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the total fair amount is disclosed in the level appropriate for the lowest level input that is significant to the total fair value of the asset or liability.

Valuation techniques
Many cash instruments and OTC derivative contracts have bid and ask prices that can be observed in the marketplace. Bid prices reflect the highest price that a party is willing to pay for an asset. Ask prices represent the lowest price that a party is willing to accept for an asset. The Company carries positions at the point within the bid-ask range that meets its best estimate of fair value. For offsetting positions in the same financial instrument, the same price within the bid-ask spread is used to measure both the long and short positions.

Fair value for many cash instruments and OTC derivative contracts is derived using pricing models. Pricing models take into account the contract terms, as well as multiple inputs including, where applicable, commodity prices, equity prices, interest rate yield curves, credit curves, correlation, creditworthiness of the counterparty, creditworthiness of the Company, option volatility and currency rates.

Where appropriate, valuation adjustments are made to account for various factors such as liquidity risk (bid-ask adjustments), credit quality, model uncertainty and concentration risk and funding.

Adjustments for liquidity risk adjust model-derived mid-market amounts of Level 2 and Level 3 financial instruments for the bid-mid or mid-ask spread required to properly reflect the exit price of a risk position. Bid-mid and mid-ask spreads are marked to levels observed in trade activity, broker quotes or other external

3. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

d. **Fair value (continued)**

Valuation techniques (continued)

third-party data. Where these spreads are unobservable for the particular position in question, spreads are derived from observable levels of similar positions.

Valuation process
Valuation Control ("VC") within the Finance is responsible for the Company's fair value valuation policies, processes and procedures. VC is independent of the business units and reports to the Chief Financial Officer of the Morgan Stanley Group ("CFO"), who has final authority over the valuation of the Company's financial instruments. VC implements valuation control processes designed to validate the fair value of the Company's financial instruments measured at fair value including those derived from pricing models.

Model Review
VC, in conjunction with the Model Risk Management Department ("MRM"), which reports to the Chief Risk Officer of the Morgan Stanley Group ("CRO"), independently reviews valuation models' theoretical soundness, the appropriateness of the valuation methodology and calibration techniques developed by the business units using observable inputs. Where inputs are not observable, VC reviews the appropriateness of the proposed valuation methodology to determine that it is consistent with how a market participant would arrive at the unobservable input. The valuation methodologies utilised in the absence of observable inputs may include extrapolation techniques and the use of comparable observable inputs. As part of the review, VC develops a methodology to independently verify the fair value generated by the business unit's valuation models.

Independent Price Verification
The business units are responsible for determining the fair value of financial instruments using approved valuation models and valuation methodologies. Generally on a monthly basis, VC independently validates the fair values of financial instruments determined using valuation models by determining the appropriateness of the inputs used by the business units and by testing compliance with the documented valuation methodologies approved in the model review process described above.

The results of this independent price verification and any adjustments made by VC to the fair value generated by the business units are presented to management of the Morgan Stanley Group's three business segments (i.e. Institutional Securities, Wealth Management and Investment Management), the CFO and the CRO on a regular basis.

VC uses recently executed transactions, other observable market data such as exchange data, broker/ dealer quotes, third-party pricing vendors and aggregation services for validating the fair values of financial instruments generated using valuation models. VC assesses the external sources and their valuation methodologies to determine if the external providers meet the minimum standards expected of a third-party pricing source. Pricing data provided by approved external sources are evaluated using a number of approaches; for example, by corroborating the external sources' prices to executed trades, by analyzing the methodology and assumptions used by the external source to generate a price and/ or by evaluating how active the third-party pricing source (or originating sources used by the third-party pricing source) is in the market. Based on this analysis, VC generates a ranking of the observable market data designed to ensure that the highest-ranked market data source is used to validate the business unit's fair value of financial instruments.

VC reviews the models and valuation methodology used to price new material Level 2 and Level 3 transactions and both Finance and MRM must approve the fair value of the trade that is initially recognised.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

e. Modification and 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.

The renegotiation or modification of the contractual cash flows of a financial instrument can lead to derecognition where the modification is "substantial", determined by qualitative assessment of whether the revised contractual terms of a financial instrument, such as a loan, are significantly different from those of the original financial instrument. In the event that the qualitative assessment is unclear, a quantitative 10% cash flow test is performed.

Where modifications do not result in derecognition of the financial instrument, the gross carrying amount of the financial instrument is recalculated and a modification gain/ (loss) is recognised in the statement of comprehensive income.

Upon derecognition of a financial asset, the difference between the previous carrying amount and the sum of any consideration received, together with the transfer of any cumulative gain/ loss previously recognised in equity, are recognised in the statement of comprehensive income.

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

f. Impairment of financial instruments

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.

Where a financial asset is credit-impaired at the reporting date, the ECL is measured as the difference between the asset's gross carrying amount and the present value of future cash flows, discounted at the original 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

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Impairment of financial instruments (continued)

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.

Assessment of significant increase in credit risk

When assessing SICR, 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.

The probability of default ("PD") is derived from internal credit rating grades (based on available information about the borrower) and multiple forward-looking macroeconomic scenarios which are probability weighted. Credit risk is considered to have increased significantly if the PD has significantly increased at the reporting date relative to the PD of the facility, at the date of initial recognition. The assessment of whether a change in PD is "significant" is based both on a consideration of the relative change in PD and on qualitative indicators of the credit risk of the facility, which indicate whether a loan is performing or in difficulty. In addition, as a backstop, the Company considers that SICR has occurred in all cases when an asset is more than 30 days past due.

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 are subject to impairment for SICR.

In general, ECL are measured so that they reflect:

- A probability-weighted range of possible outcomes
- The time value of money; and
- Relevant information relating to past, current and future economic conditions.

Calculation of ECL

ECL are calculated using three main components:

- Probability of default ("PD"): for accounting purposes, the 12 month and lifetime PD represent the expected point-in-time probability of a default over the next 12 months and over the remaining lifetime of the financial instrument respectively, based on conditions existing at the balance sheet date and future economic conditions.
- Expected loss given default ("LGD"): the LGD represents expected loss conditional on default, taking into account the mitigating effect of collateral, including the expected value of the collateral when realised and the time value of money.
- Estimated exposure at default ("EAD"): this represents the expected EAD, taking into account the expected repayment of principal and interest from the balance sheet date to the default event together with any expected drawdowns of the facility over that period.

These parameters are generally derived from internally developed statistical models, incorporating historical, current and forward-looking macro-economic data and country risk expert judgement. The macro-economic scenarios are reviewed quarterly.

The 12 month ECL is equal to the sum over the next 12 months of quarterly PD multiplied by LGD and EAD, with such expected losses being discounted at the EIR. Lifetime ECL is calculated using the discounted present value of total quarterly PDs multiplied by LGD and EAD, over the full remaining life of the facility.

When measuring ECL, the Company considers multiple scenarios, except where practical expedients are used to determine ECL. Practical expedients are used where they are consistent with the principles described above. Where there is a history of no credit losses, and where this is expected to persist into the future for

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Impairment of financial instruments (continued)

structural or other reasons, such as collateral or other credit enhancement, it is determined that the ECL for a financial instrument is de minimis (highly immaterial) and it may not be necessary to recognise the ECL.

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

If a financial asset has been the subject of modification which does not lead to its derecognition (refer accounting policy [3c]), SICR is assessed by comparing the risk of default of the financial instrument, based on the modified terms at the reporting date, with the risk of default of the financial instrument at inception, based on the financial instrument's original, unmodified terms.

Where the modification of contractual cash flows of a financial asset leads to its derecognition and the recognition of a new asset (refer note [3c]), the date of modification is treated as the date of initial recognition for the new financial asset when determining whether a SICR has occurred for that modified financial asset. In rare circumstances, after modification, the new asset is considered to be credit impaired, in which case it is treated as an asset which was credit-impaired at origination.

More information on measurement of ECL is provided in note 19 Financial risk management.

Presentation of ECL

ECL is recognised in the statement of comprehensive income. ECL on financial assets measured at amortised cost are presented as an ECL allowance. The allowance reduces the net carrying amount on the face of the statement of financial position.

Credit-impaired financial instruments

In assessing the impairment of financial instruments under the ECL model, the Company defines credit-impaired financial instruments in accordance with Credit Risk Management Department's policies and procedures. A financial instrument is credit-impaired when, based on current information and events, it is probable that the Company will be unable to collect all scheduled payments of principal or interest when due according to the contractual terms of the agreement.

Definition of Default

In assessing the impairment of financial instruments under the ECL model, the Company defines default in accordance with Credit Risk Management Department's policies and procedures. This considers whether the borrower is unlikely to pay its credit obligations to the Company in full and takes into account qualitative indicators, such as breaches of covenants. The definition of default also includes a presumption that a financial asset which is more than 90 days past due ("DPD") has defaulted.

Write-offs

Loans and debt securities are written off (either partially or in full) when they are deemed uncollectible which generally occurs when all commercially reasonable means of recovering the loan balance have been exhausted. Such determination is based on an indication that the borrower can no longer pay the obligation, or that the proceeds from collateral will not be sufficient to pay the loan. Partial write-offs are made when a portion of the loan is uncollectable. However, financial assets that are written off could still be subject to enforcement activities for recoveries of amounts due. If the amount to be written off is greater than the accumulated loss allowance, the difference is reflected directly in the income statement and is not recognised in the loss allowance account. Any subsequent recoveries are credited to income statement.

Impairment losses on investments in subsidiaries are measured as the difference between cost and the current estimated recoverable amount. When the recoverable amount is less than the cost, an impairment is recognised within the statement of comprehensive income in 'Net loss on investment in subsidiary' and is reflected against the carrying amount of the impaired asset on the statement of financial position.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

g. Cash and cash equivalents

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

h. Income tax

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

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.

4. INTEREST INCOME AND INTEREST EXPENSE

'Interest income' and 'Interest expense' represent total interest income and total interest expense for financial assets and financial liabilities that are not carried at fair value. Interest income primarily represents interest income on loans to other Morgan Stanley Group undertakings totalling £701,000 (2018: £704,000) and interest income from financing arrangements with external parties of £10,110,000 (2018: £10,593,000). Interest expense represents interest expense on loans from Morgan Stanley Group undertakings of £40,000 (2018: £7,000) and preference share dividends payable of £10,181,000 (2018: £10,663,000).

No other gains or losses have been recognised in respect of financial assets measured at amortised cost other than as disclosed as 'Interest income' within the statement of comprehensive income.

All interest income and expense relates to financial assets and financial liabilities at amortised cost and is calculated using the EIR method (see accounting policy 3(c) (iii)).

5. NET LOSSES ON INVESTMENTS IN SUBSIDIARIES

	2019	2018
	£'000	£'000
Impairment loss	52	-

Details of all investments in subsidiaries of the Company at 31 December 2019 and 31 December 2018 are disclosed in the investment in subsidiaries note (note 12).

6. OTHER EXPENSE

	2019	2018
	£'000	£'000
Auditor's remuneration:		
Fees payable to the Company's auditor for the audit of the Company's annual financial statements	10	10
Other	-	(2)
	10	8

The Company employed no staff during the year (2018: nil).

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 23).

MORGAN STANLEY GAMMA INVESTMENTS

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2019

7. INCOME TAX EXPENSE

	2019	2018
	£'000	£'000
Current tax expense		
UK corporation tax at 19% (2018: 19%)		
- Current year	-	-
- Adjustments in respect of prior years	-	(1)
Income tax expense	-	(1)

Finance Act 2016 enacted a reduction in the UK corporation tax rate to 17% with effect from 1 April 2020. This reduction impacts the current tax charge in future periods. However, following the UK Budget on 11 March 2020 and subsequent resolutions given statutory effect under the Provisional Collection of Taxes Act 1968, for the financial year 2020 the UK statutory rate is 19%. While this change does not affect the income tax charge for the year, it will affect future years.

Reconciliation of effective tax rate

The current year income tax expense is lower (2018: lower) than that resulting from applying the average standard rate of corporation tax in the United Kingdom ("UK") for the year of 19% (2018: 19%). The main differences are explained below:

	2019	2018
	£'000	£'000
Profit before taxation	417	509
Income tax using the average standard rate of corporation tax in the UK of 19% (2018: 19%)	79	97
Impact on tax of:		
Expenses not deductible for tax purposes	10	-
Group relief received for no cash consideration	(2,023)	(2,123)
Non-deductible dividends on preference shares shown as interest expense	1,934	2,026
Adjustment in respect of prior year	-	(1)
Total income tax expense in the statement of comprehensive income	-	(1)

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES BY MEASUREMENT CATEGORY

The following table analyses financial assets and financial liabilities as presented in the statement of financial position by IFRS 9 classification.

31 December 2019	**FVPL (mandatorily)**	**Amortised cost**	**Total**
	£'000	£'000	£'000
Cash and short-term deposits	-	321	321
Trading financial assets	42	-	42
Loans and advances	-	217,560	217,560
Other receivables	-	69	69
Total financial assets	42	217,950	217,992

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES BY MEASUREMENT CATEGORY (CONTINUED)

31 December 2019	FVPL (mandatorily) £'000	Amortised cost £'000	Total £'000
Trading financial liabilities	47	-	47
Other payables	-	2,408	2,408
Debt and other borrowings	-	187,375	187,375
Total financial liabilities	47	189,783	189,830

31 December 2018

Cash and short-term deposits	-	109	109
Trading financial assets	41	-	41
Loans and advances	-	226,470	226,470
Other receivables	-	133	133
Total financial assets	41	226,712	226,753
Trading financial liabilities	46	-	46
Other payables	-	58	58
Debt and other borrowings	-	196,752	196,752
Total financial liabilities	46	196,810	196,856

9. TRADING FINANCIAL ASSETS AND LIABILITIES

Trading assets and trading liabilities are summarised as follows:

	2019		2018	
	Assets £'000	Liabilities £'000	Assets £'000	Liabilities £'000
Derivatives				
- Total return swaps	42	47	41	46

There are no terms and conditions of any trading asset or trading liability that may individually significantly affect the amount, timing and certainty of future cash flows for the Company.

10. LOANS AND ADVANCES

	2019 £'000	2018 £'000
Loans and advances at amortised cost	217,560	226,470

11. OTHER RECEIVABLES

	2019 £'000	2018 £'000
Amounts due from other Morgan Stanley Group undertakings	69	133

12. INVESTMENTS IN SUBSIDIARIES

	Subsidiary undertakings £'000
Cost	
At 1 January 2019 and 31 December 2019	1,100
Impairment provisions	
At 1 January 2019	-
Provisions made in the year	52
At 31 December 2019	52
Carrying amounts	
At 31 December 2018	1,100
At 31 December 2019	1,048

Details of all investments in subsidiaries of the Company at 31 December 2019 and 31 December 2018 are as follows:

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
			2019	2018	2019	2018	
Morgan Stanley Portland Investments Limited	20 Bank Street Canary Wharf, London E14 4AD United Kingdom	Ordinary	100%	100%	100%	100%	Financing Company

13. OTHER PAYABLES

	2019 £'000	2018 £'000
Other payables (amortised cost)		
Amounts due to other Morgan Stanley Group undertakings	2,408	58

14. DEBT AND OTHER BORROWINGS

	2019 £'000	2018 £'000
Debt and other borrowings (amortised cost)		
Preference shares	142,017	152,623
Preference share dividends payable	45,358	44,129
	187,375	196,752

As at 31 December 2019, the issued share capital of the Company includes 53 Class A34-A86 redeemable non-cumulative £1 preference shares, 1,000,000 Class B redeemable non-cumulative £1 preference shares and 1 Class AR redeemable non-cumulative £1 preference shares, classified as financial liabilities.

MORGAN STANLEY GAMMA INVESTMENTS

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2019

14. DEBT AND OTHER BORROWINGS (CONTINUED)

Preference Shares

As at 31 December 2019, the issued share capital of the Company included 53 Class A34-A86 redeemable non-cumulative £1 preference shares, classified as financial liabilities.

	Class A1-A86 preference shares of £1 each: £'000
Authorised:	
At 1 January 2018	162,205
Decrease in the year:	
Reduction in paid up capital – 15 March 2018	(2,626)
Reduction in paid up capital – 15 June 2018	(2,652)
Reduction in paid up capital – 14 September 2018	(2,652)
Reduction in paid up capital – 14 December 2018	(2,652)
At 31 December 2018	151,623
Decrease in the year:	
Reduction in paid up capital – 15 March 2019	(2,652)
Reduction in paid up capital – 14 June 2019	(2,652)
Reduction in paid up capital – 13 September 2019	(2,651)
Reduction in paid up capital – 13 December 2019	(2,651)
At 31 December 2019	141,017

	Number	Class A1-A86 preference shares of £1 each: £'000
Allotted and fully paid:		
At 1 January 2018		162,205
Decrease in the year:		
Reduction in paid up capital – 15 March 2018	A-26	(2,626)
Reduction in paid up capital – 15 June 2018	A-27	(2,652)
Reduction in paid up capital – 14 September 2018	A-28	(2,652)
Reduction in paid up capital – 14 December 2018	A-29	(2,652)
At 31 December 2018		151,623
Decrease in the year:		
Reduction in paid up capital – 15 March 2019	A-30	(2,652)
Reduction in paid up capital – 14 June 2019	A-31	(2,652)
Reduction in paid up capital – 13 September 2019	A-32	(2,651)
Reduction in paid up capital – 13 December 2019	A-33	(2,651)
At 31 December 2019		141,017

As at 31 December 2019, the issued share capital of the Company included 1 Class AR redeemable non-cumulative £1 preference shares, classified as financial liabilities.

14. DEBT AND OTHER BORROWINGS (CONTINUED)

Preference Shares (continued)

	Number	Class AR preference shares of £1 each: £'000
Authorised, allotted and fully paid:		
At 1 January 2018 and 31 December 2018	1	-
At 1 January 2019 and 31 December 2019	1	-

As at 31 December 2019, the issued share capital of the Company included 1,000,000 Class B redeemable non-cumulative £1 preference shares, classified as financial liabilities.

	Number	Class B preference shares of £1 each: £'000
Authorised, allotted and fully paid:		
At 1 January 2018 and 31 December 2018	1,000,000	1,000
At 1 January 2019 and 31 December 2019	1,000,000	1,000

The holders of Classes A1-A86 preference shares and Class B preference shares are entitled, pari passu, in priority to any payment of dividend of any other class of shares which are not preference shares, a cumulative fixed preferential dividend at a fixed rate per annum per preference share of 6.4709% of the nominal value (as such value may be reduced on a reduction or repayment of part of the capital in accordance with the Company's Articles of Association) of each preference share of that class. Pursuant to the Company's Articles of Association, the capital of the Classes A1-A86 preference shares is scheduled to be reduced without resolution of the Directors or of the members commencing 15 December 2011 in quarterly instalments until 15 March 2033. Accordingly, on 15 March 2019 (£2,652,000), 14 June 2019 (£2,652,000), 13 September 2019 (£2,651,000) and 13 December 2019 (£2,651,000) the total amount of £10,606,000 was paid off the capital of the Class A30, Class A31, Class A32 and Class A33 preference shares respectively.

With effect from the date on which the capital of the last of the Classes A1-A86 preference shares to be reduced, is reduced, out of the profits available for distribution, the holder of the Class AR preference share is entitled, pari passu, to the holders of the Class B preference shares, in priority to any payment of dividend to the holders of any other class of shares which are not preference shares, a cumulative preferential dividend at a fixed rate per annum of £50,000, as defined in the Company's Articles of Association. The Class AR preference share is scheduled for redemption without resolution of the Directors or of the members on 15 June 2153.

The preference shares carry no voting rights in the Company. The Company may by special resolution at any time, redeem the whole or any part of the preference shares upon giving not less than 14 days' prior notice in writing of the date when such redemption is to be effective. No premium is payable on redemption. The circumstances (if any) in which the Company may exercise its rights under the Articles of Association shall be determined by the Directors on allotment of a preference share.

During the year, dividends of £10,110,000 (2018: £10,593,000) were charged as interest expense out of which dividends of £8,893,000 (2018: £8,917,000) were paid to the holders of the Class A1-A86 preference shares. In addition, dividends of £71,000 (2018: £70,000) were charged as an interest expense out of which dividends of £60,000 (2018: £56,000) were paid to the holders of the Class B preference shares. Further capital repayments in aggregate of £10,606,000 (2018: £10,582,000) were made to the holders of the Classes A30, A31, A32 and A33 preference shares.

14. DEBT AND OTHER BORROWINGS (CONTINUED)

Preference Shares (continued)

In addition to the share capital of class A and B preference shares of £142,017,000 (2018: £152,623,000) above, there are contractual preference dividends of £45,358,000 (2018: £44,129,000) accrued at 31 December 2019. Total share capital and accrued dividends classified within liabilities is therefore £187,375,000 (2018: £196,752,000)

15. EQUITY

Ordinary share capital

	Ordinary shares of £1 each	Ordinary shares of £1 each	Total ordinary shares
	Number	£'000	£'000
Authorised, Allotted and fully paid			
At 1 January 2018 and 31 December 2018	24,500,002	24,500	24,500
At 1 January 2019 and 31 December 2019	24,500,002	24,500	24,500

The holders of 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, except that preference shareholders participate only to the extent of the nominal value of the shares plus any accrued dividends.

Other shares classified as financial liabilities

The terms of other shares classified as financial liabilities are detailed in note 14, Debt and other borrowings.

16. DIVIDENDS

During the year, the Company accrued Class A preference share dividends of £10,110,000 (2018: £10,593,000) and Class B preference share dividends of £71,000 (2018: £70,000) which were charged as interest expense.

The following amounts represent the dividends paid in the current and prior year:

	2019		2018	
	Per share £	Total £'000	Per share £	Total £'000
Dividends on preference shares	-	8,953	-	8,973

Pursuant to the Company's Articles of Association, on 13 March 2020 the Company paid dividends of £2,296,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares. On 15 June 2020 the Company paid dividends of £2,248,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares. On 15 September 2020 the Company paid dividends of £2,223,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares.

17. 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, recognised or settled.

At 31 December 2019	Less than or equal to Twelve Months £'000	More than Twelve Months £'000	Total £'000
ASSETS			
Cash and short-term deposits	321	-	321
Trading financial assets	42	-	42
Loans and advances	19,499	198,061	217,560
Other receivables	69	-	69
Investment in subsidiary	-	1,048	1,048
	19,931	199,109	219,040
LIABILITIES			
Trading financial liabilities	47	-	47
Other payables	2,408	-	2,408
Debt and other borrowings			
Preference shares	10,533	131,484	142,017
Preference share dividends payable	9,031	36,327	45,358
	22,019	167,811	189,830

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	109	-	109
Trading financial assets	41	-	41
Loans and advances	19,499	206,971	226,470
Other receivables	133	-	133
Investment in subsidiary	-	1,100	1,100
	19,782	208,071	227,853
LIABILITIES			
Trading financial liabilities	46	-	46
Other payables	58	-	58
Debt and other borrowings			
Preference shares	10,606	142,017	152,623
Preference share dividends payable	8,953	35,176	44,129
Current tax liabilities	2,204	-	2,204
	21,867	177,193	199,060

18. SEGMENT REPORTING

The Company has only one class of business as described in the Strategic report and operates in one geographic region being Europe, Middle East and Africa ("EMEA").

19. 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 appropriate senior management personnel of the Company.

Significant risks faced by the Company resulting from its trading, financing and investment activities are set out below.

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 to corporate entities through its Institutional Securities business segment.

Credit risk management

Credit risk exposure is managed on a global basis and in consideration of each significant legal entity within the Morgan Stanley Group. The credit risk management policies and procedures establish the framework for identifying, measuring, monitoring and controlling credit risk whilst ensuring transparency of material credit risks, compliance with established limits and escalating risk concentrations to appropriate senior management.

The Company may incur credit risk in its Institutional Securities business segment through a variety of activities, including, but not limited to, the following:

- entering into swap or other derivative contracts under which counterparties may have obligations to make payments to the Company; and
- extending credit to clients through lending commitments;

Monitoring and Control

In order to help protect the Company from losses, the Credit Risk Management Department establishes firm-wide practices to evaluate, monitor and control credit risk at the transaction, obligor and portfolio levels. The Credit Risk Management Department approves extensions of credit, evaluates the creditworthiness of the Company's counterparties and borrowers on a regular basis, and helps ensure that credit exposure is actively monitored and managed. The evaluation of counterparties and borrowers 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. In addition, credit risk exposure is actively managed by credit professionals and committees within the Credit Risk Management Department and through various risk committees, whose membership includes individuals from the Credit Risk Management Department.

A Credit Limits Framework is utilised to manage credit risk levels across the Company. The Credit Limits Framework is calibrated within the Morgan Stanley Group's risk tolerance and includes single-name limits and portfolio concentration limits by country and industry. The Credit Risk Management Department helps ensure timely and transparent communication of material credit risks, compliance with established limits and escalation of risk concentrations to appropriate senior management.

19. FINANCIAL RISK MANAGEMENT (CONTINUED)

Credit risk management (continued)

Monitoring and Control (continued)

The Credit Risk Management Department also works closely with the Market Risk Department ("MRD") and applicable business units to monitor risk exposures and to perform stress tests to identify, analyse and control credit risk concentrations arising from the Company's lending and trading activities. The stress tests shock market factors (e.g. interest rates, commodity prices, credit spreads), risk parameters (e.g. default probabilities and LGD), in order to assess the impact of stresses on exposures, profit and loss, and the Company's capital position. Stress tests are conducted in accordance with established Company policies and procedures.

Credit Evaluation

The evaluation of corporate and institutional counterparties and borrowers includes assigning obligor credit ratings, which reflect an assessment of an obligor's PD and LGD. Credit evaluations typically involve the assessment of financial statements, leverage, liquidity, capital strength, asset composition and quality, market capitalisation, access to capital markets, the adequacy of collateral, if applicable, and in the case of certain loans, cash flow projections and debt service requirements. The Credit Risk Management Department also evaluates strategy, market position, industry dynamics, management and other factors that could affect the obligor's risk profile. Additionally, the Credit Risk Management Department evaluates the relative position of the Company's exposure in the borrower's capital structure and relative recovery prospects, as well as adequacy of collateral (if applicable) and other structural elements of the particular transaction. At 31 December 2019, the Company's material credit exposure was to corporate entities.

Risk Mitigation

The Credit Risk Management Department may seek to mitigate credit risk from its lending and trading activities in multiple ways, including collateral provisions, guarantees and hedges. At the transaction level, the Credit Risk Management Department seeks to mitigate risk through management of key risk elements such as size, tenor, financial covenants, seniority and collateral. The Morgan Stanley Group actively hedges its lending and derivatives exposure through various financial instruments that may include single-name, portfolio and structured credit derivatives. Additionally, the Morgan Stanley Group may sell, assign or syndicate funded loans and lending commitments to other financial institutions in the primary and secondary loan markets. In connection with its derivatives trading activities, the Morgan Stanley Group generally enters into master netting agreements and collateral arrangements with counterparties. These agreements provide the Morgan Stanley Group with the ability to demand collateral, as well as to liquidate collateral and offset receivables and payables covered under the same master agreement in the event of a counterparty default.

Exposure to credit risk

The maximum exposure to credit risk ("gross credit exposure") of the Company as at 31 December 2019 is disclosed below, based on the carrying amounts of the financial assets, which the Company believes are subject to credit risk. The table includes financial instruments subject to ECL and not subject to ECL. Those financial instruments that bear credit risk but are not subject to ECL are subsequently measured at fair value. The Company has not entered into any credit enhancements to manage its exposure to credit risk therefore gross credit exposure reflected in the below table is also the net credit exposure.

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.

19. FINANCIAL RISK MANAGEMENT (CONTINUED)

Exposure to credit risk (continued)

Exposure to credit risk by class

	Gross credit exposure [(1)]	
	2019	**2018**
	£'000	**£'000**
Subject to ECL:		
Cash and short-term deposits	321	109
Loans and advances	217,560	226,470
Other receivables	69	133
Not subject to ECL:		
Trading financial assets	42	41
Derivatives		
	217,992	226,753

(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

At 31 December 2019, the carrying amount of financial assets at amortised cost subject to accounting ECLs was £217,950,000. No ECL has been recognised on these financial assets as there is no history of credit risk losses and this is expected to persist into the future for structural reasons, including credit risk mitigants.

Exposure to credit risk by internal rating grades

Internal credit ratings, as below, are derived using methodologies generally consistent with those used by external agencies:

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

The table below shows gross carrying amount by internal rating grade. All exposures subject to ECL are Stage 1, unless otherwise shown.

19. FINANCIAL RISK MANAGEMENT (CONTINUED)

Exposure to credit risk by internal rating grades (continued)

	Investment grade: A	
	2019	**2018**
	£'000	**£'000**
Subject to ECL:		
Cash and short-term deposits	321	109
Loans and advances	217,560	226,470
Other receivables	69	133
Total subject to ECL	217,950	226,712

a. Financial assets measured at FVPL

	Gross credit exposure	
Credit rating	**2019**	**2018**
	£'000	**£'000**
A	42	41
Total	42	41

Liquidity risk

Liquidity risk refers to the risk that the Company will be unable to finance its operations due to a loss of access to the capital markets or difficulty in liquidating its assets. Liquidity risk encompasses the Company's ability (or perceived ability) to meet its financial obligations without experiencing significant business disruption or reputational damage that may threaten the Company's viability as a going concern. Liquidity risk also encompasses the associated funding risks triggered by the market or idiosyncratic stress events that may cause unexpected changes in funding needs or an inability to raise new funding. Generally, the Company incurs liquidity risk as a result of its trading, lending, investing and client facilitation activities.

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 Liquidity Risk Department is a distinct area in Risk Management, which oversees and monitors liquidity risk. The Liquidity Risk Department ensures transparency of material liquidity risks, compliance with established risk limits and escalation of risk concentrations to appropriate senior management. To execute these responsibilities, the Liquidity Risk Department:

- Establishes limits in line with the Morgan Stanley Group's risk appetite;
- Identifies and analyses emerging liquidity risks to ensure such risks are appropriately mitigated;
- Monitors and reports risk exposures against metrics and limits, and;
- Reviews the methodologies and assumptions underpinning the Morgan Stanley Group's Liquidity Stress Tests to ensure sufficient liquidity and funding under a range of adverse scenarios.

The liquidity risks identified by these processes are summarised in reports produced by the Liquidity Risk Department that are circulated to and discussed with the EMEA Assets/ Liability Management Committee ("ALCO"), EMEA Risk Committee and the MSI Risk Committee as appropriate.

19. FINANCIAL RISK MANAGEMENT (CONTINUED)

Liquidity risk (continued)

The Treasury Department and applicable business units have primary responsibility for evaluating, monitoring and controlling the liquidity risks arising from the Morgan Stanley Group's business activities, and for maintaining processes and controls to manage the key risks inherent in their respective areas. The Liquidity Risk Department coordinates with the Treasury Department and these business units to help ensure a consistent and comprehensive framework for managing liquidity risk across the Morgan Stanley Group.

The Company's liquidity risk management policies and procedures are consistent with those of the Morgan Stanley Group.

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 following principles guide the Company's liquidity risk management framework:

- Sufficient liquid assets should be maintained to cover maturing liabilities and other planned and contingent outflows;
- Maturity profile of assets and liabilities should be aligned, with limited reliance on short-term funding;
- Source, counterparty, currency, region, and term of funding should be diversified; and
- Liquidity Stress Tests should anticipate, and account for, periods of limited access to funding.

The Company hedges all of its financial liabilities with financial assets of similar maturity profile.

The core components of the Morgan Stanley Group's liquidity management framework that support our target liquidity profile, which includes consideration of the liquidity risk for each individual legal entity, are the Required Liquidity Framework, Liquidity Stress Tests and the Global Liquidity Reserve.

Required Liquidity Framework

The Required Liquidity Framework establishes the amount of liquidity the Morgan Stanley Group 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 Required Liquidity Framework considers the most constraining liquidity requirement to satisfy all regulatory and internal limits at a consolidated and legal entity level.

Liquidity Stress Tests

The Morgan Stanley Group uses Liquidity Stress Tests to model external and intercompany 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.

The Liquidity Stress Tests are produced for Morgan Stanley and its major operating subsidiaries, as well as at major currency levels, to capture specific cash requirements and cash availability at various legal entities. The Liquidity Stress Tests assume that subsidiaries will use their own liquidity first to fund their obligations before drawing liquidity from Morgan Stanley. It is also assumed that Morgan Stanley will support its subsidiaries and will not have access to cash that may be held at certain subsidiaries. In addition to the assumptions underpinning the Liquidity Stress Tests, Morgan Stanley Group takes into consideration the settlement risk related to intra-day settlement and clearing of securities and financial activities.

19. FINANCIAL RISK MANAGEMENT (CONTINUED)

Liquidity risk (continued)

Since the Company hedges the liquidity risk of its financial liabilities with financial assets that match the maturity profile of the financial liabilities, the Company is not considered a major operating subsidiary for the purposes of liquidity risk. However, the Company would have access to the cash or liquidity reserves held by Morgan Stanley in the unlikely event that it was unable to access adequate financing to service its financial liabilities when they become payable.

The Required Liquidity Framework and Liquidity Stress Tests are evaluated on an ongoing basis and reported to the Firm Risk Committee, ALCO, and other appropriate risk committees including the Morgan Stanley International Limited Board Risk Committee.

Global Liquidity Reserve

The Morgan Stanley Group maintains sufficient liquidity reserves ("the Global Liquidity Reserve") to cover daily funding needs and to meet strategic liquidity targets sized by the Required Liquidity Framework and Liquidity Stress Tests. The size of the Global Liquidity Reserve is actively managed by the Morgan Stanley Group considering the following components: unsecured debt maturity profile; balance sheet size and composition; funding needs in a stressed environment inclusive of contingent cash outflows; and collateral requirements. In addition, the Morgan Stanley Group's Global Liquidity Reserve includes a discretionary surplus based on the Morgan Stanley Group's risk tolerance and is subject to change depending on market and firm-specific events. The Global Liquidity Reserve consists of cash and unencumbered securities sourced from trading assets, investment securities and securities received as collateral.

The Morgan Stanley Group's Global Liquidity Reserve, to which the Company has access, is held within Morgan Stanley and its major operating subsidiaries and is composed of diversified cash and cash equivalents and unencumbered highly liquid securities.

Eligible unencumbered highly liquid securities include US government securities, US agency securities, US agency mortgage-backed securities, non-US government securities and other highly liquid investment grade securities.

The Global Liquidity Reserve may fluctuate from period to period based on the overall size and composition of the balance sheet, the maturity profile of our unsecured debt and estimates of funding needs in a stressed environment, among other factors.

The ability to monetise assets during a liquidity crisis is critical. The Morgan Stanley Group believes that the assets held in its Global Liquidity Reserve can be monetised within five business days in a stressed environment given the highly liquid and diversified nature of the reserves.

Funding management

The Morgan Stanley Group manages its funding in a manner that reduces the risk of disruption to the Morgan Stanley Group's and the Company's operations. The Morgan Stanley Group pursues a strategy of diversification of secured and unsecured funding sources (by product, investor and region) and attempts to ensure that the tenor of the Morgan Stanley Group's, and the Company's, liabilities equals or exceeds the expected holding period of the assets being financed.

The Morgan Stanley Group funds its balance sheet on a global basis through diverse sources, which includes consideration of the funding risk of each legal entity. These sources include the Morgan Stanley Group's equity capital, long-term borrowing, securities sold under agreements to repurchase ("repurchase agreements"), securities lending, deposits, letters of credit and lines of credit. The Morgan Stanley Group has active financing programmes for both standard and structured products targeting global investors and currencies.

19. FINANCIAL RISK MANAGEMENT (CONTINUED)

Liquidity risk (continued)

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 the 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

In the following maturity analysis of financial assets and financial liabilities, derivative contracts, financial assets designated at fair value through profit or loss and financial liabilities designated at fair value through profit or loss are disclosed according to their earliest contractual maturity; all such amounts are presented at their fair value, consistent with how these financial instruments are managed. All other amounts represent undiscounted cash flows receivable and payable by the Company arising from its financial assets and financial liabilities to earliest contractual maturities as at 31 December 2019 and 31 December 2018. Receipts of financial assets and repayments of financial liabilities that are subject to immediate notice are treated as if notice were given immediately and are classified as on demand. This presentation is considered by the Company to appropriately reflect the liquidity risk arising from these financial assets and financial liabilities, presented in a way that is consistent with how the liquidity risk on these financial assets and financial liabilities is managed by the Company.

31 December 2019	On demand £'000	Equal to or more than 3 months but less than 1 year £'000	Equal to or more than 1 year but less than 5 years £'000	Equal to or more than 5 years £'000	Total £'000
Financial assets					
Cash and short-term deposits	321	-	-	-	321
Trading financial assets					
Derivatives	42	-	-	-	42
Loans and advances					
External counterparties		19,499	77,997	162,548	260,044
Morgan Stanley Group undertakings	-	-	30,467	1,000	31,467
Other receivables					
Morgan Stanley Group undertakings	-	69	-	-	69
Total financial assets	363	19,568	108,464	163,548	291,943
Financial liabilities					
Trading financial liabilities					
Derivatives	47	-	-	-	47
Other payables					
Morgan Stanley Group undertakings		2,408	-	-	2,408
Debt and other borrowings					
Preference shares		10,533	41,997	164,299	216,829
Preference share dividend payable		9,031	36,327	-	45,358
Total financial liabilities	47	21,972	78,324	164,299	264,642

MORGAN STANLEY GAMMA INVESTMENTS

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2019

19. FINANCIAL RISK MANAGEMENT (CONTINUED)

Liquidity risk (continued)

Maturity analysis (continued)

31 December 2018	On demand £'000	Equal to or more than 3 months but less than 1 year £'000	Equal to or more than 1 year but less than 5 years £'000	Equal to or more than 5 years £'000	Total £'000
Financial assets					
Cash and short-term deposits	109	-	-	-	109
Trading financial assets					
Derivatives	41	-	-	-	41
Loans and advances					
External counterparties	-	19,499	77,997	182,047	279,543
Morgan Stanley Group undertakings	-	-	29,988	1,000	30,988
Other receivables					
Morgan Stanley Group undertakings	-	133	-	-	133
Total financial assets	150	19,632	107,985	183,047	310,814

Financial liabilities

	On demand £'000	Equal to or more than 3 months but less than 1 year £'000	Equal to or more than 1 year but less than 5 years £'000	Equal to or more than 5 years £'000	Total £'000
Trading financial liabilities					
Derivatives	46	-	-	-	46
Other payables					
Morgan Stanley Group undertakings		58	-	-	58
Debt and other borrowings					
Preference shares		10,606	43,119	183,892	237,617
Preference share dividend payable		8,953	35,176	-	44,129
Total financial liabilities	46	19,617	78,295	183,892	281,850

19. 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.

The Company manages the market risk associated with its trading activities at both division and an individual product level, and includes consideration of market risk at the legal entity level.

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.

To execute these responsibilities, the Morgan Stanley Group monitors the market risk of the firm against limits on aggregate risk exposures, performs a variety of risk analyses including monitoring Value-at-risk ("VaR") and stress testing analyses, routinely reports risk summaries and maintains the VaR and scenario analysis methodologies. 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 exposed to the following types of market risk under this definition: interest rate risk.

Interest rate risk

Interest rate risk is defined by IFRS 7 'Financial instruments: Disclosures' 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 having exposure on the net position between the proxy based intercompany loans, and the basis swap which is paying out variable but earning fixed interest.

The application of a parallel shift in market interest rates of 50 basis points increase or decrease to these positions, would result in a net gain or loss of approximately £146,616 (2018: £153,520) in the statement of comprehensive income.

20. 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'* 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.

a. Financial assets and liabilities recognised at fair value on a recurring basis

The following tables present the carrying value of the Company's financial assets and financial liabilities recognised at fair value on a recurring basis, classified according to the fair value hierarchy.

20. ASSETS AND LIABILITIES MEASURED AT FAIR VALUE (CONTINUED)

a. Financial assets and liabilities recognised at fair value on a recurring basis (continued)

2019	Quoted prices in active market (Level 1) £'000	Valuation techniques using observable inputs (Level 2) £'000	Valuation techniques with significant unobservable inputs (Level 3) £'000	Total £'000
Trading financial assets:				
Derivatives	-	42	-	42
Total financial assets measured at fair value	-	42	-	42
Trading financial liabilities:				
Derivatives	-	47	-	47
Total financial liabilities measured at fair value	-	47	-	47

2018	Quoted prices in active market (Level 1) £'000	Valuation techniques using observable inputs (Level 2) £'000	Valuation techniques with significant unobservable inputs (Level 3) £'000	Total £'000
Trading financial assets:				
Derivatives	-	41	-	41
Total financial assets measured at fair value	-	41	-	41
Trading financial liabilities:				
Derivatives	-	46	-	46
Total financial liabilities measured at fair value	-	46	-	46

The Company's valuation approach and fair value hierarchy categorisation for certain significant classes of financial instruments recognised at fair value on a recurring basis are as follows:

20. ASSETS AND LIABILITIES MEASURED AT FAIR VALUE (CONTINUED)

a. Financial assets and liabilities recognised at fair value on a recurring basis (continued)

Asset and Liability / Valuation Technique	Valuation Hierarchy Classification
Derivatives	
OTC Derivative Contracts • OTC derivative contracts include total return swap with another Morgan Stanley Group undertaking. • Depending on the product and the terms of the transaction, the fair value of OTC derivative products can be modeled using a series of techniques, including closed-form analytic formulas, such as the Black-Scholes option-pricing model, simulation models or a combination thereof. Many pricing models do not entail material subjectivity as the methodologies employed do not necessitate significant judgement, since model inputs may be observed from actively quoted markets, as is the case for generic interest rate swaps, many equity, commodity and foreign currency option contracts and certain credit default swaps. In the case of more established derivative products, the pricing models used by the Company are widely accepted by the financial services industry.	• Generally Level 2 – OTC derivative products valued using observable inputs, or where the unobservable input is not deemed significant.

b. Significant transfers between the levels of the fair value hierarchy for financial assets and liabilities recognised at fair value on a recurring basis

There were no material transfers between levels of the fair value hierarchy during the current or prior year.

21. 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 '*Fair value measurement*' 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.

The tables below present the carrying value, fair value and fair value hierarchy category of certain financial assets and financial liabilities that are not measured at fair value in the statement of financial position.

Financial assets and financial liabilities not measured at fair value for which the carrying value is considered a reasonable approximation of fair value are excluded from the tables below.

21. ASSETS AND LIABILITIES NOT MEASURED AT FAIR VALUE (CONTINUED)

31 December 2019

	Carrying value £'000	Fair value £'000	Quoted prices in active market (Level 1) £'000	Valuation techniques using observable inputs (Level 2) £'000	Fair Value Valuation Techniques with Significant Unobservable Inputs (Level 3) £'000
Financial assets					
Loans and advances	186,093	233,431	-	233,431	-
Financial liabilities					
Debt and other borrowings	(187,375)	(233,431)	-	(233,431)	-

31 December 2018

	Carrying value £'000	Fair value £'000	Quoted prices in active market (Level 1) £'000	Valuation techniques using observable inputs (Level 2) £'000	Fair Value Valuation Techniques with Significant Unobservable Inputs (Level 3) £'000
Financial assets					
Loans and advances	195,482	236,723	-	236,723	-
Financial liabilities					
Debt and other borrowings	(196,752)	(236,723)	-	(236,723)	-

22. CAPITAL MANAGEMENT

The Morgan Stanley Group manages its capital on a global basis with consideration for its legal entities. The capital managed by the Morgan Stanley Group broadly includes ordinary share capital, preference share capital, subordinated loans and reserves.

22. CAPITAL MANAGEMENT (CONTINUED)

The Morgan Stanley Group's required capital ("Required Capital") estimation is based on the Required Capital Framework, an internal capital adequacy measure. This framework is a risk-based and leverage use-of-capital measure, which is compared with the Morgan Stanley Group's regulatory capital to ensure that the Morgan Stanley Group maintains an amount of going concern capital after absorbing potential losses from stress events where applicable, at a point in time.

The Required Capital Framework is expected to evolve over time in response to changes in the business and regulatory environment, for example, to incorporate stress testing or enhancements in modelling techniques. The Morgan Stanley Group will continue to evaluate the framework with respect to the impact of future regulatory requirements, as appropriate.

The Morgan Stanley Group manages its consolidated capital position based upon, among other things, business opportunities, risks, capital availability and rates of return together with internal capital policies, regulatory requirements and rating agency guidelines. In the future, the Morgan Stanley Group may adjust its capital base in reaction to the changing needs of its businesses.

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.

The Morgan Stanley Group also aims to adequately capitalise at a legal entity level whilst safeguarding that entity's ability to continue as a going concern and ensuring that it meets all regulatory capital requirements, so that it can continue to provide returns for the Morgan Stanley Group.

In order to maintain or adjust the capital structure as described above, the Company may adjust the amount of dividends paid, return capital to shareholders, or issue new shares.

The Company manages the following items as capital:

	2019 £'000	2018 £'000
Ordinary share capital	24,500	24,500
Reserves	4,710	4,293
	29,210	28,793

23. RELATED PARTY DISCLOSURES

Parent and subsidiary relationships

Parent and ultimate controlling entity

The Company's immediate parent undertaking is MS Lion LLC, which has its registered office at c/o The Corporation Trust Company, Corporation Trust Center, 1209 Orange Street, Wilmington DE 19801, United States of America and is incorporated in the state of Delaware, the United States of America. MS Lion LLC does not produce publicly available financial statements.

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, 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.

MORGAN STANLEY GAMMA INVESTMENTS

NOTES TO THE FINANCIAL STATEMENTS
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23. RELATED PARTY DISCLOSURES (CONTINUED)

Directors' remuneration

The Company has three directors during the year who are employed by other Morgan Stanley Group entities. The directors' services to the Company are considered to be incidental to their other responsibilities within the Morgan Stanley Group and as such, directors' remuneration is £nil for the current year (2018: nil).

24. EVENTS AFTER THE REPORTING DATE

Pursuant to the Company's Articles of Association, on 13 March 2020 the Company paid dividends of £2,296,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares. On 15 June 2020 the Company paid dividends of £2,248,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares. On 15 September 2020 the Company paid dividends of £2,223,000 to the holders of the Classes A1-A86 preference shares and £16,000 to the holders of the Class B preference shares.

In addition, pursuant to the Company's Articles of Association, on 13 March 2020 the Company repaid capital of £2,578,000 in respect of the Company's Class A34 preference shares. On 15 June 2020 the Company repaid capital of £2,627,000 in respect of the Company's Class A35 preference shares. On 15 September 2020 the Company repaid capital of £2,652,000 in respect of the Company's Class A36 preference shares.

On 15 June 2020 by passing a Special Resolution, the ordinary share capital of the Company was reduced by £6,125,000 by reducing the par value of the Company's 24,500,002 issued £1.00 ordinary shares to £0.75 each (the "**Capital Reduction**").

Since the balance sheet date, the coronavirus disease (COVID-19) pandemic has, and will likely continue to, severely impact global economic conditions, resulting in substantial volatility in the global financial markets and operational challenges. The extent of the impact is highly uncertain and cannot be predicted and could adversely affect the future operations and financial condition of Morgan Stanley and the Company.