



One Priority: Performance

Morgan Stanley Annual Report 2005

January 17, 2006: Morgan Stanley common stock began trading on the New York Stock Exchange under the symbol “MS.” The change aligns our ticker with the Morgan Stanley name and reflects the actions we’re taking to move forward as “one firm” and realize the full potential of our global franchise.

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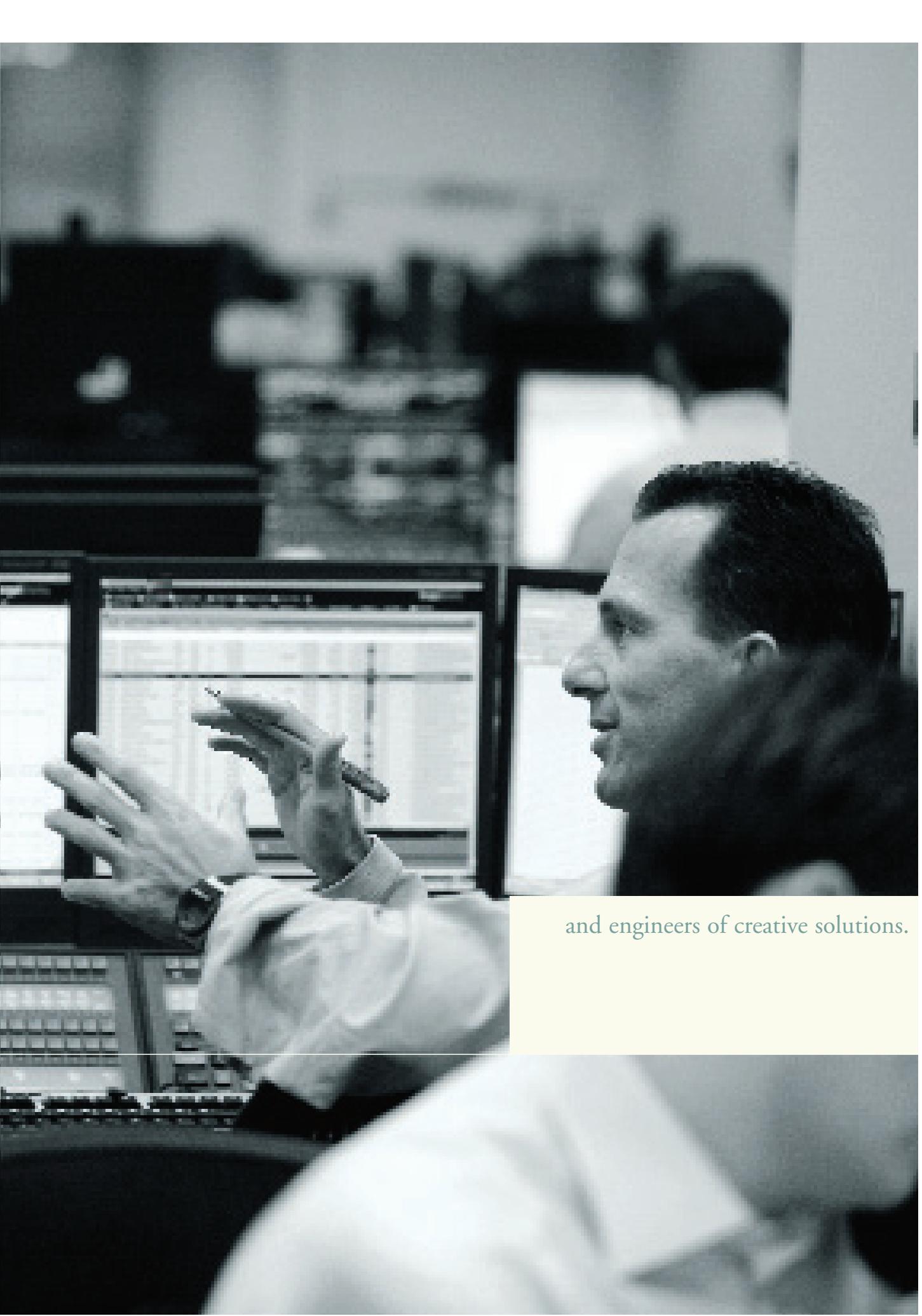
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Today, the power of the Morgan Stanley franchise has never been stronger. We have remarkably talented people. We have unmatched client relationships. We have a clear blueprint for building and further improving upon our global business performance. And we are more determined and better equipped than ever to deliver superior returns to our shareholders.



We are masters of complexity





and engineers of creative solutions.



We are trusted advisors





and powerful distribution muscle.



We are experienced risk managers



and over \$600 billion in client assets.

We are in the right mix of businesses—businesses our competitors want to be in. We have the scale, expertise and capabilities to succeed globally.

To Our Shareholders:

2005 was a year of challenge and change for Morgan Stanley—a turbulent period for employees and shareholders alike. Nevertheless, through constant dedication and commitment to our clients, we finished the year strongly, and we have begun 2006 with renewed momentum and focus on performance.

This firm has tremendous potential. We are in the right mix of businesses—businesses our competitors want to be in. We have the scale, expertise and capabilities to succeed globally. We are an unrivaled leader in delivering innovative solutions to our clients' most complex problems. We boast a superb investment banking franchise, preeminence in key businesses such as prime brokerage and commodities, and leading positions in high-growth emerging markets. Our Retail Brokerage business holds more than \$600 billion in client assets, and our Asset Management business manages more than \$400 billion for both retail and institutional clients. Our credit card business is a unique, successful franchise that generates high-quality earnings and cash flow.

Most important, the Morgan Stanley franchise has never been stronger, and our people remain the most talented in the industry. Indeed, this past summer when I returned home to the firm where I had spent nearly 30 years, my most profound impression was of the quality and commitment of Morgan Stanley's people.

This team took full advantage of an attractive market environment in 2005 to deliver a strong finish to the year. The firm's focus and commitment delivered record revenues for the year, record earnings for the fourth quarter and two consecutive quarters of improving financial performance.

This powerful finish was helped by particularly strong results in Institutional Securities, which continued to demonstrate its broad and powerful franchise. In 2005, we achieved record fixed income sales and trading revenues, record prime brokerage revenues and the highest advisory revenues in five years. In our U.S. Retail Brokerage business, we increased the percentage of client households with over \$1 million in assets to 62% of total assets. Asset Management continued to deliver solid margins of 29% during 2005, excluding private equity, and we believe we can generate profitable growth in this area. At Discover, we saw pressure on earnings from the rising cost of funds, but benefited from positive underlying credit trends, despite the rise in bankruptcy filings this past fall.

Focus on Performance

Even with this improvement at the end of 2005, there clearly is substantial room for further gains across all of our businesses. We have the right team, the right assets and the right business mix in place. Now we must maintain a relentless focus on one priority: performance.

What is our plan to achieve the level of performance our firm is capable of delivering and our investors have every right to expect?

Strategically, we will continue to be a diversified, global firm focused on improving growth, profit margins and return on equity. We will take full advantage of our global scale and our world-class franchise by further integrating our businesses and putting more of our own capital to work in principal investments. We are committed to addressing underinvestment in both our Retail and Asset Management businesses and will build our capabilities in areas where the firm is underrepresented. We will aggressively pursue new opportunities for organic growth and, when appropriate, acquisitions that will help grow the scope and scale of our key businesses. We will tear down any barriers that impede our ability to work as one team across Morgan Stanley and create a cohesive “one firm” culture where every employee acts and feels like an owner of the firm. We will continue to nurture and support the first-rate talent that makes this firm what it is, and we will relentlessly execute on the operating plan we’ve developed to drive growth and increase earnings.

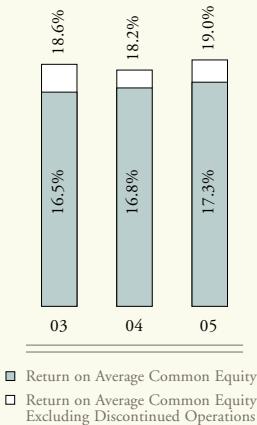
We have already undertaken significant steps to improve our overall performance. We’ve further strengthened our management team, drawing on talent from both inside and outside the firm. We hired, among others, James Gorman to lead Retail Brokerage and Gary Lynch, the former head of enforcement for the Securities and Exchange Commission, to be our Chief Legal Officer. We have assembled a new leadership team and organizational structure in Institutional Securities, where Neal Shear and Jerker Johansson have continued to integrate the firm’s equity and fixed income businesses to drive revenue growth and improve the delivery of multi-asset-class opportunities to our clients. Owen Thomas was appointed our new head of Asset Management in December, and he has already started to implement a strategy to deliver growth and profitability in that business. We also reached an agreement in January 2006 to sell our non-core aircraft leasing business, and we plan to invest the sale proceeds in our core businesses.

We are moving aggressively to improve performance:

- In Institutional Securities, we’re focusing on maintaining a leadership position in areas with the highest expected growth while investing to increase our scale in areas where we are underrepresented, such as principal investments, equity derivatives and European mortgages. We will expand our capabilities across fixed income, equities and investment banking by creating structured products and more innovative solutions for clients. For instance, we plan to enhance our strong commodities business by using it as a platform for investing in physical assets such as power plants. We also are committed to building our leveraged finance business to better focus on profitable and underexploited opportunities in the middle market.
- Emerging markets, with their high projected GDP growth rates, offer significant opportunities for expansion, particularly

In 2005, we achieved record fixed income sales and trading revenues, record prime brokerage revenues and the highest advisory revenues in five years.

Return on Average
Common Equity
By Percent



□ Return on Average Common Equity
□ Return on Average Common Equity
Excluding Discontinued Operations

Net Revenues
Dollars in Millions



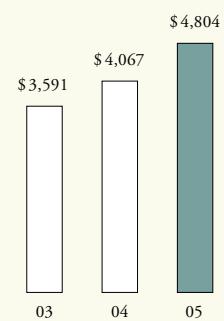
Institutional Securities
Net Revenues
Dollars in Millions



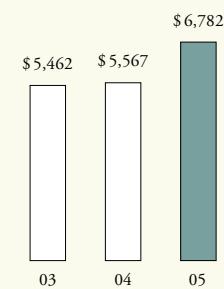
Institutional Securities
Advisory Revenues
Dollars in Millions



Institutional Securities
Equity Sales and
Trading Revenues
Dollars in Millions



Institutional Securities
Fixed Income Sales and
Trading Revenues⁽¹⁾
Dollars in Millions



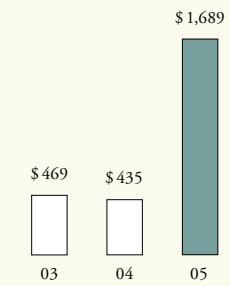
All charts are based on fiscal year results of operations
for the 12 months ended November 30.

⁽¹⁾ Amounts include interest rate and currency products, credit products and
commodities. Amounts exclude revenues from corporate lending activities.

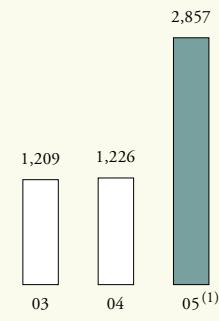
Retail Brokerage
Total Client Assets
Dollars in Billions



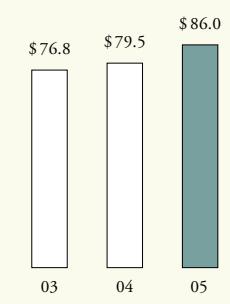
Retail Brokerage
Bank Deposit Program
Dollars in Millions



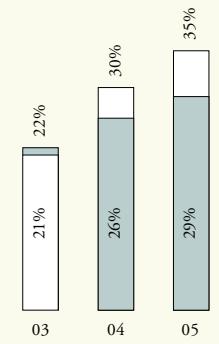
Discover
Payment Services
Network Volume
Transactions in Millions



Discover
Net Sales
Dollars in Billions

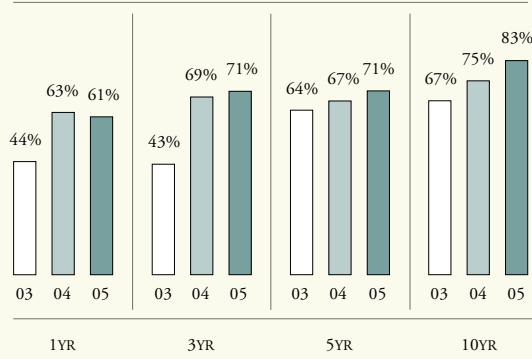


Asset Management
Pre-tax Profit Margin
By Percent



□ Pre-tax profit margin
■ Pre-tax profit margin excluding private equity

Asset Management
Percent of Fund Assets in
Top Half of Lipper Rankings⁽²⁾
November End



All charts are based on fiscal year results of operations
for the 12 months ended November 30.

⁽¹⁾ 2005 includes PULSE network transaction volume of 1,556 million.
⁽²⁾ Performance excludes money market funds.

in countries like Russia, China, India, Turkey, Brazil, South Korea, Mexico and in the Middle East. We plan to capitalize on this potential by marshaling our current strengths, improving cooperation across divisions and adding resources to these areas. For example, we enhanced our presence in both South Korea and Russia by obtaining bank licenses to better serve our clients. We also are continuing to build on our decade-old relationship with China.

We will tear down any barriers that impede our ability to create a cohesive “one firm” culture in which every employee acts and feels like an owner of the firm.

- We are employing more of our own equity capital to work in principal investing, both independently and together with clients as investment partners. Morgan Stanley’s global franchise provides us with a vast array of investment ideas, and we believe that applying our own capital in this fashion will have significant benefits in terms of client collaboration and increased returns for the firm.
- In Asset Management, we are shifting our focus to manage for growth rather than just maximizing margins. We are addressing the major growth opportunities in alternative investments and in international markets through both organic growth and acquisitions. We also are taking steps to improve performance and stem outflows from our proprietary funds.
- In Retail Brokerage, we continue to build our high-net-worth business, which is a key growth opportunity. We are expanding our product offerings and adding other banking capabilities and investment products to further improve the breadth of services we offer to individual investors. A recent example of these new initiatives is the successful offering of a BlackRock closed-end fund—our first such launch since 1998—which leveraged both institutional and retail capabilities. We also are investing in technology and compliance to help get this business where we want it to be.
- Discover offers significant growth potential, driven by attractive market conditions and the October 2004 ruling in the U.S. Department of Justice’s antitrust suit, which opened the debit and third-party issuance markets to us for the first time. We already have begun to move aggressively into these markets, acquiring the PULSE Network and expanding our third-party relationships. International opportunities also are just beginning to accelerate. In 2005, we launched a strategic alliance with China UnionPay, the only national bankcard payment network in China, and agreed to acquire the Goldfish credit card business in the U.K. to build scale in that attractive market.

Achieving all of the demanding targets we have set for ourselves won’t happen overnight. During 2006, you will see investment in these initiatives and progress on many of these plans. But some areas—like Retail Brokerage—may take two or three years to improve margins. Nevertheless, we will be vigilant in executing on our strategy and maintaining our focus on superior performance. And we will be open and transparent with you about our progress along the way.

Our strategy is designed to help us deliver superior returns to our shareholders, but we intend to remain open to other opportunities and mindful of changing circumstances. If businesses aren't performing, we'll take the necessary action to ensure we are maximizing shareholder value. As the marketplace changes, we will move quickly to take advantage of opportunities we see to enhance our businesses or accelerate our growth. We will evaluate how we are doing along the way, whether opportunities have changed and whether we need to adjust our strategy accordingly.

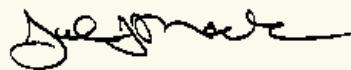
During the past year, the firm also undertook significant corporate governance changes, which include:

- Modifying the Board's corporate governance policies to create a lead independent director position and to consider "withhold" votes in the election of directors; and
- Approving several charter amendments to recommend to shareholders for approval at the company's 2006 shareholders' meeting, including accelerating Board de-staggering, eliminating supermajority vote requirements to remove directors and eliminating the requirement that directors be elected by plurality vote.

Further, between June 2005 and year-end, the Board of Directors was substantially reshaped through the resignation of nine directors and the election of four new, non-employee directors: Roy Bostock, Erskine Bowles, Charles Noski and Griff Sexton. We appreciate the dedicated service of all the directors who stepped down this past year and thank them for their commitment and many contributions to the firm.

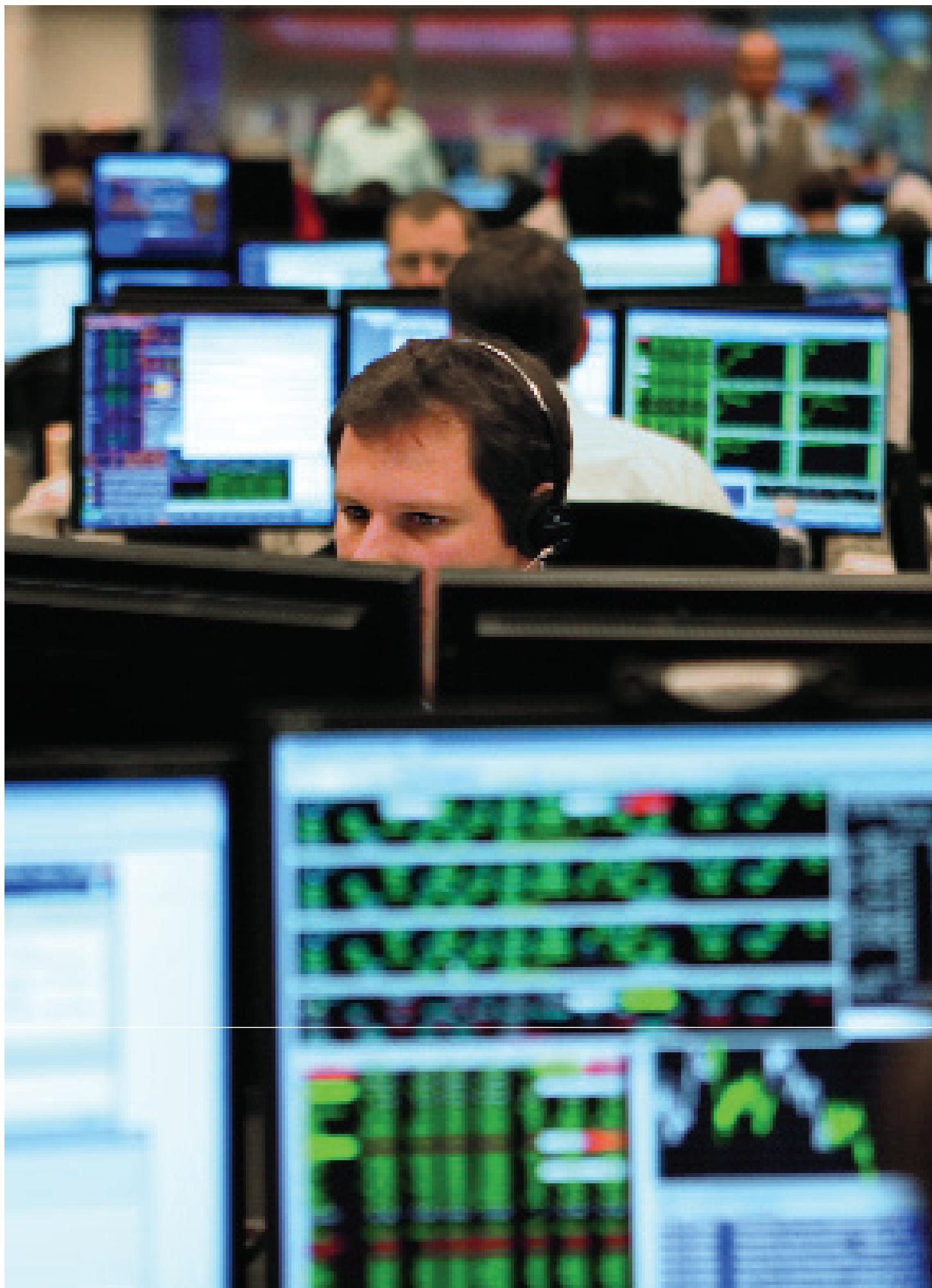
This year truly tested Morgan Stanley, but the firm has emerged a stronger and more unified organization. We are grateful to all of you who continue to put your faith in the people of this great firm. As we mark Morgan Stanley's 70th anniversary this year, I strongly believe that the firm's finest years lie ahead of us, and I am confident that those who continue to invest in Morgan Stanley will reap the rewards of the performance we are committed to achieving.

Sincerely,




John J. Mack
Chairman and Chief Executive Officer

February 1, 2006



Q1.

Morgan Stanley's share price has underperformed many of its peers in recent years. You have said correcting that will take some time. Why should investors stay with Morgan Stanley, given the firm's recent track record and the fact that your peers are delivering greater performance?

Answer:

We're intensely focused on improving overall firm performance, and we are moving aggressively on many fronts to do so—reducing the number of underperforming brokers in our Retail Brokerage business, pursuing acquisitions in key areas, expanding our alternative investment offerings in Asset Management, expanding our derivatives and mortgage businesses, pursuing a better balance between our client and principal risk-taking businesses, and focusing on emerging markets, among other steps. It is true that there are no quick fixes. But given the strength of our franchise, if we improve Morgan Stanley's underperforming businesses, there is tremendous upside for us to create shareholder value. While investors may not see the bottom-line impact from some of our initiatives immediately in 2006, we will maintain constant transparency in providing shareholders with data on key metrics so they can accurately measure the progress we are making toward our goals.

Q2.

Why did Morgan Stanley decide to keep Discover, and how can the firm grow that business ahead of the credit card industry's slower pace?

Answer:

Discover is an attractive asset for Morgan Stanley. It is a unique and successful franchise that diversifies the company's earnings and broadens our scale and capital base. The income before taxes generated by Discover—more than \$3 billion over the last three years—provides a cushion for risk taking elsewhere in the firm. And while the U.S. credit card industry is growing at only 3%-5% right now, we see opportunities to exceed this growth rate—especially in the payments business and internationally. Following a favorable 2004 ruling in the U.S. Department of Justice's antitrust suit, we have expanded our business in the debit card market and with third-party issuers. Internationally, we launched a strategic alliance in 2005 with China UnionPay, that country's only national bankcard payment network, and we agreed to acquire the Goldfish credit card business to enhance our business in the U.K.

Q3.

What do you see as Morgan Stanley's competitive advantages and in what areas do you see the firm getting out in front of the market?

Answer:

We have a wide range of businesses where we are second to none. Equity sales, prime brokerage, credit derivatives, real estate finance and commodities are examples of businesses where we have clear leadership positions. We also enjoy particular strength in global transactions and are uniquely well-positioned for growth in emerging markets like Russia and China, among others. We will stay in front of the market by both extending and capitalizing on these strengths, as well as by addressing those businesses where we aren't leaders today but have the potential to be, given the strength of our franchise and the quality of our people.

Q4.

You have talked about the benefits of more fully integrating Morgan Stanley's businesses. What are the opportunities that you see there?

Answer:

The Morgan Stanley-Dean Witter merger gave us the scale and scope that we need to compete in the current global marketplace. However, we need to more fully integrate the two businesses. For example, in the Retail Brokerage business, we still have two technology platforms and two compensation systems. We are focused now on fully integrating the businesses and truly creating one firm, and we already have started realizing some of that potential. For instance, we have had increased success in delivering to individual investors some of the more sophisticated products, such as our real estate private equity funds, that leverage our leadership and capabilities in Institutional Securities.

Q5.

You've talked about the need to make greater investments in technology. What are Morgan Stanley's highest priorities in this area?

Answer:

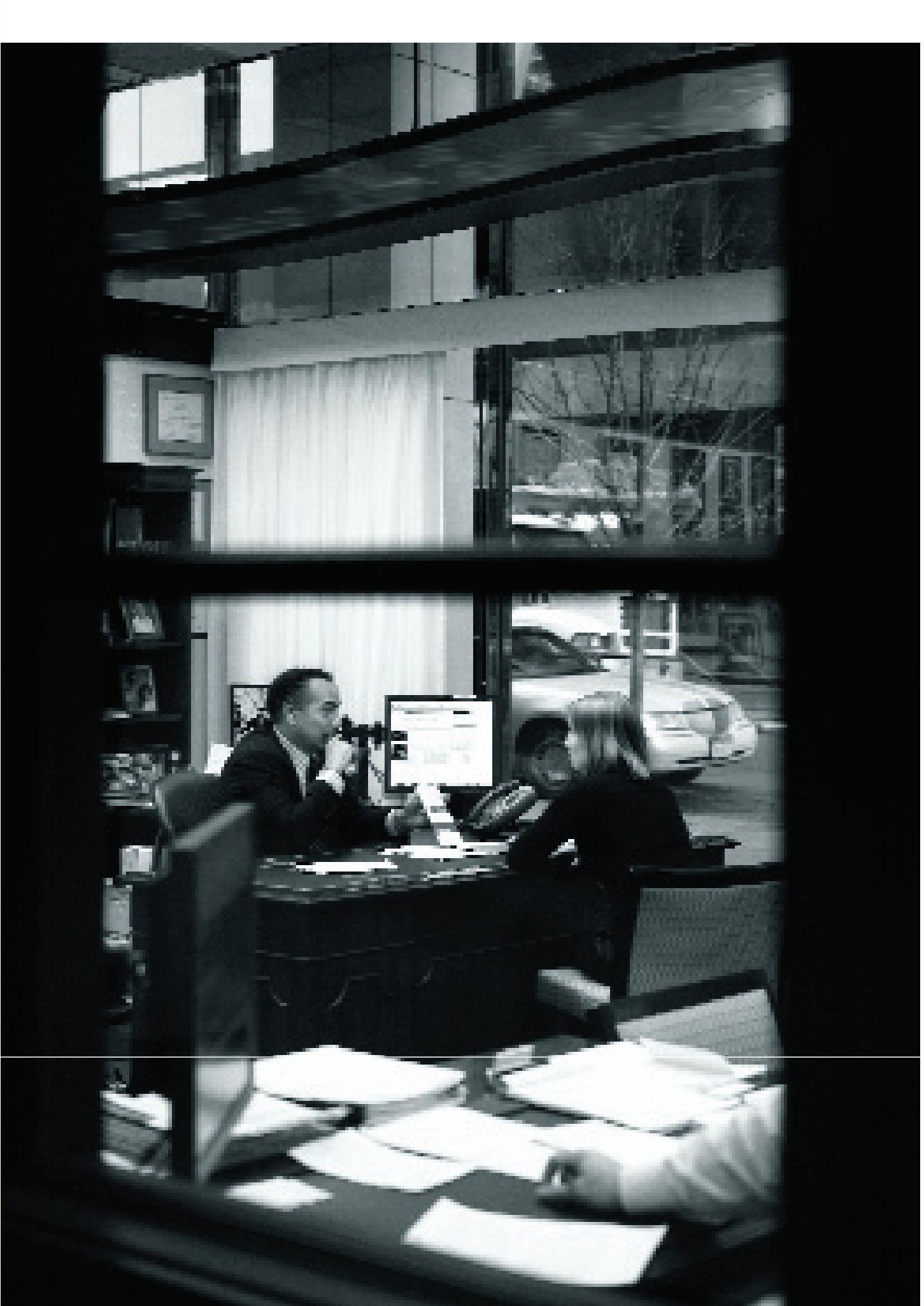
On the retail side of the business, we want to ensure that all our people have the best possible tools to serve our clients, so we're going to upgrade our technology platforms and provide our financial advisors and investment representatives with a tool kit that is as competitive as that of our leading peers. On the institutional side of the business, we're very focused on ensuring we have the technology in our fixed income and equities divisions to deliver multi-asset-class products for our clients. We'll also look at opportunities to integrate the technology platforms across our businesses, but we're going to do it in a very disciplined and economic way.

Q6.

Margins in the Retail Brokerage business have, for some time, lagged those of leading peers. How are you going to close that gap, and what makes you think Morgan Stanley can be competitive in the retail business?

Answer:

We have a strong Retail Brokerage franchise. It's a tremendous asset with many high-quality financial advisors and investment representatives and \$617 billion in client assets. We need to invest in the retail business to realize its full potential. We need to expand our product offerings, bringing new and creative products to our retail client base through our retail sales force. We also need to continue to build our high-net-worth and ultra-high-net-worth business, which is a key target for growth and investment. And we need to invest in technology and compliance, as well as in our most productive financial advisors and investment representatives. It's going to take time to get the retail business where we want it to be, but we've already begun taking some of the necessary steps to improve profitability and margins, and James Gorman will be helping us to achieve the full potential of this business.





Q7.

What steps is Morgan Stanley taking to broaden its retail product offering?

Answer:

One of our biggest priorities in the Retail Brokerage business is filling out our product platform and leveraging our Institutional Securities capabilities to deliver new and attractive products to our more sophisticated retail clients. The success of our recent offering of a BlackRock closed-end fund, our first such launch since 1998, illustrates our ability to do just that. We also intend to add structured products developed by our equity capital markets division and alternative investments developed by both our Institutional Securities and Asset Management businesses. The progress we have made in new product development is helping to energize our broker sales force and will help us create a best-in-class platform with best-in-class products.

Q8.

You've talked about some of Morgan Stanley's misses in strategy and execution. Why did the firm fail to make the most of these areas, and how will it do better moving forward?

Answer:

Past strategic decisions precluded us from participating in a number of profitable and attractive opportunities—but we can change that by relentlessly focusing on execution, driving decision making down through the organization and holding people accountable for results. For instance, we did not make the necessary investments in our Retail Brokerage and Asset Management businesses. But we have already begun to do so, and we are committed to getting these businesses where we want them to be. We largely missed the expansion in the mortgage business, where our competitors grew aggressively. Now we can and will make sure that our role in the mortgage markets is commensurate with the scope of our fixed income operation. We also missed out in equity derivatives. Given our leading cash equities franchise and derivatives expertise, we have the ability to fill that gap, too. Our balance sheet was underleveraged; now we are going to consider more acquisitions to drive growth and commit sufficient capital to attractive principal investment opportunities.

Q9.

You have said you plan to increase your principal investments by about \$1 billion over time. Does Morgan Stanley have the expertise and orientation to be successful in this business?

Answer:

Without question, Morgan Stanley has the expertise to successfully make principal investments. Our global franchise presents us with a vast array of investment ideas. We have successfully pursued a number of principal investments in the past, although less frequently than we should have and on an ad hoc basis. Now we are formalizing the process for making equity-based principal investments, enabling us to be more focused on these investment ideas and to make decisions in an expeditious manner. In the process, we hope to strengthen our client relationships and leverage our intellectual capital and global capabilities while striving to enhance returns to the firm.

Q10.

What kinds of acquisitions will Morgan Stanley consider, and how will they benefit the firm?

Answer:

We are looking across a range of businesses for acquisitions to accelerate our growth or strengthen our market position. For instance, we agreed to acquire the Goldfish credit card business in the United Kingdom, which will help us to increase the scale of our U.K. card business in a market where size is critical. Asset management, alternative investments, international mortgages and commodities are some of the other areas where we will consider such acquisitions.

Q11.

You've talked about a firmwide approach to emerging markets. What cross-company opportunities does Morgan Stanley intend to pursue in these markets, and where?

Answer:

Emerging markets are becoming an increasingly important part of Morgan Stanley's business, and we want to focus on those markets we believe will yield the greatest returns, such as Russia, China, India, Turkey, Brazil, South Korea, Mexico and the Middle East. Strong regional managers for those businesses are working across offices and functions to meet the needs of our local clients and international investors. Our experiences in Russia and China are useful examples of what we can do. In 2005 we led the largest IPO both in Russia and in China, and we have played a leading role in the large-scale privatizations and public offerings of state-owned enterprises. This past year, we led our first local IPO ever in Brazil. We also built on our presence in both Russia and South Korea by acquiring bank licenses in those countries. In the coming year, we plan to continue to build on our strong position in all of these emerging markets.

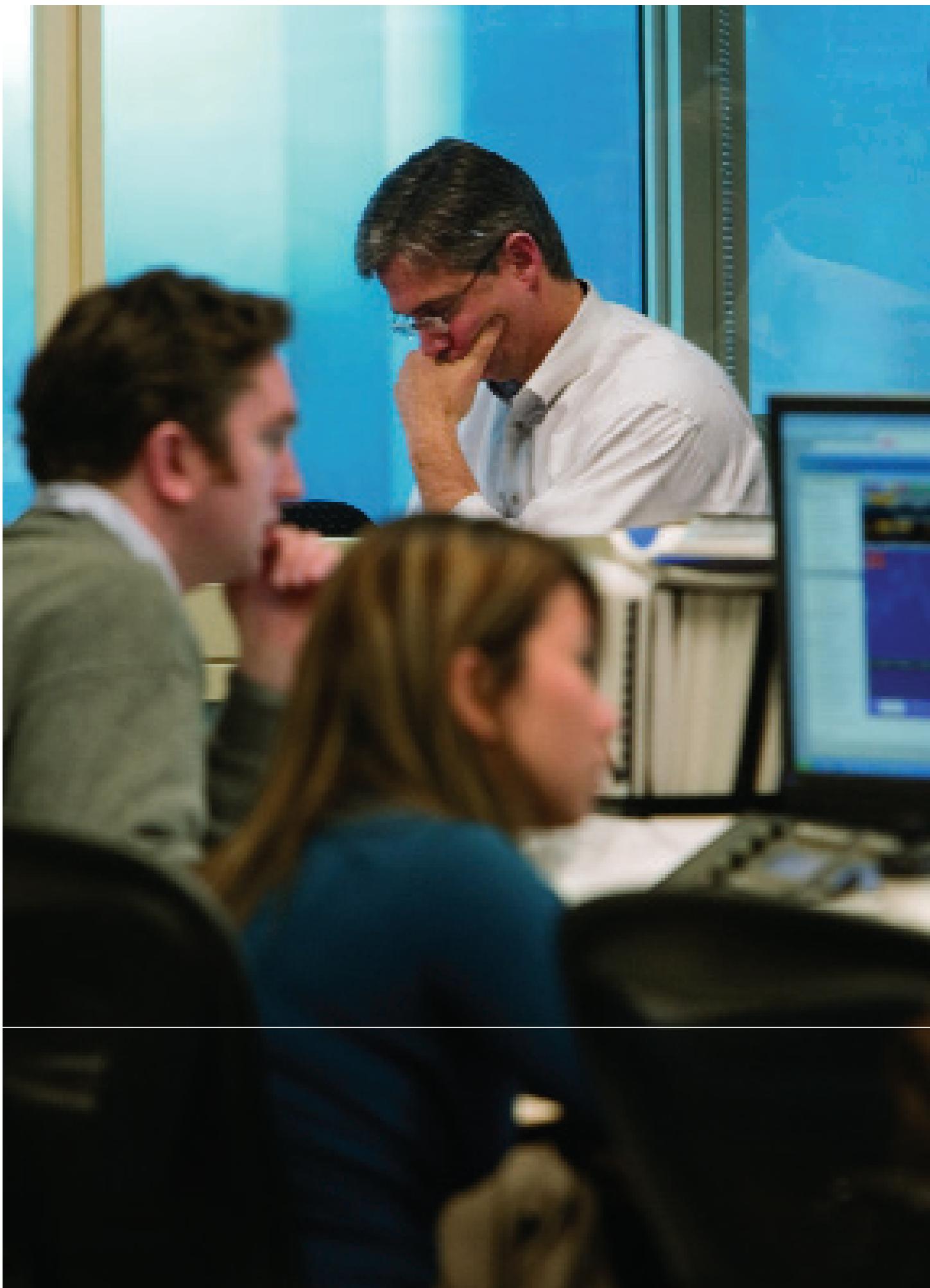
Q12.

What are the advantages of configuring your asset management business for growth as opposed to profitability?

Answer:

By managing the Asset Management business to maximize margins, we missed a number of fast-growing, profitable opportunities. We now are pursuing a number of opportunities that will allow us to grow and achieve even greater profitability over the long term. For example, we plan to use our scale internationally to build our alternative investment portfolio offerings through a combination of organic growth and acquisitions. We also are taking steps designed to improve our performance and stem outflows from our proprietary funds.





Q13.

Morgan Stanley was criticized for its corporate governance in 2005. What is the firm doing to address these concerns?

Answer:

We have been vigilant in addressing all of these criticisms and have substantially restructured our corporate governance platform. The Board of Directors adopted a range of new policies during the past year regarding the creation of a lead independent director position, the periodic rotation of Board committee assignments and chair positions, and the consideration of “withhold” votes in the election of directors. The Board also has approved several charter amendments to recommend to shareholders for approval at the company’s 2006 shareholders’ meeting, including accelerating Board de-staggering, eliminating supermajority vote requirements to remove directors and eliminating the requirement that directors be elected by plurality vote. Since June, the Board also has been substantially reshaped—with nine resignations between June 2005 and year-end, as well as the addition of four new highly qualified non-employee directors.

Q14.

Morgan Stanley faced a tough year in 2005. How did that impact the firm’s performance?

Answer:

Morgan Stanley achieved a remarkably strong finish to 2005. We took advantage of the attractive market environment to deliver record revenues for the year, record earnings for the fourth quarter and two straight quarters of improving financial performance in the second half of the year. We saw record revenues in fixed income, record revenues in prime brokerage, and significant increases in equities and investment banking. We achieved a #2 position in global announced M&A, a #2 position in global IPOs and a #3 position in global equity, according to Thomson Financial. There is certainly room for improvement across all of our businesses, but the franchise remains strong, our people are the most talented in the industry, and there is a renewed energy and focus on performance that should allow us to build on the strengths of the firm and realize the enormous potential of our global franchise.

Q15.

The firm’s new senior management team has talked a lot about the culture at Morgan Stanley. What kind of culture are you trying to build among the people of Morgan Stanley?

Answer:

One of the keys to improving our performance is building a “one firm” culture that is driven by a commitment to excellence, integrity and diversity. We want our employees to think like owners and focus on improving our profitability and ROE. We want them to work together across businesses and speak up when they see a problem or an opportunity to do something better. To help our employees do that, we’re getting rid of “silos” and roadblocks within the firm, and we’re eliminating bureaucracy. We’re driving decision making down through the organization, and we’re holding people accountable for results. Despite the challenges we faced this past year, Morgan Stanley continues to have an unmatched depth and breadth of talent. We’re committed to attracting and retaining the best people in the industry and ensuring we have a culture that provides those people with the best possible opportunities to achieve their full potential.

Institutional Securities

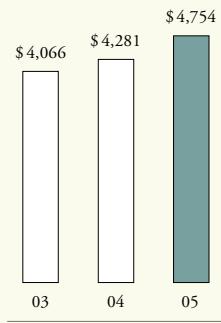
Morgan Stanley is a leading global provider of investment banking and sales and trading services to domestic and international corporate, government and other institutional clients.

Investment Banking Morgan Stanley offers its investment banking clients underwriting and distribution services for debt and equity offerings in addition to financial advisory services regarding key strategic matters, such as mergers and acquisitions, restructurings, real estate and project finance. Morgan Stanley also selectively provides loans or lending commitments to its clients.

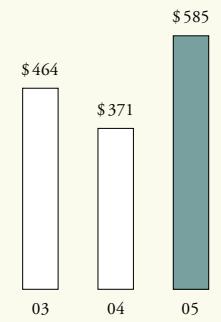
Sales, Trading, Financing and Market-Making Institutional investors receive sales, trading and market-making services in virtually every type of financial instrument, including stocks, bonds, derivatives, foreign exchange and commodities. Morgan Stanley is involved in these activities in all major global financial markets. The firm also offers prime brokerage and financing services, including securities lending.

Other Morgan Stanley produces and distributes research on global economics, market strategies, industries, individual companies and other related financial matters. The firm also engages in principal investing. Through its subsidiary, Morgan Stanley Capital International Inc., it markets and distributes equity and fixed income indices.

Institutional Securities
Income before Taxes
Dollars in Millions



Retail Brokerage
Income before Taxes
Dollars in Millions



All charts are based on fiscal year results of operations for the 12 months ended November 30.

Amounts on charts represent income from continuing operations before losses from unconsolidated investees, income taxes, dividends on preferred securities subject to mandatory redemption and cumulative effect of accounting change, net.

Retail Brokerage

Retail Brokerage provides comprehensive brokerage, investment and financial services to individual investors globally. Morgan Stanley has one of the largest retail brokerage networks, with 9,526 worldwide representatives at year-end and more than 500 global retail locations, including 485 U.S. locations.

Client Coverage In the U.S., Morgan Stanley's representatives cover multiple client segments from affluent to ultra-high-net worth. Morgan Stanley also offers financial advisory services outside the U.S. to serve the needs of affluent and ultra-high-net worth clients in Europe, Asia and Latin America.

Client Solutions Morgan Stanley's representatives offer services that are tailored to their clients' individual investment objectives, risk tolerance and liquidity needs. The product range spans mutual funds, equities, fixed income products, alternative investments, separately managed accounts, banking, mortgages, insurance and annuities. Morgan Stanley offers financial solutions to small businesses through BusinesScape and provides defined contribution plan services, including 401(k) plans and stock plan administration, to businesses of all sizes.

Client Support Client Coverage and Client Solutions are supported by Morgan Stanley's infrastructure and technology platform. Morgan Stanley executes and clears its transactions through its own facilities and memberships in various clearing corporations.

Asset Management

Morgan Stanley Investment Management is a global asset manager offering individual and institutional clients a diverse array of equity, fixed income and alternative investment strategies. Managed by experienced investment professionals, products include many highly rated U.S. and international strategies that span the risk and asset-class spectrum. These products are distributed in multiple channels on a variety of platforms and markets under two distinct brands. Our portfolio managers and research analysts are located throughout the world, enhancing investment capabilities through a combination of global information sharing and local decision making.

Individual Investors Affiliated Channel: Morgan Stanley Investment Management reaches individual investors through our affiliated network of representatives who offer, among a range of product providers, Morgan Stanley- and Van Kampen-branded products.

Third-Party Channels: Morgan Stanley Investment Management also offers investment products under our affiliated brand, Van Kampen (in the U.S.), as well as under Morgan Stanley Investment Management (globally) through a diversified network of broker-dealers, banks, insurance companies and financial planners.

Institutional Investors Institutional investors, including pension plans, corporations, nonprofit organizations, governmental agencies, insurance companies and banks, are serviced by a global proprietary sales force and a team dedicated to covering the investment consultant industry.

Asset Management
Income before Taxes
Dollars in Millions



Discover
Income before Taxes
Dollars in Millions



Discover

Discover Financial Services, through Discover Bank, is one of the largest issuers of general purpose credit cards in the U.S., with over 50 million Cardmembers. It offers the Discover Card and other general purpose credit cards. The cards are accepted on the Discover Network, the largest proprietary credit card network in the U.S., with more than 4 million merchant and cash access locations.

Discover also offers Discover Gift Cards and a variety of financial services, including home loans and credit protection products, and is a leading credit card company on the Internet, with more than 14 million Cardmembers registered at Discovercard.com.

Discover Card was ranked #1 in fraud protection services by Javelin Strategy & Research, and its Cashback Bonus is America's #1 cash rewards program.

In 2005, Discover acquired PULSE, one of the nation's fastest-growing ATM/debit networks. Issuing relationships with GE Consumer Finance, Metris (HSBC) and others have resulted in new credit cards being issued on the Discover Network.

The company's international credit card business has continued to grow, with 1.5 million accounts in the U.K. and \$2.7 billion in loans. In 2005, Discover launched a strategic alliance with China UnionPay, the only national bankcard payment network in China.

Board of Directors

John J. Mack
Chairman of the Board and
Chief Executive Officer

Roy J. Bostock
Chairman
The Partnership for a
Drug-Free America

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Commitment to Diversity

Morgan Stanley prizes innovation and creativity, and we maximize these assets by building diverse teams. As we grow our businesses around the world, the talents and diversity of our workforce become all the more important. We continue to foster an environment that encourages employees of all backgrounds to flourish individually as they contribute to our team effort. We were pleased with the continuing recognition we received in 2005 as a leading employer that is implementing its diversity commitment with success. Our commitment to respect for individuals and cultures, one of our core values, is the cornerstone of our culture at Morgan Stanley. To learn more about the firm's initiatives in this area, access the firm's diversity information at www.morganstanley.com/about/diversity/ or send an email to diversity@morganstanley.com.

Community Involvement

Morgan Stanley is committed to doing our share as a good neighbor and to improving the quality of life in the communities where we operate. For years, our employees have spent time and money giving back to the communities where they live and work, with the full support of the firm. Through company contributions, our Foundation and individual gifts, Morgan Stanley assists charities in four key areas: youth; diversity; arts and culture; and employee volunteerism. We also aid relief efforts for the many victims of devastating natural disasters. Services are delivered locally across the globe, embracing communities in the United States, Europe and Asia. We are proud of this generosity and compassion—and every day, we look forward to making a positive difference to our neighbors worldwide. To learn more about our philanthropic programs, access the company's Charitable Annual Report through our website at www.morganstanley.com or write to: Morgan Stanley Community Affairs, 1633 Broadway, 20th Floor, New York, NY 10019.

FINANCIAL HIGHLIGHTS

Selected Financial Data

(Dollars in Millions, Except Share and Per Share Data)

Fiscal Year ¹	2005	2004	2003	2002	2001
Income Statement Data:					
Revenues:					
Investment banking	\$ 3,843	\$ 3,341	\$ 2,440	\$ 2,478	\$ 3,413
Principal transactions:					
Trading	7,365	5,510	6,262	3,521	5,600
Investments	981	607	110	(25)	(371)
Commissions	3,363	3,264	2,887	3,191	3,066
Fees:					
Asset management, distribution and administration	4,958	4,473	3,814	4,033	4,304
Merchant, cardmember and other	1,323	1,317	1,377	1,421	1,348
Servicing and securitization income	1,609	1,921	1,922	2,032	1,861
Interest and dividends	28,175	18,584	15,738	15,876	24,112
Other	464	324	226	399	217
Total revenues	52,081	39,341	34,776	32,926	43,550
Interest expense	24,425	14,707	12,693	12,515	20,491
Provision for consumer loan losses	878	926	1,266	1,337	1,051
Net revenues	26,778	23,708	20,817	19,074	22,008
Non-interest expenses:					
Compensation and benefits	11,313	9,853	8,522	7,910	9,352
Other	8,355	7,037	6,135	6,070	6,847
Restructuring and other charges	—	—	—	235	—
September 11-related insurance recoveries, net	(251)	—	—	—	—
Total non-interest expenses	19,417	16,890	14,657	14,215	16,199
Income from continuing operations before losses from unconsolidated investees, income taxes, dividends on preferred securities subject to mandatory redemption and cumulative effect of accounting change, net	7,361	6,818	6,160	4,859	5,809
Losses from unconsolidated investees	311	328	279	77	30
Provision for income taxes	1,858	1,856	1,707	1,625	2,076
Dividends on preferred securities subject to mandatory redemption	—	45	154	87	50
Income from continuing operations before cumulative effect of accounting change, net	5,192	4,589	4,020	3,070	3,653
Discontinued operations:					
Loss from discontinued operations	(486)	(172)	(393)	(138)	(124)
Income tax benefit	184	69	160	56	51
Loss on discontinued operations	(302)	(103)	(233)	(82)	(73)
Cumulative effect of accounting change, net	49	—	—	—	(59)
Net income	\$ 4,939	\$ 4,486	\$ 3,787	\$ 2,988	\$ 3,521
Earnings applicable to common shares ²	\$ 4,939	\$ 4,486	\$ 3,787	\$ 2,988	\$ 3,489
Per Share Data:					
Earnings per basic share:					
Income from continuing operations	\$ 4.94	\$ 4.25	\$ 3.74	\$ 2.84	\$ 3.33
Loss on discontinued operations	(0.29)	(0.10)	(0.22)	(0.08)	(0.07)
Cumulative effect of accounting change, net	0.05	—	—	—	(0.05)
Earnings per basic share	\$ 4.70	\$ 4.15	\$ 3.52	\$ 2.76	\$ 3.21
Earnings per diluted share:					
Income from continuing operations	\$ 4.81	\$ 4.15	\$ 3.66	\$ 2.76	\$ 3.23
Loss on discontinued operations	(0.29)	(0.09)	(0.21)	(0.07)	(0.07)
Cumulative effect of accounting change, net	0.05	—	—	—	(0.05)
Earnings per diluted share	\$ 4.57	\$ 4.06	\$ 3.45	\$ 2.69	\$ 3.11
Book value per common share	\$ 27.59	\$ 25.95	\$ 22.93	\$ 20.24	\$ 18.64
Dividends per common share	\$ 1.08	\$ 1.00	\$ 0.92	\$ 0.92	\$ 0.92
Balance Sheet and Other Operating Data:					
Total assets	\$ 898,523	\$ 747,334	\$ 602,843	\$ 529,499	\$ 482,628
Consumer loans, net	22,916	20,226	19,382	23,014	19,677
Total capital ³	125,891	110,793	82,769	65,936	61,633
Long-term borrowings ³	96,709	82,587	57,902	44,051	40,917
Shareholders' equity	29,182	28,206	24,867	21,885	20,716
Return on average common shareholders' equity	17.3%	16.8%	16.5%	14.1%	18.0%
Average common and equivalent shares ²	1,049,896,047	1,080,121,708	1,076,754,740	1,083,270,783	1,086,121,508

¹ Certain prior-period information has been reclassified to conform to the current year's presentation.

² Amounts shown are used to calculate earnings per basic share.

³ These amounts exclude the current portion of long-term borrowings and include Capital Units and junior subordinated debt issued to capital trusts.

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Common Stock

The common stock of Morgan Stanley is listed on the New York Stock Exchange and on the Pacific Exchange. Ticker Symbol: MS

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Stock Transfer Agent

For information about the direct stock purchase and dividend reinvestment program (DRIP), address changes, dividend checks, lost stock certificates, share ownership and other administrative services, contact:
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P.O. Box 3315
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Phone: (800) 622-2393
For investors outside the U.S.,
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www.melloninvestor.com

Electronic Delivery of Annual Meeting Materials

You may elect to receive your future annual meeting and proxy statement material via the Internet rather than receiving mailed copies.
For shareholders of record, please visit www.melloninvestor.com.

Equal Opportunity Employer

Morgan Stanley is committed to providing a discrimination-free workplace and equal opportunity for its employees, including recruitment, hiring, training and promotion. For more information, including the company's Diversity and EEO-1 Reports, write to:
Marilyn F. Booker, Managing Director,
Global Head of Diversity,
Morgan Stanley, 750 Seventh Avenue,
New York, NY 10019, or email:
diversity@morganstanley.com.

Political Contributions

Morgan Stanley is committed to participating in the political process in a manner consistent with good corporate governance practices and in compliance with legal requirements. Our Corporate Political Contributions Policy Statement is available through our website at www.morganstanley.com.

For a copy of our most recent Corporate Political Contributions Disclosure Statement, write to: Morgan Stanley Government Relations,
401 9th Street, N.W., Suite 650,
Washington, DC 20004.

Investor Relations

Security analysts, portfolio managers and representatives of financial institutions seeking information about the company are invited to contact: Investor Relations at (212) 762-8131. General information about the company and copies of the company's Annual Report on Form 10-K and other filings can be obtained online at www.morganstanley.com or by calling (800) 622-2393.

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Morgan Stanley Closed-End Funds: (800) 221-6726
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For a more complete discussion of our 2005 results,
please refer to our Annual Report on Form 10-K
and visit us online at www.morganstanley.com.

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