MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Introduction

The Company

Morgan Stanley Dean Witter & Co. (the "Company") is a global financial services firm that maintains leading market positions in each of its three business segments—Securities, Asset Management and Credit Services. The Company's Securities business includes securities underwriting and distribution; merger, acquisition, restructuring, real estate, project finance and other corporate finance advisory activities; full-service brokerage and financial advisory services; sales, trading, financing and market-making in equity and fixed income securities, foreign exchange and commodities, and derivatives; and private equity and other principal investing activities. The Company's Asset Management business provides global asset management products and services to individual and institutional investors primarily through Morgan Stanley Dean Witter Advisors, Van Kampen Investments, Morgan Stanley Dean Witter Investment Management and Miller Anderson & Sherrerd. The Company's Credit Services business includes the issuance of the Discover® Card, the Discover Platinum Card, the Morgan Stanley Dean Witter℠ Card and other proprietary general purpose credit cards; and the operation of Discover Business Services, a proprietary network of merchant and cash access locations in the U.S.

The Company's results of operations for the 12 months ended November 30, 2000 ("fiscal 2000"), November 30, 1999 ("fiscal 1999") and November 30, 1998 ("fiscal 1998") are discussed below.

Results of Operations

Certain Factors Affecting Results of Operations

The Company's results of operations may be materially affected by market fluctuations and by economic factors. In addition, results of operations in the past have been, and in the future may continue to be, materially affected by many factors of a global nature, including economic and market conditions; the availability and cost of capital; the level and volatility of equity prices and interest rates; currency values and other market indices; technological changes and events (such as the increased use of the Internet to conduct electronic commerce and the continued development of electronic communications trading networks); the availability and cost of credit; inflation; investor sentiment; and legislative, legal and regulatory developments. Such factors also may have an impact on the Company's ability to achieve its strategic objectives on a global basis, including (without limitation) continued increased market share in its securities activities, growth in assets under management and the expansion of its Credit Services business.

The Company's Securities business, particularly its involvement in primary and secondary markets for all types of financial products, including derivatives, is subject to substantial positive and negative fluctuations due to a variety of factors that cannot be predicted with great certainty, including variations in the fair value of securities and other financial products and the volatility and liquidity of global trading markets. Fluctuations also occur due to the level of global market activity, which, among other things, affects the size, number and timing of investment banking client assignments and transactions and the realization of returns from the Company's private equity and other principal investments. The level of global market activity also could impact the flow of investment capital into mutual funds and the way in which such capital is allocated among money market, equity, fixed income or other investment alternatives, which could cause fluctuations to occur in the Company's Asset Management business. In the Company's Credit Services business, changes in economic variables, such as the number and size of personal bankruptcy filings, the rate of unemployment and the level of consumer debt, may substantially affect consumer loan levels and credit quality, which, in turn, could impact overall Credit Services results.

The Company's results of operations also may be materially affected by competitive factors. Included among the principal competitive factors affecting the Securities business are the quality of its professionals and other personnel, its products and services, relative pricing and innovation. Competition in the Company's Asset Management business is affected by a number of factors, including investment objectives and performance; advertising and sales promotion efforts; and the level of fees, distribution channels and types and quality of services offered. In Credit Services, competition centers on merchant acceptance of credit cards, credit cardmember acquisition and customer utilization of credit cards, all of which are impacted by the type of fees, interest rates and other features offered.

In addition to competition from firms traditionally engaged in the financial services business, there has been increased competition in recent years from other sources, such as commercial banks, insurance companies, online service providers, sponsors of mutual funds and other companies offering financial services both in the U.S. and globally. The financial services industry has continued to experience consolidation and convergence as financial institutions involved in a broad range of financial services industries have merged. This convergence trend is expected to continue and could result in the Company's competitors gaining greater capital and other resources, such as a broader range of products and services and geographic diversity. In addition, the passage of the Gramm-Leach-Bliley Act in the U.S., effectively repealing certain sections of the 1933 Glass-Steagall Act, has allowed commercial banks, securities firms and insurance firms to affiliate, which has accelerated consolidation and may lead to increasing competition in markets which traditionally have been dominated by investment banks and retail securities firms.

The Company also has experienced increased competition for qualified employees in recent years, including from companies engaged in Internet-related businesses and private equity funds, in addition to the traditional competition for employees from the financial services, insurance and management consulting industries. The Company's ability to sustain or improve its competitive position will substantially depend on its ability to continue to attract and retain qualified employees.

As a result of the above economic and competitive factors, net income and revenues in any particular period may not be representative of full-year results and may vary significantly from year to year and from quarter to quarter. The Company intends to manage its business for the long term and to mitigate the potential effects of market downturns by strengthening its competitive position in the global financial services industry through diversification of its revenue sources and enhancement of its global franchise. The Company's overall financial results will continue to be affected by its ability and success in maintaining high levels of profitable business activities, emphasizing fee-based assets that are designed to generate a continuing stream of revenues, evaluating credit product pricing, managing risks in the Securities, Asset Management and Credit Services businesses, and managing costs. In addition, the complementary trends in the financial services industry of consolidation and globalization present, among other things, technological, risk management and other infrastructure challenges that will require effective resource allocation in order for the Company to remain competitive.

The Company believes that technological advancements in the Internet and the growth of electronic commerce will continue to present both challenges and opportunities to the Company and has led to significant changes and innovations in the financial markets and financial services industry as a whole. The Company's initiatives in this area have included Web-enabling existing businesses or enhancing client communication and access to information and services as well as making investments, or otherwise participating, in alternative trading systems, electronic communications networks and related businesses or technologies. The Company expects to continue to augment these initiatives in the future.

Global Market and Economic Conditions in Fiscal 2000

Global market and economic conditions during fiscal 2000 were generally more challenging in comparison with those experienced during the prior fiscal year. During fiscal 1999 and the first half of fiscal 2000, the vigorous pace of global economic expansion frequently gave rise to indications of increasing inflationary pressures. In an effort to mitigate these conditions, several interest rate increases were initiated by major central banks globally, particularly in the U.S. and Europe, which increased corporate and consumer borrowing costs. As a result of the rising global interest rate environment and a sharp rise in the level of energy prices, it appeared more likely that the rate of global economic growth would decelerate in the future. These conditions, coupled with indications of slowing corporate earnings growth, led to difficult conditions in global equity and fixed income securities markets, particularly during the latter half of fiscal 2000. However, despite the presence of less favorable global market and economic conditions, the Company achieved record results in fiscal 2000 as each of its three business segments (Securities, Asset Management and Credit Services) generated record levels of net income. The Company's Securities business benefited from record revenues in its investment banking, equity trading and commodity trading activities and ended the fiscal year with record levels of financial advisors and customer accounts. In the Company's Asset Management business, customer assets under management or supervision increased to record levels during fiscal 2000, while results in the Company's Credit Services business reflected a continued improvement in the credit quality of cardmember receivables as well as record levels of cardmember transaction volume and managed consumer loans (see "Business Segments" herein).

In the U.S., the domestic economy exhibited positive fundamentals and a strong rate of growth during much of fiscal 2000. Several favorable economic trends, such as historically low levels of unemployment, high levels of consumer confidence and spending, strong productivity gains and a high demand for imports, continued to persist. However, throughout fiscal 1999 and the first half of fiscal 2000, the ongoing expansion of the U.S. economy, coupled with a tight domestic labor market, increased fears of accelerating inflation. In an effort to slow the U.S. economy and to mitigate inflationary pressures, the Federal Reserve Board (the "Fed") continued to tighten monetary policy during fiscal 2000 by raising the overnight lending rate on two separate occasions by an aggregate of 0.75%. Between June 1999 and May 2000, the Fed raised the overnight lending rate on six occasions aggregating 1.75%. During the latter half of fiscal 2000, there were indications that the Fed's interest rate actions were beginning to have the desired impact on the U.S. economy. However, the prospects for slower economic growth in the future and its impact on corporate earnings contributed to declines in U.S. financial markets as the major stock market indices (the Standard & Poor's 500, the Dow Jones Industrial Average and the NASDAQ) all were lower at the end of fiscal 2000 than at the beginning of the year. The decline in the market values of Internet and technology stocks and high-yield fixed income securities was particularly significant. The sharp rise in global energy prices, coupled with lingering uncertainty over the resolution of the U.S. presidential election, also contributed to periods of increased volatility in the financial markets during the latter half of fiscal 2000. At fiscal year-end, there remained much uncertainty as to whether the Fed would ease its interest rate policy should the indications of slowing economic growth in the U.S. persist in the future.

Economic conditions within Europe also contributed to periods of heightened volatility in the region's financial markets during fiscal 2000. The rates of economic growth within the U.K. and the European Union (the "EU") were generally strong in the first half of fiscal 2000, although the euro fell to record lows against the U.S. dollar during fiscal 2000 as the growth rate of the U.S. economy continued to outpace the growth rate within the EU. The region's level of economic growth, coupled with the falling value of the euro and the sharp rise in global energy prices, gave rise to fears of accelerating inflation. As a result, during fiscal 2000, the European Central Bank (the "ECB") raised interest rates within the EU on six occasions by an aggregate of 1.75%. The Bank of England also raised interest rates within the U.K. on two occasions by an aggregate of 0.50%. Investor uncertainty as to the region's future growth prospects in light of rising energy prices and a potential slowdown of the U.S. economy contributed to the decline in many of the major stock market indices within the European region during fiscal 2000.

Economic conditions also were challenging in the Far East during fiscal 2000. In Japan, there were indications that the steps taken by its government to increase economic activity, including bank bailouts, emergency loans, stimulus packages and tax cuts for both individuals and corporations, were beginning to have a favorable impact on the nation's economic performance. As a result, during fiscal 2000, the Bank of Japan raised interest rates by 0.25% amid indications of growing business confidence and industrial production. However, Japan's financial markets were adversely impacted by continuing concerns about the nation's banking system, its growing budget deficit and the economy's future growth prospects. Investors also were concerned with the impact of rising energy prices and the potential for a slowdown in the level of global economic growth, which would have an adverse effect on the level of Japan's exports. Certain financial markets elsewhere in the Far East also experienced declines during fiscal 2000, reflecting lower levels of economic activity. In addition, political instability existed within the region, particularly in Thailand, Indonesia and the Philippines, which had an adverse impact on the region's financial markets during the year.

The worldwide market for mergers and acquisitions continued to be robust during fiscal 2000. The volume of global merger and acquisition transactions reached record levels and contributed to record revenues by the Company's investment banking business. The merger and acquisition market reflected ongoing consolidation and globalization, and transaction activity was strong across many industries, particularly in the technology, media and telecommunications sectors. The volume of merger and acquisition transactions was particularly strong during the first half of fiscal 2000, while increased volatility in the financial markets adversely impacted transaction activity in the latter part of the year. During fiscal 2000, the level of cross-border transactions remained strong, although the level of activity in the European merger and acquisition markets declined, reflecting volatility in the region's financial markets and the continued depreciation in the value of the euro.

Similarly, the worldwide market for debt and equity underwriting transactions was generally strong in fiscal 2000, fueled by a need to raise capital to finance merger and acquisition transactions and other strategic initiatives. However, increased uncertainty in the global financial markets significantly reduced transaction volumes during the latter half of fiscal 2000. Declines in the global equity markets led to the postponement or cancellation of many new equity issues, particularly during the fourth quarter of fiscal 2000. Fixed income underwriting activity was negatively affected by the rising global interest rate environment, which increased borrowing costs. The market for new issuances of high-yield fixed income securities was particularly difficult during the latter half of fiscal 2000 as heightened concerns of deteriorating credit quality and rising default rates reduced investor demand for these securities.

In fiscal 2000, U.S. consumer demand and purchases continued to increase at a strong pace. The relatively strong domestic economy that continued to exist in the U.S. for much of the year enabled consumers to manage finances advantageously while still allowing for steady growth in consumer credit. Similarly, the level of loan losses and personal bankruptcies continued to decline.

U.S. economic growth moderated during the latter half of fiscal 2000, reflecting, among other things, the Fed's efforts to slow the rate of economic growth. The Company continued to invest in the growth of its credit card business through the expansion of Discover Business Services, as evidenced by a record number of new merchant enrollments in fiscal 2000, the second consecutive year of achieving record new merchant enrollments. The Company also increased its marketing and solicitation activities with respect to the Discover Card brand, as well as the Morgan Stanley Dean Witter Card in the U.K.

Fiscal 2000 and Fiscal 1999 Results of the Company

The Company achieved record net income of $5,456 million in fiscal 2000, a 14% increase from fiscal 1999. In fiscal 1999, the Company's net income was $4,791 million, an increase of 46% from fiscal 1998. Fiscal 1998's net income included a net gain of $345 million from the sale of the Company's Global Custody business, its interest in the operations of SPS Transaction Services, Inc. ("SPS") and certain BRAVO® Card receivables ("BRAVO") (see "Results of Operations—Business Acquisitions and Dispositions" herein). Fiscal 1998's net income also included a $117 million charge resulting from the cumulative effect of an accounting change. This charge represents the effect of an accounting change adopted in the fourth quarter of fiscal 1998 (effective December 1, 1997) with respect to the accounting for offering costs paid by investment advisors of closed-end funds, where such costs are not specifically reimbursed through separate advisory contracts (see Note 2 to the consolidated financial statements). Excluding the net gain from the sale of the businesses noted above and the charge resulting from the cumulative effect of an accounting change, fiscal 1999's net income increased 57%.

The Company's income tax rate was 36%, 38% and 37% in fiscal 2000, fiscal 1999 and fiscal 1998, respectively. The decrease in fiscal 2000 primarily reflected reduced U.S. state and local taxes. The increase in fiscal 1999 reflected an increase in provisions for certain tax matters, partially offset by reduced U.S. state and local taxes resulting from the resolution of certain audit issues.

Basic earnings per common share increased 14% to $4.95 in fiscal 2000 and 55% to $4.33 in fiscal 1999. Excluding the net gain from the sale of the businesses noted above and the impact of the cumulative effect of an accounting change, fiscal 1999's basic earnings per common share increased 67%. Diluted earnings per common share increased 15% to $4.73 in fiscal 2000 and 54% to $4.10 in fiscal 1999. Excluding the net gain from the sale of the businesses noted above and the impact of the cumulative effect of an accounting change, fiscal 1999's diluted earnings per common share increased 65%.

The Company's return on average shareholders' equity was 31%, 33% and 25% in fiscal 2000, fiscal 1999 and fiscal 1998, respectively. Excluding the net gain from the sale of the businesses noted above and the impact of the cumulative effect of an accounting change, fiscal 1998's return on average shareholders' equity was 23%.

Business Acquisitions and Dispositions

In December 2000, the Company announced that it had entered into a definitive agreement to acquire Quilter Holdings Limited ("Quilter"). Quilter is a leading U.K.-based investment management business providing segregated account management and advisory services to private individuals, pension funds and trusts. The transaction is subject to certain regulatory and other consents and is expected to be completed in the first quarter of fiscal 2001.

In fiscal 2000, the Company completed its acquisition of Ansett Worldwide Aviation Services ("Ansett Worldwide"). Ansett Worldwide is one of the world's leading aircraft leasing groups, supplying new and used commercial jet aircraft to airlines around the world. The Company's fiscal 2000 results include the operations of Ansett Worldwide since April 27, 2000, the date of acquisition.

In fiscal 1999, the Company completed its acquisition of Morgan Stanley Dean Witter, S.V., S.A. (formerly AB Asesores), the largest independent financial services firm in Spain. Morgan Stanley Dean Witter, S.V., S.A. has leading positions in personal investment, asset management, institutional research and brokerage. Through its financial advisors, it offers its individual investors proprietary mutual funds and other financial products. The Company's fiscal 1999 results include the operations of Morgan Stanley Dean Witter, S.V., S.A. since March 25, 1999, the date of acquisition.

In fiscal 1998, the Company completed the sale of its Global Custody business. At that time, the Company recorded a pre-tax gain of $323 million from the sale. Such gain included estimates for certain payments and purchase price adjustments which, under certain circumstances pursuant to the sales agreement, were payable by the Company to the buyer. As a result of the resolution of these payments and purchase price adjustments, during fiscal 2000, the Company recorded an additional pre-tax gain of $35 million related to the sale of the Global Custody business.

In fiscal 1998, the Company sold its interest in the operations of SPS, a 73%-owned, publicly held subsidiary of the Company. In addition, the Company sold certain credit card receivables relating to its discontinued BRAVO Card. The Company's aggregate net pre-tax gain resulting from these transactions was $362 million.

In addition, during fiscal 1998, the Company sold its Prime Option℠ MasterCard® portfolio ("Prime Option"), a business it had operated with NationsBank of Delaware, N.A., and its Correspondent Clearing business. The gains resulting from the sale of these businesses were not material to the Company's results of operations or financial condition.

Business Segments

The remainder of "Results of Operations" is presented on a business segment basis. Substantially all of the operating revenues and operating expenses of the Company can be directly attributed to its three business segments: Securities, Asset Management and Credit Services. Certain revenues and expenses have been allocated to each business segment, generally in proportion to their respective revenues or other relevant measures. The segment data presented below reflect the Company's fiscal 1999 adoption of Statement of Financial Accounting Standards ("SFAS") No. 131, "Disclosures about Segments of an Enterprise and Related Information." Prior to the adoption of SFAS No. 131, the Company had presented the results of its Securities and Asset Management segments on a combined basis. The following discussion excludes the cumulative effect of the accounting change in references to fiscal 1998 net income. Certain reclassifications have been made to prior-period amounts to conform to the current year's presentation.

SECURITIES

STATEMENTS OF INCOME
(dollars in millions)

	Fiscal 2000	Fiscal 1999	Fiscal 1998
Revenues:			
Investment banking	$ 4,881	$ 4,430	$ 3,314
Principal transactions:			
Trading	7,393	5,830	3,159
Investments	133	712	390
Commissions	3,629	2,770	2,208
Asset management, distribution and administration fees	1,967	1,374	1,079
Interest and dividends	18,308	12,573	13,405
Other	491	248	250
Total revenues	36,802	27,937	23,805
Interest expense	16,822	11,625	12,305
Net revenues	19,980	16,312	11,500
Compensation and benefits	9,557	7,225	5,428
Occupancy and equipment	621	493	419
Brokerage, clearing and exchange fees	425	378	354
Information processing and communications	986	756	591
Marketing and business development	706	511	414
Professional services	817	578	445
Other	631	507	408
Total non-interest expenses	13,743	10,448	8,059
Income before income taxes	6,237	5,864	3,441
Provision for income taxes	2,190	2,183	1,199
Net income	$ 4,047	$ 3,681	$ 2,242

Securities provides a wide range of financial products, services and investment advice to individual and institutional investors. Securities business activities are conducted in the U.S. and throughout the world and include investment banking, institutional sales and trading, full-service brokerage services and principal investing activities. At November 30, 2000, the Company's financial advisors provided securities and investment services to more than 5.4 million client accounts in the U.S. and had client assets of $659 billion. The Company had the second largest financial advisor sales organization in the U.S. On a global basis, the Company had 13,910 professional financial advisors at November 30, 2000.

Securities achieved record net revenues of $19,980 million and record net income of $4,047 million in fiscal 2000, increases of 22% and 10%, respectively, from fiscal 1999. In fiscal 1999, Securities net revenues and net income increased 42% and 64%, respectively, from fiscal 1998. In both fiscal 2000 and fiscal 1999, the levels of net revenues and net income in the Company's Securities business reflected a strong global market for mergers and acquisitions and securities underwritings, higher principal trading and commission revenues, higher levels of customer trading volume and the continued increase in the levels of client accounts and asset balances. The results of both years were partially offset by increased costs for incentive-based compensation, as well as increased non-compensation expenses associated with the Company's higher level of global business activities. In addition, fiscal 2000's results were negatively affected by more difficult economic and market conditions during the latter half of the year, which reduced the volume of merger and acquisition and underwriting transactions and contributed to a more difficult trading environment. In fiscal 2000, declines in certain equity markets also resulted in unrealized losses in the Company's private equity business.

Investment Banking

Investment banking revenues are derived from the underwriting of securities offerings and fees from advisory services. Investment banking revenues were as follows:

	Fiscal 2000	Fiscal 1999	Fiscal 1998
	(dollars in millions)		
Advisory fees from merger, acquisition and restructuring transactions	$2,137	$1,886	$1,322
Equity underwriting revenues	1,741	1,272	815
Fixed income underwriting revenues	1,003	1,272	1,177
Total investment banking revenues	$4,881	$4,430	$3,314

Investment banking revenues increased 10% to record levels in fiscal 2000, surpassing the Company's previous record attained in fiscal 1999. Revenues in fiscal 2000 reflected higher advisory fees from merger, acquisition and restructuring transactions and increased revenues from underwriting equity securities, partially offset by lower revenues from underwriting fixed income securities. In fiscal 1999, the 34% increase in investment banking revenues reflected higher advisory fees from merger, acquisition and restructuring transactions as well as increased revenues from underwriting both equity and fixed income securities.

The worldwide merger and acquisition markets remained robust with $3.5 trillion of activity announced during calendar year 2000 (per Thomson Financial Securities Data), an increase of 6% over 1999's then-record volume. The pace of transactions slowed, however, during the fourth quarter as activity in Europe declined. During calendar year 2000, the Company's volume of announced merger and acquisition transactions surpassed $1 trillion for the second consecutive year. In fiscal 2000, the high level of transaction activity reflected the continuing trends of consolidation and globalization as well as a high level of merger and acquisition transaction volume in the technology, media and telecommunications sectors. However, transaction volume decreased in the latter half of fiscal 2000 as volatility in the global equity markets and a decrease in equity valuations reduced the purchasing power of potential acquirers. The high transaction volumes in the merger and acquisition markets, coupled with the Company's global presence and strong market share, had a positive impact on advisory fees, which increased 13% in fiscal 2000. The 43% increase in advisory fees in fiscal 1999 also reflected high transaction volumes resulting from the strong global market for merger, acquisition and restructuring activities as well as increased revenues from real estate advisory transactions.

Equity underwriting revenues increased 37% to a record level in fiscal 2000, reflecting the Company's strong global market share. Equity underwriting revenues also benefited from a high volume of equity issuances, particularly in the technology, telecommunications and energy sectors. However, new issue volume declined toward the end of fiscal 2000 due to difficult conditions in the global financial markets, including reduced investor confidence. Equity underwriting revenues increased 56% in fiscal 1999 and reflected a high volume of equity offerings and the Company's strong global market share. In fiscal 1999, the Company's equity underwriting revenues benefited from favorable global economic conditions, which led major equity market indices higher and new issue activity to then-record levels. The primary market for equity issuances was particularly strong in the U.S. and in Europe and reflected the Company's participation in some of the year's largest transactions and its leadership in the underwriting of technology-related issuances.

Fixed income underwriting revenues decreased 21% in fiscal 2000. The volume of fixed income underwriting transactions was adversely affected by a higher interest rate environment in both the U.S. and Europe, resulting in higher borrowing costs. Revenues from underwriting global high-yield fixed income securities declined significantly, reflecting difficult conditions in this market sector. In addition, investor demand for these securities declined due to heightened concerns over credit quality. Revenues from underwriting derivative fixed income products also declined. These decreases were partially offset by higher revenues from securitized debt issuances, resulting from an increased volume of asset-backed transactions. Revenues from fixed income underwriting increased 8% in fiscal 1999. The volume of fixed income underwritings was generally strong during much of fiscal 1999, reflecting favorable global market conditions. In addition, the relatively low levels of interest rates in the U.S. during much of the year allowed issuers to take advantage of lower borrowing costs. The European Economic and Monetary Union, which permitted many corporate issuers to access the euro-denominated credit market, and the need for strategic financing in light of the robust global market for mergers and acquisitions also had a favorable impact on the volume of fixed income underwriting transactions. Higher revenues from underwriting derivative fixed income products also contributed to the increase in fiscal 1999.

Principal Transactions

Principal transactions include revenues from customers' purchases and sales of securities in which the Company acts as principal and gains and losses on securities held for resale. Decisions relating to principal transactions in securities are based on an overall review of aggregate revenues and costs associated with each transaction or series of transactions. This review includes an assessment of the potential gain or loss associated with a trade and the interest income or expense associated with financing or hedging the Company's positions. The Company also engages in proprietary trading activities for its own account.

Principal transaction trading revenues were as follows:

	Fiscal 2000	Fiscal 1999	Fiscal 1998
	(dollars in millions)		
Equities	$4,705	$3,065	$2,048
Fixed income	1,760	1,937	331
Foreign exchange	349	397	587
Commodities	579	431	193
Total principal transaction trading revenues	$7,393	$5,830	$3,159

Principal transaction trading revenues increased 27% in fiscal 2000, primarily reflecting higher equity and commodity trading revenues, partially offset by a decline in fixed income and foreign exchange trading revenues. Principal transaction trading revenues increased 85% in fiscal 1999, primarily reflecting higher fixed income, equity and commodity trading revenues, partially offset by a decline in foreign exchange trading revenues.

Equity trading revenues increased 54% to a record level in fiscal 2000, reflecting higher revenues from both cash and derivative equity products. Higher revenues from trading in equity cash products were primarily driven by significantly increased levels of customer trading volumes and volatility in both over-the-counter and listed securities, particularly in the U.S. and Europe. Revenues from equity derivative products also benefited from these conditions. Higher revenues from certain proprietary trading activities also contributed significantly to the increase in equity trading revenues. In fiscal 1999, equity trading revenues increased 50%, primarily reflecting higher revenues from equity cash products. The increase was primarily driven by higher levels of customer trading volumes in both listed and over-the-counter securities, particularly in the U.S. and Europe, as generally favorable global market and economic conditions increased investor demand for equity securities. Higher revenues from trading equity derivative products, which benefited from strong trading volumes and periods of market volatility, and certain proprietary trading activities also contributed significantly to the increase.

Fixed income trading revenues decreased 9% in fiscal 2000, primarily reflecting lower revenues from global high-yield and investment grade fixed income securities. Trading revenues from global high-yield fixed income securities decreased significantly due to lighter trading activity and decreased market liquidity, which resulted in markdowns of certain high-yield positions. During fiscal 2000, several high-yield issuers experienced financial difficulties, triggering an increased number of credit downgrades and defaults, particularly in the telecommunications sector. As a result, investors became more concerned about the credit quality of issuers, particularly during the latter half of fiscal 2000. Revenues from investment grade fixed income securities also declined, reflecting more difficult market conditions, which resulted in reduced liquidity and widening credit spreads. These decreases were partially offset by higher revenues from trading derivative and government agency products. In fiscal 1999, fixed income trading revenues increased 485%, primarily reflecting higher revenues from investment grade, high-yield and securitized fixed income securities as well as swap transactions. Fiscal 1999's revenues benefited from significantly improved conditions in the global fixed income markets as compared with the periods of extreme volatility and illiquidity that existed at the end of fiscal 1998. During the first half of fiscal 1999, the continuing recovery of global economic and market conditions led to strong investor demand for fixed income products and contributed to high transaction volumes. In addition, fears of accelerating inflation in the U.S. and the interest rate actions taken by the Fed and the ECB resulted in periods of volatility in the global fixed income markets, which resulted in increased trading opportunities. Market conditions and trading volumes were more moderate during the latter half of fiscal 1999, primarily reflecting a rising interest rate environment in the U.S. and Europe.

Foreign exchange revenues decreased 12% in fiscal 2000, reflecting lower levels of trading volumes and volatility in the global foreign exchange markets. Trading volumes were negatively affected by the exit of certain hedge funds from the foreign exchange market and by reduced liquidity in the Japanese yen and euro markets. During fiscal 2000, volatility levels between the U.S. dollar and Japanese yen decreased to a 10-year low, creating reduced market liquidity. In addition, the euro continued to depreciate against the U.S. dollar, reflecting the strong relative performance of the U.S. economy. However, at the end of fiscal 2000, economic indicators in the U.S. signaled a potential slowing of the economy, and, as a result, the euro strengthened against the U.S. dollar. In fiscal 1999, foreign exchange revenues declined 32% from the record level of revenues achieved in fiscal 1998.

The decrease primarily reflected reduced customer trading volumes and lower levels of volatility in the global foreign exchange markets as compared with the prior year.

Commodity trading revenues rose 34% to a record level in fiscal 2000, primarily driven by higher revenues from certain energy-related products, including electricity, natural gas and crude oil. Trading revenues from energy-related products benefited from periods of rising prices and increased volatility across the entire energy sector. Such conditions were primarily attributable to low inventory levels, strong demand and concerns regarding the adequacy of production levels. In fiscal 1999, commodities trading revenues rose 123%, primarily driven by higher revenues from certain energy-related products, including crude oil, refined energy products, electricity and natural gas. Revenues from trading energy-related products benefited from the sharp rise in energy prices that occurred during the latter half of fiscal 1999. Increases in energy prices were primarily attributable to strong demand for energy products, relatively low inventory levels and reduced production volumes. Revenues from natural gas trading benefited from periods of price volatility during the year, which was primarily attributable to changing weather conditions and varying levels of demand. Higher revenues from metals trading also contributed to the increase.

Principal transaction investment revenues aggregating $133 million were recognized in fiscal 2000 as compared with $712 million in fiscal 1999. Fiscal 2000's revenues included realized gains from certain of the Company's private equity investments, including Commerce One, Inc. and Equant N.V., as well as gains from the Company's other principal investment activities. These gains were partially offset by unrealized losses in the private equity business, reflecting difficult market conditions in the telecommunications, technology and Internet sectors. Fiscal 1999's revenues reflected a record level of revenues recorded by the Company's private equity business and included realized and unrealized gains from the Company's positions in Equant N.V. and Knight/Trimark Group Inc. Net gains from increases in the value of certain other private equity and venture capital investments also contributed to fiscal 1999's results.

Securities purchased in principal investment transactions generally are held for appreciation and are not readily marketable. It is not possible to determine when the Company will realize the value of such investments since, among other factors, such investments are generally subject to sales restrictions. Moreover, estimates of the eventual realizable value of the investments fluctuate significantly over time in light of business, market, economic and financial conditions generally or in relation to specific transactions.

Commissions

Commission revenues primarily arise from agency transactions in listed and over-the-counter equity securities and sales of mutual funds, futures, insurance products and options. Commission revenues increased 31% in fiscal 2000, primarily reflecting higher revenues from equity cash products from markets located in Europe, the U.S. and the Far East. Revenues from European markets benefited from a significant increase in market volumes, particularly in the telecommunications and technology sectors. In the U.S., trading volumes on the New York Stock Exchange and the NASDAQ increased to record levels. Commission revenues from markets in Japan and elsewhere in the Far East increased as improved economic prospects within the region during the first half of fiscal 2000 increased investor interest and led to higher transaction volumes. Commission revenues increased 25% in fiscal 1999, reflecting higher revenues from equity cash products in markets located in the U.S., Europe, and the Far East. In the U.S., favorable market conditions and strong investor demand for equity products contributed to a high volume of customer securities transactions, including listed and over-the-counter equity securities. Revenues from markets in Europe also benefited from strong customer transaction volumes, as improved economic and market conditions in the region increased investor demand for European equity securities. Commission revenues from markets in Japan and elsewhere in the Far East increased as improved economic prospects within the region increased investor interest and led to higher transaction volumes. In both fiscal 2000 and fiscal 1999, commission revenues also benefited from higher sales of mutual funds and the continued growth in the number of the Company's financial advisors.

In October 1999, the Company launched *i*choice℠, a new service and technology platform available to individual investors. *i*choice provides each of the Company's individual investor clients with the choice of self-directed investing online; a traditional full-service brokerage relationship through a financial advisor; or some combination of both. *i*choice provides a range of pricing options, including fee-based pricing. As a result, the amount of revenues recorded within the "Commissions" and "Asset management, distribution and administration fees" income statement categories is affected by the number of the Company's clients electing a fee-based pricing arrangement.

Net Interest

Interest and dividend revenues and interest expense are a function of the level and mix of total assets and liabilities, including financial instruments owned, reverse repurchase and repurchase agreements, trading strategies associated with the Company's institutional securities business, customer margin loans and the prevailing level, term structure and volatility of interest rates. Interest and dividend revenues and interest expense are integral components of trading activities. In assessing the profitability of trading activities, the Company views net interest and principal trading revenues in the aggregate. In addition, decisions relating to principal transactions in securities are based on an overall review of aggregate revenues and costs associated with each transaction or series of transactions. This review includes an assessment of the potential gain or loss associated with a trade and the interest income or expense associated with financing or hedging the Company's positions. Net interest revenues increased 57% in fiscal 2000 and decreased 14% in fiscal 1999, partially reflecting the level and mix of interest earning assets and interest bearing liabilities (including liabilities associated with the Company's aircraft financing activities) during the respective periods as well as certain trading strategies utilized in the Company's institutional securities business. In fiscal 2000, higher net interest revenues from brokerage services provided to institutional and individual customers, including an increase in the level of customer margin loans, also had a positive impact on net interest revenues.

Asset Management, Distribution and Administration Fees

Asset management, distribution and administration fees include revenues from asset management services, including fees for promoting and distributing mutual funds ("12b-1 fees") and fees from investment management services provided to segregated customer accounts pursuant to various contractual arrangements in connection with the Company's Investment Consulting Services ("ICS") business. The Company receives 12b-1 fees for services it provides in promoting and distributing certain open-ended mutual funds. These fees are based on either the average daily fund net asset balances or average daily aggregate net fund sales and are affected by changes in the overall level and mix of assets under management or supervision. Asset management, distribution and administration fees also include revenues from individual investors electing a fee-based pricing arrangement under the Company's *i*choice service and technology platform.

Asset management, distribution and administration fees increased 43% in fiscal 2000 and 27% in fiscal 1999. The increase in both periods was primarily attributable to higher 12b-1 fees from promoting and distributing mutual funds to individual investors through the Company's financial advisors. Higher revenues from investment management services associated with the ICS business and the continued growth in the level of client asset balances, which rose to $659 billion at November 30, 2000 from $595 billion at November 30, 1999, also contributed to the increase. In addition, the increase in fiscal 2000 reflected higher revenues from individual investors electing fee-based pricing.

Non-Interest Expenses

	Fiscal 2000	**Fiscal 1999**	**Fiscal 1998**
		(dollars in millions)	
Compensation and benefits	$ 9,557	$ 7,225	$5,428
Occupancy and equipment	621	493	419
Brokerage, clearing and exchange fees	425	378	354
Information processing and communications	986	756	591
Marketing and business development	706	511	414
Professional services	817	578	445
Other .	631	507	408
Total non-interest expenses	$13,743	$10,448	$8,059

Fiscal 2000's total non-interest expenses increased 32% to $13,743 million. Compensation and benefits expense increased 32%, reflecting increased levels of incentive compensation based on record fiscal 2000 revenues and earnings, incremental costs related to the Company's continued focus on increasing the number of its financial advisors and increased competitive pressures in certain institutional businesses. Excluding compensation and benefits expense, non-interest expenses increased $963 million. Occupancy and equipment expense increased 26%, primarily due to additional rent associated with new U.S. branch locations and increased office space in New York and certain other locations. Brokerage, clearing and exchange fees increased 12%, primarily due to higher brokerage costs related to increased global trading volume, particularly in North America and Europe. Brokerage costs associated with the business activities of Morgan Stanley Dean Witter, S.V., S.A. also contributed to the increase. Information processing and communications expense increased 30%, primarily due to increased costs associated with the Company's information processing infrastructure, including data processing, market data services and telecommunications costs for network equipment associated with increased business activity and higher employment levels. These increases were partially offset by the exclusion of certain Year 2000 costs from fiscal 2000's results. Marketing and business development expense increased 38%, primarily due to increased travel and entertainment costs associated with a high level of business activity in the global financial markets, new advertising campaigns and additional promotional expenses in the individual securities business. Professional services expense increased 41%, primarily reflecting higher consulting costs associated with certain strategic initiatives, including e-commerce. The increase also reflected higher costs for employment fees and temporary staffing due to increased global business activity. Other expense increased 24%, reflecting the impact of a higher level of business activity on various operating expenses. Higher costs associated with the Company’s aircraft leasing business (including Ansett Worldwide that was acquired in April 2000) and amortization of goodwill associated with the Company’s acquisition of Morgan Stanley Dean Witter, S.V., S.A. also contributed to the increase.

Fiscal 1999’s total non-interest expenses increased 30% to $10,448 million. Compensation and benefits expense increased 33%, reflecting increased levels of incentive compensation based on record fiscal 1999 revenues and earnings as well as an increase in the number of employees. Excluding compensation and benefits expense, non-interest expenses increased $592 million. Occupancy and equipment expense increased 18%, principally reflecting additional office space in New York and certain other locations as well as incremental rent attributable to the opening of new U.S. branch locations. Brokerage, clearing and exchange fees increased 7%, primarily attributable to higher brokerage expenses due to higher levels of trading volume in the global securities markets. Information processing and communications costs increased 28%, primarily due to increased costs associated with the Company’s information technology infrastructure, including server and data center costs. A higher number of employees utilizing communications systems and certain data services also contributed to the increase. Marketing and business development expense increased 23%, reflecting higher advertising expenses associated with the Company’s individual securities business. Increased travel and entertainment costs associated with the high levels of activity in the global financial markets also contributed to the increase. Professional services expense increased 30%, primarily reflecting higher consulting costs as a result of certain information technology initiatives, including the Company’s preparations for the Year 2000. Higher legal costs associated with increased levels of business activity and higher temporary staffing fees also contributed to the increase. Other expense increased 24%, primarily reflecting the impact of a higher level of business activity on various operating expenses. An increase in charitable donations and the amortization of goodwill associated with the Company’s acquisition of Morgan Stanley Dean Witter, S.V., S.A. in March 1999 also contributed to the increase.

ASSET MANAGEMENT

STATEMENTS OF INCOME
(dollars in millions)

	Fiscal 2000	Fiscal 1999	Fiscal 1998
Revenues:			
Investment banking	$ 127	$ 93	$ 26
Principal transactions:			
Investments	60	13	(301)
Commissions	16	4	—
Asset management, distribution and administration fees	2,252	1,950	1,924
Interest and dividends	78	61	252
Other	—	—	27
Total revenues	2,533	2,121	1,928
Interest expense	7	9	165
Net revenues	2,526	2,112	1,763
Compensation and benefits	751	648	659
Occupancy and equipment	89	96	97
Brokerage, clearing and exchange fees	94	107	198
Information processing and communications	77	92	87
Marketing and business development	161	127	125
Professional services	101	137	135
Other .	143	138	91
Total non-interest expenses	1,416	1,345	1,392
Gain on sale of businesses	35	—	323
Income before income taxes and cumulative effect of accounting change	1,145	767	694
Provision for income taxes	462	319	264
Income before cumulative effect of accounting change	683	448	430
Cumulative effect of accounting change	—	—	(117)
Net income	$ 683	$ 448	$ 313

Asset Management ranks among the top eight global active asset managers and provides a wide range of investment advisory products through both proprietary and non-proprietary distribution channels. Morgan Stanley Dean Witter Advisors and Van Kampen Investments (“VK”) offer individual investors a broad array of mutual fund and wealth management tools that cover the full spectrum of investment categories, including growth, income, sector and global. Morgan Stanley Dean Witter Investment Management and Miller Anderson & Sherrerd serve the specialized needs of global institutional and high net worth investors. Asset Management’s product breadth includes mutual funds, closed-end funds, managed accounts, managed futures funds, pooled vehicles, variable annuities and unit investment trusts. In fiscal 2000, Asset Management’s assets under management or supervision increased $30 billion to $502 billion at November 30, 2000.

Asset Management achieved record net revenues of $2,526 million in fiscal 2000, an increase of 20% from fiscal 1999. Asset Management’s net income for fiscal 2000 was a record $683 million, an increase of 52% from fiscal 1999. The increase in net income in fiscal 2000 primarily reflected higher asset management, distribution and administration fees resulting from the continued accumulation and management of customer assets and a more favorable asset mix, partially offset by higher incentive-based compensation expenses. Net income for fiscal 2000 included a net gain of $21 million from the sale of the Company’s Global Custody business (see “Results of Operations—Business Acquisitions and Dispositions” herein). Asset Management achieved net revenues and net income of $2,112 million and $448 million in fiscal 1999, increases of 20% and 43%, respectively, from fiscal 1998. Fiscal 1998’s net income included a net gain of $182 million from the sale of the Company’s Global Custody business (see “Results of Operations—Business Acquisitions and Dispositions” herein). Fiscal 1998 net income also included a $117 million charge resulting from the cumulative effect of an accounting change. This charge represents the effect of an accounting change adopted in the fourth quarter of fiscal 1998 (effective December 1, 1997) with respect to the accounting for offering costs paid by investment advisors of closed-end funds, where such costs are not specifically reimbursed through separate advisory contracts (see Note 2 to the consolidated financial statements). Excluding the net gain from the sale of the Global Custody business and the charge resulting from the cumulative effect of an accounting change, fiscal 1999’s net income increased 81%.

Investment Banking

Asset Management primarily generates investment banking revenues from the underwriting of Unit Investment Trust products. Investment banking revenues increased 37% in fiscal 2000 and 258% in fiscal 1999. In both periods, the increases were primarily associated with higher levels of Unit Investment Trust sales volumes. Unit Investment Trust sales volumes rose 35% to a record $16.6 billion in fiscal 2000 and increased 36% to $12.3 billion in fiscal 1999.

Principal Transactions

Asset Management's principal transaction revenues are primarily generated from the Company's net gains on capital investments in certain of its funds and other investments.

Principal transaction investment revenues aggregating $60 million were recognized in fiscal 2000 as compared with $13 million in fiscal 1999. In both periods, principal transaction investment revenues primarily consisted of net gains from the Company's capital investments in certain of its funds.

Commissions

Asset Management primarily generates commission revenues from dealer and distribution concessions on sales of certain funds as well as certain allocated commission revenues.

Commission revenues were $16 million in fiscal 2000 and $4 million in fiscal 1999. In both periods, the fluctuations were associated with changes in the level of sales volume of certain VK products and allocated commission revenues.

Net Interest

Asset Management generates net interest revenues from certain investment positions as well as from certain allocated interest revenues and expenses. Net interest revenues in fiscal 1998 also included revenues from global custody and correspondent clearing services.

Net interest revenues increased 37% in fiscal 2000, primarily reflecting higher net revenues from certain investment positions and allocations. Net interest revenues decreased 40% in fiscal 1999, primarily reflecting the Company's sale of its Global Custody and Correspondent Clearing businesses in fiscal 1998.

Asset Management, Distribution and Administration Fees

Asset management, distribution and administration fees primarily include revenues from the management and administration of assets. These fees arise from investment management services the Company provides to investment vehicles pursuant to various contractual arrangements. Generally, the Company receives fees primarily based upon mutual fund average net assets or quarterly assets for other vehicles. Revenues in fiscal 1998 also include other administrative fees and non-interest revenues earned from global custody and correspondent clearing services.

The Company's customer assets under management or supervision at fiscal year-end were as follows:

	Fiscal 2000	Fiscal 1999	Fiscal 1998
	(dollars in billions)		
Products offered primarily to individuals:			
Mutual funds:			
Equity	$ 103	$ 94	$ 75
Fixed income	46	53	57
Money markets	57	47	37
Total mutual funds	206	194	169
ICS assets	31	23	19
Separate accounts, unit trust and other arrangements	82	75	59
Total individual	319	292	247
Products offered primarily to institutional clients:			
Mutual funds	36	33	27
Separate accounts, pooled vehicle and other arrangements	147	147	138
Total institutional	183	180	165
Total assets under management or supervision(1)	$ 502	$472	$412

(1) Revenues and expenses associated with ICS and certain other assets are included in the Company's Securities segment.

Asset management, distribution and administration fees increased 15% in fiscal 2000 and 1% in fiscal 1999. In both years, the increases in revenues primarily reflected higher levels of management fees as well as other revenues resulting from a higher level of assets under management or supervision. The increase in fiscal 2000 also reflected a more favorable asset mix, primarily due to a shift in asset mix to a greater percentage of equity products, which typically generate higher management fees. The increase in fiscal 1999 was partially offset by the absence of revenues from global custody and correspondent clearing activities, attributable to the Company's sale of its Global Custody business in the fourth quarter of fiscal 1998 and its Correspondent Clearing business in the third quarter of fiscal 1998.

As of November 30, 2000, assets under management or supervision increased $30 billion from fiscal year-end 1999. In fiscal 2000, virtually all of the increase in assets under management or supervision was attributable to net inflows of customer assets. The increases in assets under management or supervision due to market appreciation in the first three quarters of the fiscal year were offset by market depreciation during the fourth fiscal quarter. This market depreciation reflected the declines in many global financial markets that occurred during that period. In fiscal 1999, approximately 25% of the increase in assets under management or supervision was attributable to net inflows of customer assets, while the remaining 75% reflected market appreciation.

Non-Interest Expenses

	Fiscal 2000	Fiscal 1999	Fiscal 1998
	(dollars in millions)		
Compensation and benefits	$ 751	$ 648	$ 659
Occupancy and equipment	89	96	97
Brokerage, clearing and exchange fees	94	107	198
Information processing and communications	77	92	87
Marketing and business development	161	127	125
Professional services	101	137	135
Other	143	138	91
Total non-interest expenses	$1,416	$1,345	$1,392

Fiscal 2000's total non-interest expenses increased 5% to $1,416 million. Compensation and benefits expense increased 16%, reflecting higher incentive-based compensation costs due to Asset Management's higher level of revenues and earnings. Excluding compensation and benefits expense, non-interest expenses decreased $32 million. Occupancy and equipment expense decreased 7%, primarily due to lower depreciation expense on certain data processing equipment. These decreases were partially offset by higher occupancy costs at certain office locations. Brokerage, clearing and exchange fees decreased 12%, primarily attributable to lower sales of closed-end funds through the non-proprietary distribution channel and higher redemption fees associated with certain VK products. These decreases were partially offset by a higher level of deferred commission amortization. Information processing and communications expense decreased 16%, primarily due to lower costs incurred in fiscal 2000 related to outside data processing and computer software costs. Marketing and business development expense increased 27%, primarily due to higher promotional and distribution costs for certain mutual funds. Professional services expense decreased 26%, reflecting higher consulting costs in fiscal 1999 related to the Company's preparation for the Year 2000, partially offset by higher consulting costs in fiscal 2000 for various e-commerce initiatives. Other expense increased 4%, primarily due to new and increased business activity.

Fiscal 1999's total non-interest expenses decreased 3% to $1,345 million. Compensation and benefits expense decreased 2%, reflecting lower costs due to the sale of the Company's Global Custody business in fiscal 1998, partially offset by higher incentive-based compensation costs due to higher fiscal 1999 revenues and earnings. Excluding compensation and benefits expense, non-interest expenses decreased $36 million. Occupancy and equipment expense was comparable with the prior year as higher occupancy costs at certain office locations were offset by lower costs due to the Company's sale of its Global Custody business. Brokerage, clearing and exchange fees decreased 46%, primarily attributable to commissions paid in fiscal 1998 in connection with the Company's launch of the Van Kampen Senior Income Trust mutual fund and lower sales of closed-end funds through the non-proprietary distribution channel. In addition, lower agent bank costs were incurred in fiscal 1999 due to the Company's sale of its Global Custody business. These decreases were partially offset by a higher level of deferred commission amortization. Information processing and communications costs increased 6%, primarily due to increased costs associated with the Company's information technology infrastructure as well as higher market data costs. These increases were partially offset by lower costs due to the Company's sale of its Global Custody business. Marketing and business development expense increased 2% as higher costs due to business growth, including new product launches, were partially offset by lower costs due to the Company's sale of its Global Custody business. Professional services expense increased 1% as higher consulting fees were partially offset by lower legal expenses and lower costs due to the Company's sale of its Global Custody business. Other expense increased 52%, reflecting the impact of a higher level of business activity on various operating expenses, as well as costs associated with the consolidation of certain office locations.

CREDIT SERVICES

STATEMENTS OF INCOME
(dollars in millions)

	Fiscal 2000	Fiscal 1999	Fiscal 1998
Fees:			
Merchant and cardmember	$1,780	$ 1,492	$1,647
Servicing	1,450	1,194	928
Other	—	—	5
Total non-interest revenues	3,230	2,686	2,580
Interest revenue	2,848	2,246	2,729
Interest expense	1,347	881	994
Net interest income	1,501	1,365	1,735
Provision for consumer loan losses	810	529	1,173
Net credit income	691	836	562
Net revenues	3,921	3,522	3,142
Compensation and benefits	628	525	549
Occupancy and equipment	62	54	67
Information processing and communications	493	477	462
Marketing and business development	1,191	1,041	872
Professional services	119	121	97
Other	284	207	207
Total non-interest expenses	2,777	2,425	2,254
Gain on sale of businesses	—	—	362
Income before income taxes	1,144	1,097	1,250
Provision for income taxes	418	435	529
Net income	$ 726	$ 662	$ 721

The Company's Credit Services business is operated by Discover Financial Services, a business unit which issues quality consumer credit products and operates Discover Business Services, a proprietary network of merchant and cash access locations in the U.S. The credit cards issued by the Company include the Discover Card, the Discover Platinum Card, the Morgan Stanley Dean Witter Card and other proprietary general purpose credit cards.

In fiscal 2000, Credit Services achieved record net income of $726 million, an increase of 10% from fiscal 1999. The increase reflected higher merchant and cardmember fees, servicing fees and net interest income, reflecting overall growth of the business, including record levels of transaction volume and a record level of period-end managed consumer loans. The increase in net income was partially offset by a higher provision for consumer loan losses and higher non-interest expenses.

The results of fiscal 2000 and 1999 do not include the results from Prime Option, the operations of SPS and certain receivables associated with the discontinued BRAVO Card, all of which were sold during fiscal 1998. Prime Option, a business the Company had operated with NationsBank of Delaware, N.A., was sold during the second quarter of fiscal 1998. The Company sold its interest in the operations of SPS, which was a 73%-owned, publicly held subsidiary of the Company, in the fourth quarter of fiscal 1998. The Company discontinued its BRAVO Card in fiscal 1998 and sold certain credit card receivables associated with the BRAVO Card in the fourth quarter of fiscal 1998. Fiscal 1998's net after-tax gain from the sale of the operations of SPS and certain receivables associated with the BRAVO Card was $163 million.

In fiscal 1999, Credit Services' net income decreased 8% to $662 million, primarily due to fiscal 1998's inclusion of the $163 million net gain on the sale of businesses. Excluding this gain, net income increased 19% in fiscal 1999. The increase was primarily attributable to a lower provision for consumer loan losses and increased servicing fees, partially offset by lower net interest income and merchant and cardmember fees and higher marketing and business development expenses.

Credit Services' statistical data were as follows:

	Fiscal 2000	Fiscal 1999	Fiscal 1998
	(dollars in billions)		
Consumer loans at fiscal year-end:			
Owned	$21.9	$21.0	$16.0
Managed	$47.1	$38.0	$32.5
General purpose credit card transaction volume	$90.1	$70.6	$58.0

The higher level of managed consumer loans at November 30, 2000 and 1999 was primarily attributable to growth in the Company's Discover Platinum Card.

Merchant and Cardmember Fees

Merchant and cardmember fees include revenues from fees charged to merchants on credit card sales, late payment fees, overlimit fees, insurance fees and cash advance fees.

Merchant and cardmember fees increased 19% to $1,780 million during fiscal 2000 and decreased 9% to $1,492 million during fiscal 1999. The increase in fiscal 2000 was primarily due to higher merchant discount revenue and late payment fees associated with the use of the Discover Card. The increase in Discover Card merchant discount revenues was primarily due to a record level of sales volume, coupled with an increase in the average merchant discount rate. Late payment fees increased in fiscal 2000, primarily due to a fee increase introduced during April 1999, coupled with an increase in the number of late fee occurrences, reflecting higher levels of transaction volume and consumer loans subject to such fees. Merchant and cardmember fees decreased in fiscal 1999, primarily due to the Company's sale of the operations of SPS and the sale of Prime Option. Fiscal 1999 also was impacted by higher merchant discount revenue offset by lower levels of overlimit fees and cash advance fees. The increase in merchant discount revenue was associated with higher levels of sales volume. Overlimit fees decreased, primarily due to a lower level of overlimit fee occurrences. Cash advance fees decreased due to lower cash advance transaction volume, primarily attributable to the Company's actions to limit cash advances in an effort to improve credit quality.

Servicing Fees

Servicing fees are revenues derived from consumer loans which have been sold to investors through asset securitizations. Cash flows from the interest yield and cardmember fees generated by securitized loans are used to pay investors in these loans a predetermined fixed or floating rate of return on their investment, to reimburse the investors for losses of principal resulting from charged-off loans and to pay the Company a fee for servicing the loans. Any excess cash flows remaining are paid to the Company. The servicing fees and excess net cash flows paid to the Company are reported as servicing fees in the consolidated statements of income. The sale of consumer loans through asset securitizations, therefore, has the effect of converting portions of net credit income and fee income to servicing fees. The Company completed asset securitizations of $9.8 billion in fiscal 2000 and $3.0 billion in fiscal 1999. The asset securitizations in fiscal 2000 and 1999 have expected maturities ranging from approximately three to seven years from the date of issuance.

The table below presents the components of servicing fees:

	Fiscal 2000	Fiscal 1999	Fiscal 1998
	(dollars in millions)		
Merchant and cardmember fees	$ 627	$ 552	$ 505
Interest revenue	3,432	2,694	2,598
Interest expense	(1,462)	(996)	(1,010)
Provision for consumer loan losses	(1,147)	(1,056)	(1,165)
Servicing fees	$ 1,450	$ 1,194	$ 928

Servicing fees are affected by the level of securitized loans, the spread between the interest yield on the securitized loans and the yield paid to the investors, the rate of credit losses on securitized loans and the level of cardmember fees earned from securitized loans. Servicing fees increased 21% in fiscal 2000 and 29% in fiscal 1999. The increase in fiscal 2000 was due to higher levels of net interest cash flows and increased cardmember fee revenue, partially offset by higher credit losses associated with a higher level of average securitized consumer loans. The increase in credit losses was partially offset by a lower level of charge-offs related to the securitized portfolio. The increase in fiscal 1999 was due to higher levels of cardmember fees and net interest income, primarily resulting from higher levels of average securitized loans. The increase also reflected a decline in credit losses from securitized consumer loans resulting from a lower level of charge-offs related to the Discover Card portfolio and the positive impact of the sale of the operations of SPS, partially offset by an increase in the level of average securitized loans.

Net Interest Income

Net interest income represents the difference between interest revenue derived from Credit Services consumer loans and short-term investment assets and interest expense incurred to finance those assets. Credit Services assets, consisting primarily of consumer loans, earn interest revenue at both fixed rates and market-indexed variable rates. The Company incurs interest expense at fixed and floating rates. Interest expense also includes the effects of any interest rate contracts entered into by the Company as part of its interest rate risk management program. This program is designed to reduce the volatility of earnings resulting from changes in interest rates and is accomplished primarily through matched financing, which entails matching the repricing schedules of consumer loans and related financing. The following tables present analyses of Credit Services average balance sheets and interest rates in fiscal 2000, fiscal 1999 and fiscal 1998 and changes in net interest income during those fiscal years:

Average Balance Sheet Analysis

	Fiscal 2000			Fiscal 1999(3)			Fiscal 1998(3)		
	Average Balance	Rate	Interest	Average Balance	Rate	Interest	Average Balance	Rate	Interest
	(dollars in millions)								
ASSETS									
Interest earning assets:									
General purpose credit card and other consumer loans	$ 21,910	12.15%	$2,662	$ 16,177	13.10%	$2,118	$ 18,558	14.07%	$2,612
Investment securities	594	6.37	38	672	5.16	35	496	6.25	31
Other	2,194	6.74	148	1,656	5.61	93	1,465	5.88	86
Total interest earning assets	24,698	11.53	2,848	18,505	12.14	2,246	20,519	13.30	2,729
Allowance for loan losses	(777)			(774)			(847)		
Non-interest earning assets	1,589			1,544			1,517		
Total assets	$ 25,510			$ 19,275			$ 21,189		
LIABILITIES AND SHAREHOLDER'S EQUITY									
Interest bearing liabilities:									
Interest bearing deposits									
Savings	$ 1,513	5.62%	$ 85	$ 1,492	4.51%	$ 67	$ 1,073	4.79%	$ 51
Brokered	7,732	6.62	512	5,609	6.37	357	5,656	6.62	375
Other time	3,032	6.19	188	1,927	5.61	108	2,189	6.16	135
Total interest bearing deposits	12,277	6.39	785	9,028	5.90	532	8,918	6.29	561
Other borrowings	8,484	6.62	562	6,046	5.76	349	7,162	6.05	433
Total interest bearing liabilities	20,761	6.49	1,347	15,074	5.84	881	16,080	6.18	994
Shareholder's equity/other liabilities	4,749			4,201			5,109		
Total liabilities and shareholder's equity	$ 25,510			$ 19,275			$ 21,189		
Net interest income			$ 1,501			$ 1,365			$ 1,735
Net interest margin(1)			6.08%			7.38%			8.46%
Interest rate spread(2)		5.04%			6.30%			7.12%	

(1) Net interest margin represents net interest income as a percentage of total interest earning assets.

(2) Interest rate spread represents the difference between the rate on total interest earning assets and the rate on total interest bearing liabilities.

(3) Certain prior-year information has been reclassified to conform to the current year's presentation.

Rate/Volume Analysis

Increase/(Decrease) due to Changes in:	Fiscal 2000 vs. Fiscal 1999 Volume	Rate	Total	Fiscal 1999 vs. Fiscal 1998 Volume	Rate	Total
	(dollars in millions)					
Interest Revenue						
General purpose credit card and other consumer loans	$ 752	$(208)	$544	$ (369)	$(125)	$(494)
Investment securities	(4)	7	3	11	(7)	4
Other	30	25	55	11	(4)	7
Total interest revenue	753	(151)	602	(268)	(215)	(483)
Interest Expense						
Interest bearing deposits:						
Savings	1	17	18	20	(4)	16
Brokered	136	19	155	(3)	(15)	(18)
Other time	62	18	80	(16)	(11)	(27)
Total interest bearing deposits	192	61	253	7	(36)	(29)
Other borrowings	140	73	213	(67)	(17)	(84)
Total interest expense	331	135	466	(62)	(51)	(113)
Net interest income	$ 421	$(285)	$ 136	$ (206)	$(164)	$(370)

Net interest income increased 10% in fiscal 2000 and decreased 21% in fiscal 1999. The increase in fiscal 2000 was primarily due to higher average levels of consumer loans, partially offset by a lower yield on these loans and increased financing costs incurred by the Company. The increase in average consumer loans was due to higher levels of sales and balance transfer volume and promotional programs. The lower yield on Discover Card loans was primarily due to lower interest rates offered to new cardmembers and certain existing cardmembers, partially offset by the Company's repricing of certain credit card receivables discussed below. The lower yield also reflected an increase in consumer loans from balance transfers and from promotional purchases, which are generally offered at lower interest rates for an introductory period. The increase in interest expense was due to a higher level of interest bearing liabilities, coupled with an increase in the Company's average cost of borrowings, reflecting interest rate increases made by the Fed in fiscal 1999 and the first half of fiscal 2000. The average prime rate for fiscal 2000 was 9.19% as compared with 7.98% for fiscal 1999. The decrease in net interest income in fiscal 1999 was primarily due to lower average levels of consumer loans and a lower yield on these loans. The decrease in average consumer loans was due to the sale of the operations of SPS, the sale of Prime Option and the discontinuance of the BRAVO Card in fiscal 1998 as well as a higher level of securitized Discover Card loans. The lower yield in fiscal 1999 was due to a lower yield on Discover Card loans, coupled with the exclusion of SPS loans from the Company's portfolio. The lower yield on Discover Card loans was primarily due to the more competitive interest rates offered to both existing and new cardmembers as well as an increase in consumer loans from balance transfers.

In response to the rising interest rate environment in the U.S., the Company repriced a substantial portion of its existing credit card receivables to a market-indexed variable interest rate during the second and third quarters of fiscal 2000.

The supplemental table below provides average managed loan balance and rate information, which takes into account both owned and securitized loans:

Supplemental Average Managed Loan Information

	Fiscal 2000 Average Balance	Rate	Fiscal 1999 Average Balance	Rate	Fiscal 1998 Average Balance	Rate
	(dollars in millions)					
General purpose credit card and other consumer loans	$43,540	13.82%	$33,534	14.23%	$34,619	14.86%
Total interest earning assets	46,328	13.39	35,862	13.66	36,580	14.38
Total interest bearing liabilities	42,391	6.54	32,431	5.74	32,141	6.15
Consumer loan interest rate spread		7.28		8.49		8.71
Interest rate spread		6.85		7.92		8.23
Net interest margin		7.40		8.47		8.98

Provision for Consumer Loan Losses

The provision for consumer loan losses is the amount necessary to establish the allowance for loan losses at a level that the Company believes is adequate to absorb estimated losses in its consumer loan portfolio at the balance sheet date. The Company's allowance for loan losses is regularly evaluated by management for adequacy and was $780 million at November 30, 2000 and $769 million at November 30, 1999.

The provision for consumer loan losses, which is affected by net charge-offs, loan volume and changes in the amount of consumer loans estimated to be uncollectable, increased 53% in fiscal 2000 and decreased 55% in fiscal 1999. The increase in fiscal 2000 was primarily due to higher levels of average consumer loans in the Discover Card portfolio, partially offset by a lower net charge-off rate. In addition, the provision for consumer loan losses in fiscal 1999 benefited from a decline in the loan loss allowance in connection with securitization transactions entered into prior to the third quarter of 1996. This loan loss allowance was fully amortized by the end of fiscal 1999. The decrease in fiscal 1999 was primarily due to a lower level of charge-offs related to the Discover Card portfolio and the positive impact of the sale of the operations of SPS, the sale of Prime Option and the discontinuance of the BRAVO Card. The provision for consumer loan losses also was positively impacted by a decline in the loan loss allowance in connection with securitization transactions entered into prior to the third quarter of 1996 as discussed above.

The Company's future charge-off rates and credit quality are subject to uncertainties that could cause actual results to differ materially from what has been discussed above. Factors that influence the provision for consumer loan losses include the level and direction of consumer loan delinquencies and charge-offs, changes in consumer spending and payment behaviors, bankruptcy trends, the seasoning of the Company's loan portfolio, interest rate movements and their impact on consumer behavior, and the rate and magnitude of changes in the Company's consumer loan portfolio, including the overall mix of accounts, products and loan balances within the portfolio.

Consumer loans are considered delinquent when interest or principal payments become 30 days past due. Consumer loans are charged-off when they become 180 days past due, except in the case of bankruptcies and fraudulent transactions, where loans are charged-off earlier. Loan delinquencies and charge-offs are primarily affected by changes in economic conditions and may vary throughout the year due to seasonal consumer spending and payment behaviors. The net charge-off rate decreased in fiscal 2000 as compared with fiscal 1999, reflecting the Company's continued focus on credit quality and account collections and a reduction in consumer bankruptcies as a result of the favorable U.S. economic environment.

The following table presents delinquency and net charge-off rates with supplemental managed loan information:

Asset Quality

	Fiscal 2000		Fiscal 1999		Fiscal 1998	
	Owned	Managed	Owned	Managed	Owned	Managed
			(dollars in millions)			
Consumer loans at fiscal year-end	$21,870	$47,126	$20,998	$37,975	$15,996	$32,502
Consumer loans contractually past due as a percentage of fiscal year-end consumer loans:						
30 to 89 days	3.01%	3.50%	3.35%	3.79%	3.54%	3.69%
90 to 179 days	2.04%	2.42%	2.20%	2.53%	2.67%	2.84%
Net charge-offs as a percentage of average consumer loans	3.63%	4.40%	4.78%	5.42%	6.75%	6.90%

Non-Interest Expenses

	Fiscal 2000	Fiscal 1999	Fiscal 1998
	(dollars in millions)		
Compensation and benefits	$ 628	$ 525	$ 549
Occupancy and equipment	62	54	67
Information processing and communications	493	477	462
Marketing and business development	1,191	1,041	872
Professional services	119	121	97
Other	284	207	207
Total non-interest expenses	$2,777	$2,425	$2,254

Total non-interest expenses increased 15% to $2,777 million in fiscal 2000 and 8% to $2,425 million in fiscal 1999. Increased business activity related to the Discover Platinum Card as well as the expansion of the Morgan Stanley Dean Witter Card in the U.K. were contributing factors for a portion of the increase in non-interest expenses in fiscal 2000.

Employee compensation and benefits expense increased 20% in fiscal 2000 and decreased 4% in fiscal 1999. The increase in fiscal 2000 reflected higher domestic and international compensation costs associated with increased employment levels associated with higher levels of business activity and transaction volume. The decrease in fiscal 1999 was primarily due to lower compensation costs resulting from the sale of Prime Option and the operations of SPS. These decreases in fiscal 1999 were partially offset by higher compensation costs associated with increased employment levels due to increased levels of business activity and transaction volume.

Occupancy and equipment expense increased 15% in fiscal 2000 and decreased 19% in fiscal 1999. The increase in fiscal 2000 was due primarily to higher occupancy costs associated with increased office space, including new transaction processing centers. The decrease in fiscal 1999 was primarily due to the exclusion of the results of Prime Option and SPS, partially offset by higher occupancy costs associated with Discover Financial Services.

Information processing and communications expense increased 3% in both fiscal 2000 and fiscal 1999. The increase in fiscal 2000 was primarily due to an increase in volume-related external data processing costs associated with the Morgan Stanley Dean Witter Card in the U.K., partially offset by the termination of an external transaction processing contract in fiscal 1999. The increase in fiscal 1999 was due to higher external data processing costs incurred for domestic operations, including cardmember data analysis associated with increased portfolio activity, partially offset by the exclusion of the results of Prime Option and SPS in fiscal 1999.

Marketing and business development expense increased 14% in fiscal 2000 and 19% in fiscal 1999. The increase in fiscal 2000 was primarily due to higher cardmember rewards expense associated with increased sales volume as well as increased advertising and direct mailing costs associated with both domestic and international operations. Marketing and business development expense increased in fiscal 1999 due to direct mailing and other promotional activities related to the launch and promotion of the Discover Platinum and Morgan Stanley Dean Witter Cards, higher cardmember rewards expense and a new advertising campaign for the Discover Card. Higher cardmember rewards expense was due to increased sales volume. Cardmember rewards expense includes the Cashback Bonus® award program, pursuant to which the Company annually pays Discover Card cardmembers and Morgan Stanley Dean Witter Card cardmembers electing this feature a percentage of their purchase amounts ranging up to 1% based upon a cardmember’s annual level and type of purchases.

Professional services expense decreased 2% in fiscal 2000 and increased 25% in fiscal 1999. The decrease in fiscal 2000 reflects the exclusion of Year 2000 consulting costs in fiscal 2000’s results, partially offset by higher costs associated with account collections, consumer credit counseling and the outsourcing of certain call center operations. The increase in fiscal 1999 was due to higher costs associated with account collections, consumer credit counseling and Year 2000 consulting costs, partially offset by a decrease in expenses associated with the sale of the operations of SPS.

Other expense primarily includes fraud losses, credit inquiry fees and other administrative costs. Other expense increased 37% in fiscal 2000 and remained unchanged in fiscal 1999 as compared with fiscal 1998. In fiscal 2000, the increase was primarily due to increases in certain domestic and international operating expenses due to higher levels of transaction volume and business activity. In fiscal 1999, increased operational costs associated with higher application and transaction volumes and costs associated with the launch of the Morgan Stanley Dean Witter Card in the U.K. were offset by a decrease in expenses associated with the sale of the operations of SPS.

Seasonal Factors

The credit card lending activities of Credit Services are affected by seasonal patterns of retail purchasing. Historically, a substantial percentage of credit card loan growth occurs in the fourth calendar quarter, followed by a flattening or decline of consumer loans in the following calendar quarter. Merchant fees, therefore, historically have tended to increase in the first fiscal quarter, reflecting higher sales activity in the month of December. Additionally, higher cardmember rewards expense historically have been accrued in the first fiscal quarter, reflecting seasonal growth in retail sales volume.

Liquidity and Capital Resources

The Balance Sheet

The Company's total assets increased to $426.8 billion at November 30, 2000 from $367.0 billion at November 30, 1999, primarily attributable to increases in securities borrowed, financial instruments owned, and cash and securities deposited with clearing organizations or segregated under federal and other regulations ("Segregated Cash and Deposits"). Segregated Cash and Deposits increased due to an increase in customer cash balances, coupled with a decrease in the level of customers trading on margin. Aircraft under operating leases increased due to the purchase of Ansett Worldwide. These increases were partially offset by a decrease in securities purchased under agreements to resell. A substantial portion of the Company's total assets consists of highly liquid marketable securities and short-term receivables arising principally from securities transactions. The highly liquid nature of these assets provides the Company with flexibility in financing and managing its business.

Funding and Capital Policies

The Company's senior management establishes the overall funding and capital policies of the Company, reviews the Company's performance relative to these policies, monitors the availability of sources of financing, reviews the foreign exchange risk of the Company, and oversees the liquidity and interest rate sensitivity of the Company's asset and liability position. The primary goal of the Company's funding and liquidity activities is to ensure adequate financing over a wide range of potential credit ratings and market environments.

Many of the Company's businesses are capital-intensive. Capital is required to finance, among other things, the Company's securities inventories, underwritings, principal investments, private equity activities, consumer loans, bridge loans and other financings, and investments in fixed assets. As a policy, the Company attempts to maintain sufficient capital and funding sources in order to have the capacity to finance itself on a fully collateralized basis at all times, including periods of financial stress. Currently, the Company believes it has sufficient capital to meet its needs. In addition, the Company attempts to maintain total equity, on a consolidated basis, at least equal to the sum of all of its subsidiaries' equity. Subsidiary equity capital requirements are determined by regulatory requirements (if applicable), asset mix, leverage considerations and earnings volatility.

The Company views return on equity to be an important measure of its performance, in the context of both the particular business environment in which the Company is operating and its peer group's results. In this regard, the Company actively manages its consolidated capital position based upon, among other things, business opportunities, capital availability and rates of return together with internal capital policies, regulatory requirements and rating agency guidelines and, therefore, in the future may expand or contract its capital base to address the changing needs of its businesses. The Company returns internally generated equity capital which is in excess of the needs of its businesses to its shareholders through common stock repurchases and dividends.

The Company's liquidity policies emphasize diversification of funding sources. The Company also follows a funding strategy that is designed to ensure that the tenor of the Company's liabilities equals or exceeds the expected holding period of the assets being financed. Short-term funding generally is obtained at rates related to U.S., Euro or Asian money market rates for the currency borrowed. Repurchase transactions are effected at negotiated rates. Other borrowing costs are negotiated depending upon prevailing market conditions (see Notes 5 and 6 to the consolidated financial statements). Maturities of both short-term and long-term financings are designed to minimize exposure to refinancing risk in any one period.

The volume of the Company's borrowings generally fluctuates in response to changes in the amount of repurchase transactions outstanding, the level of the Company's securities inventories and consumer loans receivable, and overall market conditions. Availability and cost of financing to the Company can vary depending upon market conditions, the volume of certain trading activities, the Company's credit ratings and the overall availability of credit. The Company, therefore, maintains a surplus of unused short-term funding sources at all times to withstand any unforeseen contraction in credit capacity. In addition, the Company attempts to maintain cash and unhypothecated marketable securities equal to at least 110% of its outstanding short-term unsecured borrowings. The Company has in place a contingency funding strategy, which provides a comprehensive one-year action plan in the event of a severe funding disruption.

The Company views long-term debt as a stable source of funding for core inventories, consumer loans and illiquid assets and, therefore, maintains a long-term debt-to-capitalization ratio at a level appropriate for the current composition of its balance sheet. In general, fixed assets are financed with fixed rate long-term debt, and securities inventories and the majority of current assets are financed with a combination of short-term funding, floating rate long-term debt or fixed rate long-term debt swapped to a floating basis. Both fixed rate and floating rate long-term debt (in addition to sources of funds accessed directly by the Company's Credit Services business) are used to finance the Company's consumer loan portfolio. Consumer loan financing is targeted to match the repricing and duration characteristics of the loans financed. The Company uses derivative products (primarily interest rate, currency and equity swaps) to assist in asset and liability management, reduce borrowing costs and hedge interest rate risk (see Note 6 to the consolidated financial statements).

The Company's reliance on external sources to finance a significant portion of its day-to-day operations makes access to global sources of financing important. The cost and availability of unsecured financing generally are dependent on the Company's short-term and long-term debt ratings. In addition, the Company's debt ratings can have a significant impact on certain trading revenues, particularly in those businesses where longer term counterparty performance is critical, such as over-the-counter derivative transactions.

As of January 31, 2001, the Company's credit ratings were as follows:

	Commercial Paper	Senior Debt
Dominion Bond Rating Service Limited	R-1 (middle)	AA (low)
Fitch(1)	F1+	AA
Moody's Investors Service	P-1	Aa3
Rating and Investment Information, Inc.(2)	a-1+	AA
Standard & Poor's(3)	A-1+	AA-

(1) Fitch IBCA, Inc. and Duff & Phelps Credit Rating Co. merged on June 1, 2000. In addition, on December 1, 2000, Fitch completed its acquisition of Thomson Financial BankWatch. The combined company is using the former Fitch IBCA, Inc. rating scale.

(2) On August 1, 2000, Japan Rating & Investment Information, Inc. changed its name to Rating and Investment Information, Inc.

(3) On May 17, 2000, Standard & Poor's upgraded the Company's commercial paper rating from A-1 to A-1+ and upgraded the Company's senior debt rating from A+ to AA-.

As the Company continues its global expansion and derives revenues increasingly from various currencies, foreign currency management is a key element of the Company's financial policies. The Company benefits from operating in several different currencies because weakness in any particular currency often is offset by strength in another currency. The Company closely monitors its exposure to fluctuations in currencies and, where cost-justified, adopts strategies to reduce the impact of these fluctuations on the Company's financial performance. These strategies include engaging in various hedging activities to manage income and cash flows denominated in foreign currencies and using foreign currency borrowings, when appropriate, to finance investments outside the U.S.

Principal Sources of Funding

The Company funds its balance sheet on a global basis. The Company's funding for its Securities and Asset Management businesses is raised through diverse sources. These sources include the Company's capital, including equity and long-term debt; repurchase agreements; U.S., Canadian, Euro and Japanese commercial paper; letters of credit; unsecured bond borrowings; securities lending; buy/sell agreements; municipal reinvestments; master notes; and committed and uncommitted lines of credit. Repurchase agreement transactions, securities lending and a portion of the Company's bank borrowings are made on a collateralized basis and, therefore, provide a more stable source of funding than short-term unsecured borrowings.

The funding sources utilized for the Company's Credit Services business include the Company's capital, including equity and long-term debt; asset-backed securitizations; deposits; Federal Funds; and short-term bank notes. The Company sells consumer loans through asset securitizations using several transaction structures. During the second quarter of fiscal 2000, an extendible asset-backed certificate program was launched.

Fiscal 2000 and Subsequent Activity

During fiscal 2000, the Company issued senior notes aggregating $22,363 million, including non-U.S. dollar currency notes aggregating $3,298 million, primarily pursuant to its public debt shelf registration statements. These notes have maturities from 2001 to 2030 and a weighted average coupon interest rate of 6.55% at November 30, 2000. The Company has entered into certain transactions to obtain floating interest rates based primarily on short-term London Interbank Offered Rates ("LIBOR") trading levels. At November 30, 2000, the aggregate outstanding principal amount of the Company's Senior Indebtedness (as defined in the Company's public debt shelf registration statements) was approximately $65.2 billion (including senior indebtedness consisting of guaranteed obligations of the indebtedness of subsidiaries). Between November 30, 2000 and January 31, 2001, the Company's long-term borrowings, net of repayments and repurchases, decreased by approximately $305 million.

Effective June 22, 2000, the Company's Board of Directors authorized the Company to purchase, subject to market conditions and certain other factors, an additional $1.5 billion of the Company's common stock for capital management purposes. The Company also has a separate ongoing repurchase authorization in connection with awards granted under its equity-based compensation plans. During fiscal 2000, the Company purchased $3,628 million of its common stock. Subsequent to November 30, 2000 and through January 31, 2001, the Company purchased an additional $256 million of its common stock; the unused portion of the capital management common stock repurchase authorization at January 31, 2001 was approximately $911 million (without giving effect to any outstanding put options).

In an effort to enhance its ongoing stock repurchase program, the Company may sell put options on shares of its common stock to third parties. These put options entitle the holder to sell shares of the Company's common stock to the Company on certain dates at specified prices. As of November 30, 2000, put options were outstanding on an aggregate of 3 million shares of the Company's common stock. These put options have various expiration dates that range from January 2001 through April 2001. The Company may elect cash settlement of the put options instead of taking delivery of the stock.

In fiscal 2000, the Company and Morgan Stanley Finance, plc, a U.K. subsidiary, redeemed all of the outstanding 8.4% Capital Units, 8.2% Capital Units and 9.0% Capital Units. The aggregate principal amount of the Capital Units redeemed was $513 million.

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In connection with certain of its business activities, the Company provides financing or financing commitments to companies in the form of senior and subordinated debt, including bridge financing, on a selective basis. The borrowers may be rated investment grade or non-investment grade. These loans and funding commitments typically are secured against the borrower's assets, have varying maturity dates and are generally contingent upon certain representations, warranties and contractual conditions applicable to the borrower. As part of these activities, the Company may syndicate and trade certain positions of these loans. At November 30, 2000 and 1999, the aggregate value of investment grade loans and positions was $2.1 billion and $0.1 billion, respectively, and the aggregate value of non-investment grade loans and positions was $2.2 billion and $1.3 billion, respectively. At November 30, 2000, the Company also had provided additional commitments associated with these activities to investment grade issuers aggregating $12.2 billion and commitments to non-investment grade issuers aggregating $2.3 billion.

The Company has contracted to develop a one million-square-foot office tower in New York City. Pursuant to this agreement, the Company will own the building and has entered into a 99-year lease for the land at the development site. Construction began in 1999, and the Company intends to occupy the building upon project completion, which is anticipated in fiscal 2002. The total investment in this project is estimated to be approximately $700 million.

The gross notional and fair value amounts of derivatives used by the Company for asset and liability management and as part of its trading activities are summarized in Notes 6 and 9, respectively, to the consolidated financial statements (see also "Derivative Financial Instruments" herein).

Regulatory Capital Requirements

Dean Witter Reynolds Inc. ("DWR") and MS&Co. are registered broker-dealers and registered futures commission merchants and, accordingly, are subject to the minimum net capital requirements of the Securities and Exchange Commission ("SEC"), the New York Stock Exchange and the Commodity Futures Trading Commission. MSIL, a London-based broker-dealer subsidiary, is regulated by the Securities and Futures Authority ("SFA") in the U.K. and, accordingly, is subject to the capital requirements of the SFA. MSDWJL, a Tokyo-based broker-dealer, is subject to the capital requirements of the Financial Services Agency. DWR, MS&Co., MSIL and MSDWJL have consistently operated in excess of their respective regulatory requirements (see Note 11 to the consolidated financial statements).

Certain of the Company's subsidiaries are Federal Deposit Insurance Corporation ("FDIC") insured financial institutions. Such subsidiaries, therefore, are subject to the regulatory capital requirements adopted by the FDIC. These subsidiaries have consistently operated in excess of these and other regulatory requirements.

Certain other U.S. and non-U.S. subsidiaries are subject to various securities, commodities and banking regulations, and capital adequacy requirements promulgated by the regulatory and exchange authorities of the countries in which they operate. These subsidiaries have consistently operated in excess of their applicable local capital adequacy requirements. In addition, Morgan Stanley Derivative Products Inc., a triple-A rated subsidiary through which the Company conducts some of its derivative activities, has established certain operating restrictions which have been reviewed by various rating agencies.

Effects of Inflation and Changes in Foreign Exchange Rates

Because the Company's assets to a large extent are liquid in nature, they are not significantly affected by inflation. However, inflation may result in increases in the Company's expenses, which may not be readily recoverable in the price of services offered. To the extent inflation results in rising interest rates and has other adverse effects upon the securities markets, upon the value of financial instruments and upon the markets for consumer credit services, it may adversely affect the Company's financial position and profitability.

A portion of the Company's business is conducted in currencies other than the U.S. dollar. Non-U.S. dollar assets typically are financed by direct borrowing or swap-based funding in the same currency. Changes in foreign exchange rates affect non-U.S. dollar revenues as well as non-U.S. dollar expenses. Those foreign exchange exposures that arise and are not hedged by an offsetting foreign currency exposure are actively managed by the Company to minimize risk of loss due to currency fluctuations.

Derivative Financial Instruments

The Company actively offers to clients and trades for its own account a variety of financial instruments described as “derivative products” or “derivatives.” These products generally take the form of futures, forwards, options, swaps, caps, collars, floors, swap options and similar instruments which derive their value from underlying interest rates, foreign exchange rates, commodities, equity instruments, equity indices, reference credits or other assets. All of the Company’s trading-related divisions use derivative products as an integral part of their respective trading strategies, and such products are used extensively to manage the market exposure that results from a variety of proprietary trading activities (see Note 9 to the consolidated financial statements). In addition, as a dealer in certain derivative products, most notably interest rate and currency swaps, the Company enters into derivative contracts to meet a variety of risk management and other financial needs of its clients. Given the highly integrated nature of derivative products and related cash instruments in the determination of overall trading division profitability and the context in which the Company manages its trading areas, it is not meaningful to allocate trading revenues between the derivative and underlying cash instrument components. Moreover, the risks associated with the Company’s derivative activities, including market and credit risks, are managed on an integrated basis with associated cash instruments in a manner consistent with the Company’s overall risk management policies and control structure (see “Risk Management” following “Management’s Discussion and Analysis of Financial Condition and Results of Operations”). It should be noted that while particular risks may be associated with the use of derivatives, in many cases derivatives serve to reduce, rather than increase, the Company’s exposure to market, credit and other risks.

The total notional value of derivative trading contracts outstanding at November 30, 2000 was $3,891 billion (as compared with $3,404 billion at November 30, 1999). While these amounts are an indication of the degree of the Company’s use of derivatives for trading purposes, they do not represent the Company’s market or credit exposure and may be more indicative of customer utilization of derivatives. The Company’s exposure to market risk relates to changes in interest rates, foreign currency exchange rates, or the fair value of the underlying financial instruments or commodities. The Company’s exposure to credit risk at any point in time is represented by the fair value of such contracts reported as assets. Such total fair value outstanding as of November 30, 2000 was $27.3 billion. Approximately $19.9 billion of that credit risk exposure was with counterparties rated single-A or better (see Note 9 to the consolidated financial statements).

The Company also uses derivative products (primarily interest rate[0.00064(g)6.4(f5)5.9(olidated)8.1)19od f5olidas( )e-cts s).9(olidato1

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

RISK MANAGEMENT

Risk Management Policy and Control Structure

Risk is an inherent part of the Company's business and activities. The extent to which the Company properly and effectively identifies, assesses, monitors and manages each of the various types of risk involved in its activities is critical to its soundness and profitability. The Company's broad-based portfolio of business activities helps reduce the impact that volatility in any particular area or related areas may have on its net revenues as a whole. The Company seeks to identify, assess, monitor and manage, in accordance with defined policies and procedures, the following principal risks involved in the Company's business activities: market risk, credit risk, operational risk, legal risk and funding risk. Funding risk is discussed in the "Liquidity and Capital Resources" section of "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Risk management at the Company is a multi-faceted process with independent oversight that requires constant communication, judgment and knowledge of specialized products and markets. The Company's senior management takes an active role in the risk management process and has developed policies and procedures that require specific administrative and business functions to assist in the identification, assessment and control of various risks. In recognition of the increasingly varied and complex nature of the global financial services business, the Company's risk management policies, procedures and methodologies are evolutionary in nature and are subject to ongoing review and modification.

The Management Committee, composed of the Company's most senior officers, establishes the overall risk management policies for the Company and reviews the Company's performance relative to these policies. The Management Committee has created several Risk Committees to assist it in monitoring and reviewing the Company's risk management practices. These Risk Committees, as well as other committees established to manage and monitor specific risks, review the risk monitoring and risk management policies and procedures relating to the Company's market and credit risk profile, sales practices, pricing of consumer loans and reserve adequacy, legal enforceability, and operational and systems risks.

The Firm Risk Management, Controllers, Treasury, and Law and Compliance Departments, which are all independent of the Company's business units, also assist senior management and the Risk Committees in monitoring and controlling the Company's risk profile. The Firm Risk Management Department is responsible for risk policy development, risk analysis and risk reporting to senior management and the Risk Committees and has operational responsibility for measuring and monitoring aggregate market and credit risk with respect to institutional trading activities. In addition, the Internal Audit Department, which also reports to senior management, periodically examines and evaluates the Company's operations and control environment. The Company continues to be committed to employing qualified personnel with appropriate expertise in each of its various administrative and business areas to implement effectively the Company's risk management and monitoring systems and processes.

The following is a discussion of the Company's risk management policies and procedures for its principal risks (other than funding risk). The discussion focuses on the Company's securities trading (primarily its institutional trading activities) and consumer lending and related activities. The Company believes that these activities generate a substantial portion of its principal risks. This discussion and the estimated amounts of the Company's market risk exposure generated by the Company's statistical analyses are forward-looking statements. However, the analyses used to assess such risks are not predictions of future events, and actual results may vary significantly from such analyses due to events in the markets in which the Company operates and certain other factors described below.

Market Risk

Market risk refers to the risk that a change in the level of one or more market prices, rates, indices, volatilities, correlations or other market factors, such as liquidity, will result in losses for a position or portfolio. For a discussion of the Company's currency exposure relating to its net monetary investments in non-U.S. dollar functional currency subsidiaries, see Note 11 to the consolidated financial statements.

Trading and Related Activities

Primary Market Risk Exposures and Market Risk Management

During fiscal 2000, the Company had exposures to a wide range of interest rates, equity prices, foreign exchange rates and commodity prices — and associated volatilities and spreads — related to the global markets in which it conducts its trading activities. The Company is exposed to interest rate risk as a result of maintaining market-making activities and proprietary trading in interest rate sensitive financial instruments (e.g., risk arising from changes in the level or volatility of interest rates, the timing of mortgage prepayments, the shape of the yield curve and credit spreads for corporate bonds, asset-backed securities and emerging market debt). The Company is exposed to equity price and implied volatility risk as a result of making markets in equity securities and equity derivatives and maintaining proprietary positions. The Company is exposed to foreign exchange rate and implied volatility risk in connection with making markets in foreign currencies and foreign currency options and with maintaining foreign exchange positions. The Company's foreign exchange trading covers many currencies, including the yen, euro and pound sterling. The Company is exposed to commodity price and implied volatility risk as a result of trading in physical commodities, such as crude and refined oil, natural gas, electricity, precious and base metals, and in related derivatives.

The Company manages its trading positions by employing a variety of strategies. These strategies include diversification of risk exposures and hedging through the purchase or sale of positions in related securities and financial instruments, including a variety of derivative products (e.g., futures, forwards, swaps and options). The Company manages the market risk associated with its trading activities on a Company-wide basis, on a trading division level worldwide and on an individual product basis. The Company manages and monitors its market risk exposures in such a way as to maintain a portfolio that the Company believes is well-diversified in the aggregate with respect to market risk factors and reflects the Company's aggregate risk tolerance as established by the Company's senior management.

Market risk limits have been approved for the Company and each major trading division of the Company worldwide (equity, fixed income, foreign exchange and commodities). Additional market risk limits are assigned to trading desks and, as appropriate, products and regions. Trading division risk managers, desk risk managers and the Firm Risk Management Department monitor market risk measures against limits in accordance with policies set by senior management.

The Firm Risk Management Department independently reviews the Company's trading portfolios on a regular basis from a market risk perspective utilizing Value-at-Risk ("VaR") and other quantitative and qualitative risk measurements and analyses. The Company's trading businesses and the Firm Risk Management Department also use, as appropriate, measures such as sensitivity to changes in rates, prices, volatilities and time decay to monitor and report market risk exposures. Stress testing, which measures the impact on the value of existing portfolios of specified changes in market factors for certain products, is performed periodically and reviewed by trading division risk managers, desk risk managers and the Firm Risk Management Department.

Value-at-Risk

The statistical technique known as VaR is one of the tools used by management to measure, monitor and review the market risk exposures of the Company's trading portfolios. The Firm Risk Management Department calculates and distributes daily VaR-based risk measures to various levels of management.

VaR Methodology, Assumptions and Limitations

The Company estimates VaR using a model based on historical simulation for major market risk factors and Monte Carlo simulation for name-specific risk in certain equity and fixed income exposures. Historical simulation involves constructing a distribution of hypothetical daily changes in the value of trading portfolios based on historical observation of daily changes in key market indices or other market factors ("market risk factors") and on information on the sensitivity of the portfolio values to these market risk factor changes. In the case of the Company's VaR, approximately four years of historical data are used to characterize potential changes in market risk factors. The Company's one-day 99% VaR corresponds to the negative change in portfolio value that, based on observed market risk factor movements, would have been exceeded with a frequency of 1%, or once in 100 trading days.

The Company's VaR model generally takes into account linear and non-linear exposures to price and interest rate risk and linear exposure to implied volatility risks. Market risks that are incorporated in the VaR model include equity and commodity prices, interest rates, foreign exchange rates and associated volatilities. As a supplement to the use of historical simulation for major market risk factors, the Company's VaR model uses Monte Carlo simulation to capture name-specific risk in equities and in corporate and high-yield bonds. For example, the model includes measures of name-specific risk for approximately 10,000 equity names and 100 classes of corporate and high-yield bonds.

VaR models such as the Company's should be expected to evolve over time in response to changes in the composition of trading portfolios and to improvements in modeling techniques and systems capabilities. For example, during fiscal 2000, as part of the Company's ongoing program of VaR model enhancement, position and risk coverage were broadened and risk measurement methodologies were refined for certain energy and fixed income products.

Among their benefits, VaR models permit estimation of a portfolio's aggregate market risk exposure, incorporating a range of varied market risks; reflect risk reduction due to portfolio diversification; and can cover a wide range of portfolio assets yet are relatively easy to interpret. However, VaR risk measures should be interpreted in light of the methodology's limitations, which include the following: past changes in market risk factors will not always yield accurate predictions of the distributions and correlations of future market movements; changes in portfolio value in response to market movements may differ from the responses calculated by a VaR model; VaR using a one-day time horizon does not fully capture the market risk of positions that cannot be liquidated or hedged within one day; the historical market risk factor data used for VaR estimation may provide only limited insight into losses that could be incurred under market conditions that are unusual relative to the historical period used in estimating the VaR; and published VaR results reflect past trading positions while future risk depends on future positions. The Company is aware of these and other limitations and, therefore, uses VaR as only one component in its risk management review process. This process also incorporates stress testing and extensive risk monitoring and control at the trading desk, division and Company levels.

VaR for Fiscal 2000

The table below presents the Company's VaR for each of the Company's primary market risk exposures and on an aggregate basis at November 30, 2000 and November 30, 1999, incorporating substantially all financial instruments generating market risk that are managed by the Company's institutional trading businesses. This measure of VaR incorporates most of the Company's trading-related market risks. However, a small proportion of trading positions generating market risk was not covered, and the modeling of the risk characteristics of some positions involved approximations that could be significant under certain circumstances. Aspects of market risk associated with positions reflected in the VaR results below that the Company has found particularly difficult to model include certain risks associated with fixed income instruments (such as prepayment behavior of mortgage-backed securities and elements of credit derivatives price risk), name-specific equity price risk in newly public companies, certain commodity price risks (such as electricity price risk) and certain liquidity risks.

Aggregate VaR also incorporates (a) the funding liabilities related to institutional trading positions and (b) public-company equity positions recorded as principal investments by the Company. The incremental impact on VaR of these non-trading positions was not material as of November 30, 2000 and 1999, and, therefore, the table below does not separately report trading and non-trading VaRs.

Non-publicly traded principal investments made by the Company are not reflected in the VaR results reported below. As of November 30, 2000, the total amount of such investments was approximately $1 billion.

Since VaR statistics reported below are estimates based on historical position and market data, VaR should not be viewed as predictive of the Company's future financial performance or its ability to monitor and manage risk. There can be no assurance that the Company's actual losses on a particular day will not exceed the VaR amounts indicated below or that such losses will not occur more than once in 100 trading days.

Primary Market Risk Category	99%/One-Day VaR at November 30	
	2000	1999
	(dollars in millions, pre-tax)	
Interest rate	$ 28	$33
Equity price	27	32
Foreign exchange rate	5	3
Commodity price	17	16
Subtotal	77	84
Less diversification benefit(1)	35	33
Aggregate VaR	$ 42	$51

(1) Equals the difference between Aggregate VaR and the sum of the VaRs for the four risk categories. This benefit arises because the simulated 99%/one-day losses for each of the four primary market risk categories occur on different days; similar diversification benefits also are taken into account within each such category.

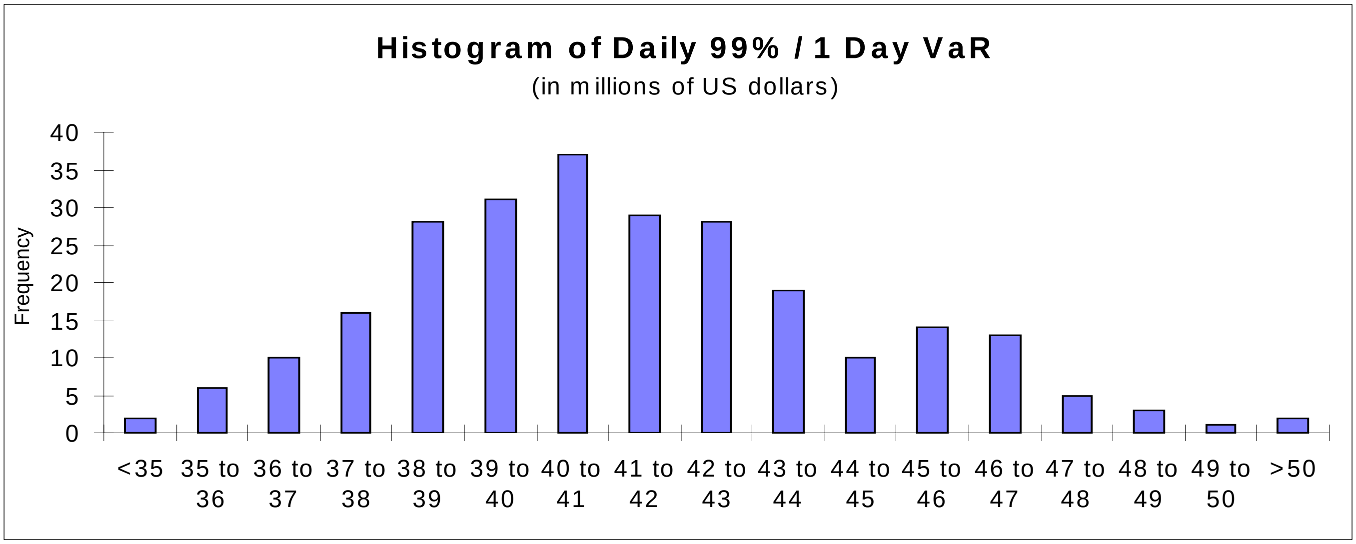
The change in aggregate VaR and its interest rate and equity price components from November 30, 1999 to November 30, 2000 primarily reflected a reduction in municipal, emerging market and high-yield debt positions in the Company's trading portfolio and the sale of certain private equity positions.

In order to facilitate comparisons with other global financial services firms, the Company notes that its Aggregate VaR values at November 30, 2000 for other confidence levels and time horizons were as follows: $29 million for 95%/one-day VaR and $134 million for 99%/two-week VaR.

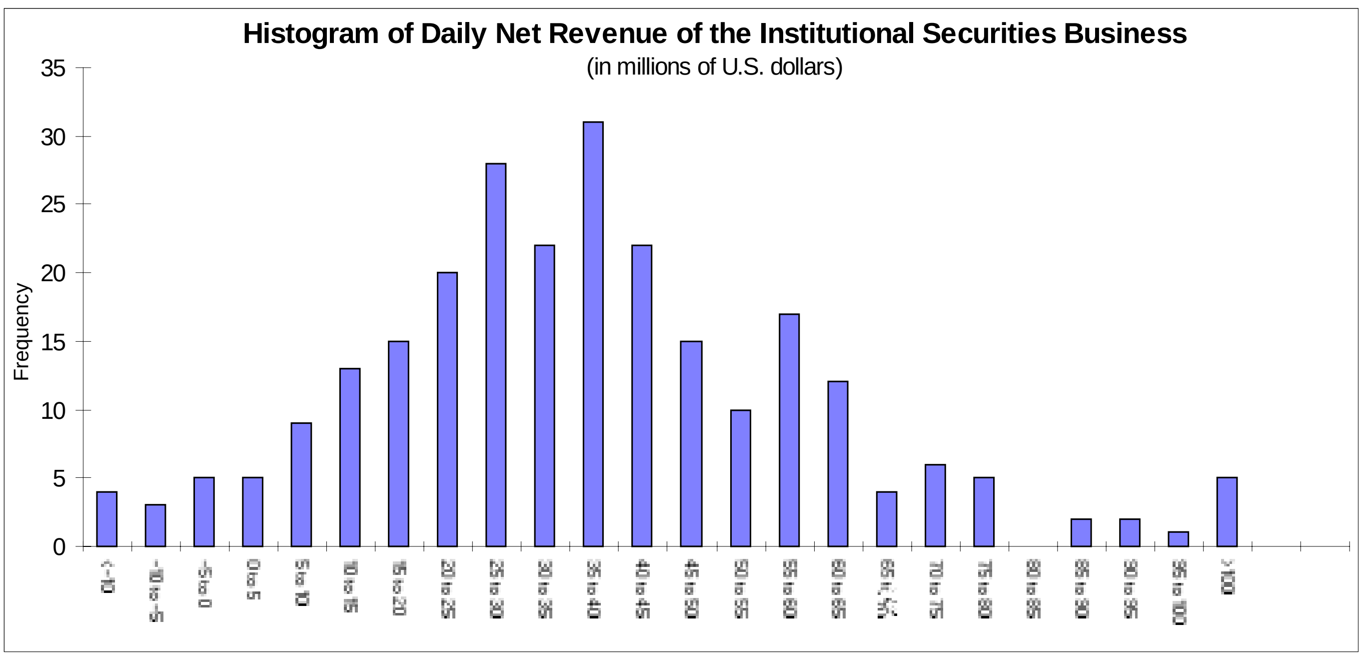
The table below presents the high, low and average 99%/one-day trading VaR over the course of fiscal 2000 for substantially all of the Company's institutional trading activities. Certain market risks included in the year-end VaR discussed above are excluded from this measure (e.g., equity price risk in public-company equity positions recorded as principal investments by the Company and certain funding liabilities related to trading positions).

Primary Market Risk Category	Daily 99%/One-Day VaR for Fiscal 2000		
	High	Low	Average
	(dollars in millions, pre-tax)		
Interest rate	$ 48	$21	$ 29
Equity price	36	17	24
Foreign exchange rate	11	3	5
Commodity price	21	11	16
Trading VaR	$ 51	$33	$ 40

The histogram below presents the Company's daily 99%/one-day VaR for its institutional trading activities during fiscal 2000:



The histogram below shows the distribution of daily revenues during fiscal 2000 for the Company's institutional trading businesses (net of interest expense and including commissions and primary revenue credited to the trading businesses):



The Company evaluates the reasonableness of its VaR model by comparing the potential declines in portfolio values generated by the model with actual trading results. There were no days during fiscal 2000 in which the Company incurred daily mark-to-market losses (trading revenue net of interest income and expense and excluding commissions and primary revenue credited to the trading businesses) in its institutional trading business in excess of the 99%/one-day VaR.

Consumer Lending and Related Activities

Interest Rate Risk and Management

In its consumer lending activities, the Company is exposed to market risk primarily from changes in interest rates. Such changes in interest rates impact interest earning assets, principally credit card and other consumer loans and net servicing fees received in connection with consumer loans sold through asset securitizations, as well as the interest-sensitive liabilities which finance these assets, including asset-backed securitizations; long-term borrowings; deposits; Federal Funds; and short-term bank notes.

The Company's interest rate risk management policies are designed to reduce the potential volatility of earnings which may arise from changes in interest rates. This is accomplished primarily by matching the repricing of credit card and consumer loans and the related financing. To the extent that asset and related financing repricing characteristics of a particular portfolio are not matched effectively, the Company utilizes interest rate derivative contracts, such as swap agreements, to achieve its matched financing objectives. Interest rate swap agreements effectively convert the underlying asset or financing from fixed to variable repricing, from variable to fixed repricing or, in more limited circumstances, from variable to variable repricing.

Sensitivity Analysis Methodology, Assumptions and Limitations

For its consumer lending activities, the Company uses a variety of techniques to assess its interest rate risk exposure, one of

Credit Risk

The Company's exposure to credit risk arises from the possibility that a customer or counterparty to a transaction might fail to perform under its contractual commitment, which could result in the Company incurring losses. With respect to its institutional securities activities, the Company has credit guidelines which limit the Company's current and potential credit exposure to any one counterparty and to each type of counterparty (by rating category). The Credit Department that is responsible for the Company's institutional securities activities administers and monitors these credit limits on a worldwide basis. In addition to monitoring credit limits, the Company manages the credit exposure relating to its trading activities by reviewing periodically counterparty financial soundness, by entering into master netting agreements and collateral arrangements with counterparties in appropriate circumstances, and by limiting the duration of exposure. In certain cases, the Company also may close out transactions, enter into risk reducing transactions, assign transactions to other counterparties or purchase credit protection to mitigate credit risk. With respect to the leveraged lending business, the Leveraged Financing Commitment Committee, which is composed of senior managers from various departments within the Company, including the Credit Department, reviews each leveraged loan request.

With respect to its consumer lending activities, potential credit card holders undergo credit reviews by the Credit Department of Discover Financial Services to establish that they meet standards of ability and willingness to pay. Credit card applications are evaluated using scoring models (statistical evaluation models) based on information obtained from applicants and credit bureaus. The Company's credit scoring systems include both industry and customized models using the Company's criteria and historical data. Each cardmember's credit line is reviewed at least annually, and actions resulting from such review may include raising or lowering a cardmember's credit line or closing the account. In addition, the Company, on a portfolio basis, performs periodic monitoring and review of consumer behavior and risk profiles. The Company also reviews the creditworthiness of prospective Discover Business Services merchants and conducts annual reviews of merchants with the greatest scrutiny given to merchants with substantial sales volume.

The Company is subject to concentration risk by holding large positions in certain types of securities or commitments to purchase securities of a single issuer, including sovereign governments and other entities, issuers located in a particular country or geographic area, public and private issuers involving developing countries or issuers engaged in a particular industry (see Note 9 to the consolidated financial statements).

Operational Risk

Operational risk refers generally to the risk of loss resulting from the Company's operations, including, but not limited to, improper or unauthorized execution and processing of transactions, deficiencies in the Company's operating systems, and inadequacies or breaches in the Company's control processes. The Company operates different businesses in diverse markets and is reliant on the ability of its employees and systems to process high numbers of transactions. These transactions may cross multiple markets and involve different currencies. In the event of a breakdown or improper operation of systems or improper action by employees, the Company could suffer financial loss, regulatory sanctions and damage to its reputation.

In order to mitigate and control operational risk, the Company has developed and continues to enhance specific policies and procedures that are designed to identify and manage operational risk at appropriate levels. For example, the Company's securities business has procedures that require that all transactions are accurately recorded and properly reflected in the Company's books and records and are confirmed on a timely basis; that position valuations are subject to periodic independent review procedures; and that collateral and adequate documentation (e.g., master agreements) are obtained from counterparties in appropriate circumstances. With respect to its consumer lending activities, the Company manages operational risk through its system of internal controls which provides checks and balances to ensure that transactions and other account-related activity (e.g., new account solicitation, transaction authorization and processing, billing and collection of delinquent accounts) are properly approved, processed, recorded and reconciled. Disaster recovery plans are in place for critical systems on a Company-wide basis, and redundancies are built into the systems as deemed appropriate. The Company also uses periodic self-assessments and Internal Audit reviews as a further check on operational risk.

Legal Risk

Legal risk includes the risk of non-compliance with applicable legal and regulatory requirements and the risk that a counterparty's performance obligations will be unenforceable. The Company is generally subject to extensive regulation in the different jurisdictions in which it conducts its business. The Company has established procedures based on legal and regulatory requirements on a worldwide basis that are designed to ensure compliance with all applicable statutory and regulatory requirements. The Company, principally through the Law and Compliance Department, also has established procedures that are designed to ensure that senior management's policies relating to conduct, ethics and business practices are followed globally. In connection with its businesses, the Company has various procedures addressing issues, such as regulatory capital requirements, sales and trading practices, new products, use and safekeeping of customer funds and securities, credit granting, collection activities, money-laundering and recordkeeping. The Company also has established procedures to mitigate the risk that a counterparty's performance obligations will be unenforceable, including consideration of counterparty legal authority and capacity, adequacy of legal documentation, the permissibility of a transaction under applicable law and whether applicable bankruptcy or insolvency laws limit or alter contractual remedies.