Morgan Stanley

Morgan Stanley Europe SE

Annual Report 2023

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TABLE OF CONTENTS [1]

(1) Please note that the English version of the Annual Financial Statements and Management Report as at 31 December 2023 is a convenience translation. Deloitte GmbH Wirtschaftprüfungsgesellschaft, Frankfurt am Main, issued the Independent Auditors' Report only for the German version of the Financial Statements and the Management Report as at 31 December 2023. Therefore, the German version prevails.

MANAGEMENT REPORT

Company Overview

Morgan Stanley Europe SE, Frankfurt am Main (the "Company" or "MSESE") is part of the Morgan Stanley Europe Holding SE Group (the "Group" or the "MSEHSE Group").

The Company is Morgan Stanley's primary hub to facilitate European Union clients' ("EU27 clients") business. The Company's business strategy is closely integrated into the global strategy of Morgan Stanley's Institutional Securities Group ("ISG"). The Company's principal business units within ISG are the Institutional Equities Division ("IED"), the Fixed Income Division ("FID"), the Investment Banking Division ("IBD") and Global Capital Markets ("GCM").

In executing Morgan Stanley's ISG strategy, the Company is a key contributor in the following areas:

- sales, trading, financing and market-making activities in equity and fixed income products, including foreign exchange and commodities;
- financial advisory services, including advice on mergers, acquisitions and restructurings;
- investment activities; and
- capital raising.

The Company makes global products available to EU27 clients, and also provides EU27 products to global clients via other Morgan Stanley entities. Market making activities such as Euro interest rate swaps, European Union ("EU") government bonds, Euro inflation swaps, Covered Bonds, automated market-making of European equity stocks (for EU exchanges) are market risk managed by the Company. In alignment with its business strategy and regulatory expectations, in 2023, the Company increased its market risk management capabilities in certain EU products and plans to further expand its capabilities in 2024.

Corporate Structure

Morgan Stanley Europe Holding SE, Frankfurt am Main ("MSEHSE") is the parent company of the Company and authorised by the European Central Bank ("ECB") as a financial holding company in accordance with Section 2f (1) and (3) of the German Banking Act (Kreditwesengesetz or "KWG"). MSEHSE is a superordinated undertaking in accordance with Section 10a (2) of the KWG.

MSEHSE directly holds 100% of the shares in MSESE, which in turn directly holds 100% of the shares in Morgan Stanley Bank AG, Frankfurt am Main ("MSBAG"). MSESE operates branches in France, Italy, the Netherlands, Poland, Spain, Sweden and Denmark.

There are control agreements (*Beherrschungs-verträge)* in place between MSEHSE and MSESE and between MSESE and MSBAG which include loss compensations in accordance with Section 302 of the German Stock Corporation Act (*Aktiengesetz* or "AktG"). Letters of Comfort are provided by MSEHSE to benefit MSESE and MSBAG as well as by MSESE to benefit MSBAG. A Profit and Loss Transfer Agreement exists between MSESE and MSBAG. As a result, MSESE and MSBAG form an income tax group (*Ertragsteuerliche Organschaft*) in accordance with the Corporation Tax Act (*Körperschaftsteuergesetz*).

The Company's ultimate parent undertaking and controlling entity is Morgan Stanley, Delaware, United States of America ("US"). Morgan Stanley is a global financial services firm authorised as a Financial Holding Company and regulated by the Board of Governors of the Federal Reserve System in the US. All companies of the MSEHSE Group are fully integrated into the global Morgan Stanley Group (the "Morgan Stanley Group").

Supervision and Authorisations

The Company is subject to joint supervision by the ECB, the Federal Financial Supervisory Authority ("BaFin") and the Deutsche Bundesbank.

MSESE is conditionally registered with the Securities and Exchange Commission ("SEC") as a Securities Based Swap Dealer ("SBSD"). MSESE is complying with home country capital requirements in lieu of SEC capital requirements pursuant to applicable substituted compliance rules.

MSESE is also registered with the Commodity Futures Trading Commission ("CFTC") as a Swap Dealer.

MSESE is a Capital Requirements Regulation ("CRR") credit institution (Class 1 Investment Firm). MSESE is not authorised to provide either deposit taking services or lending.

Economic Report

Business Environment

The Management Report contains certain forward-looking statements. These statements are made by the Management Board in good faith, based on the information available at the time of the approval of this report and such statements should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying any such forward-looking information.

The market environment in aggregate for much of 2023 remained mixed, characterised by inflationary pressures and uncertainty regarding the future path of interest rates, which have remained high. Towards the end of the year, the market environment has improved somewhat with the expectation of lower interest rates into 2024. However, there remains uncertainty regarding the timing and pace of the rate reductions along with concerns regarding heightened geopolitical risks that could impact capital markets in 2024. This environment has impacted the performance of the Group and the Company. Despite the challenging market conditions, the Company's performance remained solid in 2023 although reported profitability was below forecast expectations. To the extent that the business environment continues to remain uncertain it could further adversely impact client confidence and related activity.

Global Markets and Economic Conditions

Growth in global Gross Domestic Product ("GDP") has weakened in 2023. Throughout the year, the main macroeconomic factors that have weighed on growth globally have been the restrictive monetary policy introduced by central banks to curb the record-high inflation and a reversal of the manufacturing cycle after its strong rebound post-pandemic. The euro area economy saw subdued growth, with considerable heterogeneity across countries. Weak global trade, consequences of energy supply shocks, and restrictive monetary policy have all been a drag on growth in the euro area.

The policy mix in 2023 has been a continuation of the one of late 2022. Fiscal policy measures in the euro area remained accommodative as governments spent generously on energy-related measures. The monetary policy tightening accelerated in 2023, with the ECB entering into restrictive territory. Further tightening was seen across other regions as well, as central banks tried to bring inflation back to target and avoid inflation expectations getting entrenched at elevated levels.

In the euro area, the ECB ended reinvestments under its Asset Purchase Programme in June 2023. The ECB kept raising rates until September 2023, reaching a deposit facility rate of 4.0%. Fiscal deficits in 2023 are expected to remain above 3%, reaching (an estimated) 3.3% of euro area GDP. Euro area inflation reached 5.5% in 2023, driven by increasing core inflation. After a peak at 10.6% in October 2022 headline inflation declined rapidly throughout the year to 2.9% in December 2023.

War in the Middle East

The Company continues to monitor the war and increased tensions in the Middle East and its impact on the regional economy, as well as on other world economies and the financial markets.

Net Assets, Financial Position and Results of Operations

The MSEHSE Group`s regulatory reporting and internal management reporting are both based upon International Financial Reporting Standards ("IFRS"). The Company is also principally managed using IFRS.

A reconciliation of profit after tax and balance sheet of MSEHSE Group under IFRS to profit after tax and balance sheet of MSESE under the German Commercial Code (Handelsgesetzbuch or "HGB") is shown below. Subsequently, the income statement and balance sheet of MSESE according to HGB is shown along with supporting commentary.

Reconciliation from IFRS to HGB

The following table summarises profit after tax and balance sheet size under IFRS for the MSEHSE Group and also for MSESE.

€ in millions		Profit after tax	Balance Sheet
MSEHSE Group	2023	187	106,711
	2022	142	118,977
Thereof:			
MSESE	2023	186	105,778
	2022	133	117,588

The following table provides a reconciliation from IFRS to HGB of the profit after tax of the Company for the years 2023 and 2022:

€ in millions	2023	2022
PROFIT AFTER TAX (IFRS)	**186**	**133**
Risk valuation adjustment according to section 340e (3) and (4) HGB	(51)	(37)
Adjustments for AT1 capital instruments within equity capital	(48)	(43)
Decrease of deferred tax assets	11	–
Valuation adjustments for pensions and similar obligations	(1)	3
Goodwill depreciation	(5)	(8)
Write downs of goodwill from transfer of Real Assets business	–	(20)
Others	(8)	14
PROFIT AFTER TAX (HGB)	**84**	**42**

The following table provides a reconciliation of the Company's balance sheet from IFRS to HGB for the years 2023 and 2022:

€ in millions	2023	2022
BALANCE SHEET (IFRS)	**105,778**	**117,588**
Derivatives and related cash collateral netting	(42,683)	(44,709)
Secured financing netting	(2,438)	(4,578)
Others	(147)	613
BALANCE SHEET (HGB)	**60,510**	**68,914**

Income Statement

Set out below is an overview of the financial results according to HGB for the years 2023 and 2022.

€ in millions	2023	2022	Increase/ (decrease)	Variance %
Sales and trading	643	495	148	30%
Investment banking	96	125	(29)	(23%)
Other	68	31	37	119 %
Net revenues	**807**	**651**	**156**	**24%**
Staff related expenses	293	251	42	17%
Non-staff related expenses	370	335	35	10%
Operating expenses	**663**	**586**	**77**	**13%**
Profit before tax	**144**	**65**	**79**	**122%**
Extraordinary income	–	37	(37)	(100)%
Income taxes	60	60	–	–%
Profit after tax	**84**	**42**	**42**	**100%**

Net Revenues

Sales and trading
Sales and trading income is comprised of commission and trading income. Commission income arises from arrangements in which the client is charged commission for executing and clearing transactions related to securities and other listed products. Trading income is largely derived from client activity and was affected by a variety of interrelated factors, including market volumes, bid-offer spreads and the impact of market conditions on inventory held to facilitate client activity.

Although sales and trading revenues in 2023 increased compared to 2022 as the business benefited from higher interest rates and increased market risk management, the performance remained below forecast expectations.

Investment banking
Investment banking fee income is derived from client engagements in which the Company acts as an advisor in relation to mergers and acquisitions, divestitures and corporate

restructurings, underwriter of equity and fixed income securities or distributor of capital.

Investment banking revenues in 2023 decreased compared to 2022, reflecting lower advisory revenues driven by fewer completed M&A transactions in the Morgan Stanley Group on lower market volumes.

Other

Other revenues include €121 million of revenues recognised from the Profit and Loss Transfer agreement with MSBAG. The result of the ordinary operating activities of MSBAG for the financial year ending 31 December 2023 was transferred to the Company in full. Refer to the section “Corporate Structure” for further details.

Operating Expenses

Staff related expenses

Staff related expenses include: base salaries and fixed allowances, discretionary incentive compensation, amortisation of deferred cash and equity awards and other items including health and welfare benefits.

Staff related expenses increased in 2023 compared to 2022. This was driven by higher salary expenses and severance costs primarily associated with the employee action recorded in the second quarter of 2023.

Non-staff related expenses

Non-staff related expenses include brokerage fees, administration and corporate services, professional services, transaction taxes and management charges from other Morgan Stanley Group undertakings relating to other services. Non-staff related expenses increased in 2023 compared to 2022, reflecting an increase in transaction-related expenses, including brokerage and transaction taxes, and increased management charges from other Morgan Stanley Group undertakings.

Extraordinary income

Extraordinary income of €37 million in 2022 reflected gains recognised from the sale of the Real Assets business unit.

Income Taxes

The Company’s income taxes for the period are €60 million. The main driver for the lower effective tax rate in 2023 is the geographic mix of profits and tax rates in jurisdictions outside Germany.

Balance Sheet

€ in millions	2023	2022	Increase/ (decrease)	Variance %
ASSETS				
Cash	327	–	327	>100%
Receivables from credit institutions and customers	17,630	32,320	(14,690)	(45%)
Trading assets	41,462	35,486	5,976	17%
Investments in affiliated companies	603	603	–	–%
Other assets	488	505	(17)	(3%)
TOTAL ASSETS	**60,510**	**68,914**	**(8,404)**	**(12%)**
LIABILITIES				
Liabilities to credit institutions and customers	14,990	28,063	(13,073)	(47%)
Trading liabilities	34,582	33,448	1,134	3%
Subordinated debt	3,511	1,006	2,505	249%
Instruments for Additional Tier 1 Regulatory Capital	1,000	1,000	–	–%
Debt securities	92	0	92	>100%
Provisions	155	157	(2)	(1%)
Other liabilities	121	316	(195)	(62%)
Fund for general banking risks	77	26	51	196%
TOTAL LIABILITIES	**54,528**	**64,016**	**(9,488)**	**(15%)**
EQUITY				
TOTAL EQUITY	**5,982**	**4,898**	**1,084**	**22%**
TOTAL LIABILITIES AND EQUITY	**60,510**	**68,914**	**(8,404)**	**(12%)**

Cash

The increase compared with the prior year is driven by cash placed on demand with the Deutsche Bundesbank.

Receivables from and liabilities to credit institutions and customers

Receivables from and liabilities to credit institutions and customers decreased compared to the prior year. This was primarily driven by a decrease in cash collateral pledged and received in relation to derivative transactions and a reduction in overnight cash deposits received from MSBAG and placed at the Deutsche Bundesbank.

Trading portfolio

Trading assets and trading liabilities increased compared with the prior year. These increases were driven by an increase in European government bond inventory as well as increases in the value of securities financing transactions.

Investments in affiliated companies
Investments in affiliated companies all relate to shares held in MSBAG.

Other assets
Other assets mainly consist of variation margin posted to central counterparties and the receivable in relation to revenues recognised from the Profit and Loss Transfer agreement with MSBAG.

Subordinated debt
The increase compared to the prior year is driven by the issuance of senior subordinated debt to MSEHSE.

Debt securities
The increase in the year is driven by the Company issuing structured notes to non-affiliated companies.

Provisions
Provisions primarily consist of variable, deferred and share-based compensation, pension obligations and tax provisions.

Other liabilities
The decrease compared to the prior year is mainly driven by a reduction in the balance of variation margin received in relation to listed derivative transactions.

Fund for general banking risks
The fund for general banking risks, as prescribed within section 340e (4) HGB, increased from €26 million in 2022 to €77 million in 2023 in line with the increase in net trading income in 2023.

Capital Structure
The equity presented in the balance sheet consists of share capital, capital and earnings reserves and retained earnings. The increase in equity in the year from €4,898 million to €5,982 million is mainly due to a capital contribution in cash of €1,000 million from MSEHSE to MSESE.

In 2023, the return on investment pursuant to Section 26a (1) Sentence 4 KWG is positive 0.14% (2022: positive 0.06%).

Capital Management

The Group actively manages and monitors its capital in line with established policies and procedures and in compliance with local regulatory requirements.

Effective 1 January 2023, MSESE has been granted a Capital waiver in accordance with Article 9 of the CRR, allowing its capital requirements to be met on an individual consolidated basis (MSESE incorporating its subsidiary MSBAG, "MSESE Consol"). MSBAG has been granted a Capital waiver in accordance with Article 7 of the CRR and therefore its capital requirements are met at the MSESE Consol level. Capital requirements are managed at both the MSEHSE Group level and at the MSESE Consol level.

Consistent with the Morgan Stanley Group's capital management policies, the Group manages its capital position based upon, among other things, business opportunities, risks, capital availability and rates of return together with internal capital policies, regulatory requirements and rating agency guidelines.

Regulatory Capital

The Group is subject to minimum capital requirements as calculated in accordance with the CRR and the Capital Requirements Directive (Directive 2013/36/EU or "CRD") as transposed into German Law.

The Group conducts an Internal Capital Adequacy Assessment Process ("ICAAP") at least quarterly in order to meet its obligations under CRD and the requirements of the ECB. The ICAAP is a key information tool for the Group Management Boards to approve capital adequacy targets and limits, establish ongoing monitoring processes and internal thresholds, and review identified risks in line with the business strategy. Refer to the section "Risk Report" for further information on the ICAAP.

Liquidity and Funding Management

The primary goal of the Group's liquidity and funding management framework is to ensure that the Group has sufficient liquidity to cover its business operations and regulatory requirements, as well as access to adequate funding across a wide range of market conditions and time horizons. It manages resources mainly based on business opportunities, risks, availability and rates of return, which are driven by internal policies, regulatory requirements and rating agency guidelines.

MSESE and MSBAG have been granted a waiver in accordance with Article 8 of the CRR which permits liquidity requirements to be managed at the MSESE Consol level for MSESE and its subsidiary MSBAG as a sub-group. In addition to the MSESE Consol level, capital and liquidity requirements must also be managed at the MSEHSE Group level.

Liquidity Resources, Funding and Balance Sheet Management

The Group maintains sufficient liquidity resources to comply with internal liquidity stress testing and regulatory requirements. The total amount of Liquidity Resources is actively managed by the Group considering the following components:

- balance sheet size and composition;
- funding needs in a stressed environment inclusive of contingent cash outflows;
- collateral requirements; and
- regulatory requirements.

The amount of Liquidity Resources held is based on the Group's risk tolerance and is subject to change dependent on market and Group-specific events.

The Liquidity Resources consist of cash at central banks and high-quality unencumbered assets. Eligible unencumbered highly liquid securities include primarily Level 1 (as defined in the Commission Delegated Regulation (EU) 2015/61) government bonds and German sub-sovereign obligations.

Refer to the section "Risk Report" for further information on the Liquidity Risk framework, Liquidity framework and Liquidity Stress Tests.

Credit Ratings

The cost and availability of financing and cash collateral are impacted by the credit ratings of the Company, among other variables. In addition, credit ratings can impact trading revenues, particularly in those businesses where longer-term counterparty performance is a key consideration, such as certain over the counter ("OTC") derivative transactions. When determining credit ratings, rating agencies consider both company-specific and industry-wide factors. The Company's senior unsecured ratings are provided in the section "Non-financial key performance indicators".

Recovery and Resolution Planning ("RRP")

The Group prepares a recovery plan which identifies mitigation tools available to the Group in times of severe stress. The recovery plan is updated on an annual basis and submitted to the ECB.

In terms of resolution planning, the Single Resolution Board ("SRB") as well as the BaFin as the national resolution authority are the responsible authorities for the Group. The Group produces information for the aforementioned authorities in the form of resolution reporting templates and ad-hoc regulatory submissions, in accordance with the EU statutory and regulatory requirements.

The Morgan Stanley Group has developed a resolution plan in accordance with the requirements of Section 165(d) of Title I of the Dodd-Frank Wall Street Reform and Consumer Protection Act and its implementing regulations adopted by the Federal Reserve Board and the Federal Deposit Insurance Corporation. The resolution plan presents the Morgan Stanley Group's strategy for resolution of the Morgan Stanley Group upon material financial distress or failure. Both MSESE and MSBAG are considered Material Operating Entities of the Morgan Stanley Group and are within the scope of the resolution strategy adopted by the Morgan Stanley Group.

Minimum Requirement for own funds and Eligible Liabilities ("MREL") and Total Loss Absorbing Capacity ("TLAC")

MREL serves to ensure that the Group has sufficient eligible liabilities in a resolution scenario to absorb losses and safeguard existing capital requirements. The BaFin, as the Group's national supervisor, shares the responsibility to determine MREL requirements with the SRB. The Group is subject to internal MREL requirements. MSESE Consol is also subject to MREL requirements from 1 January 2024.

With a similar objective, TLAC requirements serve to ensure that the Group has sufficient resources to absorb losses. TLAC is applied only at the Group level.

In 2023, the Company issued senior subordinated debt funding to MSEHSE in the amount of €2,500 million in order to meet its MREL requirements.

Financial and Non-financial Key Performance Indicators

The financial and non-financial key performance indicators ("KPIs") are managed on the MSEHSE Group level and based on IFRS. They are also applicable for the Company.

The financial and non-financial KPIs of the Group are aligned to its objective to further expand its business activities and strengthen performance, soundness and sustainability of the business considering regulatory requirements. To assess the effectiveness of the execution of the Group's strategy, a broad range of KPIs were set by the Group Management Boards. These are assessed on a quarterly basis and include the following.

Financial Key Performance Indicators

The major financial KPIs used to assess the performance of the Group include Profit before Tax ("PBT"), Return on Equity ("ROE"), Efficiency Ratio, Tier 1 Capital Ratio, Liquidity Coverage Ratio ("LCR") and Net Stable Funding Ratio ("NSFR").

ROE represents profit for the year in relation to year-to-date average equity.

Efficiency Ratio, defined as operating expenses as a percentage of net revenues, measures the Group's year-to-date operating performance.

Tier 1 Capital Ratio is the sum of CET1 and AT1 capital of the Group expressed as a percentage of the total RWAs.

LCR measures the extent to which liquidity outflows less liquidity inflows in stressed conditions are covered by high quality liquid assets.

NSFR is defined as the amount of available stable funding relative to the amount of required stable funding, both calculated using factors, which reflect the liquidity characteristics of each category of instruments according to the supervisory assumptions.

The Group's financial KPIs at the years ended 31 December 2023 and 31 December 2022 are as follows:

	2023	2022
PBT (€ millions)	265	236
ROE	2.6%	2.6%
Efficiency Ratio	75%	75%
Tier 1 Capital Ratio	26.2%	21.9%
LCR	151%	145%
NSFR	213%	194%

Forecast expectations for financial KPIs in 2023 were disclosed in the 2022 Management Report. Actual year on year performance versus those expectations are summarised below. Refer to the section "Opportunities and Outlook" for forecast expectations in 2024.

The increase in PBT was less than forecast, as a result of lower underwriting revenues.

ROE remained flat year on year at 2.6%. This is in line with expectations. PBT was lower than forecast, however this was offset by a lower effective tax rate and lower than forecast capital increase.

Efficiency Ratio remained at 75%. The Group had expected a moderate decrease in Efficiency Ratio due to expected growth in business. The actual performance was lower than expected mainly driven by lower revenue growth.

Tier 1 Capital Ratio and increased from 21.9% to 26.2%. The Group had expected a moderate decrease in the ratio. The increase in ratio reflected lower than expected growth in RWAs.

The increase in LCR was less than forecast as a result of lower inflows.The LCR remained significantly above the minimum regulatory requirement of 100%.

NSFR increased from 194% to 213% as at 31 December 2023. The Group had expected a moderate decrease. The increase which was observed was as a result of a lower required stable funding than forecast..

Non-financial Key Performance Indicators

Credit Rating

The credit ratings of the Company were stable and have not changed throughout the financial year.

		2023	2022
Moody's Investor Service, Inc ("Moody's")	Short Term	P-1	P-1
	Long Term	Aa3	Aa3
	Outlook	Stable	Stable
Standard & Poor's Rating Service ("S&P")	Short Term	A-1	A-1
	Long Term	A+	A+
	Outlook	Stable	Stable

In February 2024, Fitch Ratings assigned a Long-Term Issuer Default Rating (IDR) of 'AA-' and a Short-Term IDR of 'F1+' to MSESE. The Rating Outlook is Stable.

Risk Report

During 2023, the Group's Risk Division continued to focus on enhancing the Group's Risk Management Framework and on regulatory engagements. Key areas of focus included:

- evolution of the Risk Management Framework to support business expansion;
- management of risks primarily from volatility in interest rates markets within the Group's Risk Appetite;
- further incorporation of climate risk in the Risk Management Framework; and
- regulatory approvals for the use of advanced capital models.

Risk Management Framework

Risk taking is an inherent part of the Group's business activities and effective risk management is vital to the success of the Group.

Consistent with the waivers granted to the entities of the Group, and as described in the "Capital Management" and "Liquidity and Funding Management" sections, the MSEHSE Group's Risk Management Framework has been established at the MSESE Consol and MSEHSE Group levels, encompassing the risk management culture, risk governance, approach and practices that support risk identification, measurement, monitoring, escalation and decision-making processes. The Risk Management Framework is consistent between MSESE Consol and MSEHSE Group. Given the group structure, the risk, capital and liquidity profile of MSESE Consol largely reflects the risk profile of MSEHSE Group.

The Group's Risk Management culture is rooted in the following key principles: integrity, comprehensiveness, independence, accountability and transparency. The MSEHSE Group Management Boards are responsible for overseeing the adoption of the Morgan Stanley Group's risk culture.

The MSEHSE Group Management Boards have established a Risk Management Framework, including a Committee Structure and a "Three Lines of Defence" framework. The framework creates a clear delineation of responsibilities between risk owners and independent risk control functions with a view to addressing potential conflicts of interest. The structure applies to all legal entities and branches within the Group. The functions responsible for carrying out the activities across the Three Lines of Defence are summarised below:

- First Line of Defence: Business Units are responsible for managing their strategy and business activities in accordance with the Group's Risk Strategy and Risk Appetite. This includes the consideration of risks arising from climate change and environmental degradation. Support functions are independent of the Business Units and support strategy execution of the Group's revenue-generating activities.
- Second Line of Defence: Responsible for independent identification, analysis, reporting, management and escalation of risks arising from the Group's activities, including the risks arising from climate change and environmental degradation. It further sets policies and monitors adherence with these policies. This includes (but is not limited to) the below:
  - The Risk Division is responsible for the independent identification, measurement, monitoring and reporting of credit, market, liquidity and model risk arising from the Group's business activities. It reports to the Chief Risk Officer ("CRO"), who is also a member of the MSEHSE Group Management Boards.
  - The Operational Risk Department ("ORD") provides independent oversight of Operational Risk and assesses, measures and monitors Operational Risk against tolerances. ORD works with the divisions and control groups to help ensure a transparent, consistent and comprehensive framework for managing Operational Risk within each area and across the Group.
  - The Compliance Department maintains an enterprise-wide Compliance Risk Management Programme and is responsible for the design and development of the overall Conduct Risk Framework of the Group. The

Compliance Department is independent of the business units and reports directly to the MSEHSE Group Management Boards.

- The Global Financial Crimes Department is responsible for the Financial Crimes Risk Management Framework covering money laundering as well as fraud and other relevant criminal offences. The department acts independently from the business units, reporting directly to the MSEHSE Group Management Boards.
- The Compliance Department, the Global Financial Crimes Department and ORD form the Non-Financial Risk ("NFR") organisation.
- The Group's Central Outsourcing Control Office ("COCO") is independent of individual business divisions and is responsible for ensuring the proper execution of outsourcing frameworks and guidelines, working closely with divisional management accountable for supervising any outsourcings by their division to ensure outsourcing regulatory requirements are maintained on a continuous basis.

- Third Line of Defence: The Internal Audit Department ("IAD") is independent of the First and Second Lines of Defence. The IAD provides an independent assessment of the Group's control environment and risk management processes and further reviews and tests the Group's compliance with internal guidelines set for risk management and risk monitoring, as well as external rules and regulations governing the Group.

Morgan Stanley Group has several well-established policies and procedures which set out the standards that govern the identification, measurement, monitoring, management and reporting of the various types of risk involved in its business activities. The MSEHSE Group has implemented specific risk management policies to address local business and regulatory requirements, where appropriate. These policies are approved by the MSEHSE Group Management Boards, as required, and reviewed at least annually.

Committee Governance

The MSEHSE Group Management Boards are responsible for the establishment, implementation and oversight of an effective Risk Management Framework. Therefore, the MSEHSE Group Management Boards have established a committee structure for the governance of material risks. This includes the cross-divisional MSEHSE Group Executive Risk Committee and MSESE Executive Risk Committee ("ERCs"), which are chaired by the CRO and assist the MSEHSE Group Management Boards in the oversight of the Group's management of risk (including financial and non-financial risks). The Committees are responsible for overseeing:

(i) the development and implementation of a risk strategy, including the risk appetite statement;

(ii) risk identification and measurement;

(iii) risk framework and policies;

(iv) risk culture;

(v) financial resource management and capital; and

(vi) assessment of recovery and/or resolution limits.

The ERCs have established a series of sub-committees with dedicated responsibilities for particular risk matters directly reporting to the ERCs. The following provides an overview of these sub-committees:

- MSESE Credit Risk Committee: Reviews, approves and recommends actions on matters related to Credit Risk Management ("CRM") as well as provides oversight of policies, procedures and frameworks.
- MSESE Market Risk Committee: Provides oversight of the risk profile, control and governance framework on matters related to the Market Risk Department ("MRD") as well as provides oversight of policies, procedures and frameworks.
- MSEHSE Group Operational Risk Oversight Committee and MSESE Operational Risk Oversight Committee: Assist the ERCs to discharge its responsibilities in relation to Operational Risk.

- MSEHSE Group Stress Testing Committee and MSESE Stress Testing Committee: Review all aspects of the MSEHSE Group and MSESE Stress Testing Framework.
- MSEHSE Group Model Oversight Committee and MSESE Model Oversight Committee ("MOCs"): Provide MSEHSE Group and MSESE with oversight of the development, validation, performance and management of the Market, Credit, Operational, Liquidity Risk and Stress Testing models.
- MSEHSE Group Data Governance Forum: Reviews and monitors MSEHSE Group impacting data quality issues, reviews consolidated data quality reporting and data quality KPIs for the MSEHSE Group risk reports and assists in the oversight and management of MSESE Group impacting data initiatives.

In addition to the Committees directly reporting to the ERCs outlined above, the MSEHSE Group Risk Governance Committee ("RGC") provides the CRO with oversight of the control framework within the Risk Division and the MSEHSE Group Risk Capital Committee ("RCC") provides the CRO with oversight of the calculations under advanced capital models for the Normative Perspective and the capital assessment under the Economic Perspective.

Furthermore, the MSEHSE Group Asset and Liability Committee and MSESE Asset and Liability Committee assist the MSEHSE Group Management Boards in the oversight of the capital adequacy, funding and liquidity risk management.

Risk Identification, Risk Appetite and Risk Limits/Tolerances

Risk Identification

The Group has established a framework to identify and assess material risks and risk factors stemming from the Group's business activities. The materiality of risks is assessed quarterly on a quantitative and qualitative basis, using risk specific stress tests where possible. In addition, other risk management processes such as regular risk reviews, horizon scanning and ad-hoc stress tests are conducted to assess impacts of potential market events and regulations and thereby support the continuous process of risk identification. Material risks identified through these processes inform the design of key risk and capital management processes, including the Group's Risk Strategy and Risk Appetite Statement, individual risk management frameworks, macroeconomic stress testing scenarios, as well as the Group's Internal Capital and Liquidity Adequacy Assessment Processes ("ICAAP" / "ILAAP").

The following risk types involved in the Group's business activities were assessed as material as determined through the Group's Risk Identification Framework.

- Credit Risk;
- Market Risk;
- Liquidity Risk;
- Operational Risk;
- Model Risk;
- Conduct Risk;
- Compliance Risk;
- Leverage Risk;
- Valuation Risk;
- Earnings at Risk / Strategic Risk;
- Reputational Risk.

For information on the incorporation of climate and environmental risks into the Risk Management Framework, refer to the section "Climate and Environmental Risk Management".

The MSEHSE Group Management Boards have established frameworks to identify, analyse, monitor, mitigate and report these risks. Information on how these risks are managed is summarised in the respective sections of this Risk Report.

Risk Appetite

The MSEHSE Group Management Boards determine the Risk Strategy of the Group consistent with the business strategy and the risks stemming from it. The Risk Strategy sets the framework for how risks will be identified, measured, monitored and reported.

The centrepiece of the Risk Strategy are the Risk Appetite Statements for MSEHSE Group and MSESE Consol ("RAS"), which articulate the aggregate level and type of risk that the Group entities are willing to accept in executing the business strategy while protecting the capital and liquidity resources. The RAS consist of both qualitative and quantitative statements.

To remain adequate in a changing environment, the RAS and the underlying limits and tolerance frameworks are reviewed by the MSEHSE Group Management Boards when required (e.g., when the business strategy is amended by the Management Boards), but at least annually. This review takes into account changes in the Group's business strategy, financial resources and plans as well as any anticipated changes in risk appetite.

Risk Limits / Tolerances

The Risk Appetite of the MSEHSE Group and MSESE Consol is translated into a comprehensive set of risk limits and risk tolerances across credit risk, market risk, operational risk and liquidity risk, each at different granularity levels to manage risk taking in line with the MSEHSE Group's and MSESE Consol's Risk Appetite.

The Group's aggregate Risk Appetite for Market and Credit Risk is expressed as a percentage of Total Capital Resources. It is operationalised through the Macroeconomic Stress Loss Limit ("MSLL") and monitored through a suite of severe, but plausible Macroeconomic Scenarios, designed to capture key portfolio vulnerabilities of the Group. The credit and market risk limits are calibrated to reflect the MSEHSE Group's and MSESE Consol's Market and Credit Risk Appetite. As at 31 December 2023, the stress loss in the Group's binding macroeconomic stress scenario was €238 million.

Stress Testing

Stress testing provides a flexible approach to understanding the aggregate risk for the Group and assessing the Group's resilience to different scenarios over a range of severities. At a more granular level, stress tests provide detailed insights of potential areas of weakness in portfolios at the business area and counterparty level, respectively. Stress testing is a key risk management tool for the Group, informing a number of processes and associated decisions and is performed in line with internal and external regulatory requirements. The Group conducts both cross-risk stress tests and risk specific stress tests with the following objectives:

- Risk Identification: Identification of material risk concentrations and vulnerabilities in adverse scenarios;
- Risk Aggregation: Estimation of aggregate size of exposure and losses in adverse shocks;
- Risk Management: Management of tail risks or vulnerabilities against risk appetite;
- Capital and Liquidity Management: Informing capital and liquidity risk assessment processes and plans (ICAAP, ILAAP, Recovery Plan);
- Regulatory Requirements: Meeting regulatory requirements.

Results are communicated to interested parties and committees, such as the ERCs, the MSEHSE Group Management Boards and the Group's Supervisory Boards and their Risk Committees on a regular basis.

Cross-risk Stress Tests

Cross-risk stress tests ensure that concentration risks are captured and measured across the material risks. Cross-risk stress tests can be classified into macroeconomic stress tests, reverse stress tests and topical stress tests.

Macroeconomic scenarios are the Group's primary stress testing tool to monitor, assess and manage the Group's vulnerability to downside risk. The Group runs a suite of macroeconomic stress test scenarios on a regular basis to measure its market and credit risk loss potential and monitor those against the MSLL. Each scenario is supported by a macroeconomic narrative, a detailed set of macroeconomic projections and instantaneous market shocks, and selected credit risk default rules as appropriate.

There are internal models in place to quantify stress losses for credit risk, market risk and risks from Derivative Valuation Adjustments ("xVA").

- Stress losses for credit risk are calculated as the sum of a portfolio loss (stressed expected loss) and an unexpected loss (concentration add-on supplemented with idiosyncratic default losses).
- Stress losses for market risk (including xVA) are computed by applying risk factor shocks across all asset classes, either using full revaluation or a combination of full revaluation and a sensitivities based approach.

The potential impact of climate-related risks on Credit and Market Risk is assessed through a specific transition risk/carbon repricing scenario and managed via the Climate Stress Loss Limit ("CSLL"). For more information refer to the section "Climate and Environmental Risk Management".

Existential threats to the Group's business model are captured through the Group's Reverse Stress Tests ("RST"). The scenarios used in RST are extreme and border-line plausible and are designed to test a pre-defined outcome (e.g., viability of the Group's business model). RST are used to inform capital and liquidity planning and are a key input for recovery planning.

Specific market events or portfolio vulnerabilities are assessed through Topical Stress Tests, such as scenarios related to the war and increased tensions in the Middle East, to evaluate a possible impact of "downside" scenarios on the Group's risk and resource profile.

Risk-specific Stress Tests

Risk-specific stress tests identify and measure vulnerabilities and concentrations that may arise in a particular risk area, country or industry. The Group conducts risk-specific stress tests for Operational Risk, Market Risk, Credit Risk and Liquidity Risk.

Risk Reporting

The Group has put in place a Risk Reporting Framework to monitor and report the Group's risk profile against set risk limits and tolerances, and to provide timely risk information and/or escalation to responsible limit owners, relevant Group governance forums and the MSEHSE Group Management Boards, as appropriate. The Group's Risk Reporting Framework covers all material risks, it identifies matters for escalation and decisions and highlights emerging risks, mitigating actions and other risk matters that are deemed significant to the Group's Risk Committees and/or the MSEHSE Group Management Boards.

The key purpose of risk reporting is to provide decision makers and risk managers with an accurate and timely representation of risk exposures, including risk concentrations, at the group level, across business lines and between legal entities. To provide this information, the Group generates various risk reports across individual risk functions, including Market, Credit, Operational, Liquidity and Model Risk, at different frequencies (e.g., daily, weekly).

In addition, the Group has established a set of principles for risk reports which are applied to risk reporting, such as the appropriate level of aggregation, balance between qualitative and quantitative information or implementation of controls to ensure reported information is complete and accurate. The Group's Data Quality ("DQ") monitoring and reporting processes are integrated into the Morgan Stanley Group's global DQ management processes. The data quality for risk-related data is reviewed through defined KPIs which are summarised in respective DQ Dashboards for certain risk areas such as Credit Risk, Market Risk and Liquidity Risk. At the Group level, any material data limitations/issues on risk data goes through governance and is escalated to the MSEHSE Group Management Boards if necessary.

Detailed information about the reporting for each risk type is included in the respective risk sections on the following pages.

Internal Capital Adequacy Assessment Process

The ICAAP is a key information tool for the MSEHSE Group Management Boards to plan the Group's capital actions, approve capital adequacy targets and limits, establish ongoing monitoring processes and internal thresholds and review identified risks in line with the business strategy. As such, the ICAAP is designed to ensure that all material risks, which the Group is exposed to, are appropriately capitalised. The ICAAP is updated at the beginning of each year in line with the annual strategic planning process as well as quarterly for material changes.

The ICAAP comprises of two capital assessment perspectives, the "Normative Perspective" and the "Economic Perspective". While methodologies differ in forecasting horizon and objectives, the two perspectives complement and inform each other.

Normative Perspective

The assessment under the Normative Perspective is conducted over a three-year planning horizon, assessing the Group's ability to fulfil all its capital-related supervisory requirements. It assesses the Group's capital adequacy under expected and stressed operating environments. It uses stress testing to size capital buffers aimed at ensuring the Group will continue to operate above regulatory requirements under a range of severe but plausible stress scenarios. The Normative Perspective takes into account all material risks affecting the relevant regulatory ratios, over the planning horizon. It is also used as a basis to set and review internal capital targets.

The Normative Perspective requires base and adverse scenarios to be assessed over the planning horizon. The Group's base scenario considers the main macroeconomic variables, including GDP growth, inflation rate changes, interest rates and currency market movements. These variables are applied on the business growth laid down in the Group's Business Strategy. In addition to the base forecast, the Group assesses its capital-related supervisory requirements in two macroeconomic stress scenarios. These scenarios comprehensively and conservatively measure the relevant risks for the Group.

To model stress capital impacts under the Normative Perspective, the Group uses internal models (refer to the "Stress Testing" section) that appropriately cover all material risk types.

Capital requirements are calculated in accordance with regulatory rules, taking into account the Group's permissions to use internal models. In addition to capital-related supervisory requirements, internal capital ratio minima are set to ensure the Group has sufficient capital to meet its regulatory requirements at all times.

Set out below are details of the Group's Capital Resources.

€ in millions	**2023**	**2022**
Normative Perspective		
CET1 Capital	6,136	5,069
AT1 Capital	1,000	1,000
Tier 1 Capital	7,136	6,069
Tier 2 Capital	1,000	1,000
Total Own Funds	**8,136**	**7,069**
Risk Weighted Assets ("RWAs")	27,283	27,760
CET1 Capital Ratio	22.5%	18.3%
Tier 1 Capital Ratio	26.2%	21.9%
Total Capital Ratio	**29.8%**	**25.5%**

The Group's Tier 1 Capital Ratio increased from 21.9% as at 31 December 2022 to 26.2% as at 31 December 2023 due to the capital actions totaling €1,000 million executed in 2023, primarily required to support the execution of the Business Strategy.

Additional information is presented in the "Capital Management" section.

Economic Perspective

In the Economic Perspective, the Group assesses its capital adequacy by ensuring that all material risks that could cause losses or have other material impacts on its capital position are quantified and adequately covered by its internal capital ("Risk Bearing Capacity" or "RBC"). In line with the ECB ICAAP guidelines, capital requirements are assessed using internal methodologies, which generally target a 99.9% loss severity over a time horizon of one year.

Credit Risk: For the calculation of credit risk capital requirements, the Group employs a multifactor credit concentration model, using internal credit risk parameters for Exposure at Default ("EAD"), Probability of Default ("PD") and Loss Given Default ("LGD"). The model simulates the asset returns of the individual counterparties in a correlated manner to capture the dependency between the defaults. The default triggers are derived from the PDs of the counterparties and internal downturn LGDs are used to quantify the default losses. Counterparty credit risk ("CCR") exposures are quantified using Morgan Stanley's global Internal Model Method ("IMM") model for the calculation of Own Funds Requirements, which has a wider product scope than the Group's IMM model. Default events are simulated using a Monte-Carlo model, and capital requirement is determined as the tail loss at a 99.9% confidence level.

Operational Risk: To calculate the capital requirements related to operational risk, the Group utilises an internal model. Under this model, operational risk capital is calculated for each of the Group's Risk Segments, some of which are designated as Top Operational Risks ("TORs") and Top Operational Risk Pathways ("TORPs"). Standalone capital is calculated for each of the Risk Segments by fitting parametric distributions to Scenario Analysis loss estimates. The aggregate loss distribution for the Group is derived from the marginal loss distributions of the Risk Segments. The 99.9% percentile of the final distribution is chosen as the loss estimate.

Market Risk: Market risk capital is primarily calculated using the Group's Economic Value-at-Risk ("EVaR") and Incremental Risk Charge ("IRC") models. The EVaR is calculated using historical simulation and includes xVA risk factors in its scope. The EVaR is derived as the 99.9% percentile of a loss distribution calculated using 15 years of historical returns. A six-month liquidity horizon is used for portfolios with low market depth or hedging ability (such as xVA), while a three-month liquidity horizon is applied to portfolios with higher market activity and ability to hedge, such as market making portfolios. Risks Not in VaR ("RNIV") capital add-ons are also used as a component to calculate market risk capital. The IRC is calculated at 99.9% confidence level over a one-year time horizon. Refer to the "Market Risk" section for more information.

Other risks under the Economic Perspective include: Interest Rate Risk in the Banking Book and Credit Spread Risk in the Banking Book ("IRRBB" and "CSRBB") as well as pension risk and valuation risk.

Capital requirements are conservatively aggregated without diversification benefits. Total internal capital requirements are then compared with available internal capital resources, i.e., the RBC. The RBC are taken at regulatory Own Funds (CET1 capital) with minor adjustments made to reflect other risks.

The Group aims to maintain an Economic Capital Adequacy Ratio (RBC divided by Economic Capital requirements) of at least 100%. Economic Capital Adequacy is assessed on a quarterly basis.

The table below presents a comparison of internal capital (RBC) and economic capital requirements for year-end 2022 and 2023.

€ in millions	**2023**	**2022**
Economic Perspective		
Risk Bearing Capacity	**6,184**	**5,053**
Capital Requirements	**3,211**	**2,870**
Credit risk	2,038	1,929
Market risk	352	279
Operational risk	609	535
Other	212	127

As at 31 December 2023, the Group was adequately capitalised and reported an economic capital adequacy ratio of 193% (2022: 176%).

Under the Economic Perspective, the Group has performed stress testing to understand sensitivities of the capital assessment to severe, but plausible macroeconomic stress scenarios. At the time of assessment, the Group remains well capitalised under these stress scenarios.

Credit Risk

Credit Risk is an inherent part of the Group's business activities. Credit Risk refers to the risk of loss arising when an obligor, i.e. a borrower, counterparty or issuer, does not meet its financial obligations. Credit Risk includes country risk – i.e., the risk that economic, social and political conditions and events in a country will adversely affect a client's[1] ability and/or willingness to fulfil its obligations. As part of credit risk, credit concentration risk refers to the risk of loss due to an outsized exposure to a client or a group of connected counterparties in the same industry or geographic region. The assessment of credit risk also considers climate risk, in particular the credit exposure to obligors and counterparties highly vulnerable to transition and/or physical climate risks. Respective definitions and further information are disclosed in the section "Climate and Environmental Risk Management".

The CRM Department reports to the CRO and is independent from the business units. It is responsible for managing and overseeing the credit risk profile of the Group. CRM has put in place a Risk Management Framework to identify, measure, control and report credit risks. Key components of the Credit Risk Framework include:

(1) Risk Identification: The identification and assessment of credit risks forms an integral part of CRM and is performed on an ongoing, continuous basis. To identify and assess credit risks, CRM uses ongoing monitoring of clients' credit quality, the utilisation of credit limits, credit risk concentrations and single factor as well as multi-factor stress results. Additionally, the New Product Approval ("NPA") process is leveraged to identify and assess credit risks arising from new activities.

(2) Risk Measurement: The measurement of credit risks primarily comprises of the analysis of clients' credit quality and credit

[1] Client refers to a borrower, counterparty or issuer in this context.

risk exposures generated from transactions.

The analysis of obligors' credit quality results in the assignment of internal credit ratings which reflect the obligor's likelihood of default and are subject to credit officer review and approval. As part of this internal rating process, each rating is linked to a single name credit limit and mapped to a specific PD. The Group has developed industry specific rating templates, of which the templates for supranationals, financial institutions, including banks and broker-dealers, and corporates are the most material. To estimate the PD, the Group maps internal ratings to S&P ratings and then applies S&P's extensive default history to determine the PD. The Group takes different approaches to estimate PDs for its low default portfolio ("LDP") and its non-LDP. Internal models are used to estimate the expected loss in the event of default; these include, in addition to the PD, the LGD and EAD.

To measure credit risk exposures, the Group uses a range of metrics such as current and simulated future exposures, as well as single and multi-factor stress metrics and portfolio risk sensitivities, all of which are calculated using internal models.

(3) Risk Appetite and Limits: In order to ensure that credit losses remain within the defined risk appetite, CRM has implemented a Credit Limits Framework at the MSESE Consol level to manage credit risk on a single name and portfolio level, including limits on country, industry (including sub-industries such as shadow banks and climate segments), and product concentrations. The Credit Limit Framework also includes a Credit limit specific for Morgan Stanley Affiliates. The limits are subject to different levels of governance comprising the MSESE and MSBAG Management Boards, the MSESE ERC, the MSESE Credit Risk Committee and CRM.

(4) Risk Reporting: All significant credit risk exposures, concentrations and limit utilisations are reported on a regular and ad-hoc basis to the ERCs, the MSEHSE Group Management Boards and other interested parties.

The Group's credit risk results mainly from:

- **Treasury Placements:** Credit risk arising from Treasury activities primarily relates to deposit placements at the ECB via the Deutsche Bundesbank.
- **Counterparty Risk:** Counterparty risk arises from the Group's sales and trading business. The Group offers clients a wide spectrum of traded products, including listed and OTC derivatives, foreign exchange, secured financing transactions, all of which give rise to counterparty credit risk.
- **Lending:** Lending risk arises from extending loans in the form of relationship or event loans.
- **Morgan Stanley Affiliates:** Credit risk to Morgan Stanley Affiliates results from indirect activity with clearing houses via Affiliates, back-to-back trades with Morgan Stanley Group entities and loan sub-participations or guarantees.
- **Inventory:** Inventory risk arises from secondary trading activity and is mostly driven by European government bonds and covered bonds.

To reduce credit and counterparty risks, CRM relies on standard risk mitigants including netting provisions and the provision of collateral, including with Morgan Stanley Affiliates. Collaterals for derivatives are mostly cash and liquid securities. Lending risk may be mitigated through the transfer of risk to Morgan Stanley Affiliates, for example to reduce concentrations.

The Group's issuer risk exposures are managed within the market risk limits framework and feed into aggregated credit risk exposure metrics.

Consistent with its business and risk strategy, the Group's credit risk portfolio is dominated by investment grade quality obligors in the EEA.

The Group has established processes to calculate ECL for provisions in accordance with IFRS 9 "Financial Instruments". The Group's provisioning levels are not material which is a reflection of the high credit quality of the Group's loan book and the use of risk transfers within the Morgan Stanley Group.

The below table shows RWAs and EADs for credit risk as at 31 December 2023 and 31 December 2022, including Credit Valuation Adjustment risk ("CVA risk"). The RWAs calculated via the advanced capital models (IMM and Foundation Internal Ratings Based or "F-IRB") and under the standardised approach are shown separately. Consistent with its regulatory approvals, the Group calculates its own fund requirements for credit risk with an IMM and F-IRB approach. For counterparty credit risk, the EADs, which serve as an input for the calculation of the own funds requirements, are computed with a IMM approach.

	2023		2022	
€ in millions	**RWAs**	**EADs**	**RWAs**	**EADs**
Credit risk[(1)]	2,812	13,762	2,562	18,892
Of which, internal models (F-IRB)	2,249	3,015	2,028	2,801
Counterparty credit risk (excluding CVA risk)[(2)]	11,001	23,268	12,330	21,249
Of which, internal models (IMM)	6,997	10,426	8,165	11,503
Total (excluding CVA and Settlement risk)	**13,813**	**37,030**	**14,892**	**40,141**
Credit Valuation Adjustment (CVA risk)	4,246	9,915	3,415	9,228
Settlement risk	7	9	45	12
Total	**18,066**	**46,954**	**18,353**	**49,382**

(1) Credit risk from lending, treasury and other sources of credit risk.

(2) Exposures subject to Equity IRB approach are reported under Credit Risk. Exposures to central counterparties are reported under Counterparty credit risk.

The Group has implemented a Credit Limits Framework to monitor credit concentration risk. Credit risks are primarily concentrated in treasury and counterparty exposures with regional focus on EU 27-countries. From a counterparty perspective, the credit portfolio is primarily concentrated with Financials and from a country perspective in the US, France, Italy and Germany; whereas treasury exposures are mostly driven by cash balances placed with central banks. The country risk evaluation includes a determination of Country of Risk and Country of Jurisdiction. The Country of Risk is the country whose political, economic and commercial environment most affects an entity's ability to meet its obligations. The Country of Jurisdiction is defined as the country of registered incorporation or formation of the obligor. For calculation purposes, the breakdown in the following table is based on the Country of Risk whilst the Industry classifications are based on the Global Industry Classification Standards ("GICS").

The following tables provide an overview of the Group's industry and country concentration, whereby the exposure metric used is consistent with internal credit risk management. This metric captures exposure from Treasury placements, lending commitments and trading activities, offset by credit risk mitigants such as collateral.

Breakdown per industry

Exposure € in millions	**2023**	**2022**
Financials	8,866	9,534
Sovereigns	10,193	17,249
All others	5,907	3,588
Total	**24,966**	**30,371**

Breakdown per country

Exposure € in millions	**2023**	**2022**
Supranational	10,652	16,563
US	5,274	5,390
France	3,485	3,225
Italy	1,052	617
Germany	932	1,408
All others	3,571	3,168
Total	**24,966**	**30,371**

The Group's credit risk remained within risk appetite for 2023. The impact of the sharp rise in interest rates on credit risk exposures and obligors' credit quality was a key focus throughout 2023 and will remain a key focus throughout 2024. The volatility across interest rates and foreign exchange, led to selected single name and portfolio exposure increases, for which appropriate mitigation actions were taken.

Market Risk

Market Risk is an inherent part of the Group's business activities. Market Risk is the risk that a change in the level of one or more market prices, rates, indices, implied volatilities (the price volatility of the underlying instrument imputed from option prices), correlations or other market factors, such as market liquidity, will result in losses for a position or portfolio. This includes risks from xVA, which refers to the risk of changes in derivative valuation adjustments due to changes in credit spreads and other market factors. Market Risk includes the consideration of financial risk arising from climate change as well as non-traded market risk such as IRRBB and CSRBB.

Price risk arises for example, in trading portfolios, lending portfolios measured at fair value and associated mark-to-market hedges.

The Market Risk Department ("MRD"), which is independent from the business units, has put in place a Risk Management Framework to identify, measure, control and report market risks. Key components of the Market Risk Framework include:

(1) Risk Identification: To identify and assess market risks, MRD monitors significant changes in the market risk profile on an ongoing basis, including key risk factor sensitivities, limit usage, risk concentrations, stress testing results, and exposure to climate risk. Additionally, the NPA process is leveraged to identify and assess market risks arising from new activities.

(2) Risk Measurement: Market risks are measured by applying shocks to a selection of input market parameters from securities and derivatives valuation models, the results of which are used as standard risk sensitivities and stress testing measures. MRD measures market risks using internal Value at Risk ("Management VaR"), Regulatory VaR, Regulatory Stressed VaR ("SVaR") and IRC models. The VaR models are maintained to be measured against limits and used for capital requirement purposes. The potential loss is calculated by the VaR model over a given time horizon (1 day or 10 days) and confidence interval (95% or 99%). For the Regulatory SVaR, the same methodology and portfolio composition as Regulatory VaR is used, however, the Regulatory SVaR is based on a continuous one-year historical period of significant market stress which is recalibrated on a regular basis. For the IRC model, a potential loss from default and migration risk of non-securitised credit products in the trading book over a one-year time horizon and 99.9% level of confidence is used.

(3) Risk Appetite and Limits: To ensure that market risk losses remain within risk appetite, MRD has established at the MSESE Consol level a comprehensive market risk limit framework, which includes VaR limits, exposure limits and stress exposure limits. The limits are subject to different levels of governance comprising the MSEHSE Group Management Boards, the ERCs, the CRO and MRD.

(4) Risk Reporting: All significant changes in market risk exposures, market risk concentrations and market risk limit utilisations are reported on a regular and ad-hoc basis to the ERCs, the MSEHSE Group Management Boards and other interested parties.

Interest rate risk is inherent in the business of financial institutions. Interest rate risk is the exposure of the Group's financial condition arising from adverse movements in interest rates and credit spreads both in absolute and relative terms. Interest Rate and Credit spread risk in the Banking Book are defined as the risk of losses arising from adverse changes in the interest rate and credit curves within the defined banking book population either from a present value (Delta Economic Value of Equity or "Delta EVE") or Net Interest Income (Delta Net Interest Income, or "Delta NII") perspective. Interest Rate and Credit spread risk arises from exposures derived from traditional treasury and banking activities such as customer lending as well as inter-affiliates borrowing and lending. The Group's Treasury Department and MRD are responsible for the monitoring and control of these exposures through the calculation of the measures Delta EVE and Delta NII. As 31 December 2023, IRRBB exposure is a small component of the Group's market risk profile. Delta EVE and NII are monitored daily and monthly, respectively, and reported at least quarterly to senior management. Both, Delta EVE and NII are subject to risk limits to ensure the IRRBB remains within the Group's Risk Appetite.

The following table presents the results for the regulatory prescribed scenarios as 31 December 2023:

€ in millions	2023 Delta EVE
Parallel shock down	(2.8)
Parallel shock up	1.4
Flattener shock	0.6
Steepener shock	(0.6)
Short rates shock down	(1.9)
Short rates shock up	1.0

As at 31 December 2023IRRBB was approximately 0.04% of CET1 capital under the Delta EVE perspective with "Parallel shock down" as the relevant scenario as it results in the highest loss.

The following table presents the Delta NII results for the regulatory prescribed scenarios with a base NII of €279 million as at31 December 2023

€ in millions	2023 Delta NII
200 bps up	159
200 bps down	-156

Market Risk from trading in EUR Interest Rate Swaps, EUR Inflation, European Government Bonds, Covered Bonds as well as Equity Automated Market Making ("AMM") is retained and managed by the Group. Risk from xVA is also hedged by a dedicated trading desk within the Group which manages exposures coming from counterparties such as credit and funding risk. The main risk factors resulting from these exposures are credit, interest rates, funding basis, equity and foreign exchange related exposures. The organic growth of the client activity in the EEA led to an increase in xVA risk.

The Group uses the Management and Regulatory VaR to assess portfolio market risk. The Regulatory VaR is calibrated and scoped using regulatory requirements to capitalise for market risk and is subject to a daily backtesting calculation validating the accuracy of the model. In addition, the Management VaR is used for internal risk management purposes to ensure the Group's risk appetite stays within approved limits. The average Management VaR of the Group for the year 2023 was €3.8 million (2022: €3.9 million), equally driven by credit, interest rate and basis risk sensitivities from fixed income trading activities and xVA.

The following shows the market risk RWAs as 31 December 2023 and 31 December 2022, as calculated using the advanced capital model (Internal Model Approach, "IMA") and under the standardised approach, where applicable. Consistent with its regulatory approvals, the Group currently uses the advanced capital model for the calculation of own funds requirements for market risk.

RWAs

€ in millions	2023	2022
Standardised approach	88	81
Internal model approach(1)	7,728	8,522
Total	**7,816**	**8,603**

(1) Including RWAs for Risk not in VaR ("RNIV")

The decrease in RWA under the IMA is attributable to a reduction in RNIV RWA due to a methodology change, which was partially offset by an increase in IRC and SVaR driven by changes in the risk profile throughout the year.

The first quarter of 2023 was characterised by US regional bank defaults which triggered sell-off across asset classes and led to increased volatility. In the second quarter of 2023 rates and prices increased alongside a reduction in volatilities. In the second half of the year a significant rates rally was observed driven by strong economic data and the "higher for longer" rates narrative.

The Group has ensured that appropriate mitigation actions were taken to remain within the Group's risk appetite throughout 2023. The continued impact of the high interest rate environment on market risk exposures will remain a key focus throughout 2024.

Liquidity Risk

Liquidity Risk is an inherent part of the Group's business activities. Liquidity Risk is the risk that the Group's financial condition or overall soundness is adversely affected by an inability or perceived inability to meet its financial obligations in a timely manner. Liquidity Risk encompasses the associated funding risk triggered by stress events which may cause unexpected changes in funding needs or an inability to raise new funding.

Liquidity risks from the Group's business activities primarily arise from listed and OTC derivatives as well as its lending and secured funding activities. Intraday risk continues to be a key driver of liquidity risk for the Group and remains a core focus area. These liquidity risks are covered by the Group's liquidity resources.

Treasury is responsible for daily liquidity management activities in their capacity as the First Line of Defence, while the Liquidity Risk Department ("LRD"), as the Second Line of Defence, is responsible for the independent oversight of liquidity risk. LRD has put in place a Risk Management Framework to identify, measure, control and report liquidity risks arising from business activities. Key components of the Liquidity Risk Framework include:

(1) Risk Identification: The identification and assessment of liquidity risks forms an integral part of the Group's liquidity risk management and is performed on an ongoing basis, considering risks to the financial condition or overall soundness in a business-as-usual environment and in stress conditions. To identify and assess liquidity risks, LRD uses ongoing monitoring of limit utilisations, regulatory as well as internal liquidity risk metrics, including the Internal Liquidity Stress Test ("ILST") results. Additionally, the NPA process is leveraged to identify and assess liquidity risks arising from new activities.

(2) Risk Measurement: Liquidity risks are measured using established methods and processes for the assessment of current and projection of future cash and securities flows over various time horizons (including intraday) in base and stress scenarios. Key metrics include the Liquidity Coverage Ratio, the Net Stable Funding Ratio and the coverage of assumed cash outflows under internally developed liquidity stress scenarios as part of the ILST, which consider market wide idiosyncratic as well as combined stress scenarios.

(3) Risk Appetite and Limits: Risk Appetite for Liquidity Risk is expressed via Liquidity and Funding Limits, which are owned by the MSEHSE Group Management Boards are are in place at the MSEHSE Group and MSESE Consol levels. These limits consider the ILST scenarios for a period of one day up to 12 months, the LCR and NSFR. The Group maintains limits, Key Risk Indicators ("KRIs"), targets and thresholds at various levels of the governance structure to support links between the Liquidity Risk Appetite and more granular risk-taking decisions and activities.

(4) Risk Reporting: The monitoring of adherence to relevant regulatory requirements, internal limits and KRIs, to ensure sufficient levels of highly liquid assets is reported on a regular and ad-hoc basis to the ERCs and the MSEHSE Group Management Boards.

The LCR, per the Delegated Act (EU) 2015/61 as a supplement to the CRR, is a regulatory stress test with the objective of promoting short-term resilience of the Group's liquidity risk profile by ensuring that it has sufficient high-quality liquid assets ("HQLA") to withstand a significant stress scenario lasting 30 days. The Group's LCR exceeded the regulatory minimum requirement as at 31 December 2023 and 31 December 2022. The details of the Group's LCR are presented in the following table:

€ in millions	2023	2022
HQLA	11,783	16,801
Cash Outflows	14,477	18,248
Cash Inflows	6,696	6,653
Net Outflow	7,781	11,595
LCR Ratio	151%	145%

Cash outflows decreased during 2023 primarily due to a decrease in deposits received from other Morgan Stanley Group affiliates, which were subsequently deposited at the Deutsche Bundesbank. Cash inflows remained relatively stable during 2023. As of 31 December 2023, the Group's HQLA comprises of cash balances as well as central bank and government bonds.

The NSFR is another regulatory metric which measures the stability of the Group's funding profile over a one-year time horizon, as determined by the prescribed factors assigned to on-balance sheet and specific off-balance sheet assets (Required Stable Funding or "RSF") and liabilities (Available Stable Funding or "ASF"). It complements the LCR by requiring the Group to maintain minimum amounts of stable funding to support the Group's assets, commitments and derivatives exposures over the one-year horizon. The Group's NSFR ratio exceeded the regulatory minimum requirement as at 31 December 2023 and 31 December 2022.

The Group further uses Liquidity Stress Tests to model external and intercompany liquidity flows across multiple scenarios over a range of time horizons. The ILST is designed to simulate severe but plausible stress conditions with eligible liquidity resources having to exceed ILST requirements for a period of one day up to 12 months with limited reliance on parent support beyond month one.

As 31 December 2023, the Group maintained sufficient liquidity to meet current and contingent funding obligations as modelled in its Liquidity Stress Tests.

Operational Risk

Operational Risk is defined as the risk of loss, or damage to the Group's reputation, resulting from inadequate or failed processes or systems, human factors or from external events (e.g., fraud, theft, legal and compliance risks, cyber-attacks or damage to physical assets). This includes legal risk and risks arising from Environmental, Social and Governance factors.

Business Units, Support and Control functions and the business managers therein are primary responsible for the management of operational risk. The business managers maintain processes and controls designed to identify, assess, manage, mitigate and report operational risk. In the event of a new product or a business activity, operational risks are considered and any necessary changes in processes or controls are implemented.

The Operational Risk Department ("ORD"), which is independent from the business units, is responsible for the assessment and monitoring of operational risks. ORD has put in place a comprehensive Risk Management Framework to identify, measure, control and report operational risks. Effective operational risk management is essential to reducing the negative impact of operational risk incidents and mitigating legal and regulatory risks. The Framework is continually evolving to account for changes in the Group and to respond to the changing regulatory and business environment. Key components of the Operational Risk Framework include:

(1) Risk Identification: The Operational Risk Identification Framework provides a consistent approach to identify, quantify and evaluate operational risk inherent to the Group's business operations under normal and stressed conditions. Operational risk data and assessment systems are employed to identify operational risk, they include: internal and external operational risk events, which are captured in dedicated databases; internal control factors; and scenario analysis. Internal operational risk events are captured in the Morgan Stanley Group's internal loss database. Operational Risk and Control Self-Assessments ("RCSA") are a key instrument for operational risk identification. RCSAs are executed by the business units while the ORD oversees the process and challenges the results. Additionally, the NPA process is leveraged to identify and assess operational risks arising from new activities.

(2) Risk Measurement: ORD leverages the internal operational risk capital model for measuring operational risk within the internal capital adequacy assessment process. The model encompasses both quantitative and qualitative assessments. The quantitative part is based on scenario analysis results, which are direct inputs into the model, while the qualitative measures such as internal and external operational incidents, business environment and internal control factors are evaluated as part of the scenario analysis process.

(3) Risk Appetite and Tolerances: To ensure that potential losses remain within the defined risk appetite the MSEHSE Group Management Boards have set risk tolerance levels for the Group and MSESE Consol in aggregate and for all Top Operational Risks. ORD monitors that tolerance levels are not exceeded through a combination of loss projections from scenario analysis and realised operational risk losses. As at 31 December 2023, the largest scenario loss was €218 million.

(4) Risk Reporting: All significant Operational Risk Incidents and the operational risk profile relative to the tolerance level are reported on a regular and ad-hoc basis to the ERCs, the MSEHSE Group Management Boards and other stakeholders.

Regulatory own funds requirements for operational risk are currently calculated under the Basic Indicator Approach ("BIA"). As at 31 December 2023, the Group's operational RWAs were €1,401 million (2022: €1,005 million). The Group recognises that the BIA is not a risk-based measure and therefore uses an operational risk modelling approach to calculate internal operational risk capital requirements (refer to the operational risk figure disclosed in the table in the "Internal Capital Adequacy Assessment Process" section, "Economic perspective" sub-section).

The Group holds sufficient capital to cover the incremental capital requirement over and above the Pillar 1 requirement for Operational Risk.The ORD scope also includes oversight of technology risk, cybersecurity risk and information security risk. ORD partners with the MSEHSE Group Anti Money Laundering and

Fraud Prevention Officer to oversee fraud risk. ORD, in conjunction with the COCO, oversees third party risk (supplier and affiliate risk).

Cybersecurity

The Group's Cybersecurity and Information Security Framework, which includes policies, procedures and technologies, is designed to protect the Group's technology environment from operational risk failures due to the actions of a malicious cyber actor. This includes protecting the Group's own data, client data and the Group's employee data against unauthorised disclosure, modification or misuse and is also designed to address regulatory requirements. This Framework covers a broad range of areas including the following: identification of internal and external threats, access control, data security, protective controls, detection of malicious or unauthorised activity, incident response and recovery planning.

Business Continuity Management and Disaster Recovery

Morgan Stanley Group's Resilience organisation maintains global programmes for Business Continuity Management, Disaster Recovery ("DR") and Third Party Resilience and Key Business Service Resilience that facilitates activities designed to protect the Morgan Stanley Group during a business continuity incident. A business continuity incident is an interruption with potential impact to normal business activity of the Morgan Stanley Group's personnel, technology, suppliers and/or facilities. These programmes require plans to be documented that identify and detail the options available to recover assets and services during an incident. Additionally, plans are required to be tested to provide a reasonable expectation that, during a business continuity incident, the Business Unit will be able to recover and perform its critical business processes and limit the impact of the incident to the Morgan Stanley Group, its clients and financial markets. Forming part of Morgan Stanley Group's Resilience organisation, the MSEHSE Group has staff dedicated to managing the aforementioned programmes, which are governed by the Business Resilience Governance Committee. In addition, the MSEHSE Group Management Boards oversee the programme implementation at the Group level.

Third Party Risk Management

In connection with its ongoing operations, the Group utilises the services of third party suppliers which include other Morgan Stanley Group undertakings as well as external third party vendors. The Group mostly utilises the services of other Morgan Stanley Group undertakings as they are subject to the same global standards and frameworks. These services include, for example, outsourced processing and support functions and other professional services. The Group's risk-based approach to managing exposure to these services includes the execution of due diligence, risk assessments, implementation of service level and other contractual agreements as well as consideration of operational risks and performance of ongoing monitoring and supervision of the third party suppliers' performance. In addition, a dedicated Second Line of Defence control function (COCO) reviews adherence to applicable regulatory requirements. The Group maintains a third and fourth party inventory and an Outsourcing and Sourcing Framework which includes governance through policies, procedures, templates and technology and is designed to meet applicable regulatory requirements and be in line with the Morgan Stanley Group's third party risk management programme.

Model Risk

Model Risk is the potential for adverse consequences from decisions based on incorrect or misused model outputs. Model risk can lead to financial loss, poor business and strategic decision-making, or damage to the Morgan Stanley Group's reputation.

The independent Model Risk Management ("MRM") department performs the Second Line of Defence function with the objective that all models in use are fit for purpose. MRM establishes the standards, principles, practices, governance processes, definitions, and roles and responsibilities for sound model risk management. Key components of the Model Risk Framework include:

(1) Risk Identification: MRM employs model identification and tiering frameworks, aligning model risk management activities with the level of models' inherent risk.

(2) Risk Management and Monitoring: MRM conducts independent review and validation of models to verify that the

models are performing as expected and in line with their designed objectives and intended use. Ongoing monitoring ensures that models continue to perform consistently with their intended purpose and that the outputs of models remain reliable.

(3) Risk Appetite and Tolerances: To ensure that model risk does not pose a material risk to capital adequacy, reputation and regulatory standing, model governance and control processes have been established.

(4) Risk Reporting: MRM reports on model risk to the MOCs and provides a quarterly report on model risk to the ERCs and the MSEHSE Group Management Boards.

The Group uses internal models for valuation, risk management and capital calculations. Valuation models include models that are used to produce valuation and/or risk measures for end of day books and records related to a position and models that are used to adjust a portfolio's value. Risk models are used for the measurement and management of credit risk, market risk, counterparty risk, operational risk and liquidity risk, for stress testing, and for the calculation, planning and management of regulatory and internal capital requirements. Algorithmic trading models are in use for electronic trading activities.

Conduct Risk

Conduct Risk is defined as the risk arising from misconduct by individual employees or contingent workers (collectively, "Covered Persons") or groups of Covered Persons, or the risk arising from conduct by the Morgan Stanley Group where the outcome has an adverse impact on clients or markets.

The Group's independent Compliance Department is responsible for the design and development of a Conduct Risk Framework and for the execution of compliance-related responsibilities as defined in the Group's policies and procedures. A consistent global framework is in place for managing conduct risk and Conduct Risk Incidents ("CRIs") including within the Group.

Key components of the Conduct Risk Framework include:

(1) Risk Identification: Business units as well as support and control functions are responsible for identifying, assessing, managing and recording the conduct risks, which arise from their current or planned strategies and activities.

(2) Risk Management and Monitoring: Internal controls and processes have been established to manage conduct risks identified. CRIs are identified and escalated through a range of processes within the Three Lines of Defence. A review will be performed by the appropriate division and recommendations made to relevant decision-makers on next steps.

(3) Risk Appetite and Tolerances: The Group does not have an appetite for conduct risk. However, the Group acknowledges that it remains inherent in the Group's products, activities, processes and systems and, therefore, cannot be eliminated entirely.

(4) Risk Reporting: Processes have been established to ensure reporting of risks and incidents as well as prompt escalation and appropriate notification. The Group's Head of Compliance attends the Europe, Middle East and Africa ("EMEA") Conduct Risk Committee and reports to the MSEHSE Group Management Boards periodically on the Group relevant conduct matters and on developments in the Conduct Risk Framework as well as on developments in the applicable regulatory environment.

The MSEHSE Group Management Boards hold executive management accountable for compliance with business conduct risk standards through a variety of measures and controls.

Compliance Risk

Compliance Risk is defined as the risk of legal or regulatory sanctions, material financial loss or damage to reputation resulting from the failure to comply with laws, rules, regulations, related self-regulatory organisation standards and codes of conduct applicable to the Group's activities.

The Group's independent Compliance Department is responsible for identifying applicable compliance risks and obligations as well as for establishing and maintaining a Compliance Risk Management Programme for the Group. All of the Group's businesses and operations are subject to the Compliance Risk Management Programme. Key components of the Compliance Risk Management Programme include:

(1) Risk Identification: Business units as well as support and control functions are responsible for identifying, assessing, managing and reporting compliance risk. The Group's Compliance Department completes an annual Compliance Risk Assessment for the Group to identify material compliance risk.

(2) Risk Management and Monitoring: The annual Compliance Risk Assessment for the Group evaluates compliance risks and is reported to the MSEHSE Group Management Boards. In addition, the Compliance Department subsequently develops an Annual Compliance Plan for the Group that prioritises Compliance Department activities (including Compliance monitoring) based on the Compliance Risk Assessment and other inputs, as appropriate.

(3) Risk Appetite and Tolerances: The Group seeks to comply with applicable laws, rules and regulations. The Group has no appetite for transactions, business activities, or conduct by employees, contingents, customers, or counterparties that give rise to a significant breach of the Group's compliance obligations.

(4) Risk Reporting: The Group's Compliance Department reports to the ERCs and MSEHSE Group Management Boards on a quarterly basis on compliance risk, significant regulatory compliance related developments and the progress of the Annual Compliance Plan. The Group's Compliance Department also produces an annual Compliance report which is reviewed by the Management Boards.

Climate and Environmental Risk Management

Climate and environmental risks include impacts to biodiversity, pollution of land, water or air, climate change, deforestation and forest degradation and other negative impacts on the environment as a result of human activities. Within climate and environmental risks, the risks arising from climate change are a particular area of focus.

The Group considers climate and environmental risks through two main categories: transition risks and physical risks.

- **Transition Risks**: Transitioning to a low-carbon and more environmentally sustainable economy will entail extensive regulatory, policy, legal, technology and market initiatives as society adapts to climate change, mitigates its causes and promotes a more sustainable environment. Depending on the nature, speed and focus of these changes, transition risks may pose varying types and levels of financial and reputational risk to businesses and other organisations.
- **Physical Risks**: These risks include both acute physical events such as flooding, and chronic physical risks related to longer-term shifts in climate patterns such as more frequent and prolonged drought and progressive shifts like biodiversity loss, land use change, habitat destruction and resource scarcity. Financial implications for organisations can range from direct damage to assets to indirect impacts from supply chain disruption, driven by factors such as changes in water availability, food security and agricultural productivity. Extreme temperature changes may affect an organisation's physical locations, operations, supply chain, transport needs and employee safety.

In addition, the Group may be exposed to litigation risk or reputational risk losses arising from compliance risks related to increasing and evolving ESG-focused regulation.

Managing Climate and Environmental Risks

The Central Climate Risk Team within Risk Management is responsible for working with stakeholders in Risk and across the Morgan Stanley Group to identify, monitor, mitigate and report on the climate-related financial risks it may face. The EMEA team is led out of the MSEHSE Group with primary responsibilities consisting on partnering with stakeholders to manage and embed climate and environmental risks in the risk management framework including regional regulatory requirements and with consideration of the Group's portfolio.

Climate and environmental risks are incorporated into the MSEHSE Group Risk Management Framework as drivers of credit, market, operational and liquidity risk. The management of climate and environmental risks is also incorporated into policies and procedures. The MSEHSE Group Risk Management Framework continues to be enhanced to meet requirements set out in new and evolving regulations.

Risk Identification and Materiality Assessment

Materiality Assessment in the Short-term

As part of its Risk Identification and Materiality Assessment process, the Group conducts granular risk assessments of short-term climate and environmental risks. These include:

- **Risk Inventory:** The risk inventory captures climate and environmental risks as drivers of existing risks. In 2023, the Group expanded the assessment to consider additional risk events. Risk events assessed for their impact on credit, market, liquidity and operational risks include:
    1) Transition risk driven by climate policy (carbon repricing and accelerated green technology) and other environmental policies (reduction of pollution); and
    2) Physical risk driven by climate events (extreme temperature, wildfire, drought, riverine flood, coastal floods and storms) and other environmental events (biodiversity loss). In addition, the Group has assessed the impact of climate and environmental risks to litigation, reputational, collateral, and strategic risks.
- **Materiality Assessment:** A quantitative assessment is performed across risk types to determine the materiality of the impact of climate and environmental risks. A risk is considered material if the estimated stress loss or outflow is above the existing risk identification materiality thresholds.

Results of Short-term Materiality Assessment

In 2023 for the Group, climate transition risk driven by a carbon repricing or an accelerated green energy technology transition was assessed as material for credit risk exposures. Climate physical risks were assessed as non-material for credit risk. Climate transition and physical risks were assessed as non-material for the Group's collateral positions given low concentration in the Group's portfolio to these types of risks. Climate and environmental risks were assessed as non-material for operational risk (business disruption, litigation risk and reputational risk), market risk, liquidity risk and strategic risk given estimated losses fall below respective materiality thresholds. The assessment is performed quarterly.

Materiality Assessment in the Long-term

The Group also performed a long-term assessment of climate risks using 30-year scenarios. Long term assessments consider a late climate policy action focusing on transition risk and a no action scenario focusing on physical risk. This materiality assessment concluded that the late action scenario focused on transition risk is material for credit risk in the long term. In 2023, the two long term scenarios were assessed as non-material for market and liquidity risks.

Risk Appetite and Limit framework

Credit and Market Risk Limits: Climate Risk

Climate transition risk is incorporated into the Group's Risk Appetite and Limit Frameworks. The MSEHSE Group Management Boards set a Climate Stress Loss Limit ("CSLL") across credit and market risks which is reviewed on an annual basis.

In addition to the CSLL, climate risk is incorporated into the Credit Risk Management Framework through industry sector limits as well as country and obligor ratings. Limits and ratings are monitored as per standards in credit risk management policies and procedures.

- **Climate Stress Loss Limit:** The MSEHSE Group Management Boards express risk appetite via the CSLL. To monitor potential credit and market risk losses against this limit, the Group runs a short-term transition risk carbon repricing scenario that assumes a global effort to address carbon emissions leads to sudden and sustained carbon repricing across all countries. The results of this scenario are reported to the Group's Management Boards on a monthly basis.
- **Industry Sector Limits:** Credit risk limits are established for industries that are highly exposed to climate risk. This process includes a portfolio segmentation of industries into groups with common climate risk profiles. The credit limits for the industry sectors highly exposed to transition and physical risks enable the Group to monitor

and manage credit risks arising from climate change.

- **Country Ratings:** ESG considerations are incorporated into the internal sovereign credit rating assessment. The sovereign rating is an important input in determining country limits, therefore ESG considerations influence risk appetite at the country level.
- **Obligor Ratings:** Climate risk is incorporated into the rating assessment for corporates. The corporate rating is an important input in determining single name limits, therefore climate risk influences risk appetite at a single name level.

In addition to the credit limits, the Group includes an assessment of ESG risks in the lending transaction approval documentation in line with the European Banking Authority's guidelines on loan origination and monitoring.

Liquidity and Operational Risk Limits: Climate Risk

In 2023, climate risks are assessed as non-material for liquidity and operational risk. Hence, the Group has not established specific climate risk limits for liquidity and operational risks.

Credit, Market, Liquidity and Operational Risk Limits: Other Environmental Risks

In 2023, other environmental risks were assessed as non-material for credit, market, liquidity and operational risk. Hence, the Group manages other environmental risks within the existing risk appetite and limit frameworks.

Scenario Analysis and Stress Testing

Scenario Analysis is central to the Group's Climate Risk Management Framework.

Both transition and physical risks can materialise over different time horizons. For example, extreme flooding events present near-term physical risks to vulnerable regions and populations, while e.g., certain climate policy measures, particularly those implemented over several years, present longer-term challenges as economies adjust to increased costs and market or technological changes stemming for new policies.

Therefore, scenarios may be developed to assess potential losses over the short, medium, or long term. Morgan Stanley Risk Management defines these time horizons as:

Short Term: 0 - < 1 year

Medium Term: 1 - < 5 years

Long Term: > 5 years

The Group has implemented short term and long term scenarios to assess the impact of climate risks.

- **Short-term Credit and Market Risk Scenario Analysis**: Informed by carbon emissions data from external providers, the Group employs a bottom up approach in assessing the financial impact of climate policy (carbon repricing) in a scenario that captures both counterparties' probability of default and market price movements. An additional credit risk scenario that considers an accelerated transition to green energy technology is assessed for the counterparties in the Energy sector and updated on a quarterly basis. As transition risk is a material credit risk, a CSLL was established for a transition risk scenario. Physical risk vulnerabilities are assessed on a quarterly basis and as of 2023 are deemed as non-material.
- **Operational Risk Scenario Analysis:** A number of physical risk scenarios are assessed focusing on business disruption due to climate change events (including extreme weather). Physical risk scenarios are selected based on a combination of probability and severity.
- **Litigation and Reputational Risk Scenarios:** Litigation risk arising from Product Design is assessed, including inadequate due diligence and disclosure. Reputational risk losses are assessed for the scenario that is expected to result in the greatest harm to clients.
- **Strategic Risk:** The transition risk carbon repricing scenario was assessed for Strategic Risk.
- **Long-term Strategy Scenarios:** The Group conducted an exploratory long term scenario analysis, running two 30-year quantitative scenarios to model late action (transition risk) and no additional action (physical risk) scenarios on a static and dynamic balance sheet, to inform the Group's materiality assessment and business strategy.

Climate Stress Loss Limit

The Group remained within its portfolio CSLL throughout 2023.

Credit Exposures

The Group's exposure to industries identified as highly exposed to climate transition or physical risk is a small percentage of overall credit exposure.

Exposure to industries with high climate transition or physical risk is subject to credit industry sector limits and both independently comprise 15% of the Group's aggregate credit risk exposure. The increase in exposure to sectors highly vulnerable to transition and physical risks in 2023 compared to the previous year relates to the Group's loan retention exercise that has led to an increase in the overall MSEHSE Group loan portfolio. Further information can be found in the 'Credit Risk' section of the Risk Report. Regarding loans in the Energy, Power and Auto Manufacturing sectors, the MSEHSE Group maintains a KPI to monitor alignment of lending exposure retained on MSEHSE Group to Morgan Stanley Group's Net Zero commitment and global targets in these three sectors (further information can be found in the "Climate Strategy" section). Credit exposures to climate risk in the table below include treasury placements, lending commitments and trading activities, offset by credit risk mitigants such as collateral. Trade and other receivables are excluded.

Credit Exposures to Climate Risk

Climate Risk	2023		2022	
€ in millions	Exposure	% of Portfolio Total	Exposure	% of Portfolio Total
Transition Risk [(1)]	3,213	15%	2,091	8%
Physical Risk	3,352	15%	2,515	9%
Portfolio Total [(2)]	**22,028**		**26,651**	

[(1)] The industries identified as having high climate transition risk were updated in 2023. The 2022 figures included in this table have been revised accordingly.
[(2)] Total portfolio exposures exclude Morgan Stanley Group Affiliates.

The table includes the credit exposure to industry sectors highly vulnerable to climate transition and climate physical risks. The vulnerability of obligors is assessed based on a segmentation approach which differentiates between low, medium, high and very high (high and very high presented in the table). The segments are sub-industries with consistent climate risk profile. The assessment considers expert credit assessment, greenhouse gas emissions data and external physical risk scores.

Other Material Risks

In addition to the above risks, the Group has put in place a framework to identify, measure, control and report on the following other material risks:

- **Leverage Risk:** Leverage Risk is defined as the risk resulting from an institution's vulnerability due to leverage or contingent leverage that may require unintended corrective measures to its business plan, including distressed selling of assets that might result in losses or in valuation adjustments to its remaining assets.
- **Valuation Risk:** Valuation Risk represents the possibility that a valuation estimate of a position would differ from the price in an actual close-out transaction due to uncertainty around the actual price that could be obtained.
- **Earnings at Risk / Strategic Risk:** Earnings at Risk / Strategic Risk are defined as risks to baseline earnings stability that are generally manifested over a longer time horizon rather than an instantaneous market shock. Risk can arise from a decline in key revenue generators, significant loss of customer base, reduced standing amongst competitors, macroeconomic stress conditions, idiosyncratic or industry-wide factors, significant changes to expected expenses, transfer pricing impacts and shifting of business/product mix. This includes risks to Net Revenue, Net Interest Income ("NII"), Non-Interest Income, Non-Interest Expense and Balance Sheet that are impacted by more than just Market Risks and Credit Risks.
- **Reputational Risk:** Reputational Risk (also referred to as Franchise Risk) describes potential risks associated with the way in which the Group conducts its business and the perception of the Group by external parties including its shareholders, clients, regulators and the public. Reputational risks may be triggered by either the nature of the transaction (e.g., unusual complexity) or business practice (e.g., a transaction without appropriate economic substance or business purpose) or by the identity or reputation of the client or counterparty (e.g., a client linked

to alleged corruption or other improper activities).

Risk Summary

The Group's Risk Strategy and Risk Appetite are aligned with the Group's business strategy as well as capital and liquidity resources and are embedded into risk management processes. The Group remained within the set Risk Appetite throughout 2023 and the Group's risk bearing capacity was sufficient at each quarter-end during 2023. In addition, the Group's capital and liquidity are deemed sufficient to exceed regulatory minimums under both normal and in stressed market environments. Adequate capital and liquidity were maintained as at 31 December 2023. The Group's Risk Management Framework and the Group's Risk Governance structures are effective and commensurate with the size and complexity of the Group's risk profile and the Group's Risk Division is appropriately staffed with experienced risk managers.

Opportunities and Outlook

The outlook for global markets and economic environment, summarised in this section, represents the Group's and the Company's internal projections and expectations based upon proprietary models and research as of March 2024. The assumptions underpinning particular forward-looking statements are disclosed where appropriate.

Global Markets and Economic Outlook

In 2024, the Group anticipates the global economy to exhibit a steady growth at 2.8%, marginally below the 3.2% expansion recorded in 2023, reflecting a dynamic and adaptive economic environment. The adjustments to the monetary policy are expected to influence the broader economy gradually, with continued recalibration of demand dynamics. The deceleration of inflation is projected to proceed at a more measured pace compared to the previous year, closely aligning with (yet slightly above) the targeted benchmark in most developed markets, signalling a strategic approach to achieving price stability. Central banks are expected to start their cutting cycle only in mid-June, remaining above their respective neutral rates in 2024. Restrictive monetary policy can be expected to continue to exert pressure on the global cycle over the forecast horizon.

Despite the ongoing challenges, robust labour markets are likely to provide the backbone of a consumption led recovery in an environment of falling inflation. Looking further ahead, the international response to geopolitical dynamics and Europe's strategic recalibration of its energy strategy in response to current challenges will be pivotal in shaping the economic outlook.

In the Euro area, the Group forecasts modest annual growth of 0.5% for 2024, still reflecting a significant drag from the subdued dynamic at the end of last year. As the year progresses, quarterly growth rates are projected to accelerate on the back of increasing real incomes boosting consumer spending.

Business Priorities

The Company's business strategy remains in line with the Global and EMEA strategies, supporting the Morgan Stanley Group's overarching objective of helping people, institutions and governments raise, manage and distribute the capital they need to achieve their goals. A more stable macro environment should give rise to stronger performance in 2024, although any signs of resurgent inflation and higher rates for longer could put downside risk on the wallet and impact the delivery of the Company's revenue ambitions. The Company continues to prioritise long-term revenue growth and wallet share expansion. The latter should be driven across ISG by local and regional collaboration and efficient resource deployment, leveraging the integrated investment bank. The Company aims to book durable revenue supported by a robust and effective risk and control framework that evolves in-line with the business strategy.

Financial Projections

The following forward-looking statements are disclosed on a MSEHSE Group level, at which the KPIs and the strategy of the Group and its subsidiaries are managed. They remain applicable to the Company.

The Group is currently forecasting a significant increase in PBT in 2024 in comparison to 2023, primarily due to the assumption of increased activity in investment banking, continued elevated interest rates, increased trading revenues from client activity and the impact of increased market risk management in the Group as noted in the 'Company Overview' section. This should result in a significant increase in ROE and a moderate reduction in Efficiency Ratio.

Tier 1 Capital Ratio is expected to moderately decrease in 2024 in comparison to 2023, primarily due to an increase in RWAs. LCR is expected to moderately increase due to higher liquidity to cover the required liquidity target. NSFR is expected to moderately decrease primarily due to the impact of increased market risk management in the Group.

Regulatory Developments

Finalising Basel III Reforms

The Basel Committee on Banking Supervision ("BCBS") sets the standard for international banking prudential regulation in a series of accords ("Basel Accords") that are implemented in the EU via the CRR II and CRD V as transposed into German Law (mainly via the German Banking Act).

There are a number of remaining standards of the Basel III reform package (referred to as "Finalisation of Basel III") that are yet to be implemented. These revisions cover RWA requirements for credit, market, CVA and operational risk. They also introduce an aggregate floor for RWA generated by internal models, which will be set at 72.5% of total standardised RWA. The output floor will be phased-in over five years. Institutions will also need to disclose their RWA based upon the standardised approaches.

The European Commission published draft rules in October 2021, referred to as CRR III and CRD VI, to implement these final elements of the Basel III reform package. The draft rules are largely consistent with the Basel III reform package with some adjustments to address EU specificities. The proposed rules are currently going through the European legislative process and are subject to amendments proposed by the European Parliament and the Council of the EU. The proposal also includes an increased focus on Environmental, Social and Governance ("ESG") risks. These rules are expected to become effective from 1 January 2025.

Swap Dealer Requirements for Non-US Domiciled Entities

The CFTC are developing specific requirements to allow registered non-bank swap dealers who are domiciled outside of the US to meet CFTC capital requirements by reference to local prudential standards with a draft proposal published for Germany. Until those rules are finalised, pursuant to interim no-action relief, MSESE complies with home-country capital requirements in lieu of CFTC capital requirements.

Disclosures in Accordance With Section 340a (1a) HGB in Conjunction With Section 289b (2) HGB

The Company is exempted from the obligation under section 340a (1a) HGB to draw up a non-financial statement, including the disclosures required by Article 8 of the EU Taxonomy Regulation, as it meets the requirements under section 289b (2) HGB. The MSEHSE Group Consolidated Management Report in German language is available at http://www.unternehmensregister.de.

ANNUAL FINANCIAL STATEMENTS

Balance Sheet as at 31 December 2023

Income Statement for the period from 1 January to 31 December 2023

Cash Flow Statement for the period from 1 January to 31 December 2023

Notes

Balance Sheet as at 31 December 2023

Assets in € millions	Note		2023	2022
Cash reserve				
a) Balances with central banks			**327**	–
thereof: with Deutsche Bundesbank €327 million (2022: €0 million)				
Receivables from credit institutions	4			
a) Due on demand		10,594		17,929
b) Other receivables		–		195
			10,594	**18,124**
Receivables from customers	4		**7,036**	**14,196**
thereof: loans granted to local authorities €22 million (2022: €120 million)				
Trading assets	7		**41,462**	**35,486**
Investments in affiliated companies	8		**603**	**603**
thereof: credit institutions €603 million (2022: €603 million)				
Intangible assets	8			
a) Goodwill			**37**	**42**
Property, plant and equipment	8		**21**	**20**
Other assets	9		**426**	**441**
Prepaid expenses and deferred charges			**4**	**2**
Total assets			**60,510**	**68,914**

Liabilities and equity in € millions	Note		2023	2022
Liabilities to credit institutions	4			
a) Due on demand		4,690		11,440
b) With an agreed maturity or term		200		501
			4,890	**11,941**
Liabilities to customers	4			
a) Other liabilities				
aa) Due on demand		8,993		13,747
ab) With an agreed maturity or term		1,107		2,375
			10,100	**16,122**
Debt Issuances	11			
a) Debt Securities			**92**	–
Trading liabilities	7		**34,582**	**33,448**
Other liabilities	9		**116**	**309**
Deferred income			**5**	**7**
Provisions	12			
a) Provisions for pensions and similar obligations		11		11
b) Provisions for taxation		15		31
c) Other provisions		129		115
			155	**157**
Subordinated debt	13		**3,511**	**1,006**
Fund for general banking risks	7		**77**	**26**
thereof: special items according to Section 340e (4) HGB €77 million (2022: €26 million)				
Instruments for Additional Tier 1 Regulatory Capital	14		**1,000**	**1,000**
Equity capital	15			
a) Subscribed capital		3,901		3,901
b) Capital reserve		1,931		931
c) Earnings reserve		66		24
d) Retained earnings		84		42
			5,982	**4,898**
Total liabilities and equity			**60,510**	**68,914**

Income Statement for the period from 1 January to 31 December 2023

€ in millions	Note			2023	2022
Interest income from credit and money market transactions			1,238		181
thereof: negative interest income €0 million (2022: €29 million)					
Interest expenses			1,440		274
thereof: positive interest expenses €0 million (2022: €35 million)					
				(202)	**(93)**
Income from profit sharing, profit transfer or partial profit transfer agreements	17			**121**	**53**
Commission income			407		444
Commission expenses			95		90
				312	**354**
Net trading result				**462**	**223**
thereof: special items according to Section 340e (4) HGB €51 million (2022: €25 million)					
Other operating income	18			**19**	**24**
General administrative expenses					
a) Personnel expenses					
aa) Wages and salaries		248			215
ab) Social security and other pension costs and benefits thereof: Pension scheme €10 million (2022: €12 million)		45			36
			293		251
b) Other administrative expenses			188		158
				481	**409**
Depreciation, amortisation and write-downs of intangible assets, and property, plant and equipment	8			**10**	**13**
Other operating expenses	18			**77**	**74**
Income from ordinary activities				**144**	**65**
Extraordinary income				**–**	**37**
Income taxes				**60**	**60**
Net profit for the year				**84**	**42**
Net profit				**84**	**42**

Cash Flow Statement for the period from 1 January to 31 December 2023

€ in millions	Note	2023	2022
Net income		**84**	**42**
Non-cash items included in net income and reconciliation to cash flow from operating activities			
+/- Depreciation on intangible assets and property, plant and equipment	8	10	13
+/- Increase in/reversal of provisions	12	14	(3)
+/- Increase in/(reversal of) Fund for general banking risks		51	25
+/- Increase in/(reversal of) Risk discount value-at-risk	7	1	21
+/- Interest expense / income		202	93
- Extraordinary gains		–	(37)
+/- Income tax expense / income		60	60
+/- Other adjustments		(3)	–
= Subtotal		**419**	**214**
Changes in assets and liabilities from operating activities			
-/+ Receivables from credit institutions		7,530	(10,545)
-/+ Receivables from customers		7,112	(106)
-/+ Trading assets		(5,895)	(17,977)
-/+ Other assets from operating activities		102	161
+/- Payables to credit institutions		(7,051)	8,530
+/- Payables to customers		(5,972)	1,244
+/- Debt Issuances		92	–
+/- Trading liabilities		1,027	16,517
+/- Other liabilities from operating activities		(194)	39
+ Interest received		1,207	199
– Interest paid		(1,273)	(242)
– Income taxes paid		(166)	(30)
Cash flow from operating activities		**(3,062)**	**(1,996)**
– Payments for the acquisition of intangible assets and property, plant and equipment	8	(6)	(2)
– Payments for the sale of business units		–	57
Cash flow from investing activities		**(6)**	**55**
+ Proceeds from the issuance of instruments for Additional Tier 1 Regulatory Capital	14	–	400
+ Proceeds from contributions to equity	15	1,000	1,595
+ Proceeds from subordinated liabilities	13	2,500	–
– Interest paid for instruments for Additional Tier 1 Regulatory Capital		(48)	(41)
– Interest paid for subordinated debt		(57)	(13)
Cash flow from financing activities		**3,395**	**1,941**
= Change in cash and cash equivalents		327	–
+ Cash and cash equivalents at the beginning of the period		–	–
Cash and cash equivalents at the end of the period		**327**	**–**

General Information

1. Corporate Information

Morgan Stanley Europe SE (the "Company" or "MSESE") is a stock corporation under European Law (European Company, *Societas Europaea*) based in Frankfurt am Main. The Company is registered in the Commercial Register of the Local Court in Frankfurt am Main under number HRB 109880.

Morgan Stanley Europe Holding SE, Frankfurt am Main, ("MSEHSE") is the sole shareholder of the Company. The Company is the sole shareholder of Morgan Stanley Bank AG, Frankfurt am Main ("MSBAG"). The Company, together with its subsidiary MSBAG, form the MSESE Group.

The Company's ultimate parent undertaking is Morgan Stanley, Delaware, United States of America ("US"). Morgan Stanley together with its subsidiary undertakings form the Morgan Stanley Group.

2. Basis of Accounting

The annual financial statements as at 31 December 2023 are prepared in accordance with the regulations of the German Commercial Code (Handelsgesetzbuch or "HGB"), the German Ordinance on Accounting Policies for Banks and Financial Service Providers (Verordnung über die Rechnungslegung der Kreditinstitute und Finanzdienstleistungsinstitute or "RechKredV") and the German Stock Corporation Act (Aktiengesetz or "AktG"). Unless otherwise stated, all amounts are rounded to the nearest million Euros.

The Company is exempt from preparing consolidated financial statements and a group management report for the MSESE Group (Section 291 (1) and (2) HGB). The company which prepares the consolidated financial statements for the smallest consolidation scope is MSEHSE. Consolidated financial statements and group management report of MSEHSE are prepared in accordance with the International Financial Reporting Standards ("IFRS") as adopted by the European Union ("EU") (Section 291 (1) HGB in conjunction with Section 315e (3) HGB). The company which prepares the consolidated financial statements for the largest consolidation scope is Morgan Stanley.

Financial statements of Morgan Stanley and exempting consolidated financial statements and the group management report of MSEHSE can be obtained from https://www.morganstanley.com/about-us-ir.

The following are the key differences in the IFRS consolidated financial statements of the MSEHSE Group for the financial year 2023 when compared with the German accounting principles:

- Under HGB, financial instruments in the trading portfolio are initially measured at purchase price and subsequently measured at fair value less a risk discount on the basis of the regulatory value-at-risk. Additionally, 10% of the net trading result is allocated, if required, to the fund for general banking risk. IFRS requires initial as well as subsequent measurement of these financial instruments at fair value. Differences between the transaction price and the fair value at initial recognition are deferred if they are based on significant unobservable market parameters. HGB does not have this accounting concept.
- Under HGB, OTC traded derivatives in the trading portfolio and related cash collateral may be netted per counterparty if the variation margin is calculated and paid daily on the basis of the fair value of the derivatives. Furthermore, there are requirements for netting receivables and liabilities according to Section 10 RechKredV. Under IFRS, financial assets and financial liabilities are offset against each other, and only the net amount is reported, if there is a legal right to offset the recognised amounts in the normal course of business and in the event of a counterparty default. In addition, there must be an intention either to settle on a net basis or to realise the asset and settle the liability simultaneously.
- Commodity derivatives that are only physically settled are not treated as financial instruments under HGB. Under IFRS these transactions fulfill the criteria of a derivative.
- The valuation of provisions for pensions and similar obligations in actuarial opinions is based on different valuation assumptions. Under IFRS, pension liabilities and plan assets are measured separately and all remeasurements relating to assumption

changes are taken to other comprehensive income. Under HGB, the same valuation methodology assumptions are applied to pension liabilities and plan assets when their cash flows are matching. All remeasurements are taken to personnel expenses.

- Deferred tax assets are recognised in the consolidated financial statements in accordance with IFRS, whereas the Company applies the accounting policy choice in accordance with Section 274 HGB and does not recognise deferred taxes.
- Under IFRS, issued Additional Tier 1 instruments are reported within equity whilst under HGB these are reported within liabilities as Instruments for Additional Tier 1 Regulatory Capital.
- Structured notes in IFRS financial statements are recognised as trading liabilities designated at fair value through profit and loss. Under HGB, the Company applies hedge accounting whereby changes in fair value of structured notes are offset with changes in fair value of hedging derivatives.

3. Accounting Policies

Cash Reserve and Receivables

Cash reserve is accounted for at nominal value. Receivables from credit institutions and customers are accounted for at acquisition cost, including pro-rata interest and are net of loan loss provisions. Cash placed overnight under the deposit facility with the Deutsche Bundesbank is reported within “Receivables from credit institutions”.

Loan Loss Provision

The Company recognises loan loss provisions for receivables from credit institutions and customers.

In accordance with the requirements of IDW RS BFA 7, the Expected Credit Loss (“ECL”) model is based on the change in credit risk since initial recognition:

- Stage 1: if the credit risk of the financial instrument at the reporting date has not increased significantly since initial recognition then the loss allowance is calculated weighted with the probability of default within the next 12 months.
- Stage 2: if there has been a significant increase in credit risk (“SICR”) since initial recognition, the loss allowance is calculated as the ECL over the remaining life of the financial instrument. If it is subsequently determined that there has no longer been a SICR since initial recognition, then the loss allowance reverts to reflecting 12 month expected losses.
- Stage 3: if there has been a SICR since initial recognition and the financial instrument is deemed credit-impaired, the loss allowance is calculated as the ECL over the remaining life of the financial instrument. If it is subsequently determined that there has no longer been a SICR since initial recognition, then the loss allowance reverts to reflecting 12 month expected losses.

Notwithstanding the above, for specific receivables a lifetime ECL is always calculated, without considering whether a SICR has occurred.

When assessing SICR, the Company considers both quantitative and qualitative information and analysis. These are based on historical information and conditions expected in the future, which are assessed by credit risk experts.

The determination of a SICR is generally based on changes in the probability of default (“PD”), in conjunction with an assumption that a SICR has occurred if a financial asset is more than 30 days past due.

ECL is calculated using three main components:

- PD: the 12 month and lifetime PD represent the expected point-in-time probability of a default over the next 12 months and over the remaining lifetime of the financial instrument respectively, based on conditions existing at the balance sheet date and future economic conditions.
- Loss given default (“LGD”): the LGD represents expected loss conditional on default, taking into account the mitigating effect of collateral, including the expected value of the collateral when realised and the time value of money.
- Exposure at default (“EAD”): this represents the expected EAD, taking into account the expected repayment of principal and interest from the balance sheet date to the date of

default event together with any expected drawdowns of the facility over that period.

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

Trading Assets and Liabilities

Financial instruments classified as trading assets and liabilities are initially recognised at purchase price and subsequently measured at fair value less a risk discount in accordance with Section 340e (3) HGB. In accordance with Section 255 (4) HGB, the fair value corresponds to the market price. If an active market does not exist, fair value is determined using valuation techniques. Guarantees received or provided in respect of trading derivative contracts are accounted for as trading derivative contracts.

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

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

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

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

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

- Level 2 - Valuation techniques using observable inputs

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

- Level 3 - Valuation techniques with significant unobservable inputs

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

Where necessary, valuation adjustments will be made. Factors taken into account include liquidity risk (price range between bid and ask price), counterparty default risk, model uncertainty and concentration risks.

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

In order to capture any remaining realisation risks, the result of the valuation at fair value is reduced by a risk discount, which is deducted from trading assets. The risk discount is calculated using the regulatory value-at-risk based on a 99% confidence level over a holding period of 10 days.

In addition to the risk discount, at each year end 10% of the net trading result (after risk discount) is allocated to the fund for general banking risks in accordance with Section 340e (4) HGB. The allocation is made until this fund reaches an amount of 50% of the 5-years average of the net trading result after risk discount. The fund for general banking risks may only be reversed to offset a net trading loss for the year or if it exceeds the 50% limit.

The Company pledges cash collateral and securities in respect of its derivative portfolio in the form of initial and variation margin.

Derivatives reported within trading assets and liabilities are offset against the associated cash variation margin if, supported by a legally enforceable agreement containing a credit support annex (“CSA”), the exchange of cash collateral takes place on a daily basis taking into account the fair value of the derivative financial instruments. For each counterparty, the amount offset includes the positive and negative market values of derivatives as well as the cash variation margin paid or received.

Securities Lending and Repurchase Agreements

Securities lending and repurchase agreements are accounted for in accordance with the applicable principles of Section 340b HGB. Securities lent and securities sold under repurchase agreements continue to be recognised by the Company in accordance with their economic ownership, while securities borrowed and securities bought under repurchase agreements are not recognised on the balance sheet. Receivables and liabilities arising from repurchase agreements and securities lending transactions that meet the requirements to offset under Section 10 RechKredV are reported net.

Investments in Affiliated Companies

Investments in affiliated companies are carried at cost. If an impairment of an investment is expected to be permanent, the carrying amount is written down to the lower fair value.

Intangible Assets and Property, Plant and Equipment

Intangible assets and property, plant and equipment are reported at acquisition cost reduced by scheduled depreciation. The underlying useful lives are based on the economic useful life. Write-downs are made for any impairment that is likely to be permanent. Goodwill reported within intangible assets is amortised over its estimated useful life of 10 years in accordance with Section 253 (3) sentence 4 HGB. Low-value assets are fully depreciated in the year of acquisition.

Other Assets

Other assets are measured at acquisition cost (nominal value) considering the strict lower-of-cost-or-market principle.

Liabilities

Liabilities to credit institutions and to customers, subordinated debt and Instruments for Additional Tier 1 Regulatory Capital are recognised at their settlement amount including accrued interest, in accordance with Section 253 (1) HGB.

Prepaid Expenses and Deferred Charges

Prepaid expenses and deferred charges are released to the income statement on a straight-line basis over their term.

Provisions

Provisions for contingent liabilities are recognised at the expected settlement amount using reasonable judgement. If the remaining term is longer than one year, the provision is discounted. The Company applies the discount rate published by the Deutsche Bundesbank in accordance with the Regulation on the Discounting of Provisions.

The Company is applying accounting note IDW RH FAB 1.021 in relation to the valuation of provisions for pension and similar obligations funded by insurance contracts. This accounting note requires for matching cash flows and the use of the same valuation methodology assumptions for the asset and the liability.

For pensions and similar obligations where the cash flows do not match the plan assets and are not accounted for under IDW RH FAB 1.021, the Company continues to use the projected-unit-credit method. The valuation includes actuarial assumptions on demographic developments, increases in salaries and pensions as well as inflation rates. Demographic assumptions are based upon the “Heubeck-Richttafeln 2018G” tables. The discount rate is based upon the average market interest rate of the last 10 years with an assumed remaining term of 15 years as published by Deutsche Bundesbank according to Section 253 (2) HGB.

In accordance with Section 246 (2) HGB, the pension obligations are offset against the plan assets as well as the respective expenses and income. The Company has outsourced the reinsurance policies covering the general pension plan to a contractual trust arrangement (“CTA”).

A provision requirement for interest rate risks is annually examined as part of the loss-free valuation of interest bearing financial instruments in the banking book using the present/book value method. As at 31 December

2023, the valuation resulted in no need to recognise a provision.

Deferred Tax Assets and Liabilities

Deferred tax assets and liabilities are recognised for temporary differences between the accounting and tax values for assets, liabilities and interest carry forwards. Deferred tax liabilities are netted against deferred tax assets and the remaining deferred tax assets are not recognised on the balance sheet in accordance with the accounting option set out in Section 274 (1) sentence 2 HGB.

Company-specific tax rates at the time of recognition of temporary differences are used for the estimation of deferred taxes and liabilities. The deferred taxes related to the head office are measured using the relevant combined German income tax rate of 32% which includes corporate tax, trade tax and solidarity surcharge. The deferred taxes related to the foreign branches are measured using the applicable statutory tax rates respectively, which range from 19% to 33%.

Valuation Units

The Company has set up valuation units for physically settling commodity derivatives and structured notes to hedge against market risk. Physically settling commodity derivatives are combined with offsetting hedging transactions. During the year, the Company issued structured notes for the first time. Market risks embedded within these notes were hedged with offsetting derivatives.

For both commodity derivatives and structured notes the Company forms micro-valuation units in accordance with Section 254 HGB. There is a match in amount and maturity between the underlying and hedging transactions. In order to assess the prospective effectiveness of a valuation unit, the method of matching of critical terms is used.

For the commodity derivatives, the Company applies the freezing method, whereby the effective part of the changes in value of the hedged item and hedging instrument resulting from the hedged risk are not reported on the balance sheet.

For structured notes, the Company uses the ongoing booking method, whereby the offsetting changes in the value of the hedged risk are recognised on the balance sheet.

Provisions for impending losses are recognised for an unrealised net loss of the hedged risk (retrospective negative ineffectiveness). Any unrealised gains are not recognised.

Currency Conversion

Currency conversion is carried out in accordance with the principles of Section 256a and Section 340h HGB. Assets and liabilities denominated in a foreign currency are translated into Euros at the rates ruling at the reporting date. Foreign exchange rate fluctuations from trading assets and liabilities are reported in the net trading result. Due to the special coverage in the same currency, gains and losses resulting from currency translation in the banking book are presented net in either other operating income or expenses.

Notes to the Balance Sheet

4. Residual Maturity of Receivables and Liabilities

The following tables present maturity structure of receivables from credit institutions and customers, liabilities to credit institutions and customers, as well as debt issuances:

€ in millions	2023	2022
Receivables from credit institutions		
Due on demand	10,594	17,929
With a remaining maturity of:		
up to three months	–	195
Total	**10,594**	**18,124**

Receivables from credit institutions due on demand include overnight cash deposits placed with the Deutsche Bundesbank of €9,028 million (31 December 2022: €14,744 million).

Prior year comparatives in the table above have been restated to present €14,744 million of overnight cash deposits with the Deutsche Bundesbank as Receivables from credit institutions. This amount was previously disclosed as a Cash reserve.

Prior year comparatives in the tables above and below have been restated to present €2,055 million of banking book related secured financing transactions as Receivables from customers. This amount was previously disclosed within Receivables from credit institutions.

€ in millions	2023	2022
Receivables from customers		
Due on demand	5,303	12,673
With a remaining maturity of:		
up to three months	610	1,023
three months to one year	1,123	500
Total	**7,036**	**14,196**

€ in millions	2023	2022
Liabilities to credit institutions		
Due on demand	4,690	11,440
With a remaining maturity of:		
three months to one year	200	501
Total	**4,890**	**11,941**

€ in millions	2023	2022
Liabilities to customers		
Due on demand	8,993	13,747
With a remaining maturity of:		
up to three months	20	–
three months to one year	972	–
one year to five years	115	2,375
Total	**10,100**	**16,122**

€ in millions	2023	2022
Debt Issuances		
With a remaining maturity of:		
one year to five years	30	–
more than five years	62	–
Total	**92**	**–**

5. Receivables and Liabilities with Affiliated Companies

The following table presents receivables from and liabilities to affiliated companies:

€ in millions	2023	2022
Receivables from credit institutions	23	261
Receivables from customers	4,364	11,908
Liabilities to credit institutions	3,883	7,379
Liabilities to customers	4,237	10,133
Subordinated debt	3,511	1,006
Instruments for Additional Tier 1 Regulatory Capital	1,000	1,000

6. Repurchase Agreements

Trading assets include debt securities of €9,058 million (2022: €1,384 million) which have been sold or otherwise transferred, but remain recognised on the balance sheet.

7. Trading Assets and Liabilities

The criteria used to classify financial instruments to trading assets and trading liabilities remained unchanged in the financial year.

The Company allocated an amount of €51 million (2022: €25 million), representing 10% of the net trading result in accordance with Section 340e (4) HGB, to the fund for general banking risks in the financial year 2023.

The following table provides a breakdown of the trading assets and liabilities:

	Trading assets		Trading liabilities	
€ in millions	2023	2022	2023	2022
Derivative financial instruments	8,116	24,228	4,985	24,187
Receivables/ liabilities	23,329	9,489	29,597	9,261
Bonds and other fixed-income securities	9,230	1,380		
Shares and other non-fixed-income securities	809	410		
Risk discount	(22)	(21)		
Total	**41,462**	**35,486**	**34,582**	**33,448**

Derivative financial instruments include the offset of positive fair values of €359,227 million with negative fair values of €358,192 million with cash collateral received of €13,681 million and cash collateral paid of €12,646 million.

The following table presents the nominal value of derivative financial instruments by type:

	Nominal amount	
€ in millions	2023	2022
Interest-related transactions	11,955,687	5,675,587
Exchange-rate-related transactions	906,252	953,747
Equity-related transactions	144,660	131,753
Credit derivatives	46,464	73,927
Other transactions	23,993	20,501
Total	**13,077,056**	**6,855,515**

8. Non-current Assets

Non-current assets of the Company consist of “Intangible assets”, “Property, plant and equipment” as well as “Investments in affiliated companies”.

Intangible assets consist of goodwill of €37 million (2022: €42 million).

Property, plant and equipment of €21 million includes leasehold improvements of €14 million (2022: €13 million) and office equipment of €3 million (2022: €3 million).

Investments in affiliated companies of €603 million (2022: €603 million) relates to shares in MSBAG. The net profit of MSBAG as at 31 December 2023 transferred to the Company due to the Profit and Loss Transfer Agreement (“PLTA”) amounts to €121 million. The equity of MSBAG as at 31 December 2023 amounts to €660 million.

The following table shows changes in non-current assets:

€ in millions	Intangible assets	Property, plant and equipment
Acquisition / production cost 01 January 2023	**59**	**40**
Additions	–	6
Acquisition / production cost 31 December 2023	**59**	**46**
Accumulated depreciation 01 January 2023	**17**	**20**
Depreciation	5	5
Accumulated depreciation 31 December 2023	**22**	**25**
Carrying amount as at 31 December 2022	**42**	**20**
Carrying amount as at 31 December 2023	**37**	**21**

9. Other Assets and Liabilities

Other assets of €426 million (2022: €441 million) and other liabilities of €116 million (2022: €309 million) primarily consist of collateral received and paid in relation to listed and cleared derivatives. Other assets also include a receivable of €121 million in relation to the PLTA with MSBAG.

10. Foreign Currencies

The following table presents the Company’s assets and liabilities denominated in foreign currencies:

€ in millions	2023	2022
Assets	6,906	14,300
Liabilities	6,513	14,734

The foreign currency primarily relates USD.

11. Debt Issuances

During the year, the Company issued structured notes to non-affiliated companies of €92 million (31 December 2022: nil).

12. Provisions

Provisions for Pensions and Similar Obligations

Provisions of €11 million (2022: €11 million) were made for pensions and similar obligations. Pensions and similar obligations recorded at the reporting date relate primarily to residual risks on unfunded inflation adjustments.

The main actuarial assumptions applied are as follows:

Actuarial assumptions	2023	2022
Discount rate	1.8%	1.8%
Income dynamics	3.0%	2.5%
Pension dynamics	2.5%	2.6%

The valuation difference, in accordance with Section 253 (6) HGB, between the 10-year average interest rate of 1.8% which has been applied at the end of the financial year 2023 and the 7-year average interest rate of 1.7% is subject to a distribution ban and amounts to less then €1 million as at 31 December 2023 (2022: €1 million).

In accordance with Section 246 (2) HGB, pension obligations of €30 million are offset against the plan assets of €19 million.

Other Provisions

Other provisions of €129 million (2022: €115 million) primarily relate to variable, deferred and share-based compensation measured at the fair value of Morgan Stanley shares at the balance sheet date.

13. Subordinated Debt

As at 31 December 2023, the Company had issued subordinated debt of €1,010 million (2022: €1,006 million) and senior subordinated debt of €2,501 million (2022: nil)

The subordinated debt of €1,000 million was issued to the immediate parent MSEHSE. It has a variable interest rate of EURIBOR plus 160 basis points, matures on 27 October 2031 and has optional quarterly call dates starting from 27 October 2025.

During the year, senior subordinated debt of €2,500 million was issued to MSEHSE. It has Morgan Stanley Proxy rate[1], a maturity of 13 month evergreen which is extendable to a maximum of 10 years after issuance date, and no early call option.

The BaFin, as the German Resolution Authority, has the authority to write down or convert into shares the above mentioned instruments prior to any insolvency or liquidation of the Company, under the applicable Resolution Legislation.

In the event of a liquidation or insolvency of the Company, the claims and interest claims of the subordinated creditors will only be repaid after the claims of all non-subordinated creditors have been satisfied.

Interest expense on subordinated and senior subordinated debt as at 31 December 2023 includes interest not yet due of €11 million (2022: €6 million).

14. Instruments for Additional Tier 1 Regulatory Capital

As at 31 December 2023, liabilities include €1,000 million of Additional Tier 1 Regulatory Capital ("AT1 Notes") issued in accordance with the Capital Requirements Regulation ("CRR"). The AT1 Notes, issued in 2020 and 2022, represent the Company's perpetual, unsecured and subordinated debt and bear fixed annual interest rate of 4.7% and 5.0%, respectively. Interest expenses on these instruments as at 31 December 2023 include interest not yet due of €4 million (2022: €4 million) which is disclosed within other liabilities.

15. Equity Capital

Equity as at 31 December 2023 is composed as follows:

€ in millions	2023	2022
Subscribed capital	3,901	3,901
Capital reserve	1,931	931
Earnings reserve	66	24
Retained earnings	84	42
Total	**5,982**	**4,898**

Subscribed Capital

The subscribed capital is unchanged and is comprised of 3,901 million no-par-value registered shares of €1 each.

Capital Reserve

The Capital reserve increased by €1,000 million €1,931 million due to Common Equity Tier 1 ("CET1") capital infusion from MSEHSE.

Earnings Reserve

Net income of €42 million for the financial year ending 31 December 2022 was transferred to the earnings reserve by resolution of the Supervisory Board on 24 April 2023.

Retained Earnings

It is proposed to include the net profit for the financial year ending 31 December 2023 of €84 million in the earnings reserve.

Notes to the Income Statement

16. Income Breakdown by Geographical Markets

The total amount of interest income, commission income, net trading result and other operating income, grouped by geographical markets pursuant to Section 34 (2) RechKredV, is presented in the following table:

€ in millions	2023	2022
Germany	1,823	670
Other EU Countries	303	202
Total income	**2,126**	**872**

The information presented in the table above reflects the booking location of income prior to any internal allocation of income and expenses

[1] Interest rate at which Morgan Stanley is offering loans, in the relevant currency, to members of the Morgan Stanley Group on the issuance date

in line with applicable Morgan Stanley Group transfer pricing policies.

17. Income from Profit Sharing, Profit Transfer or Partial Profit Transfer Agreement-related Profits

As a result of the PLTA, MSBAG's net profit for the financial year ending 31 December 2023 of €121 million was transferred to the Company.

18. Other Operating Income and Expenses

Other operating income of €19 million (2022: €24 million) primarily consists of payments for securities settlement in accordance with Central Securities Depositories Regulation ("CSDR") as well as service charges from ongoing operations with affiliated companies.

Other operating expenses of €77 million (2022: €74 million) consist primarily of French and Spanish financial transaction taxes and expenses related to the settlement of securities.

Additional Information

19. Valuation Units

In the financial year, the Company continued to trade derivatives on CO_2 certificates which were hedged with offsetting derivatives with affiliated companies. These valuation units have an average residual maturity of one year and are not reported on the balance sheet. Nominal and fair value amounts as at year-end are as follows:

€ in millions	Nominal amount	Fair value positive	Fair value negative
Underlying transaction	750	4	86
Hedging Instrument	750	86	4

Market risks embedded within issued structured notes were hedged with offsetting derivatives with Morgan Stanley Group companies. Nominal and fair value amounts of these valuation units as at 31 December 2023 are as follows.

€ in millions	Nominal amount	Fair value change positive	Fair value change negative
Structured Note	90	2	0
Hedging Instrument	90	0	2

20. Contingent Liabilities

The Company has provided a Letter of Comfort (*Patronatserklärung*) to benefit MSBAG.

21. Auditor's Fee

Refer to the consolidated financial statements of the MSEHSE Group.

22. Employees

The average number of employees by business units was as follows:

Business Units	2023	2022
Infrastructure and Control	372	320
Institutional Securities Group	376	309
Real Assets	–	16
Total	**748**	**645**

Infrastructure and Control primarily consists of Operations, Finance, Risk Management, Corporate Service, Technology and Legal and Compliance.

Institutional Securities Group includes Institutional Equities Division, Fixed Income Division, Investment Banking Division and Global Capital Markets.

23. Statement of Cash Flows

The cash flow statement is prepared using the indirect method and shows the net increase/ decrease in cash and cash equivalents during the year.

Cash and cash equivalents represents the Company`s cash balance held with central banks due on demand and are not subject to any restrictions on disposal. Due to its narrow definition, cash and cash equivalents does not include overnight deposits placed with the Deutsche Bundesbank, which are reported within "Receivables from credit institutions".

24. Management Board and Supervisory Board

The Management Board is comprised as follows:

- Oliver Behrens,
  Chair of the Management Board
- David Best,
  Member of the Management Board
- Martin Borghetto,
  Member of the Management Board
- Emmanuel Goldstein,
  Member of the Management Board, appointed with effect from 1 October 2023
- Philipp Lingnau,
  Member of the Management Board
- André Munkelt,
  Member of the Management Board
- Dr. Jana Währisch,
  Member of the Management Board

The total remuneration of the Management Board payed by the Company for the financial year amounted to €8 million (2022: €8 million). Pension provisions for members of the Management Board amounted to €6 million (2022: €3 million). Compensation was paid to members of the Supervisory Board of less than €1 million (2022: €1 million).

The Company has not granted any loans to the members of the Management Board or the Supervisory Board nor has entered into liability relationships with them.

The Supervisory Board is comprised as follows:

- Frank Mattern,
  Independent advisor
  Chair of the Supervisory Board since 1 January 2023 (previously Deputy Chair)
- Clare Woodman,
  Managing Director, Morgan Stanley
  Deputy Chair of the Supervisory Board since 1 January 2023 (previously Chair)
- Raja Akram,
  Managing Director, Morgan Stanley
- David Cannon,
  Independent advisor
- Maria Luís de Albuquerque,
  Independent advisor
- Lee Guy,
  Independent advisor
  resigned with effect from 13 February 2024
- Kim Lazaroo,
  Managing Director, Morgan Stanley
- Lucrezia Reichlin,
  University Professor
  resigned with effect from 31 May 2023
- Paula Smith,
  Independent advisor
  appointed with effect from 1 January 2024

Frankfurt am Main, 16 April 2024

Morgan Stanley Europe SE

The Management Board

Oliver Behrens (Chair)	David Best
Martin Borghetto	Emmanuel Goldstein
Philipp Lingnau	André Munkelt
Dr. Jana Währisch	

INDEPENDENT AUDITOR'S REPORT

To Morgan Stanley Europe SE, Frankfurt am Main

REPORT ON THE AUDIT OF THE ANNUAL FINANCIAL STATEMENTS AND MANAGEMENT REPORT

Audit Opinion

We have audited the annual financial statements of Morgan Stanley Europe SE, Frankfurt am Main, which comprise the balance sheet as of 31 December 2023, the income statement for the financial year from 1 January 2023 to 31 December 2023, and the notes to the financial statements, including a summary of significant accounting policies. In addition, we have audited the management report of Morgan Stanley Europe SE, Frankfurt am Main, for the financial year from 1 January 2023 to 31 December 2023. In accordance with the German legal requirements, we have not audited the content of the non-financial disclosure report of Morgan Stanley Europe Holding SE, Frankfurt am Main, which is referred to in the section "Disclosures pursuant to Section 340a (1a) HGB in conjunction with Section 289b (2) HGB" and in the “Climate and Environmental Risk Management” Section within the risk report of the management report.

In our opinion on the basis of the knowledge obtained in the audit,

- the accompanying annual financial statements comply, in all material respects, with the requirements of German commercial law and give a true and fair view of the assets, liabilities and financial position of the Company as at 31 December 2023 and of its financial performance for the financial year from 1 January 2023 to 31 December 2023 in compliance with German Principles of Proper Accounting, and
- the accompanying management report as a whole provides an appropriate view of the Company's position. In all material respects, this management report is consistent with the annual financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our audit opinion to the management report does not cover the content of the aforementioned non-financial disclosure report as well as the information cross-referenced in the “Climate and Environmental Risk Management” Section within the risk report of the management report.

Pursuant to Section 322 (3) sentence 1 German Commercial Code (“HGB”), we declare that our audit has not led to any reservations relating to the legal compliance of the annual financial statements and of the management report.

Basis for Audit Opinion

We conducted our audit of the annual financial statements and of the management report in accordance with Section 317 HGB and the EU Audit Regulation (No. 537/2014; referred to subsequently as “EU Audit Regulation”) and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [in Deutschland] (IDW). Our responsibilities under those requirements and principles are further described in the section “Auditor's Responsibilities for the Audit of the Annual Financial Statements and of the Management Report” of our audit report. We are independent of the Company in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) lit. f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion on the annual financial statements and on the management report.

Key audit matters in the audit of the financial statements

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the annual financial statements for the financial year from 1 January 2023 to 31 December 2023. These matters were addressed in the context of our audit of the annual financial statements as a whole and in forming our audit opinion thereon; we do not provide a separate audit opinion on these matters.

In the following, we present the key audit matter of determining the fair value of assets and liabilities held for trading portfolio in the level 3 category.

Our presentation of these key audit matters has been structured as follows:

a. description (including reference to corresponding information in the annual financial statements)

b. audit procedures

Determination of the fair value of level 3 financial instruments that are held with a trading intent held for trading in the level 3category

a. The core business of Morgan Stanley Europe SE is, among other financial services, client-induced trading in financial instruments for its own account. The assets (EUR 41,462 million) and liabilities (EUR 34,582 million) arising from this business activity amount to EUR 76,044 million after offsetting as of 31 December 31 2023. An amount that is not considered to be immaterial relates to assets and liabilities in the trading portfolio for which significant valuation input parameters were not observable in the reporting period (level 3 category). These are reported by the Company in the trading portfolio on the asset or liability side of the balance sheet and are measured at fair value less a risk discount. Due to the provisions of section 340c of the German Commercial Code (HGB) and the associated recognition of unrealised gains and losses, measurement at fair value not only has a direct impact on the Bank's net assets but also on its earnings.

   For financial instruments for which there is no active market and therefore no observable price-determining parameters, the fair value must be determined on the basis of model prices using unobservable parameters ("level 3"). The characteristics of the unobservable inputs used represent assumptions or estimates made by management with respect to the valuation assumptions that would be used by market participants in pricing these assets and liabilities.

   In our view, the determination of fair values for financial instruments classified as level 3 is of particular importance because the assumptions or estimates are based on the judgement of the Company's management and involve inherent and significant estimation uncertainty for financial reporting purpose.

   The disclosures by the Company's legal representatives on the accounting policies for the trading portfolio are included in Annex No. 3.

b. As part of our audit of the annual financial statements, we obtained an understanding of the valuation models used by the Company to determine the fair value of level 3 financial instruments. We also assessed the extent to which the approach was influenced by subjectivity, complexity or other inherent risk factors.

   We identified the controls implemented by the Company for the fair value measurement and assessed their adequacy and operating effectiveness. For this purpose, we assessed, among other things, the appropriateness of the models and input factors used, and their consistent and proper processing. We also considered the relevant business organization and IT systems. Processes and controls that uniformly affect the entire Morgan Stanley Group are performed by a shared service centre and audited by the auditors of the Morgan Stanley Group. We have used their work as part of the audit of the annual financial statements.

   In addition, we have utilised the following substantive audit procedures of the consolidated financial statements auditor with regard to the determination of fair value for individual financial instruments of the category "level 3":

   – Carrying out a so-called back-testing for the fair values estimated by management of selected level 3 instruments for which events or transactions have taken place after the measurement date.

   – Independent fair value estimation for selected level 3 structured transactions. For these transactions, we have checked whether the assumptions made by management and the input parameters used are in line with the Company's valuation guidelines.

– Audit of income from fair value measurement for selected level 3 financial instruments. For individual transactions, we have made independent estimates of fair value to verify that the assumptions made by management and the underlying input parameters are consistent with the Company's valuation policies.

– Review of the continuous application of the material and non-observable valuation assumptions made by management for the purpose of determining fair values.

Other Information

The Management Board and the Supervisory Board are responsible for the other information. The other information comprises:

- the report of the Supervisory Board, which is not expected to be made available to us until after the date of this auditor's report;
- the separate non-financial disclosure report of Morgan Stanley Europe Holding SE, Frankfurt am Main, reffered to in the section "Disclosures pursuant to Section 340a (1a) HGB in conjunction with Section 289b (2) HGB" of the management report;
- all other parts of the published annual report;
- but not the annual financial statements, the contents of the audited disclosures in the management report, and our audit opinion thereon.

Supervisory Board is responsible for the report of the Supervisory Board. Management Board is responsible for all other information.

Our audit opinions on the annual financial statements and on the management report do not cover the other information and, consequently, we do not express an audit opinion or any other form of assurance conclusion thereon.

In connection with our audit, we have a responsibility to read the other information identified above and, in doing so, to consider whether the other information:

- is materially inconsistent with the annual financial statements, the contents of the audited disclosures in the management report, or our knowledge obtained in the audit or
- otherwise appears to be materially misstated.

Responsibility of the Management Board and the Supervisory Board for the annual financial statements and the management report

The Management Board is responsible for the preparation of the annual financial statements that comply in all material respects with the requirements of German commercial law regulations, and that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Company in compliance with German Principles of Proper Accounting. In addition, the Management Board is responsible for the internal controls which they, in accordance with German Legally Required Accounting Principles, have determined necessary to enable the preparation of annual financial statements that are free from material misstatement, whether due to fraud (i.e. fraudulent financial reporting or the misappropriation of assets) or error.

In preparing the annual financial statements, the Management Board is responsible for assessing the Company's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on going concern basis of accounting, provided no actual or legal circumstances conflict therewith.

Furthermore, the Management Board is responsible for the preparation of the management report that provides an overall appropriate view of the Company's position and is, in all material respects, consistent with the annual financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In Addition, the Management Board is responsible for the safeguards and measures (systems) that they have considered necessary to enable the preparation of a management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the management report.

The Supervisory Board is responsible for overseeing the Company's financial reporting process for the preparation of the annual financial statements and the management report.

Auditor's Responsibilities for the audit of the annual financial statements and management report

Our objective is to obtain reasonable assurance about whether the annual financial statements as a whole are free from material misstatements, whether due to fraud or error, and whether the management report provides an overall appropriate view of the Company's position and, in all material respects, is consistent with the annual financial statements and the knowledge obtained in the audit, complies with the German legal requirements, and appropriately presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our audit opinions on the annual financial statements and on the management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Section 317 HGB, the EU Audit Regulation as well as the German Generally Accepted Standards for Financial Statement Audits promulgated by IDW will always detect a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these annual financial statements and this management report.

We exercise professional judgment and maintain professional scepticism throughout the audit. In addition, we

- identify and assess the risks of material misstatements in the annual financial statements and the management report, whether due to fraud or error, design and perform audit procedures responsive to those risks and obtain audit evidence that is sufficient and appropriate to provide a basis for our audit opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, and/or the override of internal controls.
- obtain an understanding of the internal control system relevant to the audit of the annual financial statements and of arrangement and measures relevant to the audit of the management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an audit opinion on the effectiveness of these systems of the Company.
- evaluate the appropriateness of accounting policies used by the Management Board and the reasonableness of estimates made by the Management Board and related disclosures.
- conclude on the appropriateness of the Management Board's use of the going-concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the annual financial statements and in the management report or, if such disclosures are inadequate, to modify our respective audit opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to be able to continue as a going concern.
- evaluate the overall presentation, structure and content of the annual financial statements, including the disclosures, and whether the annual financial statements present the underlying transactions and events in a manner that the annual financial statements give a true and fair view of net assets, financial position and results of operations of the Company in compliance with German Principles of Proper Accounting.
- obtain sufficient appropriate audit evidence regarding the accounting information of the entity or its divisions to express opinions on the financial statements and the management report. We are responsible for the direction, supervision and performance of the audit. We bear sole responsibility for our audit opinions.
- evaluate the consistency of the management report with the annual financial statements,

its conformity with the law, and the view of the Company's position it provides.

- perform audit procedures on the prospective information presented by the Management Board in the management report. On the basis of sufficient appropriate audit evidence, we evaluate in particular the significant assumptions used by the Management Board as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate audit opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in the internal control system that we identify during our audit.

We provide those charged with governance with a statement that we have complied with the relevant independence requirements and communicate with them all relations and other matters that may reasonably be thought to impact our independence, and, where applicable, the actions taken to eliminate threats of independence or the protective measures taken.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the annual financial statements for the current reporting period and are therefore the key audit matters. We describe these matters in the auditor's report unless law or regulation precludes the public disclosure about the matter.

OTHER LEGAL AND REGULATORY REQUIREMENTS

Further information according to Article 10 EU Audit Regulation

We were elected as auditor by the Annual General Meeting on 2 May 2023. We were engaged by the Supervisory Board on 30 October 2023. We have been the auditor of Morgan Stanley Europe SE, Frankfurt am Main, without interruption since the financial year 2018 and statutory auditors since the financial year 2019.

We declare that the audit opinion expressed in this audit report is in line with the additional report to the audit committee pursuant to Article 11 of the EU Audit Regulation (Long-form Audit Report).

In addition to the financial statement audit, we have provided to the audited Company or its controlled entities the following services that are not disclosed in the annual financial statements or in the management report:

- Morgan Stanley Europe SE: Audit pursuant to Section 89 (1) WpHG (Securities Trading Act)
- Morgan Stanley Europe SE: Agreed upon procedures to fulfill the reporting obligations to the National Resolution Authority for the calculation of the 2021, 2022, 2023 and 2024 annual contribution to the Single Resolution Fund.
- Morgan Stanley Europe SE: Examination to obtain limited security in relation to the statements of the legal representatives according to 17 C.F.R. Section 240.18a-7 of the Securities Exchange Act of 1934 according to AICPA standards.
- Morgan Stanley Europe SE: Audit of consolidated financial information in accordance with IDW PS480, which were prepared in accordance with accounting principles to meet the requirements of banking supervisory law.
- Morgan Stanley Bank AG: Audit pursuant to Section 89 (1) WpHG (Securities Trading Act)
- Morgan Stanley Bank AG: Agreed upon procedures to fulfill the reporting obligations to the National Resolution Authority for the calculation of the 2021, 2022, 2023 and 2024 annual contribution to the Single Resolution Fund.

RESPONSIBLE AUDITOR

The German Public Auditor responsible for the engagement is Martin Kopatschek.

Frankfurt am Main, 18 April 2024

Deloitte GmbH

Wirtschaftsprüfungsgesellschaft

signed: Martin Kopatschek
Wirtschaftsprüfer (German Public Auditor)

signed: Kevin Vogt
Wirtschaftsprüfer (German Public Auditor)

Report of the Supervisory Board in accordance with Section 171 (2) of the German Stock Corporation Act (AktG)

In 2023, the Supervisory Board of Morgan Stanley Europe SE (the "Company") had a strong focus on the development and business activities of the Company through the provision of financial services. There were seven Supervisory Board meetings that took place during 2023. The Supervisory Board discussed fundamental aspects of the corporate planning, business policy, business development, risk situation and risk management with the Management Board. At the Supervisory Board meetings and whenever required, the Management Board regularly reported comprehensively and promptly on all incidents of significant importance and on the development of the financial figures.

The Management Board of Morgan Stanley Europe SE provided the Supervisory Board with the annual financial statements and management report for the financial year 2023 without delay after their preparation. The financial statements consist of:

- Balance sheet,
- Income statement,
- Cash flow statement and
- Notes.

The Management Board therefore carried out its obligations in accordance with section 170 (1) AktG. At the same time, the Supervisory Board was presented with the Proposal for the Profit Allocation in accordance with section 170 (2) AktG at the Annual General Meeting. This proposal provides for the net profit of € 83.950.552,76 to be allocated to other revenue reserves.

The Supervisory Board examined the documentation submitted in accordance with section 171 (1) AktG. The Auditor's information was included into the examination. The examination has not led to any reservations.

The Supervisory Board subsequently approved the annual financial statements for the financial year 2023. As a result, the annual financial statements of Morgan Stanley Europe SE were determined in accordance with section 172 AktG.

The statutory auditors, Deloitte GmbH Wirtschaftsprüfungsgesellschaft, Frankfurt am Main, have issued an unqualified audit opinion for the annual financial statement and the Management Report

23 April 2024

Frank Mattern (Chairman)