Good morning. This is Celeste Brown, Head of Investor Relations. And welcome to our Third Quarter Earnings Call. Today's presentation may include forward-looking statements which reflect management's current estimates or beliefs and are subject to risks and uncertainties that may cause actual results to differ materially.

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I will now turn the call over to Chairman and Chief Executive Officer, James Gorman.

James P. Gorman

Thank you, Celeste, good morning everyone and thank you for joining us. Before I comment on our performance I'll reflect briefly on where we're as a firm and where we are going. The management team here's been together for almost five years and while we have accomplished a number of things there's clearly more we can do. In short, we do not think that this firm is close to reaching its full potential. The stability and cohesiveness of the team, significant depth of talent across the organization, commitment from our people, re-shaping of our business model all position us for significant growth, and I would call Morgan Stanley as a client focused firm and our philosophy has always been to do first class business in a first class way. With the current regulatory paradigm having a client-centric business model is key to sustainable success.

The opportunities in front of us are based on increasing client penetration and accelerating new client acquisition and may include building on our leading position in [inaudible] cross-border M&A deals with particular success in Japan and our other strong banking franchises. The growth of our bank, both in wealth management and institutional securities, raising new fronts in merchant banking and real estate and the use of technology to improve the efficiency in which we serve our clients with a hi-tech, high touch approach across the entire franchise. Those are just some examples.

Now turning briefly to the quarter, we grew our revenue and profitability quarter-over-quarter and year-over-year in both wealth management and institutional securities. Firm wide revenues, excluding DVA were up 7% compared to the third quarter of last year. In the wealth management business our revenues grew 9% versus a year ago driven by the continued execution of our bank strategy as well as revenue tailwinds from high markets. Notably our margin improved to 22%.

Fee-based assets as a percent of client assets increased to 38%, up from 36% last year and just 23% when we closed on the initial portion of the acquisition a few years ago. Revenues in all of our major institutional businesses were up versus a year ago. Investment banking revenues were up 35%. Fixed income results, excluding DVA were up 19%, notwithstanding continued reduction in RWAs. Our equity sales and trading revenues were high versus last year as we continued to execute across products and regions and that franchise remains number one in the world. The momentum of our businesses also drove continued improvements in our earnings and ROE.

EPS excluding the tax benefits and DVA in this quarter and a year ago was up about 40% while our ROE on the same basis increased a 180 basis points to approximately 8%. We're not yet at exceptional levels but we're making consistent progress. For example we've made progress in improving the returns and reducing the capital and expenses in fixed income and commodities over the last few years. We believe there may still be meaningful opportunities to optimize the remaining components of commodities beyond the recent TransMontaigne sale as we continue to drive for higher returns.

In addition we're always vigilant with all our resources, especially the balance sheet. A final thought, we believe we remain well positioned for further capital actions given the magnitude of our fundamental strategic change and our improving earnings profile. The CCAR process is engrained in every aspect of our business.

I will now turn the call over to Ruth to discuss the quarter in details.

Ruth Porat

Good morning. I will provide both GAAP results and results excluding the effect of DVA. We have provided reconciliations in the footnotes to the earnings release to reconcile these non-GAAP measures. The impact of DVA in the quarter was positive $215 million with $132 million in fixed income sales and trading and $83 million in equity sales and trading. Excluding the impact of DVA firm-wide revenues were $8.7 billion, up 2% versus the second quarter. The effective tax rate from continuing operations for the third quarter was 21%, reflecting a discrete tax benefit of $237 million or $0.12 per diluted share principally associated with the repatriation of non-US earnings at a cost lower than originally estimated.

Earnings from continuing operations applicable to Morgan Stanley common shareholders excluding DVA were $1.5 billion. Earnings from continuing operations per diluted share excluding DVA were $0.77 after preferred dividends. On a GAAP basis including the impact of DVA firm-wide revenues for the quarter were $8.9 billion. Earnings from continuing operations applicable to Morgan Stanley common shareholders were $1.7 billion. Reported earnings from continuing operations per diluted share were $0.84 after preferred dividends. Book value at the end of the quarter was $34.17 per share and tangible book value was $29.25 per share.

Turning to the balance sheet our total assets were $814 billion at September 30, down from $827 billion at the end of the second quarter. Deposits as of quarter end were $124 billion, up $7billion versus Q1. Our liquidity reserve at the end of the quarter was $190 billion compared with $192 billion at the end of the second quarter. Year-to-date we benefited from strong global demand for our credit enabling us to pull forward issuance from future periods reflecting broad global investor participation.

Turning to capital, although our calculations are not final, we believe that our common equity Tier-1 transitional ratio will be approximately 14.3% and our Tier-1 capital ratio under this regime will be approximately 16.1%.

Basel III transitional risk-weighted assets are expected to be approximately $415 billion at September 30. Reflecting our best estimate of the final set of reserve rules our pro forma common equity Tier-1 ratio using the Basel III fully-phased in advanced approach was 12.6% at September 30, up from 12.3% in the second quarter.

Our pro forma standardized ratio was 11.7%, up from 10.7% in 2Q. Pro forma fully-phased in Basel III advanced RWAs are expected to be approximately $423 billion. We estimate our pro forma supplementary leverage ratio under the U.S. final rule to be approximately 4.9% at September 30, up from 4.6% at the end of 2Q. These estimates are preliminary and are subject to revision.

Turning to expenses, our total expenses this quarter were $6.7 billion flat versus the second quarter. Let me now discuss our businesses in detail. In institutional securities revenues, excluding DVA, were $4.3 billion up 3% sequentially. Non-interest expense was $3.3 billion flat versus the second quarter. Compensation expense was $1.8 billion for the third quarter, up 3% versus the second quarter in-line with the increase in revenues and reflecting a 41% ratio excluding DVA.

Non-compensation expense for the third quarter was $1.5 billion, down 3% versus the second quarter. The business reported a pretax profit of $1 billion excluding the impact of DVA. Including the impact of DVA revenues were $4.5 billion and the pretax profit was $1.2 billion.

In investment banking revenues of $1.3 billion were down 6% versus last quarter. According to Thomson Reuters, Morgan Stanley ranked number 1 in global IPOs and number 2 in global announced and completed M&A at the end of the second quarter. Notable transactions included in advisory, Morgan Stanley acted as sole financial adviser to Sigma-Aldrich in the announced $17 billion sales to German Merck. Morgan Stanley also acted as financial advisor to Dresser-Rand in the announced agreement to be acquired by Siemens for $7.6 billion in cash.

In equity underwriting, Morgan Stanley acted as joint Bookrunner on the U.S. $25 billion IPO of Alibaba Group, the largest IPO in history. Morgan Stanley also acted as Lead Left Bookrunner and stabilization agent on the $3.5 billion IPO for Citizens Financial Group. The IPO represented the largest U.S. bank IPO in history and the largest U.S. financial institution IPO since 2007.

In debt underwriting, Morgan Stanley acted as Lead Left Bookrunner for Tyson Foods on its $3.25 billion of senior unsecured notes in multiple tranches to finance its acquisition of Hillshire Brands. This financing complemented our role as lead financial advisor to Tyson on its acquisition Lead Left arranger for an $8.2 billion committed bridge facility and Lead Left Bookrunner and stabilization agent for the $2.4 billion offering of common stock and tangible equity units.

Advisory revenues of $392 million decreased 6% versus our second quarter results driven by lower results in EMEA and Asia Pacific. Morgan Stanley remains a leader in cross border activity.

Underwriting revenues of $948 million decreased 7% versus our second quarter results. They were strong for third quarter driven by equity underwriting revenues of $464 million, which were down 5% versus the second quarter, reflecting lower volumes in the Americas and EMEA partially offset by strength in Asia Pacific.

Fixed income underwriting revenues of $484 million were lower versus the second quarter primarily due to declines in investment grade and high yield bonds that were partially offset by higher revenue from loans. Equity sales and trading revenues, excluding DVA were $1.8 billion, flat compared to last quarter. Results were strong across products and geographies demonstrating less seasonality than is typical for the third quarter. Solid client activity and the underwriting calendar drove cash revenues above second quarter levels.

Derivative revenues also increased sequentially on higher client activity. Prime brokerage revenues were lower reflecting reduced activity in Europe.

Fixed income and commodity sales and trading revenues, excluding DVA were $1 billion, flat versus the second quarter. Macro revenues were up significantly this quarter, most notably in foreign exchange which benefited from improved market conditions with higher volatility.

Securitized products and credit products revenues declined on lower secondary client activity and less favorable market conditions. Commodities revenues were meaningfully lower reflecting lower client activity and a difficult market environment. CVA was a benefit in the quarter. Other revenues were $225 million, up versus $108 million in the second quarter, driven by a gain on the sale of TransMontaigne and the sale of our retail property space. Average trading VaR for the third quarter was $42 million, down from $48 million in the second quarter.

Turning to wealth management revenues were $3.8 billion in the quarter, up 2% sequentially. Asset management revenues of $2.2 billion were up 5% versus last quarter reflecting higher market and positive flows.

Transaction revenues were down compared to last quarter, consisting primarily of commissions of $503 million essentially flat to the prior quarter, investment banking related fees of $224 million, up 5% versus last quarter, reflecting a pickup in closed end funds and trading revenues of $185 million, down 31% versus the second quarter, driven by primarily by lower marks in our deferred compensation plans.

Net interest revenue increased 4% to $601 million, driven primarily by higher revenues from our bank deposit program. Other revenue of $112 million increased versus the second quarter primarily due to the gain on sale of a retail property space. Non-interest expense was $2.9 billion flat versus last quarter. Non-compensation expense was $767 million effectively flat to last quarter.

Compensation expense was $2.2 billion, flat versus the second quarter. The compensation ratio was 58% down versus the second quarter driven by revenue mix including ongoing growth in net interest income. The PBT margin was 22.1%, up versus 20.6% in the second quarter. PBT margin excluding the benefit from the sale of a retail property space was 21.3% in the quarter.

Profit before tax was $836 million. Total client assets were $2 trillion, global fee based asset inflows were $6.5 billion, fee-based assets under management increased to $768 billion at quarter end, representing 38% of client assets. Global representatives were 16,162, essentially flat to the second quarter. Deposits in our bank deposit program were $129 billion, up $2 billion versus the second quarter. Approximately $116 billion were held in Morgan Stanley Bank.

Wealth management lending balances continued to grow reflecting the ongoing execution of our bank strategy. Lending balances increased $3.5 billion in the quarter. Investment management revenues of $655 million were down 5% sequentially. In traditional asset management revenues of $456 million were up 5% versus the second quarter, driven by positive flows and higher markets and partially offset by lower marks and deferred compensation plans.

In real estate investing revenues of $113 million were flat to the second quarter. Merchant banking revenues were $86 million down 41% driven by lower investment gains in the quarter. Non-interest expenses were $467 million, down 4% from the second quarter consisting of compensation expense of $253 million reflecting a compensation ratio of 39% and down versus the second quarter, driven by lower marks on deferred compensation plans and the mix of revenues in the quarter.

Non-compensation expense was $214 million, up from $196 million in the second quarter primarily due to the settlement of a legal matter. Profit before tax was $188 million, down 8% sequentially. NCI was $18 million versus $7 million last quarter. Total assets under management increased to $398 billion driven by higher flows, partially offset by market depreciation driven primarily by foreign exchange.

In conclusion, our outlook is guided by the meaningful transformation we've made during the last five years and benefits from growth in our most [annuity-like] businesses. First, our wealth management business continues to have momentum with growing profitability from the secular trend toward managed money. We entered the fourth quarter with a modest tailwind from stronger equity markets at the end of Q3 and clients remain engaged as they assess evolving opportunities in markets.

Second, we continue to have earnings upside with ongoing loan growth in our bank. This remains a differentiated contributor because we benefit from asset optimization on a growing loan book even without the benefit of rising rates. As we enter the fourth quarter the pipeline for loan origination remains strong in both wealth management and institutional securities.

Third, our investment banking pipeline remains healthy. In advisory it is broad-based across industry and geography and generates financing opportunities. Ongoing market volatility may affect institutional results if it persists. However we view recent volatility as a repeat of a theme seen frequently during the last several years with growing activity levels across products and businesses building, only to be disrupted by macro events than followed by a reset. A reset could occur with recognition that stronger growth in the U.S. may offset challenges in other economies.

Finally our capital and liquidity position continue to be a source of strength. Our healthy capital ratios on both an absolute and relative basis reflect the robust foundation and evidence of our ongoing successful execution of our business and balance sheet strategy.

Thank you for listening. James and I will now take your questions.

Question-and-Answer Session

Operator

(Operator Instructions). And the first question will come from Glenn Shorr with ISI.

Glenn Shorr - ISI

Hello.

Ruth Porat

Good morning.

James Gorman

Good morning.

Glenn Shorr - ISI

Good morning. Maybe just a quick one on the mechanics of this whole fair value of deferred comps that showed up in both in your comments in both investment management and wealth management. If I heard you correctly it hits both the revenue line and the comp line.

Ruth Porat

Correct.

Glenn Shorr - ISI

And can you just help us when and why that happens.

Ruth Porat

It's a function of the assets in the deferred comp plans. So they move as the market moves and it therefore flows through revenue in comp and in essence as you can see we went through the impact on both businesses as you know that.

Glenn Shorr - ISI

Okay. Do I need to care, meaning are they comparable amounts on the revenue and expense line and they net out to not a big impact.

Ruth Porat

Yes although by definition therefore implies a higher comp ratio but, yes they net out.

Glenn Shorr - ISI

Understood. Okay, cool. Moving on, curious your comments about how you've extended the [rationale] book a little a bit, or a lot I should say, in the past but curious, [inaudible] your thoughts on NSFR, impact on prime brokerage, specifically in conjunction with the Feds recent comments on social and wholesale funding, just kind of how is it impacting, it's an important business for you, you're really good at it, how is it impacting how you run the business and the profitability of the business?

Ruth Porat

So taking the two rules obviously both of which are at this point preliminary and we're looking forward to seeing the final rules. On the net stable funding ratio as you noted we frequently said that durability of funding is important and it's the way we run the firm and as a result, probably not surprisingly we think having a measure of long-term durability is appropriate and we spent a lot of time as you noted achieving this durability through proper ALM and we spent a lot of time walking everyone through how we've done that within our secured book.

The challenge of being more direct in answering your question is the rule is preliminary but given all that we've done we don't expect to make meaningful changes. And as I said we very much look forward to seeing what the rule is. And then on the city surcharge the increase for short term wholesale funding is somewhat similar given the fed has only provided the broad contours, so what the rule is going to be is unclear, how it's going to be implemented and in particular, how it's going to be calibrated.

I think obviously the entire industry has some elements of wholesale funding and we've often said not all wholesale funding is created equal, very much to your question. Our view is that logic would suggest that proper calibration would incorporate not just size but the quality and durability of funding in particular given the fed has recently published an article about durability in the industry and when I noted in a recent conference and it's just too early to know but again given all that we've done and given the strength of our capital positions we are not looking at changing what we're doing with our business here and I guess the last point I would make on the wholesale funding is we would hope the rule is dynamic and does adjust as the industry adjusts to the new rule.

The big point is that given what we've done with our funding, with durability of our funding and the way we're managing our balance sheet we don't see it really at this point we are waiting for the rule, so I'll leave that caveat but really affecting the way we're running the business.

Glenn Shorr - ISI

Okay, last quickie is just your growth has been great in both -- as you noted in both the PLAs and the residential real estate loans. Are those FAs being -- especially incented to drive that. I know it comes at a higher profitability for the firm, does the low -- is the offset of the rates not going up for you guys low rates actually help drive the growth in those lending products?

Ruth Porat

There are a couple of different, I guess questions in that. As we've talked about loan growth is not on the comp credit, on the formulaic comp credit, so we call non-compensable revenue. So there is compensation on it but it's not part of the formulaic grid and what's really driving this is we've talked about on some prior calls is the take up, buy up and what we're finding is we're having growth in the loans per financial advisor, growth in the number of financial advisors using the product. As they use it they see the value of their clients, it's ease of using it, we've invested meaningful in the infrastructure to support financial advisors and so they are seeing the strength of this product suite, and we're also seeing higher draw down on the security space lending, that loans so origination occurs and then you have to draw down over a period of time. So really what this is, is increased penetration on what is a very sizeable client base and that's what's really driving it.

Glenn Shorr - ISI

Okay excellent, I appreciate it.

Ruth Porat

Thank you.

Operator

The next question will come from Guy Moszkowski with Autonomous.

Guy Moszkowski - Autonomous Research

Good morning.

James P. Gorman

Good morning.

Guy Moszkowski - Autonomous Research

We've heard a lot of complaints from investors who were worried about the Street reducing the liquidity that it provides, we heard a lot more about it in the last few weeks of the third quarter and at the same time in the third quarter the [GSICs] began to have to make daily reports to regulators based on more current liquidity regs, do you think this may have had an impact just because it's onerous and it kind of puts in your face every day the impact of inventory and hedging or is the issue more broadly structural on your view?

Ruth Porat

We think it's more structural and it's really the combination of other regulatory requirements. We don't think it's as a result of the Volcker reporting, people have been working on that for quite some time and as you said it now started to be submitted to regulators. But when you look at the combination of the supplementary leverage ratio with the other various tests, whether it's CCAR or for some firms it's the LCR, there are a number of factors which are really changing dynamics in the market liquidity in the market. At a recent conference I put up a slide that looks at the extent to which balance sheets have come down on the one hand and liquidity requirements have increased on the other hand and by definition that's squeezing the amount of balance sheet available for trading activities. So we do view that as a structural change in the industry driven by regulatory change in the aggregate.

Guy Moszkowski - Autonomous Research

And is there a way that you're actually seeing in which this leads to fundamentally better spreads?

Ruth Porat

Well, the gaping that you saw this week, I would say I wouldn't view that as a positive for the market. I think that one of the things that has been concerning is the increase in treasury sales, which I think initially were attributed to the SLR and there was a view that potentially there would be a readjustment in markets but in fact through the course of the third quarter, even before the last couple of weeks the trend line was up even when market volatility was low and I think that is a concern.

Guy Moszkowski - Autonomous Research

And actually, if don't mind can you comment a little bit on the early going in October. Obviously we are only a couple of weeks in and they have been an unusual couple of weeks but certainly JPMorgan commented earlier this week that their markets businesses had seemed a lot more mixed over the last couple of weeks?

Ruth Porat

Well as you said the macro environment, the trading markets are really the key issue and it has been a challenge quarter to-date but as you appropriately noted two weeks isn't a quarter and as I said in my opening comments we have seen this through the last several years, choppiness in markets and then a reset and it's tough to gauge when it resets. So it's been a choppy early start but when you look again across the franchise the investment banking pipeline is strong.

You have seen continued issuance throughout this period and yes a sustained down draft wouldn't be constructive and it could affect the timing of deals but at this point the pipeline continues to build. In fact a lot of deals that we may have thought would close in the fourth quarter were pulled into the third quarter, were executed earlier and the pipeline has replenished which really goes to the strength of the dialog across the banking franchise.

And similarly in wealth management what we are seeing, I appreciate you are asking about trading markets but as we look across our franchise what's quite relevant is just the consistency we're seeing in wealth management as well.

Guy Moszkowski - Autonomous Research

Thanks. You mentioned the SLR and thanks for giving us the figure, is there still a [Sacker] type benefit that we should be looking for?

Ruth Porat

Well, there has been no update on the rule. We do still expect that [Sacker] will be a part of the standardized risk based capital calculation and as proposed based on the third quarter number that would be about a 30 basis point benefit to our standardized ratio. On the SLR it's unclear if the rule would include [Sacker] as part of it, if it would include it we would expect a modest benefit there.

Guy Moszkowski - Autonomous Research

Thanks. I had a question on wealth management. As you pointed out the fee-based asset inflows at $6.5 billion were quite a bit lower than in either the reference quarters. I think you were $12.5 billion last quarter and $15 billion a year ago and I was wondering if there is any color you can provide there, any special factors that we should pay attention to?

Ruth Porat

No special factors. We have seen same strength in the business, it, in our view just reflects timing and as you noted we had strong flows throughout the year. So as we are looking at year-to-date we just had strong flows and there are timing issues.

Guy Moszkowski - Autonomous Research

Okay, and then I just have one more which is that you talked about the discrete tax benefit because of being able to repatriate more attractively than you had expected in terms of your tax provisions. How unusual an event is just the repatriation itself and can you give us a sense for the order of magnitude involved and I guess what I am looking for is a signal as to what we are looking at in terms of potential capital return?

Ruth Porat

So in terms of the repatriation as I noted it was due to some non-U.S. earnings that were at a cost lower than originally estimated, I think we look at requirements in geographic markets throughout the year, this one just happened to be with a benefit.

Guy Moszkowski - Autonomous Research

And can you tell us sort of what the gross amount was that you repatriated?

Ruth Porat

We indicated the tax benefit. I don't have that with me.

Guy Moszkowski - Autonomous Research

Okay, fair enough. Thanks for taking my questions. I appreciate it.

Ruth Porat

Thank you.

Operator

The next question will come from Matt O'Conner with Deutsche Bank.

Matt O'Conner - Deutsche Bank

Good morning.

Ruth Porat

Good morning.

Matt O'Conner - Deutsche Bank

I was hoping just to follow-up on your comment about further capital actions given the strategic changes. I don't know if that's just referring to the CCAR process, earnings were higher, there has been more stability, so think about higher payouts or was there something else that you are referring to maybe related to selling the commodities business, bring up capital, things like that?

James P. Gorman

Why don't I take that? I think we're just pointing out that in the context of all the things going on at this time we are obviously building pretty solid capital buffers. That said we live in a dynamic regulatory environment with potentially new G-SIFI buffers coming out but we feel strongly about where we are with our capital base and we feel strongly about where we're going coming into the CCAR process. We certainly expect to continue to return capital to shareholders in increasing amounts over the coming years.

Matt O'Conner - Deutsche Bank

And then have you guys disclosed either the assets or revenue related to the commodities business, either what you sold or just the entire unit?

Ruth Porat

No, we haven't.

Matt O'Conner - Deutsche Bank

Okay. And then just separately there was an article in the paper a couple of weeks ago related to the dividend arbitrage that some clients are using, that the US broker dealers and global broker dealers are helping. I am just wondering how big a business is that for you guys and remind us of the seasonality around that and thoughts on, I guess just the business going forward.

Ruth Porat

As we said repeatedly our equity business is strong, diversified across products and regions and that's what drives it. We don't break out particular pieces and there are seasonal patterns throughout the year.

Matt O'Conner - Deutsche Bank

Okay, is that an area that you think you and others will pull back a little bit given just that it's being highlighted and maybe scrutinize a bit more than the past.

Ruth Porat

It is one of the number of services that we provide to clients and it's really based on client activity.

Matt O'Conner - Deutsche Bank

Okay. And then just lastly the non-comp, I mean expenses overall actually came in pretty good this quarter in general. The non-comp in particular has been managed down quite nicely. Is there anything, I guess from here or more that you could do or should we think about this as a pretty reasonable run rate?

Ruth Porat

Our view is that there is more to do. We remain very focused on expenses overall and if you go back to 2012 when we first laid out our expense reduction goals we had an expense ratio at that time of about 84% and we indicated by the end of this year we’d get to 79% or lower. Year-to-date we're at 77% but the process of going over the last couple of years is really to provide the analytics, the tools, the dashboards to the businesses to ensure that engrained throughout the organization is a real focus on expenses and expense management and we view that as an ongoing part of the way we run the business.

As I talked about at a recent conference we divide our expenses into what we call run the bank and change the bank and we've been able to extract savings and run the bank to fund what we called change the bank requirements which include both regulatory requirements as well as ongoing innovation in the business, investments to ensure we're enhancing client experience and applications and across the platform. So again we got a very strict lens on that because it does create incremental capacity as well and we think it's the appropriate way to run the overall franchise.

Matt O'Conner - Deutsche Bank

Okay. Thank you very much.

Ruth Porat

Thank you.

Operator

The next question will come from Jim Mitchell with Buckingham Research.

James F. Mitchell - Buckingham Research

Thanks. Can you just updates us on the FICC RWA this quarter and maybe just more strategically as we think outward if there is more pressure from regulators with the SIFI surcharge on top of a surcharge focused primarily on repo and other aspects of the fixed income business, do you think that that there could be some changes in trying to push the RWA lower overtime. Thanks.

Ruth Porat

So risk weighted assets in fixed income are $191 billion this quarter, down from $192 billion last quarter. We just had less roll off this quarter and we remain very comfortable with the $180 billion target for fixed income which was originally end of 2016. We pulled it forward to end of 2015.

As I indicated at a recent conference we want to make it clear though that there not -- just as with the non-comp expense question there is not a line in the sand on a particular date or activity stops beyond the $180 billion. There is about $25 billion incremental risk weighted assets that run off overtime in areas like structured credit and long dated and collateralized derivatives which generated a negative ROE because we have to finance positions, legacy positions and so as we exit we take those from a negative ROE to neutral and as we redeploy them you shift to a positive ROE and we're already generating strong ROEs in a number of business within fixed income like credit and securitized products and so we have an opportunity to reallocate to get a higher return on those and that's really the way we're looking at what we're doing within fixed income.

As it relates to changing regulatory requirements and the potential surcharge, I would note that our ratios are very strong. The transitional ratio at 14.3% and even fully phased in as we're talking about, 11.7% standardized, 12.6% advanced. So what we're really looking at is how to best optimize within each business to drive the ROE within each business and we believe we've got room to really use a number of different levers to do that.

James F. Mitchell - Buckingham Research

All right. So that's helpful, so if you think about the 180 there's 25, that's sort of run off beyond that but you might be re-investing depending upon the environment. Is that the way to think about it?

Ruth Porat

Yeah, depending on the environment and client activity because we have the opportunity already resident within a number of products, within fixed income to generate an attractive return. So depending on requirements there's ample capacity.

James F. Mitchell - Buckingham Research

Okay, great thanks.

Ruth Porat

Thank you.

Operator

The next question will come from Mike Mayo with CLSA

Mike Mayo - CLSA

Hi, what inning are you in, in redeploying the deposits that you achieved from the joint venture?

Ruth Porat

So we are -- what inning, you frequently do ask the inning question. I think we're well on our way, and I think, let me give a couple of parts to that. The early days, I guess you would say even pre-game was building the infrastructure required to support the growth when once we closed out the acquisition and started onboarding the deposits. And so that a very important element of really the setup, ensuring that we had the infrastructure, the risk management, the banker supporting, the financial advisors. So that as the deposits started onboarding we could have positive growth, a good experience for our financial advisors as I already addressed and see the kind of roll-out that we've had.

The other thing is we've emphasized repeatedly that our focus is on prudent loan growth, prudent loan growth within wealth management and institutional securities and we have two broad franchises that enable us to have strong demand. But what we've been focused on is really prudent loan growth and so we have ample capacity beyond here, we've been closing the gap versus the industry average, but still believe we have ample capacity beyond here to grow and that is just with the contractual onboarding of deposits, where, as you've seen this quarter there's organic on top of the contractual.

So we view this as the opportunity to have the [inaudible] depository embedded within Morgan Stanley that creates substantial incremental opportunity in a flat rate environment or a rising rate environment and I'll give it to James because he tends to like cricket matches and they last a lot longer and that's the way we view this, this bank has got a long way to go.

James P. Gorman

Well I'm not sure you're asking about cricket innings but if I were to put a number on it I'd say we are somewhere around the bottom of the fourth in baseball and the afternoon tea session on day two of a five day test match.

Mike Mayo - CLSA

Okay, how much do interest rates help if they increase and how much do they hurt if they don't increase. I mean some of the more traditional banking peers will actually quantify this for us and you guys haven't done that. Can you just help size the benefit or the harm?

Ruth Porat

Yes, I'm glad you asked that question because it's an important one, given the way we see the outlook for the bank. So overall rising rates are a good thing. They do benefit the bank if we deploy deposits into lending and AFS. And second, it should signal an improving economy which would increase activity levels across the franchise.

But the main point and I tried to indicate that in the opening comments is that the main driver of NII growth is deposit deployment and you can see that in our year-over-year numbers we're benefiting from deploying these legacies, city deposits and with more coming on board we have a positive impact even without rates rising. And so you take that -- that to us is really differentiated and managed, we're pleased to see the underlying growth in NII, again even without rates increasing.

So now you put to the other side at some point rates will increase and for modeling a couple of key points. I guess the first is that the reason we've gone through this the giving you contractual deposit on-boarding kind of what the schedule is and what the current asset mix and what the target asset mix is, is that you can model the rate impact whenever you do expect it to occur.

The other component in modeling that we think about is one, what's the impact of higher rates on deposit outflows and the data suggests that for Morgan Stanley that would be de minimis because our deposits, our working capital and client accounts are very sticky. We've talked about that in some prior calls.

In terms of deposit pricing we model that based on historic data from both Morgan Stanley as well as for retail deposits at regional and large money center banks, notwithstanding the fact that as I just said our deposits do behave very differently than those retail deposits and our analysis in our model would reflect about a 45 basis points increase in deposit pricing with the first hundred basis points increase in rates.

We do believe that is conservative given the nature of our deposits and structural changes in deposit alternatives. But it's what we would assume kind of as something to put into a model. Fed funds is the most relevant rate for our business and the last point is that the average duration of our bank assets is about 1.5 year. So rising rates do benefit us quickly. So the way we look at it is in the flat environment there's upside given NII growth but it's all about asset optimization in a rising rate environment given the factors I went through and the cost structure of our bank, no bricks and mortar, the investments have already been made, any rise in rates does drops nicely to the bottom line.

Mike Mayo - CLSA

Just two quick follow-ups, the deposit data of 45% seem somewhat low compared to many traditional banks. Are you sure about that, I mean it's not a whole lot of sensitivity there?

Ruth Porat

When we look at the data that we've looked at overtime and again given the nature of the deposits, as I indicated, our view is that that's appropriate given the nature of the business and as I said that we're talking about the first hundred basis points so it moves overtime.

Mike Mayo - CLSA

And then low rates it stays lower for longer, what impact does that have on your refinancing of your debt. You issued a lot of debt when your credit spreads were blown out a few years ago and now they've come in. Can you take advantage of that?

Ruth Porat

We can and we have because we've started refinancing debt, as you noted, came on kind of came on in the 2010-'11 period. We do realize the benefit overtime given the weighted average maturity of our unsecured debt is about six years. So we would lag into any benefits overtime but at this point we're refinancing debt we issued post crisis and there's a benefit.

Mike Mayo - CLSA

All right, thank you.

Ruth Porat

Thank you.

Operator

The next question will come from Brennan Hawken with UBS.

Brennan Hawken - UBS

Good morning. A quick one first, the $141 million gain that you laid out, was that only on that real estate sale or does it also include the gain on TransMontaigne?

Ruth Porat

That, no, it's just on the real estate.

Brennan Hawken - UBS

Okay, can you -- is it possible to quantify the TransMontaigne gain, was that significant?

Ruth Porat

We don’t break that up that’s included within the other revenue line and just as a reminder that also includes the contribution from our joint venture with NUFG for the real estate at [inaudible] there is a number -- it’s in the other line items in that one.

Brennan Hawken - UBS

Okay, so I guess though given the fact that you broke it out would imply that you didn’t view it as a material number and it wasn’t material enough to break out, is that fair?

Ruth Porat

It’s included, as I said within the other line.

Brennan Hawken - UBS

All right, and then thinking about the rest of the physical business and the potential sale to Rosneft, what are the next steps if that doesn’t go through here by year-end can you start to shop the asset now, is there any sort of change that can be made proactively on that front?

Ruth Porat

Well as you know and the way you framed the question the terms of the contract are such that if the deal doesn’t close by year-end the contract expires and so we’re considering alternatives if that doesn’t close.

Brennan Hawken - UBS

Okay, is it possible also, while on the physical commodity front to think about what growth rates might have been if we exclude either the TransMontaigne component of these physical commodities revenue out of FICC or physical commodities overall, just given that it’s getting shopped?

Ruth Porat

So yeah, TransMontaigne would have been immaterial to the results, and as we indicated commodities overall was very low. It was down meaningfully year-over-year and quarter-over-quarter. So it wasn’t much of comp produced in across commodities generally.

Brennan Hawken - UBS

Okay, so it is possible that the growth rate might have been higher if we ex out the physical business?

Ruth Porat

Yes.

Brennan Hawken - UBS

Right, and then one last one, just when we talk about the loan book a lot of times we focus on the wealth management and I'm just kind of curious you disclosed that always half of the loan growth is going to be coming from the institutional side. How should we think about the NII from those loans flowing through your P&L and generally how should we think about the spreads on those loans versus the loans in your wealth management business. Is there a way to sort of frame how to think about that side of the loan growth?

Ruth Porat

Yes, it's a fair question because as you know in IS, in the institutional securities business NII is a function of a number of factors. So it's not as easy to parse through as in wealth management. Just to give you some loan growth numbers so in wealth management I think I indicated securities based-lendings up $2 billion, residentials up $1.5 billion and institutional securities we were up $1.5 billion on the quarter primarily in commercial real estate and we are focused continuing to build the diversified portfolio and our focus is on lending in areas where we have strong client franchise, strong domain knowledge.

So the other element of it is it's enhancing our overall client experience within institutional securities. It's in addition to what we are already doing with key clients. And so it's reflected there as well and it's in our view accretive to the overall relationship. We have some slides that we have used in prior conferences that give you yields on a blended basis.

Brennan Hawken - UBS

Okay. And when we think about those yields and how that those yields play in my guess is or my sense should be that the level of competition in those markets is probably a bit more intense than you would see on the retail side. Is that a correct assumption or is that off base?

Ruth Porat

Well again as I said part of it is on both sides wealth management and institutional securities what we are doing is really focused on our client base and in institutional securities it's adding on to what we are doing within our key franchises. So that we view all of our businesses as competitive. We don’t take anything we are doing with any of our clients for granted but we have got in our view a strong opportunity and what we said repeatedly is that we are focused on prudent loan growth. It’s not as though we are looking to originate volume merely to originate volume. There is a substantial opportunity within our client base on both sides of the house and the key lens as you have probably heard us say too many types prudent loan growth and it’s driven with the title funds on risk management and that’s what’s key to the way we are looking to build the Bank here.

Brennan Hawken - UBS

Okay, thanks for the color, Ruth.

Ruth Porat

Thank you.

Operator

The next question will come from Michael Carrier with Bank of America.

Michael Carrier - Bank of America/Merrill Lynch

Thanks a lot. Just on -- some of the regulatory ratios, any update on the bank SLR or the LCR?

Ruth Porat

So the bank, given we capitalize the bank to support the loan growth that I am pleased that we have been talking about a lot on this call, we are in a strong position on all the various capital ratios; LCR, SLR and again it’s because we capitalize the bank to support what we expect will be ongoing loan growth.

Michael Carrier - Bank of America/Merrill Lynch

Okay, and then small items, but just in terms of the tax outlook and then also the CVA, just wanted to find out, significant this quarter or kind of an average level?

Ruth Porat

So in terms of the first part of your question, overtime given our business mix the tax rate should be around 30% and then on CVA it was positive this quarter. It was a drag last quarter and last year but one point that is worth noting is fixed income excluding commodities was up quarter-over-quarter and year-over-year and if you exclude CVA that same trend would apply. So the business fixed income products broadly excluding commodities up quarter-over-quarter and year-over-year excluding CVA.

Michael Carrier - Bank of America/Merrill Lynch

Okay, and then just on trading, so on commodities anything in the quarter that you would say was like a one-off versus environmental and that's more going into the fourth quarter and the next year and then I guess same thing on equities, just given the relative strength anything that you would say was especially strong that you wouldn't expect to continue?

Ruth Porat

No, so starting with commodities not -- nothing specific to call out and so our view is that what we are looking at appears to be structural headwinds in certain commodities markets and as a result the key question is how to best maximize returns if in fact these are structural headwinds. And but there was nothing specific there and similarly in equities we had broad-based strength again across products and geographies just given the leadership in that business. We did benefit from a strong global underwriting calendar but I would say that's kind of core to the overall franchise and the strength of what we are doing in equity underwriting generally and the equity underwriting calendar remains strong but nothing specific to call out as broad-based strength again.

Michael Carrier - Bank of America/Merrill Lynch

Okay. Thanks a lot.

Ruth Porat

I guess just to add one of the things to note is that we have seen in the past that challenging result in overall poor performance. You often see reallocation but overall I think that one of the key things is typically activity slows as you go into the end of the year in particular with prime brokerage clients we've seen that in prior years.

Michael Carrier - Bank of America/Merrill Lynch

All right. Thanks.

Operator

The next question will come from Fiona Swaffield with RBC.

Fiona Swaffield - RBC

Hello. I just had two questions. Firstly was on just understanding the compensation ratio, sequentially a bit better because you took out the gain in your analysis on the pretax margins so I assume you should also do the same on the comp ratio and if we do that obviously has approved less, could you also explain this issue of the employee deferred comp and how that would affect the comp ratio sequentially? And the second question is on the SLR, could you talk a bit more about the balance sheet or the denominator, it obviously seems to have gone down which is helping and is there more prospect of that continuing. Thanks.

Ruth Porat

Certainly. So I am starting with the SLR 4.9% versus 4.6% last quarter. We had a contribution from both the numerator and denominator. The benefit on the denominator was actually primarily for mitigation of the gross up and so we've been talking for quite some time about the number of work streams against which we've been executing, including the net long CDS sold, the pickup in compression activities, the reductions in fixed income RWAs overtime and that was the bulk of the benefit that we saw on the denominator.

As you noted we also had a decrease in our GAAP balance sheet but the other items were a contributor to the benefit from the denominator. And then on the numerator beyond earnings we did have a prep issuance this past quarter. Those two drove the numerator higher. In fact the split between the numerator and the denominator was about two-thirds of the benefit came from the numerator, one-third came from the denominator.

Fiona Swaffield - RBC

Thank you.

Operator

The next question will come from Christian Bolu with Credit Suisse.

Christian Bolu - Credit Suisse

Thanks for taking my questions. Just quick one on FVA, a number of your peers have now implemented this adjustment to [inaudible] of these books, curious on your latest thoughts on where Morgan Stanley stands on this.

Ruth Porat

So FVA referring obviously to fair value adjustments, refers to the potential implied financing cost for uncollateralized derivatives and only to the extent that those are observable, we do continue to evaluate it. As you noted there is a lot of industry discussion there has also been a lot of academic discussion on the topic but in our view transparency continues to be lacking so there is no basis to take the adjustments.

Christian Bolu - Credit Suisse

Okay, and then quickly on VaR, that came down particularly interest rates, credit lines assume there was more connectivity during quarter, so just curious if you could parse out the decline debits we position in versus volatility.

Ruth Porat

It's come down, I think in line with overall, this activity level is coming down, we see it and you noted one line, I would say that in commodities it also came down so it was really just more in line with connectivity.

Christian Bolu - Credit Suisse

Got it. Thank you.

Ruth Porat

Thank you.

Operator

Your final question will come from Steven Chubak with Nomura.

Steven Chubak - Nomura

Hi. Good morning.

Ruth Porat

Good morning.

Steven Chubak - Nomura

James, I appreciate your comments on your CCAR focus internally and clearly you made considerable progress delivering stronger return over the last four quarters and one thing I was little bit surprised by just looking at your latest company run mid stress test is that your PPNR forecast of $8.3 billion was it meaningfully different than your prior company run submissions? And I was wondering this merely reflects increased conservatism on your part in an effort to maybe match the Feds historically conservative view of your PPNR profile and just given the progress that you've made over the last 12 months assuming no meaningful changes to the CCAR guidelines would you expect to see a better result this coming year?

James P. Gorman

Why don't I just take the top line for a minute on the better results this year? We didn't ask something that we didn't get last year so it's not like we have been restrictive, we have behaved according to what we thought was the right balance for the business and the right balance for capital action. So yes as we are accreting earnings which we have been doing throughout this year significantly and we've made the capital ratios which we expect to meet and we're entering the CCAR process with a reasonably high degree of confidence again I think it has six goals around -- we would expect to have further action on the capital side.

So it's not like we asked for something didn't get it last year, we're just proceeding on a plan that we've been on for several years.

Steven Chubak - Nomura

No, I certainly wasn't suggesting that it's more focus on the, I guess your perception of the PPNR in the - progress that you made and it's probably the one area where as I've -- one clear argue that the fed has been overly conservative, at least certainly that we've heard from other market participants as well.

James P. Gorman

That's a fair comment and I think I'll let Ruth take you through how we think about it this year?

Ruth Porat

So we would agree it's obviously premature to comment on 2015 CCAR since we haven't seen the royalty that we would agree. We think the PPNR calculation was very counterintuitive, last year and our view is that another year of evidence, the benefit of the change in the business mix logically should help in last year it was the completion of the most strategic transformation of the acquisition of final piece of the wealth management business and you've seen we substantially increase the quality and consistency of earnings with the acquisition.

So our view is that this is an iterative process that improves all parties have improvements throughout the course of time and it was counter intuitive and we're working hard to highlight all that we've done and the benefit of the earnings stream and so again that’s been the key focus you’ve identified we did think it was counterintuitive.

Steven Chubak - Nomura

No thanks, that commentary is extremely helpful and then just switching over this one quick question on preferreds. You issued the additional billion as you noted in the quarter. It appears that you’re at least fast approaching the 150 basis points of RWA target, others have contemplated, as has been mentioned by Basel, I'm just wondering at this juncture do you feel as though you’re full on preferreds at the moment or should we anticipate additional issuance going forward?

Ruth Porat

We have no plans for more preferred issuance this year. Over the past few years we’ve been optimized on capital stack as you said, but prospectively I'm not going to close the door prominently but at this point no plans for preferred issuance this year.

Steven Chubak - Nomura

No, I understood. Okay, thank you for taking my questions.

James P. Gorman

Thank you.

Celeste Brown

Thanks so much for joining us for our third quarter conference call and we’ll speak to you again in 13 weeks.