Sure. We were pleased to see continued retail investor engagement in the fourth quarter, and that is reflected in higher transactional revenues. The integration process is moving very much on track. As you look at what does that mean and how do we look at the overall PBT targets, we're still very much focused on PBT of 20%. That's market dependent. And so, just a couple of pieces as you look through 2011 and beyond. First of all, retail activity was important. It helped drive the transaction revenues. I would caution you, there are fewer trading days in the first quarter of '11, that's relevant. But as we look forward, the market remains constructive, the building blocks to get to that 20% PBT margin are, to your point, completion of the integration and the drag that comes from the spend. But it's also a function of building up our Lending business, as we talked about before. Because with the Lending business, we have the benefit of driving a non-compensable revenue, which are an important part to reducing our overall compensation ratio in the business. The third element, the PBT margin expansion, is market dependent. We've said that. But just to give you a couple of data points that might be helpful. Every 100-point change in the S&P, we estimate impacts margin around 1%, all else being equal. And that's not looking at kind of investor psyche and reaction, but it's really more on the Asset Management fee side. Similarly, every 50 basis-point change in fed funds can impact margin around 1% as well. So it's really those elements completing the integration, building up the Lending business and market dependent that drives us to the 20% margin over time.

Howard Chen - Crédit Suisse AG

I guess maybe asked another way. I don't know if you look at it this way. But if there's no change in revenues from, let's say, where we are to end the year in the fourth quarter, what would you anticipate your margins to be as we exit 2011?

Ruth Porat

We're not going to do a forecastable forum. We're hoping to give you the pieces so that you can model with that yourself.

James Gorman

I just say this, Howard, we're not passive in managing the business.

Howard Chen - Crédit Suisse AG

And then, finally for me, Ruth, you spoke about the impact on the monoline exposure on fixed income results. Could you just give it a little more detail on what exactly is driving that? Is that the health of the wraps or you're hedging against that, or the counterparty exposure? And what should we be watching, going forward, to just continue to see that and how it impacts thick?

Ruth Porat

So this is a legacy exposure. It's going to take time to work out. The main point that we talked about repeatedly is we're not taking on new outside risks. We were a counter party in the trade, and we hedged our exposure with detail in the Q and of course the updated data in the K. But this quarter, the hedges went the other way on tightening monoline credit exposures, which is what resulted in the losses. So it was costly to hedge this quarter. You may continue to see a drag depending on market direction. The loss this quarter was $263 million, pretty much in line with last quarter.

Operator

The next question will come from Glenn Schorr with Nomura.

Glenn Schorr - UBS

So equity was up in the quarter, assets came down a little bit on the balance sheet, but the Tier 1 common ratio was down a little bit. I'm just curious if something changed on the risk weightings or how that works? I know it's small but just interesting directionally.

Ruth Porat

Sure. First, at this point, our risk-weighted asset number is just an estimate. The final numbers will be in the K. But risk-weighted assets increased from $325 billion at the end of the third quarter to we estimate $328 billion at December 31. So to your point, it was a small move. It was really much more of a mix change that resulted in a modest change. And the Tier 1 common was a bit lower due to a higher DT8 [ph] (31:19) deduction.

Glenn Schorr - UBS

And then just curious on the 4% reduction in assets, where are you seeing the opportunities to reduce balance sheet?

Ruth Porat

You're asking about overall balance sheet size coming down?

Glenn Schorr - UBS

Yes, and I'll tell you why I'm asking. If you look at the 17-or-so times common leverage or assets, the buyback common equity, that's about in the range where I think you can rest over time. I'm just curious how you think about the improving ROA and what's left on that balance sheet that's dragging that ROA down? I mean, it's a little different question than thick improving.

Ruth Porat

So balance sheet was down this quarter. That was really much more about client activity than anything. And we still remain comfortable kind of in that $800 billion to $850 billion range that we're talking about. But the point about ROA is very important, and we are very focused on it. And to your point, it is about ensuring that we are redeploying capital out kind of the capital-heavier areas and putting them behind our core institutional money management business and sales and trading business. And in particular, on the sales and trading side, our view is as we continue to build out our footprint and our flow business, we're going to be able to drive a more efficient utilization of the balance sheet and we are very focused on ROA.

Glenn Schorr - UBS

And so, I guess it takes time? In other words, I think a simple question is where's the leverage being used, like it takes time to wean yourself off of that? Is that what I'm hearing?

Ruth Porat

There are two elements very important, as we said. In Fixed Income, we're in the first of a two-year steady build, and it is about delivering consistency and dependability to clients which will increase our flow business and efficient utilization of the balance sheet. So that's one element of it. The other is we are systematically reducing the drag from legacy positions. Whereas we're moving into more of a Basel III world, we'll be continuing to redeploy capital behind our core Sales and Trading business in the most efficient areas.

Glenn Schorr - UBS

A simple last one on balance sheet is the 10.5% Tier 1 common? I'm just curious if you had any updated thoughts on Basel III compliance today and how that plays out?

Ruth Porat

Well, as we said before, we remain very comfortable with respect to Basel, both capital and liquidity, and have capacity to absorb the new rules with parent capital, which is about $20 billion. Just to give you a bit of an update on Basel III, our RWA guidance is virtually unchanged, essentially unchanged, same zip code from the commentary after the third quarter. So if you take our RWAs at 12/31, take our balance sheet under Basel III, RWAs would be at $240 billion and then through passive mitigation, kind of through the end of 2012, it would be down about $100 billion. And I guess the other factors to layer in to how we think about Tier 1 common under Basel III, couple items affecting capital. First, we have as you know $7.8 billion of MUFG convertible to common, which is meaningful. We have the 14% Smith Barney buy-in in 2012 and the NCI associated with Morgan Stanley Smith Barney. So if we take our consensus earnings, those factors, our 12/31 balance sheet under Basel III, and the ratio at the end of 2012 would be between 8% and 10%, which is why we say we're very comfortable with respect to Basel III.

Operator

The next question will come from Mike Mayo with CLSA.

Michael Mayo - Credit Agricole Securities (USA) Inc.

Do you have any more specific financial targets? That was helpful, your commentary for the year ahead. I was wondering if we could get a little more meat on the bones. A lot of your peers have more specific financial targets. And if you don't have a specific financial target, are you looking more at revenues or earnings or ROE, or which metrics?

Ruth Porat

So we, across the businesses, I think we've -- we gave you some more specifics on GWM. What we're looking for longer term is this PBT margin of 20%. Again, I'll give you the caveat, market dependent. But we're continuing to execute on that plan as I went through. On the Investment Management side, you saw the improvements in particular this quarter. And again, it's about building the core institutional, Money Management business and being -- efficiently redeploying capital out of Merchant Banking hedge funds, seed investments to support that core institutional business. And within our Institutional Securities business, we have real strength in Investment Banking and equities, where on our steady build within fixed income, it is about driving ROA. And I think in the aggregate, what we are looking at is, overall, we're very focused on what is ROE and delivering attractive returns for shareholders. So that's what we're driving. As James said, we're outstanding still on any of these businesses, driving execution across them.

James Gorman

The only thing I'd add is that last year, we hired a lot of the people, we hired a lot of very senior people. Actually, the weighted number of folks that we bought in, a lot of MDs and these folks are getting traction. We're not aggressively hiring right now. Obviously, if a specific opportunity comes up, we fill it. But we want to see some of the progress from those hires. And the improved client penetration we're getting particularly into some of our fixed-income products. So this is a year where we are now digesting the expenses and if things go as we planned them to go, we'll see good returns come off those.

Michael Mayo - Credit Agricole Securities (USA) Inc.

And I know you said the first of a two-year of a build in the trading areas and you hired a lot of traders. Do you think it's working? What sort of conviction do you have about this hire for growth strategy within trading? Do you feel better or worse about it?

Ruth Porat

We remain very confident and comfortable with the strategy. If we look at third-party data, it would suggest that we are gaining market share in a number of the businesses. Now the key is seeing that third-party data translate into greater results. And so, when we look at kind of the drivers of the business, in particular this quarter, we think that we're seeing signs of progress. We're pleased with the steps we're taking, continuing to execute against plan. But it was challenging being in a risk on, risk off market. And so, we had client activity but trading facilitation, market making was limited. And it is about both building up what we're doing, and we do remain very much on track, on point in that regard and having a bit of a more constructive market.

Operator

The next question will come from Jeff Harte from Sandler O'Neill.

Jeffrey Harte - Sandler O'Neill & Partners L.P.

Can you talk a little bit about the Investment Banking outlook? And I guess I'm thinking we see a lot of equity deals getting done. But coming off of a record revenue quarter, are you seeing enough potential activities filling the pipeline for strength to continue?

Ruth Porat

So overall, our investment pipelines do remain healthy across products and regions. It was a bit frustrating throughout the year to keep saying our pipeline is building, and it was just a question of time seeing the transactions moving through the pipeline, and I think you saw that in the fourth quarter. But the pipelines do remain healthy across products and globally. So on the M&A front, the pipeline's strong. We do expect a positive momentum that we experienced in 2010 to continue into 2011. We're seeing increased private equity activity and cross-border activity and emerging markets M&A. And it is very much about a lot of the factors we spoke about during the year, with high corporate cash balances and now, you know, with increasingly improved corporate confidence. And on the equity side, the backlog does remain strong. And again, it's around the globe. Asia remains strong, as does Europe and Latin America. We expect also to see more of the sponsor-led financing coming through the pipeline.

Jeffrey Harte - Sandler O'Neill & Partners L.P.

And how about on the Fixed Income Trading side of the business? I mean, you built up the business. What kind of market environment or assumptions are you making for how big this business should be?

Ruth Porat

I think that we're looking for more of a -- we're not looking for a heroic move in the fixed-income market. We're looking for a more muted or a more predictable environment. So in contrast to what was a pretty stark risk on, risk off market this past quarter, the absence of that kind of whip saw is what we need. We have two things, really, the backdrop of the environment. And it is not as though we are looking for another 2009-type environment. What we are looking for is again this absence of the risk on, risk off that had, at its core, a lot of policy-related events that drove activity. And so, kind of a more benign environment, and that enables us to really close the gap we have within fixed income. So if you look across our Institutional Securities business, we have a top-tier Investment Banking franchise, a very strong institutional equities business. And what we're really just looking to do is close the gap within certain areas, not even across the board. Within certain areas of fixed income capitalizing on strengths we already have within fixed income.

James Gorman

I'd just add also, we have an important Commodities business the last couple of years. Metals and agriculture have been major drivers of revenue for the industry. Our historic strengths have been in gas and oil. And I think as those markets are now starting to move, that business becomes more important to us.

Jeffrey Harte - Sandler O'Neill & Partners L.P.

As I look at the Wealth Management business, one of the things that kind of jumps out at me is net interest income doubling plus year-over-year. But then, I look at the deposit balance, and it's essentially flat on a year-over-year basis. That implies net interest margin expansion that we're not really seeing from other players. Can you talk a little bit about what's driving that net interest income increase?

James Gorman

My guess is there are two drivers behind that. One is the business wasn't owned for 12 months, in was owned for 7 months. So you get the impact of the $50-plus billion of deposits that sat on the Citi side, in addition to the $50 billion that sat on the Morgan Stanley side. So you get $100 billion per year. And the other is the growth in the lending businesses. You look at the margin book and I saw some of the online players reported their margin balances. They've grown pretty dramatically. We don't have as volatile a margin book as that. But clearly with the rising equity markets, our margin business has grown, and some of the leading and the spreads you get on the lending product that we've been building up.

Jeffrey Harte - Sandler O'Neill & Partners L.P.

Is the margin book the bulk of the lending within GWM still? And I guess, as you look forward, is non-margin-related lending something you try to grow?

James Gorman

Sure. The margin book is significant. But we've also -- we originate prime mortgages and small business loans and other things.

Jeffrey Harte - Sandler O'Neill & Partners L.P.

And, finally, just kind of trying to reconcile some of the items in the quarter. It looks as though ex DVA, you accrued compensation expense against some of the other gains. Am I thinking of that correctly?

Ruth Porat

Yes, you are. Items like CICC are included as part of our revenue and we accrue comp against it.

Operator

The next question will come from Guy Moszkowski with Bank of America.

Guy Moszkowski - BofA Merrill Lynch

I just wanted to go back to the DVA. It's so sizable. I was just hoping that maybe you could give us some metrics that can help us get some analytical clarity around the number? I mean, we've all been kind of conditioned to look through, and even so, when it's sizable you just want to really feel like you understand it. And given what we know happened to your cash bond spread, and even though you've issued a lot of structured product, it just seems like it was a very outsized move. Could you give us some of the underlying metrics to help us understand it?

Ruth Porat

Absolutely, good question. There are a couple of things I mentioned briefly. So to expand upon them, first, the average outstanding balance was up almost about 10% from the third quarter. There was a lot of interest in this product, so up almost about 10%. Second, the weighted-average maturity of the portfolio extended. And so, the change in the 10-year spreads played a bigger role. And then about 20% of the overall DVA was due to the option of extending maturity that's embedded in certain of the notes. So on the metrics, if you go to WAM, that moved nearly five years in the fourth quarter. It was three-and-a-half years when we last disclosed it in 2009. And so, again, focusing on the 10-year cash bond spreads this quarter, they tightened 56 basis points versus 27 in the third quarter. I'm glad you pointed out, it is cash bond spreads. Because the 10-year CDF was in only seven basis points. But that was a pretty meaningful narrowing. And to your point, with the WAM ex [ph] (0:45:43) moving out, it became more relevant to look at the 10-year.

Guy Moszkowski - BofA Merrill Lynch

And has the WAM moved out partly because of the nature of what you issued and also partly because there is essentially some negative curvexity [ph] (0:45:58) built into this?

Ruth Porat

It's really by virtue of what we were issuing.

Guy Moszkowski - BofA Merrill Lynch

Just to tie it together, you were talking before about some of the monoline credit spread impact. Is that related to this as well? Is that part of the 900-and-some-odd million or is that separate?

Ruth Porat

Completely separate.

Guy Moszkowski - BofA Merrill Lynch

To the point that was brought up a minute ago on the compensation effect on the CICC, do you believe that comp really would have been lower if you hadn't had the gain? The reason I ask is that, again, as we think about modeling out future earnings power, we need to really understand what your comp dollar needs are. And based on what we heard in the press, and obviously a lot of that stuff can be wrong, it seems like the firm needed every dollar of comp that it had available to it. And so I wondered if your comp dollars actually would have been less even if you hadn't had the gain?

James Gorman

Guy, we are focused on balancing what we think is right for our shareholders and ensuring that we pay the right people the way we've got to pay them. The fact of the matter is, if we didn't have the revenues and we didn't have the earnings, we would have adjusted it through our compensation. We've been very deliberate and very focused on that. But we wouldn't do at a level where we thought we'd be putting significant risk into the franchise. We're also aware that these businesses aren't -- they don't start and begin on January 1 and close on December 31. They're multiyear processes. So we look at the total bag of earnings. We look at the various charges that we make. You could make arguments that you could extract legal reserves. You could extract restructuring of businesses, whether it be FrontPoint or other businesses. We look at the total mix, and then when we deal with what we've got on our net revenue base, that's how we think about comps. So I kind of cherry pick in that regard the CICC [ph] (0:48:12) as good revenue is generated through the wherewithal of folks at this firm, and that's something we felt very comfortable compensating on.

Guy Moszkowski - BofA Merrill Lynch

In Asset Management in the quarter, and you sort of spoke to this, the ratio of the payout in non-controlling interest as a percentage of the investment revenue that you showed was a lot lower. It was about 28% in the fourth quarter. It was almost half in the third. Can you just explain to us why the shift?

Ruth Porat

I think I'm going to need to get back to you on that one.

Guy Moszkowski - BofA Merrill Lynch

It's just sort of as we look forward and try to model revenues ahead. It's just useful to have that. And then, the final question I have for you is, was there any significant change in the cash-versus-equity component or mix of compensation this year?

Ruth Porat

So in our compensation, we did increase the deferral. But when we talk about deferred comp, we talk about both deferring cash and deferring stock. And so, the overall mix was pretty much the same with higher deferrals.

Operator

The next question will come from Roger Freeman with Barclays Capital.

Roger Freeman - Barclays Capital

I just want to come back to the sort of thick buildout and looking at some of the personnel changes and folks you moved around, to what extent does that sort of stretch out timelines or doesn't it? I mean, does that sort of impact just given the magnitude as the reporting line changes going on?

Ruth Porat

No. I think I've said it a couple of times now. This is the first of a two-year steady build. Colm left this seat a year ago. And we've been really building out the team. It does take time, but we are -- I'm going to repeat it, it's the first of a two-year steady build -- I apologize, completed the first of a two-year steady build.

Roger Freeman - Barclays Capital

But then just coming back to the other comments, I think the change you made about sort of growth or headcount because you're not really hiring. So really, it’s sort of net neutral on the year, so you still have sort of a buildout going on? But assuming there'll be some turnover in the process, is that kind of how you think about it?

James Gorman

I wouldn't. I mean, as I look at the businesses, I think institutional securities. We hired about 70% of our total plan last year. We sort of pulled the curtain over at about in August. And there are a couple of areas where we didn't quite get done what we want to get done. And a couple of our support areas, particularly in Risk and Technology, where -- but these are very small numbers. In Wealth Management, I mean, we're carrying something like 2,000 contractors working on the integration. I think that's now pretty much, if not running at peak, pretty much at peak. And I think our financial advisor head count will stay in the band that Ruth put out, 17.5

to 18.5. It may be down a couple of hundred from this year, it may not be. I wouldn't draw too much from that one way or the other if it’s up or down as long as it stays in that band. And Asset Management, some of the merchant banking businesses, we've had a lot of success in Asia and in our Infrastructure business. But they're small numbers. So I think you're probably -- we haven't actually sat down and laid out our headcount plan for the firm. But I would say, the aggregate picture would be roughly flat. I'd be surprised if it's up much. We're certainly not anticipating any big riff or anything of that nature.

Ruth Porat

So, selectively [ph] (0:52:12).

Roger Freeman - Barclays Capital

And then just coming back to the question on the net interest income in the bank. The other I guess thing that sort of popped out at us or I've noticed that is that the net interest income in the Institutional Securities business has been declining sort of at the same time. And we’re just wondering if there's any connection between the two, like transfer pricing of any sort or anything.

Ruth Porat

No, there's not a connection. And in Institutional Securities, as you know, it's more of a -- NIM is more of a banking book than a trading book concept. And so, across [ph] (52:53) in Institutional Securities is really driven by our trading and derivatives activities that have an interest component. So we think of that business holistically, there's not a link between the NIM discussion we'd have there and the NIM in TW [ph] (53:03).

James Gorman

And the way we report it in Wealth Management, we manage it internally. There are two separate -- there's the BDP [ph] (53:10), the deposit spreads, and then there's the net interest margin on the core loan book.

Roger Freeman - Barclays Capital

The tax rate, can you give us any sort of comments on the go forward? I mean, it's been low and I understand it jumps around quarter to quarter, depending on sort of levels of net income and credit, and if not [ph] (53:31) you could get. Just kind of look at it on the aggregate. I mean, you still generated $6 billion of pretax profit, not a small amount in 2010. And to the extent that goes up, I mean do you have enough of these short of shields to keep the tax rate unusually low?

Ruth Porat

No. We do our tax planning annually. So if you just exclude the discrete items from 2010, the effective annual tax rate from continuing operations would've been about 28%. And as we look forward to 2011, we suggest that you look at the statutory tax rate. So it's about 35%. Something less than 35% would be the right way to look at it for 2011.

Roger Freeman - Barclays Capital

Last question, given the charge on FrontPoint, can you say where that's carried now on the book?

Ruth Porat

Again, the backdrop is our overall strategy in this area to free up capital and merchant banking activity [indiscernible] (54:27), we're continuing to do that. But with respect to FrontPoint specifically, we're continuing to restructure our ownership to a minority stake. Given the events last quarter and with the lower AUM, there were some changes to the deal terms. We did take a higher charge in the fourth quarter. It was $126 million, if I recall correctly.

Roger Freeman - Barclays Capital

But presumably, to the extent that assets continue to flow out, that can continue to be revised, I guess, is the assumption?

Ruth Porat

The carrying value as of the fourth quarter is $30 million, just so you have that.

Operator

The final question will come from Mike Carrier from Deutsche Bank.

Michael Carrier - Deutsche Bank AG

One follow-up on the Wealth Management business, and the clarity around rates and markets, that’s helpful. If we look at what you have left in terms of consolidating the platforms, the remaining synergies and I think the last time you guys gave the number, there was about, you made $400 million or $500 million less. But if we just look at that and assume that, that gets done at some point at the end of this year beginning of next year, then if we just run those synergies through the model, based on what you can control, can you still get that pretax margin to, like, the mid-teen level, call it 15, 16, 17? And then basically, whether it's the rates, the markets, the scenarios that you gave there, would be able to push you above that 20% level? I'm just trying to figure out what you guys can still control.

Ruth Porat

I think you -- I went through the building blocks, and I think you've just articulated it well. Getting through the spend is an important part of it. We're still very much on track with the platform for the third quarter of this year and moving the Morgan Stanley FAs over the third quarter. We'll be training the Smith Barney FAs through the fourth quarter and starting to move over again next year. So there is some spend that continues. That's an important element of it, and building up the lending book, as we've talked about, is an important element of it to get comp-detectable revenues to increase. So again, driving towards that 20% PBT margin, over time, market dependent.

James Gorman

I mean I know I a lot of folks are very curious about the margin as we are. To be honest, it doesn't give us a whole lot of anxiety. This business used to have under $6 billion of revenues and had 7%, 8% margin. And now has revenues of over $12.5 billion. So you understand fixed cost, you understand the arithmetic in some normalized markets. [indiscernible] (57:05). Frankly, that's not a big anxiety for us.

Ruth Porat

In fact, where we're more focused is that it really helps us have a very attractively diversified revenue stream by business and product and geography. And we've talked a lot on this call about capital. Some are more capital-intensive businesses like TWM [ph] (57:22), Banking, Asset Management, are more capital-light. So it's really, in the aggregate, the portfolio that is, in our view, one of the most important elements.

Michael Carrier - Deutsche Bank AG

And then just based on your capital ratios, and we'll all come up with our valuation for the buy in for MFSD [ph] (57:40). But if you look at the amount of capital that you're going to generate through 2012 and then if you look at just normal leverage ratios, do you have any sense in terms of how much you would be paying in equity versus cash or debt?

Ruth Porat

No.

Michael Carrier - Deutsche Bank AG

And then last one, just on the Fixed Income side, on the legacy issues in terms of the monoline, like what's the timing on that? And is there any way to either restructure -- basically, how much is that going to weigh on the earnings? And then on the core business, is it -- like, 2010 more getting the people in place from a products, and then 2011 is more gaining traction with clients?

Ruth Porat

So on the monoline point, it is a legacy exposure. It's going to take time to work out, so I would just refer you to all the details that's in the K and was in the Q last quarter. In terms of your key issue there in terms of kind of the ongoing implementation in Sales and Trading, 2010 was about adding talent and structure around the way we cover clients and drive client relationships deeper. As we've talked about before, we have strength in a lot of our franchises across a lot of clients with this brand globally. And the strengths that we have, and it is just continuing to execute. And so, adding talent to a platform was an important element of it. But I wouldn't like to suggest we did one last year. We're doing the other this way. We had signs of market share improvement in the fourth quarter, as I said, that we are driving to bottom-line results that we can talk about, hopefully, in the not-too-distant future. But we are consistently executing, adding talent and driving relationships across our clients, and that's really what's very important in the fixed income move, closing the gaps in certain of the areas, building on the strengths in many of the others. Thank you, and thank you all for being on the call today.

Operator

Ladies and gentlemen, thank you for participating in today's conference call. You may now disconnect.

Operator

Welcome to the Morgan Stanley conference call. The following is a live broadcast by Morgan Stanley and is provided as a courtesy. Please note that this call is being broadcast on the Internet through the company's website at www.morganstanley.com. A replay of the call and webcast will be available through the company's website and by phone for a period of seven days.

This presentation may contain forward-looking statements. You are cautioned not to place undue reliance on forward-looking statements which speak only as of the date on which they are made, which reflect management's current estimates, projections, expectations or beliefs, and which are subject to risk and uncertainties that may cause actual results to differ materially. For a discussion of additional risk and uncertainties that may affect the future results of Morgan Stanley, please see Morgan Stanley's annual report on Form 10-K for the year ended December 31, 2009; annual report on Form 10-K; Morgan Stanley's quarterly report on Form 10-Q; and Morgan Stanley's current report on Form 8-K.

The presentation may also include certain non-GAAP financial measures. The reconciliation of such measures to the comparable GAAP figures are included in Morgan Stanley's annual report on Form 10-K, Morgan Stanley's quarterly reports on Form 10-Q and Morgan Stanley's current reports on Form 8-K, which are available on Morgan Stanley's website, www.morganstanley.com.

 At this time, I would like to turn the program over to the President and Chief Executive Officer, James Gorman for today's call.

James Gorman

Well, thank you, operator, for that fulsome introduction. And good morning, everyone and thank you for joining us.

Before we review our financial results, I'd like to do two things: review our accomplishments in 2010 overall and for each business and provide a brief outlook. In 2010, Morgan Stanley participated in nearly every signature transaction to raise capital and helped reinvigorate the markets. Whether it was the GM and Citi IPOs in the U.S., ABC in China, and Petrobras in Brazil, among many others, Morgan Stanley was a skilled and trusted adviser to governments, corporations and investors as we work to restore economic growth and create new investment opportunities around the world.

In Institutional Securities, we finished at or near the top of the league tables in M&A, global equity and IPOs. A great testament to the teamwork between Investment Banking, global capital markets and equities. It's Morgan Stanley at our best.

We also saw market share improvements in our Equity Sales and Trading business. Clearly, we face difficult markets in 2010. Our results reflect that more work needs to be done in some of our fixed-income businesses. While our strategy in this business remains intact, we bolstered our efforts through the following organizational changes, including Ken deRegt as Head of Global Fixed Income Sales and Trading based in the U.S., and as a result, Keiki (sic) [Keiko] Otsuki will serve as interim Chief Risk Officer.

To better align our business and geographic objectives, which we will also do in reinforcing our efforts in fixed income. Colm Kelleher, in addition, to running sales and trading, will assume coverage of Europe, the Middle East and non-Japan Asia and will now be based in London. And Paul Taubman, in addition to running Global Capital Markets and Investment Banking will assume coverage of Latin America and Japan and will remain in New York.

In Global Wealth Management [GWM], we've also made some additional organization changes driven by Charlie Johnston's decision to retire at the end of this year. Charlie will continue through the end of the year as Vice Chairman of Morgan Stanley Smith Barney, and Greg Fleming will become President of GWM in addition to Asset Management. Jim Rosenthal was appointed Chief Operating Officer in the firm in January and continues in his role in the integration of Morgan Stanley Smith Barney.

Overall, these management changes reflect our desire for superior execution and our belief in what the future environment demands from our leadership as well as obviously the departure of Tom Nides, our former Chief Operating Officer, who has moved to serve in Washington.

With regard to the Smith Barney integration, we're pleased with our progress. We remain on track as evidenced by the increased profitability this quarter and net new money for the full year. Revenues and margins will continue to improve as individual investors further engage.

In Asset Management, we refocused the business around our core institutional and merchant banking franchises, added talent and addressed the issues posed by a distressed global real estate market.

Globally, our colleagues in Japan worked hard to launch our strategic joint venture with Mitsubishi Bank, a partnership that is already starting to pay important dividends in terms of our ability to serve clients. And with the sale of CICC stake, we are poised to start a new chapter on the very strong relationships we've built in China and across Asia for many years. We're currently pursuing a domestic license in China and recently received approval to form a new investment banking joint venture with Huaxin Securities, also known as China Fortune Securities.

In Europe, the Middle East, Latin America and Australia, our people on the ground are capitalizing on the Morgan Stanley brand to take advantage of the many opportunities we now see.

Overall, we've made progress executing our strategy despite challenging market conditions this year. We remain confident as evidenced by our success in investment banking equities, our disciplined approach with Smith Barney and our substantial improvement in Asset Management. Looking forward, we continue to focus on growing revenue, earnings and ROE in each of our businesses.

Our priorities for 2011 and 2012 include: Within Institutional Securities, obviously, improving our results within Fixed Income Sales and Trading and maintaining our leadership positions in Investment Banking and Equity Sales and Trading; within Global Wealth Management, growing our Transaction and Advisory business, increasing deposit and lending revenues, and after the completion of the integration in 2012, to see commensurate cost reduction; within Asset Management, monetizing our strong investment performance in the core business and optimizing our expenses.

Let me turn to compensation. A year ago, we explicitly said you would not see the same compensation ratios in 2009 and we did not. The full-year ratio was 51%, down from 62% a year ago, which was in part driven by extremely high DVA. In absolute terms, full-year compensation was higher due to the Morgan Stanley Smith Barney completion of 12 months and the investment in sales and trading.

We also demonstrated discipline through our compensation structure. In fact our high deferral rates and call-backs balanced prudence with incentives, which were important to shareholder considerations. This management team is intently focused on improving earnings and ROE, and in the process, we will reward our shareholders and our employees.

Thank you. Now I'll turn over to Ruth to review our financial results in more detail, and we will both be available for question and answer.

Ruth Porat

Thank you, James. For the quarter ended December 31, income from continuing operations applicable to Morgan Stanley was $867 million, with diluted earnings per share of $0.43 after preferred dividends.

There were four factors that drove our results this quarter. First, ongoing strength in Investment Banking and Equity Sales and Trading, historically very strong areas for us. Second, subdued results in Fixed Income, where we continue to work on our turnaround. Third, notable progress in both Global Wealth Management and Asset Management. And finally, strategic asset sales and expense discipline.

Our fourth quarter revenues of $7.8 billion included two noteworthy items: a $668 million or $0.17 per share gain from the sale of CICC; and negative $945 million or $0.36 per share impact from the tightening of credit spreads on firm-issued structured notes, commonly referred to as DVA.

This quarter, DVA was driven by a larger outstanding balance, a longer weighted-average maturity and further maturity extension in a portion of our notes. The full-year firm-wide compensation ratio was 51%. Excluding negative DVA of $873 million and the U.K. bonus tax of $272 million, the ratio would have been 49%.

Non-compensation expenses increased 12% sequentially, including higher technology and legal cost. For the full year, non-compensation expenses were up roughly 7% annually, normalizing for 12 months of Smith Barney. The increase was driven by higher business activity as well as our ongoing investments in technology. Notably, book value at the end of the quarter was $31.49 per share, up 16% for the year.

Turning to the balance sheet. Total assets were $808 billion at December 31, down $34 billion sequentially, driven by lower client activity. Although our calculations are not yet final, we believe our Tier 1 capital ratio under Basel I will be 16%, and our Tier 1 common ratio will be 10.5%, demonstrating the strength of our balance sheet. Risk-weighted assets under Basel I are expected to be approximately $328 billion at December 31. Now turning to our businesses.

Institutional Securities revenues of $3.6 billion included the impact of CICC and DVA as mentioned earlier. Noninterest expenses were $3.2 billion in the quarter, up 20% from the third quarter on higher compensation and the seasonality of non-compensation expenses.

For the full year, noninterest expenses increased slightly. The full-year compensation ratio was 43%, excluding negative DVA of $873 million and the U.K. bonus tax of $269 million, the ratio would've been 40%. The business reported a pretax profit of $437 million.

Investment Banking revenues were $1.5 billion, up 50% from last quarter. For 2010, Morgan Stanley ranked number one in global IPOs, number one in global equity and number two in both global-completed and global-announced M&A. For the year, we advised on eight of the top 10 announced M&A transactions. In the quarter, we were a book runner on all five of the top five transactions in global equity and four of the top five transactions in global IPOs.

Advisory revenues of $484 million were up 30% sequentially, driven by higher activity in EMEA and the Americas. Significant announced M&A

transactions in the quarter were the $21 billion combination of Weather Investments and VimpelCom in Europe and the $10 billion restructuring of Westfield Group in Australia.

Equity Underwriting revenues were $661 million, our highest reported quarter. We saw improvement across all regions. Asia, once again was particularly strong with notable offerings, including AIA's $21 billion IPO, PETRONAS Chemical Group's $5 billion IPO and China Rongsheng Heavy Industries' $2 billion IPO.

Fixed-income Underwriting revenues of $370 million were relatively flat to last quarter, as lower bond issuance was largely offset by higher loan syndication fees. Overall, our Investment Banking pipelines remain healthy across products and regions.

Equity sales and trading revenues of $1.1 billion included negative DVA of $103 million. Cash equity revenues increased sequentially on higher client activity and increased market share. Derivatives revenues, similarly improved given a more stable volatility environment and increased client flows, and prime brokerage revenues increased from the third quarter as we continue to deepen relationships with our existing clients. Average client balances continued to grow, up 11% sequentially.

Fixed income sales and trading negative revenues of $29 million included negative DVA of $842 million. Interest Rate, Credit and Currency revenues were down from last quarter across all businesses. Commodities revenues were relatively flat to the third quarter as lack of market volatility continued to dampen client activity. Our results also continue to reflect a drag from the tightening of monoline credit spreads.

Turning to VaR, average trading VaR declined to $132 million from $142 million last quarter, primarily driven by reductions in interest rates and credit. Average non-trading VaR decreased to $95 million from $103 million, primarily due to the sale of our equity stake in Invesco.

Global Wealth Management revenues of $3.4 billion increased 8% sequentially as higher commissions, asset management fees and net interest income more than offset lower trading revenues.

Commissions increased 31% from last quarter as higher client activity was driven by new issuance and secondary trading. Noninterest expenses were $3 billion, up 5% from last quarter, both on a higher non-compensation and compensation expenses. Integration costs were approximately $63 million. The compensation ratio of 59% in the fourth quarter continues to be driven primarily by the formulaic grid payout. However, the lower ratio this quarter reflects reductions in non-FA compensation, which is not likely sustainable in the near term.

Profit before tax was $390 million, and the PBT margin was 12%, up from 9% last quarter. Total client assets increased 4% sequentially to $1.7 trillion on market appreciation and net asset inflows of $14.1 billion in the quarter. Net new money for the year was $22.9 billion. The number of FAs was 18,043, within our expected range of 17,500 to 18,500, while turnover within our top two quintiles, remained in line with historical lows. Deposits in our Bank Deposit Program were $113 billion, all of which $55 billion is held by Morgan Stanley banks.

Asset Management net revenues of $858 million increased 7% from the third quarter. Core Asset Management revenues of $410 million included higher asset management fees and increased gains on seed investments as well as a $126 million impairment charge related to the restructuring of FrontPoint and a $96 million gain on the sale of our equity stake in Invesco.

Merchant Banking revenues of $448 million included investment gains in real estate and private equity. Approximately $109 million was related to investment gains from consolidated Nasref [ph] (22:29) funds. Given the ownership structure of these funds, the majority of the gains are passed to third-party investors in the non-controlling interest line. Approximately $95 million of the principal investment gains were from private equity, primarily driven by Asian investments. Noninterest expenses for Asset Management declined 4% from last quarter on lower compensation and non-compensation expenses. PBT was $356 million for a margin of 41%.

Total AUM increased slightly to $279 billion, primarily due to higher market levels. Asset flows were negative $600 million during the quarter, primarily driven by $1.5 billion of outflows related to FrontPoint. As of December 2010, over 70% of our long-term strategies continue to outperform their respective benchmarks on a three-, five- and 10-year basis.

Now turning to our outlook. We are increasingly encouraged by the pace of the recovery as reflected in capital markets activity. Key indicators include: strengthening equity markets, improving corporate confidence reflected in M&A activity, successful equity issuances across industries globally, higher investor activity and ongoing growth in emerging markets. That said, the potential for more policy intervention that drove the risk on, risk off investor sentiment last year remains due to both macroeconomic issues and ongoing regulatory implementation. Sovereign credit concerns in Europe continue to be at the forefront.

And in the U.S., distressed state and local budgets as well as the deficit remain open items. Inflation risk in emerging markets could also elicit policy moves. And on regulation, added clarity regarding certain elements of Basel and Dodd-Frank are helpful, although final rules are clearly still in formation.

While our overall performance is dependent on the global market environment, we believe we are well positioned for the evolving regulatory regime, with an emphasis on client-focused businesses supported by appropriate capital and liquidity. Our growing client footprint and investments across the firm are key to leveraging the strengths we have across many of our businesses and closing gaps and others, with disciplined investment and implementation proceeding performance.

Looking forward, we are focused on growing our share of the market by leveraging our global brand and client franchise to provide the highest quality service to clients and stronger returns to our stakeholders.

Thank you. And now we will take your questions.

Operator

[Operator Instructions] And the first question will come from Howard Chen with Credit Suisse.

Howard Chen - Crédit Suisse AG

James, you spoke to more work to be done in fixed income to drive revenue and market share growth. Other than the announced management changes, could you just give us maybe your top three action items to get there? I get a lot of questions from investors on what exactly is the limiting factor in closing that gap.

Ruth Porat

Why don't I go ahead on that. As James said, as I said, we're in the first of a two-year steady build of that business. And as we've talked about in the past, our view is that we were subscale and although we had a good mix of structure solutions and flow business, we really needed to build out the flow business more. And that's really the conversation we've been having about rates and foreign exchange. And so, we built out that footprint, we're building flow. But when you look at this quarter, there's really a bit of a virtuous cycle with broader, deeper footprint allowing more efficient trading to support our client activity. And so really, with the buildout of our footprint, we're leveraging the strength we have across Institutional Securities with clients to drive those relationships deeper. But it is the first of a two-year steady build.