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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

Good morning, everyone and thank you for joining us. Before handing over the call here to Ruth, I wanted to give some brief remarks about our results and update you on our strategic initiatives.

Our quarterly financial results were clearly affected by the significant slowing of capital markets again last quarter and continued through the summer and into September. Volumes and client activity across our businesses, particularly in the first half of the quarter, were weak as institutional and retail investors continued to avoid risk assets.

That said, this quarter we achieved some key milestones in shaping our future and the firm delivered improved performance across investment banking, wealth management, and asset management. While these businesses performed well, our aggregate results for the quarter were disappointing and do not reflect the full potential of this franchise.

Morgan Stanley remains a work in progress. We are rebalancing the firm to more effectively leverage our capital base and balance sheet. We are adopting a model consistent with the legislative changes emanating from the Dodd-Frank bill and the regulatory changes being crystallized through Basel III.

We are reallocating our capital and our balance sheet away from proprietary businesses and reinvesting it in our client businesses. An initiative this quarter consistent with this rebalancing was the restructuring of our ownership in the hedge fund, FrontPoint Partners whereby we will significantly reduce our total ownership.

Within our business segments, we saw progress in many areas, although some businesses clearly remain subdued, most notably fixed income, as Ruth will detail in a moment. In institutional securities, we are broadening our client footprint and expanding our strengths and capabilities. This was evidenced by increased market share in all capital markets' underwriting products, as well as the improvement in our institutional investor rankings.

In global wealth management, while progress will never be a straight line, we saw improvement on our key metrics including pretax margin and net new money flows, while delivering steady revenue in a very challenging environment.

Encouragingly, retail investor activity appeared to bottom earlier in the quarter. The build of our technology platform is expected to be completed by the third quarter of next year, followed by a series of rollouts extending into 2012. Key decisions on the integration are being made and being executed. While this is a complex integration task, we have no major concerns about the plans or progress, although as we previously said, financial performance of the business is obviously somewhat market-dependent.

In asset management, we continue to restructure the business, as evidenced by our reduced ownership in FrontPoint Partners and the hiring of several talented executives into the long-only institutional business. We will be rolling out more detailed plans in coming months.

Let me finish briefly by commenting on the regulation environment. The regulatory changes are real, permanent and will fundamentally reshape the industry. With respect to capital, Ruth will outline the potential impact on our risk-weighted assets under the proposed framework. Morgan Stanley is embracing the changes, rapidly evolving our business model to position our firm to thrive in the future.

Now, please I'll turn it over to Ruth for more details on the specific third quarter results.

Ruth Porat

Thank you, James. For the quarter ended September 30, income from continuing operations applicable to Morgan Stanley was $313 million with diluted earnings per share of $0.05 after preferred dividend.

Our results this quarter reflected muted performance within our fixed income business. At the same time, corporate clients reengaged in investment banking and our wealth and asset management businesses delivered modestly higher profits with positive fund flows. Our revenues included the negative impact from the tightening of credit spreads on firm issued structured notes, commonly referred to as DVA, of approximately $731 million or $0.30 per share.

Specifically, our third quarter revenues were $6.8 billion, down 15% sequentially or up 4% normalizing for DVA in each period. Our non-interest expenses were $6 billion, down 4% from last quarter, primarily on lower compensation. The firm-wide compensation ratio was 54%. Excluding DVA, the compensation ratio was 49%. Non-compensation expenses were $2.3 billion, down 3% from last quarter, primarily due to lower brokerage and clearing and professional services expenses.

Results for the quarter also included $176 million or $0.12 per share associated with the repatriation of non-U.S. earnings at a cost lower than originally estimated. Excluding this, the quarterly effective tax rate from continuing operations would have been 19.1%. Including discontinued operations, we reported a net loss per diluted share of $0.07, which included a loss of $229 million associated with the planned disposition of Revel. The remaining carrying value of this investment is approximately $40 million.

Turning to our book value on Page 3 of the supplement, book value at the end of the quarter was $31.25 per share, up 5% sequentially, primarily due to the issuance of $5.6 billion in common equity to CIC.

Turning to the balance sheet data on the same page, total assets were $841 billion at September 30, an increase of 4% from the second quarter, primarily driven by interest rate products and prime brokerage.

Our capital ratios continue to demonstrate the strength of our balance sheet. Although our calculations are not final, we believe our Tier 1 capital ratio under Basel I will be 16.5% and our Tier 1 common ratio will be 10.8%. Risk-weighted assets under Basel I are expected to be approximately $326 billion as of September 30.

With respect to Basel III, many rules still require interpretation and final rule writing. Based on our analysis of the guidelines to date, we believe that our third quarter balance sheet under Basel III would result in our risk-weighted assets increasing pro forma by approximately $240 billion. This increase would be prior to run-off and mitigation opportunities, which we estimate would reduce RWAs by approximately $100 billion by the end of 2012 for a net RWA increase of about $140 billion or approximately 40%.

The primary driver of the increase in our RWAs is higher market risk for securitization and structured credit correlation products and credit risk for counterparty exposures. These are clearly preliminary estimates which are subject to final guidelines by the Federal Reserve.

I will now briefly review our business units. For institutional securities on Page 5 of the supplement, revenues were $2.9 billion, down from the second quarter on lower client volume and lower trading results across the sales and trading businesses, particularly fixed income.

Revenues included approximately $731 million of negative DVA as mentioned earlier. Normalizing for DVA, revenues were down 3% for the quarter. Principal investment revenues of $387 million included gains of approximately $313 million on an investment held by consolidated investment partnership with other third-party investors.

Non-interest expenses were $2.7 billion in the quarter, down 9% sequentially on lower compensation and non-compensation expenses. The compensation ratio was 52% in the quarter. Excluding the impact of DVA, the compensation ratio was 41%. The business reported a pretax profit of $240 million.

With respect to investment banking, revenues were $1 billion, up 14% from last quarter. For the first nine months of 2010, Morgan Stanley ranked first in global IPOs, second in global completed M&A, and third in global announced M&A and global equity. During the quarter, we gained share across capital markets' underwriting products, including global equity, as well as investment-grade and high yield debt. And we led significant deals in the market, including three of the top five transactions in global equity and in global IPOs.

Advisory revenues of $371 million were up 29% sequentially, driven by an increase in the number of closed transactions. We advised on significant announced M&A transactions in the quarter, including International Power's $25 billion acquisition by GDF Suez Energy.

Equity underwriting revenues were $260 million, down 3% from last quarter on lower volumes in Europe. Significant transactions included bookrunner positions for the two largest equity offerings this quarter, Agricultural Bank of China's $12 billion IPO and Petrobras' $69 billion follow-on offering.

Fixed income underwriting revenues increased 15% sequentially to $377 million on higher investment and non-investment grade bond issuance, partially offset by lower loan syndication fees. Significant transactions included Valeant Pharmaceuticals' $2.8 billion loan facility and $1.2 billion high yield bond offering, as well as Aon Corporation's $2.5 billion bridge and term loan to acquire Hewitt Associates.

Overall, our investment banking pipelines remain healthy across products and regions and continued to improve from last quarter.

Turning to equity sales and trading on Page 6, equity sales and trading reported revenues of $925 million that included the negative impact of DVA of $196 million. Cash equity revenues were down from the second quarter as market volumes declined sharply. However, commission levels outpaced overall market activity across most geographies. Prime brokerage revenues remained flat against the backdrop of declining hedge fund leverage. However, balances trended up in September, ending well above the quarterly average.

Derivatives revenues declined meaningfully on lower client activity and lower volatility versus the second quarter. Of note, our Asian equity business was up about 25% versus the second quarter, driven by significantly stronger client flows than overall market activity.

Turning to fixed income sales and trading, revenues of $846 million included the negative impact of DVA of $464 million. During the quarter, we continued to execute on improving distribution and footprint within interest rates, FX, and emerging markets.

Within our Interest Rate, Credit and Currencies business, IRCC, credit corporate's performance was up meaningfully versus the second quarter with particular strength in investment grade. Interest rates revenues were up modestly from the previous quarter and FX revenues declined significantly on lower client flows and lower trading revenue.

IRCC results were also negatively impacted by hedging losses of $272 million from the tightening of monoline credit spreads. In commodities, revenues were also lower on weaker client activity as markets continued to be range-bound. Other sales and trading negative revenues of $341 million primarily reflect funding costs, including the amounts liquidity being held by the U.S. banks, as well as the component of DVA.

Turning to Value-at-Risk on pages 3 and 6 of the supplement, total average trading and non-trading VaR increased to $189 million from $164 million in the second quarter, driven primarily by non-trading VaR. Average trading VaR was relatively unchanged at $142 million compared to $139 million in the second quarter as increased interest rate and credit risk was offset by reduced foreign exchange risk. However, average non-trading VaR increased to $103 million from $67 million, primarily driven by the increase in the value of our investment in Invesco.

With respect to our global wealth management business summarized on Page 8 of the supplement, revenues of $3.1 billion were relatively unchanged from last quarter as higher trading and net interest income offset lower commissions in asset management revenue. Non-interest expenses were $2.8 billion, down 2% from last quarter on lower compensation. The compensation ratio was 62%, driven by the formulaic grid payout, but offset by reduced non-FA comp expense.

Integration related costs were approximately $83 million in the quarter. Profit before tax was $281 million and the PVT margin was 9%, up from 7% last quarter. On Page 9 of the supplement, you can see the quarterly productivity measures for the business. Total client assets increased 7% sequentially to $1.6 trillion on market appreciation with asset inflows of $5 billion in the quarter. The number of FAs was relatively unchanged at 18,119 and turnover within our top two quintiles remained well below our target.

Deposits in our Bank Deposit Program were $109 billion, of which $52 billion is held by Morgan Stanley banks. The Bank Deposit Program represents the majority of the $61 billion in firm-wide deposits at quarter-end across global wealth management and institutional securities.

Now, turning to asset management on Page 10 of our supplement. Net revenues were $802 million, up substantially from the second quarter. Core asset management generated revenues of $380 million, up 27% sequentially due to positive marks on seed investments and higher performance fees.

Merchant banking revenues of $422 million increased significantly from last quarter, driven by principal investment gains in real estate and private equity. Approximately $203 million of these investment gains were from consolidated MSREF fund. As such, 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 $83 million of the investment gains were from private equity, primarily driven by Asian investments.

Non-interest expenses for asset management were up 5% from last quarter on higher non-compensation expenses that included a $31 million impairment charge on FrontPoint intangibles. PVT was $279 million for a margin of 35%. Excluding the gains attributable to the non-controlling interest, the segment was profitable with PVT of $86 million for a margin of 14%.

As summarized on Page 11 of the supplement, total AUM increased 9% to $273 billion, primarily due to higher market levels and asset inflows which totaled $2.9 billion during the quarter. As of August 2010, over 70% of our long-term strategies continued to outperform their respective benchmarks on a three, five, and 10-year basis.

Let me end by commenting on our outlook. Obviously, the key variables regarding our performance are tied to the global market environment and executing on the opportunities created in that environment. Emerging markets activity remains robust based on the volume seen in the third quarter, as well as what we see in the backlog going into the fourth quarter. We believe that firms with a global presence, such as Morgan Stanley, are well positioned to benefit from this activity.

However, the key question remains "opportunities in developed markets." Although growth in developed economics continues to be fragile, we are cautiously optimistic about the outlook for the next year. First, we have seen signs of activity beginning to pick up in September across our businesses. Corporate balance sheets remain cash-rich and clients are using cash for repurchase, which is providing some support to the equity markets and for M&A. And the pace of activity with retail investors, as James noted, has also picked up.

That being said and given the fragility of the recovery, it is too early to assume that these trends are going to continue. For example, policy decisions could still affect the scope of recovery. With three potentially important upcoming events, the expected quantitative easing from the Fed, the U.S. midterm elections, and the G-20 Meeting in Seoul in November, it's premature to gauge their impact on markets and investors.

Though the industry faces near-term cyclical challenges, we view capital markets as having long-term secular growth opportunities. We remain very focused on disciplined execution of our strategy to continue the building and enhancing of our global footprint.

Thank you. And now, we will take any questions you may have.

Question-and-Answer Session

Operator

(Operator instructions) We'll pause for just a moment to compile the Q&A roster. The first question will come from Glenn Schorr with Nomura.

Glenn Schorr – Nomura

Thanks very much. Point of clarification maybe, Ruth, on the other sales and trading loss. In your text, you talked about primarily it affecting funding costs and the liquidity held at the U.S. sub banks. Can you just give us a little more color on it, because it sounds like something that's been there all along, we just didn't know about it?

Ruth Porat

Well, first hello and welcome. The main components in the category, other sales and trading, do – have included corporate lending and relationship and leverage lending, credit spread impact on CIC, funding related costs, and a few other items.

This quarter – for the third quarter, the items were first, the amortization of the value of the de-designated hedges related to the 2008 debt buyback and retirement program – you may recall, we talked about that over several quarters, going back sometime; increased liquidity; the negative carry in the U.S. banks' portfolio as we build out the bank; a $71 million loss on credit spread tightening on our debt related to CIC's investment. And so the impact of mark-to-market P&L and corporate lending, which we had in prior quarters was not material this quarter.

Glenn Schorr – Nomura

Got you. So this – sounds like there is a ongoing cost there, like you said on liquidity and funding at the bank that is part of the ongoing operating, and in a steady-state world will be there. I just – am I thinking about that the right way? In other words, the $341 million this quarter had offsets in other quarters, maybe through leverage lending or something else, but just didn't have offset this quarter?

Ruth Porat

Right. Exactly. Leverage loans were muted this quarter, so we didn't have the offset. But you are right, you characterized it correctly.

Glenn Schorr – Nomura

Okay, cool. Moving on, just in terms of CIC franchise, I think people have had their expectation set on, it takes a while to build or rebuild a client franchise. But with VaR up a little bit and trading efficiency obviously down this quarter, I'm just curious, think – how much of that is – it takes time to build the client franchise versus a conscious decision to de-risk in a slow quarter versus are there legacy positions dragging? Just if you could help talk through some of that?

Ruth Porat

The primary issue is really the first one you articulated, which we have stressed for quite some time, which is we are still building the footprint and it takes time to realize the positive benefit of the investment.

So as we look at the quarter, in particular a slow July and August, what we saw were lower client volumes. We didn't have a lot of client activity and as a result, we didn't see as many trading opportunities coming out of the client flow. So while we didn't make a lot of money, we also didn't lose a lot of money, but it's very much in our view the first point that it takes time and we said this repeatedly, this is about quarters to build the position that we expect to have.

Glenn Schorr – Nomura

Cool. And then – I appreciate the commentary on the Basel III walk-through and risk-weighted assets. Could you help on the numeric side, or more importantly, where does that shake out at the end of 2012 in terms of steady-state ratio now, add in forward earnings, subtract out the changes on both mitigation, high-risk weightings, and the roll-forward?

Ruth Porat

So, what we were attempting to give is an analysis of RWAs and obviously, this is preliminary and there is still interpretation to come. Our Tier 1 common equity at September 30 is estimated to be approximately $35 billion. There are many items that can impact capital between now and 2013. So as I said, we are comfortable with our position, we are confident in meeting all the requirements of Basel 2.5 and III and wanted to give you the RWAs so you could do your roll-forward.

Glenn Schorr – Nomura

Understood. And last one, on Smith Barney, is that a contractual buy-in on May '12, '13, and '14 or do you have any optionality there?

Ruth Porat

That is an option.

Glenn Schorr – Nomura

That's option? Okay. So you have to make an assumption on whether or not you would exercise the option, because it's a big capital impart [ph].

James Gorman

It's an open-ended call option.

Glenn Schorr – Nomura

Got it – got it. Okay, cool. Thank you. Thanks, James.

Ruth Porat

Thank you.

Operator

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

Ruth Porat

Hello, Guy.

Guy Moszkowski – Bank of America

Good morning, Ruth. Good morning, James.

James Gorman

Hi, Guy.

Guy Moszkowski – Bank of America

We can see the impact of the capital coming in from CIC on your supplement Page 4, to the parent company. And I'm just wondering whether you intend to retain it there or whether you would look at allocating some of that down to the operating units, in particular the investment bank.

Ruth Porat

We retained it there, as we've talked about in prior quarters, with the assumption that it will be allocated over time as we have greater clarity on Basel 2.5, III, but that is precisely the intent.

Guy Moszkowski – Bank of America

Okay, thanks. And just to follow up on the Basel III question and your comments about RWA, can you give us any more detail on the type of mitigation actions that you would envision?

Ruth Porat

Sure. There are really two major categories. One is run-off, primarily the securitization book and correlation book. And the other is a more modest estimate of additional sales out of our merchant banking portfolio, hedge fund stakes, et cetera that will release capital and therefore RWA.

Guy Moszkowski – Bank of America

Right, which in a sense is mandated under Dodd-Frank anyway, right?

Ruth Porat

It is, although we like to underscore that it was strategically something we have been quite focused on even prior to Dodd-Frank and core to the way we are looking at where we want to take the business prospectively and very much a focus of Greg Fleming's since his arrival here.

James Gorman

We – actually Guy, we started this review probably 18 months ago to look at all the capital we have tied up in our principal investing businesses and the percent in each of the funds that we have, the seed capital that we have across our various asset management businesses, and obviously our ownership stake. So it's been a very long and thought-through process and we are right in the middle of executing on it now.

Guy Moszkowski – Bank of America

And that comment is sort of a good segue into a follow-up question on FrontPoint. Can you give us a little bit more of a sense for exactly what's happening there strategically, what drove that given that – my understanding there is that was really a customer investment business rather than tying up a lot of Morgan Stanley's capital. And finally, what – is there any further charge that we might anticipate in the fourth quarter beyond the goodwill impairment that you mentioned that took place this quarter?

James Gorman

On – FrontPoint was – firstly, I think it is challenging for institutions like us for lots of reasons, including conflict to own – fully own 100% of hedge funds. Secondly, we do have about $300 million of seed capital tied up in FrontPoint and we obviously have a plan to – it's sort of more than that [ph] – we have a plan to repatriate that over relatively short period of time.

And we just feel comfortable as a minority stakeholder with a different structure of compensating us as a minority holder, if you will, in terms of revenue share than we had as a 100% owner. So it has multiple benefits and it clarifies what we do and it clarifies what FrontPoint does and allows them to go about their business.

Guy Moszkowski – Bank of America

Got it, thanks. I just have one more question, which is on global wealth management. The largest single revenue item there is of course the asset management driven fees and they have been extremely consistent. Can you just give us a sense for what percent of those fees are actual – actually based on customer assets under control and to what extent there might be some variability beyond just what happens to markets?

James Gorman

Well, I'm on a roll here, so why don't I just continue? The asset management fees in that business are a mix obviously of the total assets in the various forms of asset management accounts, the discretionary accounts through to the fund-of-funds accounts, the managed money accounts, and the sort of priced fee accounts.

So they are a function of three things; one is the pricing-only accounts, two is the absolute asset volumes in the market, and three is the flow of new assets either from outside the firm or existing assets from within the firm that get moved into those accounts as clients prefer to pay by fee.

All of those three things have been positive in that business. It reflects a very strong Smith Barney leverage – legacy in this space, which is now being applied to the former Morgan Stanley Dean Witter business. And that's why we are seeing, I think, the increase in absolute asset levels and in revenues from it. And it's a good thing for the business.

Guy Moszkowski – Bank of America

Great. Thanks very much to both of you.

Ruth Porat

Thank you.

Operator

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

Ruth Porat

Good morning, Roger.

Roger Freeman – Barclays Capital

Good morning. I guess a couple of questions around your Basel III initial take here. I guess, one is with respect to mitigation, as you are thinking about the roll-offs, are you just looking at this as passive or is there – are there more sort of active tear-ups, et cetera that you are pursuing? And actually to that point, it sounds like your RWA at least on a gross basis is going up 75%. That's a lot lower than what your sort of prior – obviously pre-Basel III estimate was, and possibly a doubling a year ago. It seems like you've made a whole lot of progress here.

Ruth Porat

So, two things that – to your point, a preliminary estimate and we would rather plan for the worst and hope for the best, but the rules have continued to provide clarity and they are obviously still a bit preliminary. But we think that from what we have today, we feel comfortable that we are looking, as you said, about a 75% increase.

With respect to mitigation, we are looking at roll-offs, as I said, from the existing book. We assume that we will be able to do tear-ups as well. But we haven’t included that within the calculation. And again, this is a preliminary estimate. So wasn't in, I assume it will be in, do assume it's logical.

Roger Freeman – Barclays Capital

Do you still think that the central clearing ultimately will be a big benefit here as well? I think you had mentioned that last time we talked.

Ruth Porat

We assume it will. And again, there are added steps that we hope will continue to layer into the calculation over time. And that, to your point, would be one.

Roger Freeman – Barclays Capital

Okay. And just lastly, on that topic, do you anticipate running at some sort of a buffer above even whatever is systemic for the Fed is going to call for?

Ruth Porat

I think – again – we know the floor is 7% and there are various assumptions as to how much above that will be required as a systemically critical institution and the counter-cyclical buffer. So we want to see where those numbers come out and depending on where they come out, we will assess the appropriateness of buffer, any size of buffer.

Roger Freeman – Barclays Capital

Okay. And just one other thing. On your mark on Revel, can you just sort of help us think about that one a little bit? I know it's basically down to zero now. But was there something specific on that investment, given that commercial real estate prices were broadly flat in the quarter and also, you actually had gains in other real estate funds. So maybe it's a geography issue or –?

Ruth Porat

Well, when we decided to sell the business in earlier this year and we evaluated the most likely value to be received, we have a year in which to sell it. As we progress with discussions with buyers, our best assessment now with the benefit of more information is that we need – the value is lower and thus we are required to write down the carrying value by about $200 million. To your point, our current carrying value is now only about $40 million.

James Gorman

I'd just add to that, Roger. The valuation of that property is affected less by commercial real estate players and the valuations of the gaming industry and customer spend and traffic and so on, and specifically gaming industry in Atlantic City. This is, after all, a half-built casino in Atlantic City.

Roger Freeman – Barclays Capital

Yes, not a lot of value in that. Okay. Thanks a lot, both of you.

Ruth Porat

Yes.

Operator

The next question will come from Mike Mayo with CLSA.

Mike Mayo – CLSA

Good morning.

Ruth Porat

Hi, Mike.

Mike Mayo – CLSA

First, on the positive side, can you comment on what happened linked quarter in Asia? Looks like those revenues were up three-fourths.

Ruth Porat

Yes. So in the Asian business, we saw increases across a number of the businesses. Our advisory business was up 180%. You saw a lot of the headlines with strong equity underwriting, issuances, and IPOs. The equity markets did not see the kind of market volume declines that we saw in the U.S. and Europe and within the fixed income business, up 61% in IRCC, which was FX and credit corporate. So, real broad strength in Asia.

Mike Mayo – CLSA

And should we expect that level going forward or is that anything kind of temporary there?

Ruth Porat

From what we have seen, it continues to be strong. Whether we can expect anything of that magnitude, I would certainly not want to leave you with that assumption. But the pipeline is strong, in particular in China.

James Gorman

And longer term, strategically, Asia and China specifically have become much more important to Morgan Stanley, given our CIC relationship, our significant business in the Mainland and out of Hong Kong, and our business in other parts of – regional parts of Asia.

Mike Mayo – CLSA

And then separately, following up on Basel III, first, are you running your systems in parallel yet with Basel II?

Ruth Porat

Yes.

Mike Mayo – CLSA

How many quarters have you been running in parallel?

Ruth Porat

We entered parallel run on July 1.

Mike Mayo – CLSA

Okay. And then, I might have missed it. What is your Tier 1 common ratio under Basel III?

Ruth Porat

We – you didn't miss it. We actually – what we provided is the RWA – our best estimate, let me put it that way, at the RWA roll-forward and our best estimate at some of the run-off opportunities. Our Tier 1 common at September 30 was approximately $35 billion and there are a number of items that can affect capital between now and then. So we wanted to give you the RWA's to let you layer that in.

Mike Mayo – CLSA

So what we have to go with right now is $35 billion divided by $466 billion, with no other adjustments? But there could be some adjustments, I guess to the numerator.

Ruth Porat

Right. And – so it's $565 billion prior to any run-off, and then $465 billion.

Mike Mayo – CLSA

Okay. And can you give any rough sense of the impact to numerator? I guess that could go down some, the $35 billion, or are you – think that will be –?

Ruth Porat

No, that – I think that's all I'm prepared to say on that topic.

Mike Mayo – CLSA

Okay.

Ruth Porat

Thank you.

Mike Mayo – CLSA

All right, thanks a lot.

Ruth Porat

Thank you.

Operator

The next question will come from Howard Chen with Credit Suisse.

Howard Chen – Credit Suisse

Hi, good morning.

Ruth Porat

Good morning, Howard.

Howard Chen – Credit Suisse

James, I believe you noted at a recent conference your view that returns will restore back to the high-teens over time. I was just hoping you could expand upon that comment, and maybe frame what type of macro conditions and regulatory assumptions you broadly think about in achieving that goal.

James Gorman

Well, that's a large question, Howard, which I think we would have to have another conference to answer it accurately. Clearly, we have in our hand the ability to turn the dial up and down on the various businesses that we have.

And if we look across our businesses, historically, wealth management businesses have generated returns of up to 45% return on capital; asset management businesses have generated returns between 25% and 35%; core investment banking businesses, effectively infinity; and the sales and trading businesses, as you know, it depends which business and how much balance sheet you are using and with what risk and so on. And that's where you have dollar [ph] turning ability.

So as we think about the various pieces that make up Morgan Stanley, take into account obviously the risk-weighted asset changes, and as we extrapolate privately on what the numerator number that the previous, I think it was Roger or Mike was calling about, we clearly believe the industry and those that have survived the financial crisis and have consolidated positions are in a position, if well managed, to extract that kind of mid-high teen returns that we talked about.

So it's – obviously, our long-term desire is to meet and exceed our cost to capital and we have a lot of levers that we are working on.

Howard Chen – Credit Suisse

Great. That's helpful context. And I realize it's a big question. And then, just given the mortgage foreclosure concerns in the marketplace, I was just hoping to get your perspective on the legal climate and the liability in your view from your activities as an originator, service securitizer within the market.

Ruth Porat

So, I think it's obviously kind of a fluid topic. I think like other financial institutions, we have been named a defendant in cases in connection with CDOs and RMBS. And as you know, we don't comment on individual litigation unless we have concluded they are material to the firm or disclosures otherwise are required or meaningful.

So I think at this point, there is really no update that we have. We are obviously watching, but I would refer you to the legal proceedings section of our most recent filings.

Howard Chen – Credit Suisse

Okay, thanks. And then just I guess switching gears, Ruth, just where are we just broadly in the cost synergy realization on the global wealth management JV?

Ruth Porat

We are very much on track, continuing to execute on the integration.

Howard Chen – Credit Suisse

Okay. Is there a specific number of kind of where – what you have achieved out of the broader target?

Ruth Porat

We could probably piece together from the disclosure we have had today, we are about halfway through.

Howard Chen – Credit Suisse

Okay, many thanks. And then just last question on my end. Could we just get a brief update on the retail banking strategy? I know you noted, Ruth, kind of where the deposits lie, but I think you might have had a key departure from the business during the quarter, and I just wanted to know if there was any shift in how you broadly think about retail banking.

James Gorman

Yes, fair question. Let me take that one. We – a couple of years ago, when we hired, and the person you are talking about is CC Sutton, who is a terrific person and has gone to run part of Citigroup's retail banking network. She came out of that kind of job at Wachovia. When she joined us a couple of years ago, we were contemplating as in the world of turmoil and change in financial services of a potential roll-up strategy of different retail banking networks attaching them to our brokerage business.

Subsequent to that thinking, however, which was not particularly well formed – it was just opportunistic and we were exploring what was available in raising our deposit base. Subsequent to that thinking, we conducted the Smith Barney transaction, which has exposed us to obviously a much larger retail client base, nearly 1,000 offices domestically and a lot more deposits ultimately.

So, we had a change in strategy, which was to instead of buying banks with all the integration challenges associated with that, we decided to build effectively a shadow private bank by putting private bankers in each of our major complexes around the country.

And that process is well underway, it's generating significant loan particularly in deposit interest, and we expect it to be a very important part of our strategy going forward and it has a different compensable revenue structure than traditional equities and securities businesses. So it's well on track. We wish CC well, she's a great person. And the business remains on track and is of a different style and type than what we anticipated.

Howard Chen – Credit Suisse

Excellent. Thanks for the update on everything.

Ruth Porat

Thank you.

Operator

The next question will come from Michael Carrier with Deutsche Bank.

Michael Carrier – Deutsche Bank

Thanks. Ruth, just one follow-up on Basel. I think a lot of firms when they are giving these updates when they get more clarity, one is they are giving the adjusted or the new RWA number with some mitigation and roll-offs. And then just on the capital side, it's sort of flowing through, so you are looking at apples to apples on 2012.

So when we look at that $35 billion and we are looking forward, obviously we will all come up with our return on equity over the next year or two for you guys to generate. And I guess the other big piece would be just the MUFG in that conversion, and the price is obviously higher than where the current price is today. So I guess any update on that, and I guess at least from the regulators' perspective, is that demand for a convert, do you assume that that's already going to be in there or do you feel like you got to wait until it actually converts and it's into common for you guys to have more flexibility?

Ruth Porat

We – it is – the terms of conversion are obviously based on the stock price threshold, and we haven't assumed anything in here because this is actually a – as I said, a snapshot at 9/30, our capital position at 9/30, and so that's kind of one point. The second point, I think it was obvious, but when you started asking the question, I just wanted to make sure it is. With respect to the securitization framework and the deducts to capital, what we have done is convert this to an RWA equivalent. So that was just one piece I wanted to make sure was clear.

Michael Carrier – Deutsche Bank

Yes, I was just getting to the $35 billion is as of today, and just saying that if we assume that you have to have the ratios in place by 2012, is that $35 billion can grow into that RWA number.

Ruth Porat

Yes.

Michael Carrier – Deutsche Bank

Okay. And then just second, and I guess this is for James, just on the ROE question and I guess there's long term and maybe medium-term. I think if you look across the landscape, obviously it was a challenging quarter for most firms. And you guys are a little bit unique because, one is, I think you are still building out in certain areas where you might have had some relative strength during the quarter, and other firms were better positioned just because they already have a build-out.

And then there's other things that maybe just from a – particularly on the trading side, just either there were more severe hits or just from a risk management standpoint, maybe not as well positioned. I'm just trying to I guess gauge that, because if you look at the adjusted ROE of like a 4% versus some out there putting up like a 10%. Just trying to gauge, what is sort of very specific to the quarter versus over the next quarter or two, as long as the build-out takes place, do you still feel like you can get to a pretty decent or competitive ROE?

James Gorman

Well, there is a lot in that. Let me give you just a couple of reactions and I think your opening comment was the best one, which is that we take a long-term view. We certainly aren't going to measure our ROE over a summer month quarter where the world was trying to understand whether we would have a sovereign debt crisis in Europe and whether we would have a double-dip recession in the U.S., and whether China would be in for a hard landing. So, we have to take a longer-term view, as I'm sure and I know you understand.

We – listen, we think we have the right mix of businesses. Our business model is pretty straightforward. We spun off Discover, we spun off Van Kampen, we have now spun off FrontPoint, we spun off MSCI. We are focused on businesses that are involved in the origination, distribution, and management of capital. We have a lot of dials that I talked about earlier that we can turn.

But we are in a transition period. And we are focused on disciplined execution, not making mistakes, not creating drags unnecessarily on our business, but respecting the fact we have to invest in our platform, our distribution, and our flow businesses to get to the scale that gives us the ROE kind of numbers that I talked about earlier. And we are right in the middle of that investment now, whether it be Smith Barney, whether it be our fixed income cross rates, emerging markets, foreign exchange, particularly equity derivatives, you name it. We are making those investments, because we are planning for the long run.

Michael Carrier – Deutsche Bank

Okay. Thanks to both of you.

Ruth Porat

Thank you.

Operator

The final question will come from Mark Lane of William Blair.

Mark Lane – William Blair

Good morning. Just two quick ones. So in the global wealth management business, the last several quarters you have given us the non-recurring expense that's running through the income statement. What's that number this quarter?

Ruth Porat

That was $83 million this quarter.

Mark Lane – William Blair

Okay. And then I guess for James, on the fixed income trading side, so I acknowledge that it was a slow quarter from an activity perspective and you are still building, but how would you assess the quality of the quarter based on the people that you have right now? Was it an acceptable quarter from an execution perspective? Could you do a lot better with the people that you have? It's difficult to get a sense of how you feel, how you perform with what you have got.

James Gorman

Well, let me take a cut at it, and Ruth may want to add to it. Firstly, again, not to be silly about it, but quarters come around pretty quickly. In fact, they have an unnerving frequency of every 13 weeks, and this 13 weeks, we had a very, very difficult July on the flow side and the various positions we took, we had modest performance. It was a slow August, and it was a late Labor Day September.

So we are in a rebuild. We have hired, I believe, 70% of our target hires for this year. Most of those people came on board in the second quarter and the third quarter, and we expect them to be sort of fully productive by the first quarter of next year. It takes people with (inaudible) and all that sort of stuff, three, six months to get up and running.

So we feel pretty good about the footprint build-out. We are not exactly where we want to be, but we are a lot better off than we were 12 months ago. And it's going to – that takes a little time to root itself. We also put in place the senior relationship management program, which is covering our top institutional clients and that business is in – we have made some significant hires into that business. So we have made a lot of progress, but this is not a – this is not something that's going to happen with – in any 13-week period. We are just looking for progress.