Registered number: 35857

Registered office:
47 Esplanade
St. Helier
JE1 0BD
Jersey

MORGAN STANLEY FINANCE II LIMITED

Report and interim financial statements

30 June 2022

CONTENTS **PAGE**

DIRECTORS' REPORT

The Directors present their report and condensed interim financial statements (which comprise the condensed statement of comprehensive income, the condensed statement of changes in equity, the condensed statement of financial position, the condensed statement of cash flows, and the related notes, 1 to 11) for Morgan Stanley Finance II Limited (the "Company") for the period ended 30 June 2022.

RESULTS AND DIVIDENDS

The loss for the period, after tax, was $49,000 (period ended June 2021: $3,000 profit).

During the period, no dividends were paid or proposed (year ended December 2021: $nil).

PRINCIPAL ACTIVITY

The principal activity of the Company is the issuance of financial instruments and the hedging of the obligations arising pursuant to such issuances.

The Company's ultimate parent undertaking and controlling entity is Morgan Stanley, which, together with the Company and Morgan Stanley's other subsidiary undertakings, form the "Morgan Stanley Group".

BUSINESS REVIEW

Business environment

During 2022, the Company has continued to monitor the factors in the global environment which impact its performance and financial stability. In particular, the war in Ukraine introduced risks and uncertainties that may adversely affect the results and operations of the Company. Other factors which the Company continues to monitor are continued inflation and rising interest rates.

Escalation of War in Ukraine

The Company is monitoring the war in Ukraine and its impact on both the Ukrainian and Russian economies, as well as related impacts on other world economies and the financial markets. The Company's direct exposure to both Russia and Ukraine remains limited.

Inflationary environment

The global economic and geopolitical environment during the period, which has been characterised by continued inflation, rising interest rates and commodity prices and volatility in global financial markets, had a limited impact on the Company.

DIRECTORS' REPORT

BUSINESS REVIEW (CONTINUED)

Overview of period to June 2022

The condensed statement of comprehensive income is set out on page 9. The loss for the period is $49,000, which primarily represents interest expense for the period (period ended June 2021: $3,000 profit). The net result from financial instruments at fair value through profit and loss for the period is $nil (period ended June 2021: $nil) which is consistent with the Company's principal activity.

The condensed statement of financial position is set out on page 11. Total assets and total liabilities at 30 June 2022 were $653,747,000 (year ended December 2021: $313,895,000) and $653,317,000 (year ended December 2021: $313,416,000) respectively. The increase in total assets and total liabilities from 31 December 2021 is due to the issuance of structured notes, classified in financial liabilities designated at fair value through profit or loss, and the related hedging instruments, classified in financial assets and financial liabilities held mandatorily at fair value through profit or loss.

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

The risk management section below sets out the Company's and the Morgan Stanley Group's policies for the management of liquidity and cash flow risk and other significant business risks.

Risk management

The Directors consider that the Company's key financial risks are credit risk, primarily its concentration of exposure to other Morgan Stanley Group undertakings and liquidity risk. The Company leverages the Morgan Stanley Group's credit and liquidity risk frameworks to identify, measure, monitor and control credit risk and to ensure that the Company has access to adequate funding.

The Company also has some limited exposure to country, operational and legal, regulatory and compliance risks.

The Company leverages the risk management policies and procedures of the Morgan Stanley Group.

Note 9 provides more detailed qualitative disclosures on the Company's exposure to financial risks in addition to narrative disclosures on exposure to operational risk.

Going Concern

Business risks associated with the uncertain market and economic conditions are being actively monitored and managed by the Company. Retaining sufficient capital and liquidity to withstand these market pressures remains central to the Company's strategy. In particular, the Company's capital and liquidity is deemed sufficient to exceed regulatory minimums under both a normal and in a stressed market environment, including the current and potential stresses of the war in Ukraine for the foreseeable future. The existing and potential effects of the war in Ukraine on the business of the Company have been considered as part of the going concern analysis, including impact on operational capacity, access to liquidity and capital, contractual obligations, asset valuations and other critical accounting judgements and key sources of estimation uncertainty.

Taking all of these factors into consideration, the Directors believe it is reasonable to assume that the Company will have access to adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the condensed interim financial statements.

DIRECTORS' REPORT

DIRECTORS

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

Z Dewhurst	Director
H Herrmann	Director
S Kearns	Director

Approved by the Board and signed on its behalf by

Director

28 September 2022

DIRECTORS' RESPONSIBILITIES STATEMENT

The Directors, the names of whom are set out below, confirm that to the best of their knowledge:

(a) the condensed set of interim financial statements has been prepared in accordance with International Accounting Standard ("IAS") 34 'Interim Financial Reporting' as adopted by the European Union ("EU"), give a true and fair view of the assets, liabilities, financial position and result of the Company; and

(b) the interim management report includes a fair review of the important events that have occurred during the period and their impact on the condensed set of interim financial statements, and a description of the principal risks and uncertainties for the remaining six months of the financial year.

Approved by the Board and signed on its behalf by

Director

28 September 2022

Board of Directors

Z Dewhurst	Director
H Herrmann	Director
S Kearns	Director

INDEPENDENT REVIEW REPORT TO MORGAN STANLEY FINANCE II LIMITED

Conclusion

We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2022 which comprises the condensed statement of comprehensive income, the condensed statement of changes in equity, the condensed statement of financial position, the condensed statement of cash flows and related notes 1 to 11.

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2022 is not prepared, in all material respects, in accordance with International Accounting Standard 34 'Interim Financial Reporting', as adopted by the EU.

Basis for Conclusion

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Financial Reporting Council for use in the United Kingdom. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

As disclosed in note 2, the Company prepares its interim financial statements in accordance with International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board ("IASB") as adopted by the European Union ("EU"). Interpretations issued by the IFRS Interpretations Committee ("IFRIC") and Companies (Jersey) Law 1991. The condensed interim financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34 'Interim Financial Reporting', as adopted by the EU.

Conclusion Relating to Going Concern

Based on our review procedures, which are less extensive than those performed in an audit as described in the Basis for Conclusion section of this report, nothing has come to our attention to suggest that the directors have inappropriately adopted the going concern basis of accounting or that the directors have identified material uncertainties relating to going concern that are not appropriately disclosed.

This conclusion is based on the review procedures performed in accordance with this ISRE (UK and Ireland), however future events or conditions may cause the entity to cease to continue as a going concern.

Responsibilities of the directors

The directors are responsible for the preparation and presentation of this interim financial information in accordance with International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board ("IASB") as adopted by the European Union ("EU"), Interpretations issued by the IFRS Interpretations Committee ("IFRIC") and Companies (Jersey) Law 1991.

In preparing the half-yearly financial report, the directors are responsible for assessing the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the review of the financial information

In reviewing the half-yearly financial report, we are responsible for expressing to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report. Our conclusion, including our Conclusions Relating to Going Concern, are based on procedures that are less extensive than audit procedures, as described in the Basis for Conclusion paragraph of this report.

INDEPENDENT REVIEW REPORT TO MORGAN STANLEY FINANCE II LIMITED

Use of our report

This report is made solely to the company in accordance with International Standard on Review Engagements (UK and Ireland) 2410 “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Financial Reporting Council. Our work has been undertaken so that we might state to the company those matters we are required to state to it in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company, for our review work, for this report, or for the conclusions we have formed.

Deloitte LLP

Deloitte LLP
Statutory Auditor
London
28 September 2022

CONDENSED STATEMENT OF COMPREHENSIVE INCOME
Six months ended 30 June 2022

	Note	(Unaudited) Six months ended 30 June 2022 $'000	(Unaudited) (Restated) Six months ended 30 June 2021 $'000
Net trading expense on financial assets		(59,488)	(5,434)
Net trading expense on financial liabilities		(28,447)	-
Net trading expense		(87,935)	(5,434)
Net income/(expense) on other financial assets held at fair value		68	(171)
Net income on other financial liabilities held at fair value		87,867	5,605
Net income on other financial instruments held at fair value	3	87,935	5,434
Interest income	4	-	3
Interest expense	4	(48)	-
Net interest (expense)/ income		(48)	3
Non-interest expense		(1)	-
(LOSS)/ PROFIT BEFORE INCOME TAX		(49)	3
Income tax	5	-	-
(LOSS)/ PROFIT AND TOTAL COMPREHENSIVE INCOME FOR THE PERIOD		(49)	3

All results were derived from continuing operations.

The notes on pages 13 to 22 form an integral part of the condensed interim financial statements.

CONDENSED STATEMENT OF CHANGES IN EQUITY
Six months ended 30 June 2022

	Stated capital $'000	Retained earnings $'000	Total equity $'000
Balance at 1 January 2021 (unaudited)	14	469	483
Profit and total comprehensive income for the period (unaudited)	-	3	3
Balance at 30 June 2021 (unaudited)	14	472	486
Balance at 1 January 2022	14	465	479
Loss and total comprehensive Loss for the period (unaudited)	-	(49)	(49)
Balance at 30 June 2022 (unaudited)	14	416	430

The notes on pages 13 to 22 form an integral part of the condensed interim financial statements.

MORGAN STANLEY FINANCE II LIMITED

Registered number: 35857

CONDENSED STATEMENT OF FINANCIAL POSITION
As at 30 June 2022

	Note	(unaudited) As at 30 June 2022 $'000	(audited) As at 31 December 2021 $'000
ASSETS			
Cash and short-term deposits	6	686	981
Loans and advances	6	650,099	311,810
Trading financial assets	6	2,962	1,104
TOTAL ASSETS		653,747	313,895
LIABILITIES AND EQUITY			
LIABILITIES			
Trading financial liabilities	6	148,533	55,308
Debt and other borrowings	7	504,784	258,108
TOTAL LIABILITIES		653,317	313,416
EQUITY			
Stated capital		14	14
Retained earnings		416	465
Equity attributable to owners of the Company		430	479
TOTAL EQUITY		430	479
TOTAL LIABILITIES AND EQUITY		653,747	313,895

These condensed financial statements were approved by the Board and authorised for issue on 28 September 2022.

Signed on behalf of the Board

Director

The notes on pages 13 to 22 form an integral part of the condensed interim financial statements.

CONDENSED STATEMENT OF CASH FLOWS
Six months ended 30 June 2022

	(unaudited) Six months ended 30 June 2022 $'000	(unaudited) Six months ended 30 June 2021 $'000
OPERATING ACTIVITIES		
(Loss)/ Profit for the period	(49)	3
Adjustments for:		
Interest expense/(income)	48	(3)
Operating cash flows before changes in operating assets and liabilities	(1)	-
Changes in operating assets:		
(Increase) in loans and advances	(338,289)	(256,676)
(Increase) in trading financial assets	(1,858)	-
	(340,147)	(256,676)
Changes in operating liabilities:		
Increase in debt and other borrowings	246,628	251,166
Increase in trade and other payables	-	250
Increase in trading financial liabilities	93,225	5,514
	339,853	256,930
NET CASH FLOWS FROM OPERATING ACTIVITIES	(295)	254
NET (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS	(295)	254
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	981	-
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	686	254

The notes on pages 13 to 22 form an integral part of the condensed interim financial statements.

1. CORPORATE INFORMATION

The Company is incorporated and domiciled in Jersey, at the following address 47 Esplanade, St. Helier, Jersey, JE1 0BD. The Company engaged in the issuance of financial instruments and the hedging of the obligations arising pursuant to such issuances.

The Company's immediate parent undertaking, ultimate undertaking and controlling entity is Morgan Stanley, which, together with the Company and Morgan Stanley's other subsidiary undertakings, form the Morgan Stanley Group. Morgan Stanley is incorporated in the State of Delaware, in the United States of America. Copies of its financial statements can be obtained from www.morganstanley.com/investorrelations.

2. BASIS OF PREPARATION

Statement of compliance

The Company prepares its interim financial statements in accordance with International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board ("IASB") as adopted by the European Union ("EU"). Interpretations issued by the IFRS Interpretations Committee ("IFRIC") and Companies (Jersey) Law 1991. The condensed interim financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34 *'Interim Financial Reporting'*, as adopted by the EU.

In preparing these condensed interim financial statements, the Company has applied consistently the accounting policies and methods of computation used in the Company's annual financial statements for the year ended 31 December 2021, except where otherwise stated.

New standards and interpretations adopted during the period

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

As part of the 2018-2020 Annual Improvements Cycle published in May 2020, the IASB made an amendment to IFRS 9 *'Financial Instruments'*, relating to the treatment of fees in the assessment of whether financial liabilities are modified or exchanged, where such transactions occur on or after 1 January 2022. Early application is permitted. The amendments were endorsed by the EU in March 22.

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

New standards and interpretations not yet adopted

At the date of authorisation of these condensed interim financial statements, the following amendments to standards relevant to the Company's operations have been issued by the IASB but were not mandatory for accounting periods beginning 1 January 2022. The Company does not expect that the adoption of the following amendments to standards will have a material impact on the Company's condensed interim financial statements.

Amendments to IAS 1 *'Presentation of Financial Statements'*: Classification of Liabilities as Current or Non-current were issued by the IASB in January 2020 and revised in July 2020, for retrospective application in accounting periods beginning on or after 1 January 2023.

2. BASIS OF PREPARATION (CONTINUED)

New standards and interpretations not yet adopted (continued)

Amendments to IAS 8 *'Accounting Policies, Changes in Accounting Estimates and Errors'*: Definition of Accounting Estimates were issued by the IASB in February 2021, for prospective application in accounting periods beginning on or after 1 January 2023. Early application is permitted.

Amendments to IAS 1 *'Presentation of Financial Statements'*: Disclosure of Accounting Policies were issued by the IASB in February 2021, for prospective application in accounting periods beginning on or after 1 January 2023. Early application is permitted.

Amendments to IAS 12 *'Income taxes'*: Deferred tax related to Assets and Liabilities arising from a Single Transaction' were issued by the IASB in May 2021, for prospective application in accounting periods beginning on or after 1 January 2023. Early application is permitted.

Critical accounting judgements and key sources of estimation uncertainty

In preparing the condensed interim financial statements, the Company makes judgements and estimates that affect the application of accounting policies and reported amounts.

Critical accounting judgements are key decisions made by management in the application of the Company's accounting policies, other than those involving estimations, which have the most significant effects on the amounts recognised in the condensed interim financial statements.

Key sources of estimation uncertainty represent assumptions and estimations made by management that have a significant risk of resulting in a material adjustment to the carrying amount of assets and liabilities within the next financial year.

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

The going concern assumption

The Company's business activities, together with the factors likely to affect its future development, performance and position, are reflected in the Business review section of the Directors' report on pages 3 to 4. In addition, the notes to the condensed interim financial statements include the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments; and its exposures to credit risk and liquidity risk.

The existing and potential effects of war in Ukraine on the operational capacity of the business, access to liquidity and capital have been considered on pages 3 to 4.

As set out in the Strategic report, retaining sufficient liquidity and capital to withstand market pressures remains central to the Morgan Stanley Group's and the Company's strategy.

Taking the above factors into consideration, the Directors believe that the Company will have access to adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the interim Directors' report and condensed interim financial statements.

2. BASIS OF PREPARATION (CONTINUED)

Restatement of comparative amounts

The financial statements include a prior period restatement relating to the condensed Statement of Comprehensive Income presentation of gains and losses on trading and other financial instruments. The restated presentation appropriately reflects the gross components of net revenue. The restatement resulted in a $5,491,000 increase in both Net income on other financial instruments held at fair value and Net trading expense. The restatement had no impact to the Company's condensed Statement of Financial Position or net results in the condensed Statement of Comprehensive Income.

The Company has also presented additional line items in the condensed Statement of Comprehensive Income which are considered relevant to the understanding of its financial performance.

Net trading expense

- Net trading income/(expense) derived from financial assets have been presented separately from the net trading expense derived from financial liabilities.

Net income on financial instruments held at fair value

- Net income/(expense) on other financial assets held at fair value have been presented separately from the net income on financial liabilities held at fair value.

The comparative period amounts have been revised to enhance comparability with the current period presentation.

3. NET INCOME ON OTHER FINANCIAL INSTRUMENTS HELD AT FAIR VALUE

	(unaudited) Six months ended 30 June 2022	(unaudited) Six months ended 30 June 2021
	$'000	**$'000**
Net income/(expense) on:		
Financial assets designated at FVPL:		
Loans and advances:		
Loans	68	(171)
Financial liabilities designated at FVPL:		
Debt and other borrowings:		
Issued structured notes	87,867	5,605
	87,935	**5,434**

4. INTEREST INCOME/EXPENSE

All interest income relates to financial assets at amortised cost and is calculated using the EIR method.

5. INCOME TAX

The company is subject to Jersey income tax at the rate 0.00% (2021: 0.00%).

6. FINANCIAL ASSETS AND FINANCIAL LIABILITIES BY MEASUREMENT CATEGORY

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

30 June 2022	FVPL (mandatorily) $'000	FVPL (designated) $'000	Amortised cost $'000	Total $'000
Cash and short-term deposits	-	-	686	686
Loans and advances:				
Loans	-	650,099	-	650,099
Trading financial assets				
Derivatives	2,962	-	-	2,962
Total financial assets	2,962	650,099	686	653,747
Trading financial liabilities:				
Derivatives	148,533	-	-	148,533
Debt and other borrowings:				
Issued Structured Notes	-	501,841	-	501,841
Loans	-	-	2,943	2,943
Total financial liabilities	148,533	501,841	2,943	653,317

31 December 2021	FVPL (mandatorily) $'000	FVPL (designated) $'000	Amortised cost $'000	Total $'000
Cash and short-term deposits	-	-	981	981
Loans and advances:				
Loans	-	311,810	-	311,810
Trading financial assets:				
Derivatives	1,104	-	-	1,104
Total financial assets	1,104	311,810	981	313,895
Trading financial liabilities:				
Derivatives	55,308	-	-	55,308
Debt and other borrowings:				
Issued Structured Notes	-	257,583	-	257,583
Loans	-	-	525	525
Total financial liabilities	55,308	257,583	525	313,416

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

Financial assets and financial liabilities designated at FVPL

The financial assets and financial liabilities shown in the tables above which are designated at FVPL consist primarily of the following financial assets and financial liabilities:

Issued Structured Notes: These relate to financial liabilities which arise from selling structured products generally in the form of notes, certificates and warrants. These instruments contain an embedded derivative which significantly modifies the cash flows of the issuance. The return on the instrument is linked to an underlying that is not clearly and closely related to the debt host including, but not limited to, equity-linked notes. These Structured Notes are designated at FVPL as the risks to which the Company is a contractual party are risk managed on a fair value basis as part of the Company's trading portfolio and the risk is reported to key management personnel on this basis.

Loans: These are loans to other Morgan Stanley Group undertakings that, along with the derivative contracts classified as mandatorily at FVPL, are part of the hedging strategy for the obligations arising pursuant to the issuance of the Structured Notes. These loans are designated at FVPL to eliminate or significantly reduce an accounting mismatch which would otherwise arise.

The Company determines the amount of changes in fair value attributable to changes in counterparty credit risk or own credit risk, as relating to financial assets and financial liabilities designated at FVPL, by first determining the fair value including the impact of counterparty credit risk or own credit risk, and then deducting those changes in fair value representing managed market risk. In determining fair value, the Company considers the impact of changes in own credit spreads based upon observations of the secondary bond market spreads when measuring the fair value for issued structured notes. The Company considers that this approach most faithfully represents the amount of change in fair value due to both counterparty credit risk and the Company's own credit risk.

The carrying amount of financial liabilities held at fair value was equal to the contractual amount due at maturity (31 December 2021: $48,000 higher).

At initial recognition of a specific structured note issuance program, the Company's issuance process, and any planned hedging structure relating to the issuance of those structured notes, has been considered, to determine whether the presentation of fair value changes attributable to credit risk of those structured notes through other comprehensive income would create or enlarge an accounting mismatch in the condensed statement of comprehensive income. If financial instruments, such as derivatives and corporate loans, measured at fair value for which changes in fair value incorporating counterparty credit risk are reflected within the condensed statement of comprehensive income, are traded to economically hedge the structured note issuances in full, the fair value incorporating any counterparty credit risk arising on the hedging instruments may materially offset any DVA applied to structured notes, where the counterparties of the hedging instruments are part of the Morgan Stanley Group. In such cases, the DVA of those structured notes is not reflected within other comprehensive income, and instead is presented in the condensed statement of comprehensive income.

7. DEBT AND OTHER BORROWINGS

	30 June 2022 $'000	31 December 2021 $'000
Debt and other borrowings		
Issued structured notes (designated FVPL)	501,841	257,583
Loans (amortised cost)	2,943	525
	504,784	258,108

Refer to note 6 for details of issued Structured Notes included within debt and other borrowings designated at FVPL.

8. SEGMENT REPORTING

Segment information is presented in respect of the Company's business and geographical segments.

Business segments

Morgan Stanley structures its business segments primarily based upon the nature of the financial products and services provided to customers and Morgan Stanley's internal management structure. The Company's own business segments are consistent with those of Morgan Stanley.

The Company has one reportable business segment, Institutional Securities, which provides financial services to financial institutions. Its business includes the issuance of financial instruments and the hedging of the obligations arising pursuant to such issuances.

Geographical segments

The Company operates in two geographic regions being the Americas and Asia.

The following table presents selected statement of financial position information of the Company's operations by geographic area. The total assets disclosed in the following table reflect the regional view of the Company's operations, on a managed basis. The attribution of total assets is determined by trading desk location.

	Americas		Asia		Total	
	30 June 2022 $'000	31 December 2021 $'000	30 June 2022 $'000	31 December 2021 $'000	30 June 2022 $'000	31 December 2021 $'000
Assets	641,082	312,466	12,665	1,429	653,747	313,895

9. RISK MANAGEMENT

Risk management procedures

The Company's risk management procedures are consistent with those disclosed in the Company's 2021 annual financial statements. This disclosure is limited to quantitative data for each risk category and should be read in conjunction with the risk management procedures detailed in note 13 of the Company's 2021 annual financial statements.

9. RISK MANAGEMENT (CONTINUED)

Credit risk

Credit risk refers to the risk of loss arising when a borrower, counterparty or issuer does not meet its financial obligations to the Company. Primarily its concentration of exposure is to other Morgan Stanley group undertakings.

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

The Company enters into all of its financial asset transactions with other Morgan Stanley Group undertakings, and both the Company and the other Morgan Stanley Group undertakings are wholly owned subsidiaries of the same ultimate parent entity, Morgan Stanley. As a result of the implicit support that would be provided by Morgan Stanley, the Company is considered exposed to the credit risk of Morgan Stanley.

Exposure to credit risk

The maximum exposure to credit risk ("gross credit exposure") of the Company as at 30 June 2022 is the carrying amount of the financial assets held in the condensed statement of financial position. The Company has not entered into any credit enhancements to manage its exposure to credit risk.

The Company does not have any significant exposure arising from items not recognised on the condensed statement of financial position.

Exposure to credit risk by class

Class	**Gross credit exposure (1)**	
	30 June 2022 $'000	**31 December 2021 $'000**
Subject to ECL:		
Cash and short-term deposits	686	981
Not subject to ECL(2):		
Loans and advances	650,099	311,810
Trading financial assets:		
Derivatives	2,962	1,104
	653,747	313,895

(1) The carrying amount recognised in the condensed statement of financial position best represents the Company's maximum exposure to credit risk.
(2) Financial assets measured at FVPL are not subject to ECL.

The Company does not hold financial assets considered to be credit impaired.

9. RISK MANAGEMENT (CONTINUED)

Credit quality

Exposure to credit risk by internal rating grades

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

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

Exposure to credit risk

All gross carrying amounts have an internal rating grade of A. All exposures subject to ECL are Stage 1.

Liquidity risk

Maturity analysis

In the following maturity analysis of financial liabilities, derivative contracts and other trading financial liabilities measured at fair value are presented at fair value, consistent with how these financial liabilities are managed, and disclosed as on demand. Derivatives not held as part of the Company's trading activities and financial liabilities designated at fair value through profit or loss which contain an embedded derivative are disclosed according to their earliest contractual maturity; all such amounts are presented at their fair value, consistent with how these financial liabilities are managed. All other amounts represent undiscounted cash flows payable by the Company arising from its financial liabilities to earliest contractual maturities as at 30 June 2022. Repayments of financial liabilities that are subject to immediate notice are treated as if notice were given immediately and are classified as on demand. This presentation is considered by the Company to appropriately reflect the liquidity risk arising from those financial liabilities, presented in a way that is consistent with how the liquidity risk on these financial liabilities is managed by the Company.

30 June 2022 **$'000**	**On demand**	**Less than 1 year**	**1 year - 2 years**	**2 years - 5 years**	**Total**
Financial assets					
Cash and short-term deposits	686	-	-	-	686
Loans and advances:					
Loans	-	370,966	275,946	3,187	650,099
Trading financial assets					
Derivatives	-	1,460	1,486	16	2,962
Total financial assets	686	372,426	277,432	3,203	653,747
Financial liabilities					
Trading financial liabilities:					
Derivatives	-	122,321	25,686	526	148,533
Debt and other borrowings:					
Issued Structured Notes	-	247,418	251,746	2,677	501,841
Loans	-	-	2,943	-	2,943
Total financial liabilities	-	369,739	280,375	3,203	653,317

9. RISK MANAGEMENT (CONTINUED)

Liquidity risk (continued)

Maturity analysis (continued)

31 December 2021 **$'000**	**On demand**	**Less than 1 year**	**1 year - 2 years**	**2 years - 5 years**	**Total**
Financial assets					
Cash and short-term deposits	981	-	-	-	981
Loans and advances:					
Loans	-	311,810	-	-	311,810
Trading financial assets					
Derivatives	-	1,104	-	-	1,104
Total financial assets	981	312,914	-	-	313,895
Financial liabilities					
Trading financial liabilities:					
Derivatives	-	55,308	-	-	55,308
Debt and other borrowings:					
Issued Structured Notes	-	257,583	-	-	257,583
Loans	-	-	525	-	525
Total financial liabilities	-	312,891	525	-	313,416

Market risk

Equity price sensitivity analysis

The sensitivity analysis below is determined based on the exposure to equity price risk at 30 June 2022 and 31 December 2021.

The market risk related to such equity price risk is measured by estimating the potential reduction in total comprehensive income associated with a 10% decline in the underlying equity price as shown in the table below.

9. RISK MANAGEMENT (CONTINUED)

Market risk (continued)

Equity price sensitivity analysis (continued)

	Impact on total comprehensive income gains/(losses)	
	30 June 2022 $'000	**31 December 2021 $'000**
Trading financial liabilities	(50,478)	(25,758)
Debt and other borrowings	50,478	25,758
	-	-

The Company's equity risk price risk is mainly concentrated on equity securities in the Americas and Asia.

The Company enters into the majority of its financial asset transactions with other Morgan Stanley Group undertakings, where both the Company and the other Morgan Stanley Group undertakings are wholly-owned subsidiaries of the same group parent entity, Morgan Stanley.

The issued Structured Notes expose the Company to the risk of changes in market prices of the underlying securities, interest rate risk and, where denominated in currencies other than US Dollars, the risk of changes in rates of exchange between the Japanese Yen and the other relevant currencies. The Company uses the contracts that it purchases from other Morgan Stanley Group undertakings to hedge the market price, interest rate and foreign currency risks associated with the issuance of the Structured Notes, consistent with the Company's risk management strategy. As such, the Company is not exposed to any net market risk on these financial instruments.

10. ASSETS AND LIABILITIES MEASURED AT FAIR VALUE

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

All financial assets and financial liabilities recognised at fair value on a recurring basis at 30 June 2022 and 31 December 2021 are classified as level 2 (valuation techniques using observable inputs).

The Company's valuation approach and fair value hierarchy categorisation for certain significant classes of financial instruments recognised at fair value on a recurring basis can be found in note 14 of the Company's 2021 annual financial statements.

b. Transfers between Levels of the fair value hierarchy for financial assets and liabilities recognised at fair value on a recurring basis

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

c. Assets and liabilities measured at fair value on a non-recurring basis

Non-recurring fair value measurements of assets and liabilities are those which are required or permitted in the condensed statement of financial position in particular circumstances. There were no assets or liabilities measured at fair value on a non-recurring basis during the period or prior year.

11. ASSETS AND LIABILITIES NOT MEASURED AT FAIR VALUE

For all financial instruments not measured at fair value, the carrying amount is considered to be a reasonable approximation of fair value due to the short-term nature of these assets and liabilities.