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MARKET COMMENTARY

GLOBAL INVESTMENT COMMITTEE

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Asset Allocation and Strategy Commentary

INVESTMENT OUTLOOK

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1. On Mar. 7, 2013, Morgan Stanley Wealth Management's Global Investment Committee recommended (and still does) that investors be tactically vs. strategically overweight cash, and underweight select equities (while overweight large-cap US equities), reflecting continuing concerns about: policy efficacy; ongoing household, financial sector and sovereign balance-sheet deleveraging; peak profit margins; recession in Europe; and uneven growth in many emerging and developed economies. Even with recent successive record highs for the S&P 500, risk assets may continue in their multiyear *sideways, range-bound secular market*, given: (i) the magnitude and duration of the previous secular uptrend (i.e., a 1,300% increase from 1982 to 2000 for US equities); (ii) significant continuing imbalances for several major economies relating to central governments' budget deficits, indebtedness, savings, consumption, trade, currency relationships, global competitiveness, demographic trends, sovereign-debt quality and foreign exchange reserves; (iii) the lingering aftereffects of the severe financial and systemic recession of 2007-2009; and (iv) doubts about the timing, substance, and effectiveness of the authorities' policy measures and voters' response thereto.

2. Morgan Stanley & Co.'s global economists estimate the following annual percentage change in real GDP:

REGION	2010	2011	2012E	2013E	2014E
US	+3.0	+1.8	+2.2	+1.6	+2.5
Euro Zone	+1.9	+1.5	-0.5	-0.7	+0.9
Japan	+4.5	-0.6	+2.0	+1.6	+1.3
Emerging Markets	+7.8	+6.5	+4.9	+5.4	+5.8

3. Morgan Stanley & Co.'s US Equity Strategist Adam Parker assigned the following probabilities to the S&P 500 Index for the end of calendar-year 2013:

	2013E EPS	2014E EPS		2013E FORWARD P/E		YE 2013E INDEX LEVEL	PROBABILITY
Bull Case	$116.30	$129.50	x	15.0	=	1,936	20%
Base Case	$103.20	$110.20	x	14.5	=	1,600	60%
Bear Case	$81.10	$90.90	x	13.9	=	1,264	20%

These scenarios produce a *probability-weighted* year-end 2013 close of 1,600 on the S&P 500, which is 3.0% below the May 24, 2013 price of 1,650.

4. Significant factors that are likely to influence asset prices include: the outlook for revenue growth, profit margins and corporate profits; jobs; business and consumer confidence; taxation and spending actions by the US Congress; sovereign debt ratings; global currency relationships; fiscal austerity measures; US hydrocarbon energy production; the economic growth outlook in Japan, China, India, Mexico and Brazil; house prices; and the timing and composition of Bank of Japan, European Central Bank and Federal Reserve monetary policy actions (remaining FOMC meetings in 2013 are June 18-19, July 30-31, Sept. 17-18, Oct. 29-30, and Dec. 17-18).

The Metrics (YEAR TO DATE AS OF MAY 24, 2013)

	LEVEL	% CHANGE
S&P 500	1,649.6	+15.7
RUSSELL 2000	984.3	+15.9
MSCI WORLD	1,492.7	+11.5
MSCI EUROPE	1,532.1	+6.0
MSCI PACIFIC EX JAPAN	1,353.1	+2.0
MSCI EMERGING MARKETS	1,026.7	-2.7
10-YEAR US TREASURY YIELD	2.01	+14.3
MOODY'S BAA YIELD	4.79	+3.5
NYMEX CRUDE OIL	94.15	+2.0
DJ-UBS COMMODITY	131.98	-5.1
COMEX SPOT GOLD	1,386.7	-17.2
DXY US DOLLAR INDEX	83.70	+4.9

Note: Barclays Capital US Credit Index has an average quality of A2/A3 and is used as a proxy for the Moody's Baa total return. Source: Bloomberg, LLC and MSCI.

Asset Allocation Weightings

Tactical vs. Strategic Weights

	UNDER	EQUAL	OVER
Global Cash	○	○	●
Global Equities	●	○	○
US Large-Cap	●	○	○
Asia Pacific including Japan, Europe including UK, US Small- and Mid-Cap	○	●	○
Global Bonds	○	●	○
Short-Term Fixed Income	○	○	●
International Fixed Income, Emerging Markets	○	●	○
US Fixed Income, High Yield and Inflation-Linked	●	○	○
Alternative Investments	○	●	○
REITS, Hedge Funds, Commodities and Managed Futures Funds	○	●	○

Equities Bullish Factors

- Factors arguing in favor of equities include: stimulative monetary policy, including negative real interest rates, major central banks' coordinated liquidity provision to funding markets, the European Central Bank's Long-Term Refinancing Operation and Outright Monetary Transactions Program and major Quantitative Easing in the US and Japan.
- The consensus of analysts' forecasts for S&P 500 calendar-year earnings per share growth is 7.2% for 2013 and 11.0% for 2014, according to Thomson Reuters.
- Twelve-month forward price/earnings ratios are not excessive and the earnings yield (the inverse of the P/E ratio) is at elevated levels relative to Baa corporate bond yields.
- Recent leading economic indicators, durable goods orders, employment data, home prices, consumer sentiment, household net wealth levels, auto sales, consumer credit, and US oil and gas production reflect strength and/or improvement in these sectors.
- High US corporate cash levels enable increased dividend payouts, stock buybacks, and mergers and acquisitions activity.
- The economic, financial, and policy outlook for Italy, Japan and Mexico appears to be improving.

Equities Bearish Factors

- The payroll tax increase could reduce 2013 US GDP growth by 0.6%.
- Maximum federal tax rates on *dividend income* have risen to 23.8% from 15%; and on *capital gains*, to 23.8% from 15%.
- As of the end of March, European unemployment was 12.1%; for April, US unemployment was 7.5%; the broader measure of US unemployment, U-6, was at 13.9%.
- Medium-term GDP growth may be held back by: (i) continuing recessionary conditions in Europe and sluggish growth in China; (ii) higher payroll taxes; (iii) uneven consumer confidence, Empire State and Philly Fed business conditions, ISM manufacturing and services data, construction spending, new jobless claims, factory and durable goods orders, personal income growth and retail sales; and (iv) lackluster global trade, industrial production and business capital spending.
- In search of income, investors have driven several risk-asset classes to record high prices and record low yields.
- NYSE margin debt has reached a record $384 billion, topping the previous high of $381 billion set in June 2007. It is up 65% so far this year.
- US stocks do not appear undervalued using long-term metrics; the Shiller P/E—that is, price divided by 10-year average real earnings—for the S&P 500 is 23.7, which is 44% above its long-term average of 16.5.
- As a contrarian indicator, the AAII investor survey shows 49% bullish, 21% bearish versus long-term averages of 39% bullish and 30% bearish.

Source: Morgan Stanley Wealth Management Global Investment Committee, Morgan Stanley & Co. LLC Research, Citi Research, ECRI, and Bloomberg.
Note: Unless otherwise indicated, data are as of May 24, 2013.

Profit Forecasts

	2012E			2013E			2014E		
	MS	CITI	CONSENSUS	MS	CITI	CONSENSUS	MS	CITI	CONSENSUS
S&P Operating Earnings	103.20	103.76	102.57	103.20	110.00	109.95	110.20	117.00	122.06
MSCI All Country World Index	NA	NA	24.39	NA	NA	26.26	NA	NA	29.33

Macro Forecasts

	GDP (%)						INFLATION (%)					
	MS	CITI	MS	CITI	MS	CITI	MS	CITI	MS	CITI	MS	CITI
	2012E		2013E		2014E		2012E		2013E		2014E	
Global Economy	3.1	2.5	3.2	2.6	3.9	3.2	3.3	2.9	3.3	2.7	3.3	3.0
US Economy	2.2	2.2	1.6	1.9	2.5	2.9	2.1	1.8	1.8	1.3	1.5	2.1

	INTEREST RATE FORECASTS				
		MORGAN STANLEY		CITI	
POLICY RATES (%)	**CURRENT**	**2Q13E**	**2Q14E**	**2Q13E**	**2Q14E**
US	0.15	0.15	0.15	0.25	0.25
Euro Zone	0.50	0.25	0.10	0.50	0.25
China[1]	6.00/3.00	6.00	6.50	3.00	3.50
10-YR. GOVT. BOND YIELDS (%)	**CURRENT**	**2Q13E**	**2Q14E**	**2Q13E**	**2Q14E**
US	2.01	1.90	2.60	1.93	2.80
Germany	1.43	1.68	1.50	1.43	1.40

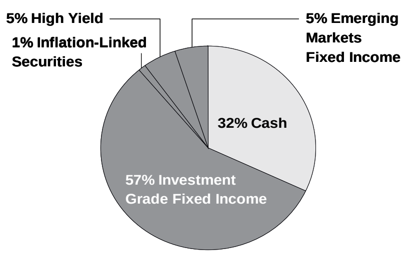
Note: (1) For China's policy-rate forecasts, Morgan Stanley uses the one-year lending rate, Citi the one-year deposit rate.
Source: Morgan Stanley Wealth Management Global Investment Committee, Morgan Stanley & Co. LLC Research, Citi Research, Bloomberg, and Thomson Reuters as of May 24, 2013.

Global Investment Committee Tactical Asset Allocation

The Global Investment Committee provides guidance on investment allocation decisions through its various model portfolios. The eight models below are recommended for accounts with less than $25 million in investable assets. They are based on an increasing scale of risk (expected volatility) and expected return.

CONSERVATIVE ››› MODERATE ›››

MODEL 1



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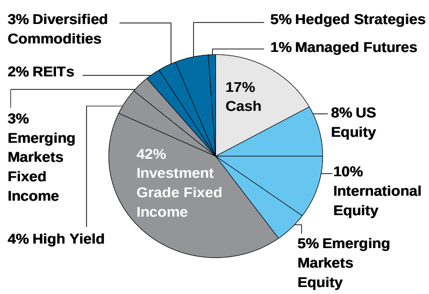

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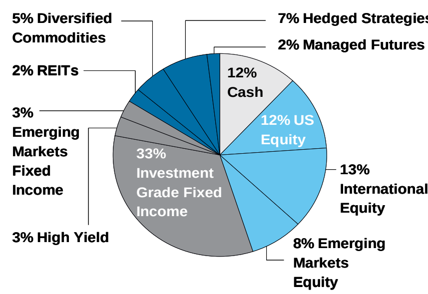
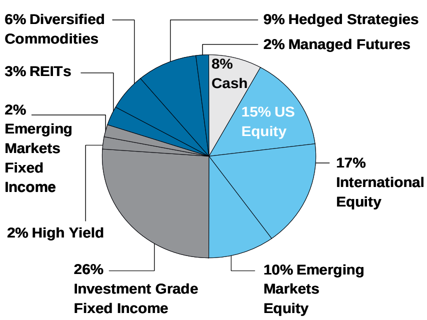


MODERATE ››› ›››

MODEL 4



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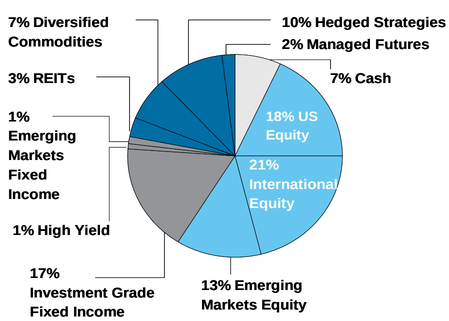

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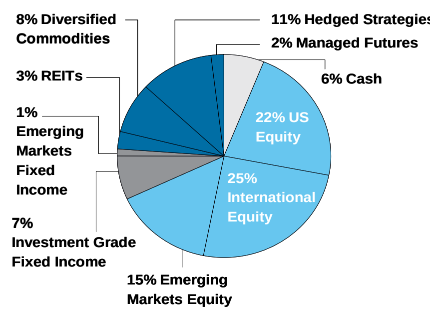
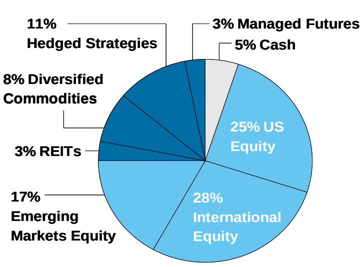
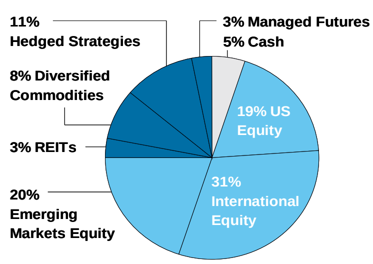


AGGRESSIVE ›››

MODEL 7



MODEL 8



KEY

- CASH
- GLOBAL FIXED INCOME
- GLOBAL EQUITIES
- ALTERNATIVE INVESTMENTS

Note: Hedged strategies consist of hedge funds and managed futures.

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Bonds are subject to interest rate risk. When interest rates rise, bond prices fall; generally the longer a bond's maturity, the more sensitive it is to this risk. Bonds may also be subject to call risk, which is the risk that the issuer will redeem the debt at its option, fully or partially, before the scheduled maturity date. The market value of debt instruments may fluctuate, and proceeds from sales prior to maturity may be more or less than the amount originally invested or the maturity value due to changes in market conditions or changes in the credit quality of the issuer. Bonds are subject to the credit risk of the issuer. This is the risk that the issuer might be unable to make interest and/or principal payments on a timely basis. Bonds are also subject to reinvestment risk, which is the risk that principal and/or interest payments from a given investment may be reinvested at a lower interest rate.

Bonds rated below investment grade may have speculative characteristics and present significant risks beyond those of other securities, including greater credit risk and price volatility in the secondary market. Investors should be careful to consider these risks alongside their individual circumstances, objectives and risk tolerance before investing in high-yield bonds. High yield bonds should comprise only a limited portion of a balanced portfolio.

Equity securities may fluctuate in response to news on companies, industries, market conditions and general economic environment.

Value investing does not guarantee a profit or eliminate risk. Not all companies whose stocks are considered to be value stocks are able to turn their business around or successfully employ corrective strategies which would result in stock prices that do not rise as initially expected.

Growth investing does not guarantee a profit or eliminate risk. The stocks of these companies can have relatively high valuations. Because of these high valuations, an investment in a growth stock can be more risky than an investment in a company with more modest growth expectations.

Investing in foreign emerging markets entails greater risks than those normally associated with domestic markets, such as political, currency, economic and market risks.

Investing in smaller companies involves greater risks not associated with investing in more established companies, such as business risk, significant stock price fluctuations and illiquidity.

Stocks of medium-sized companies entail special risks, such as limited product lines, markets, and financial resources, and greater market volatility than securities of larger, more-established companies.

Treasury Inflation Protection Securities' (TIPS) coupon payments and underlying principal are automatically increased to compensate for inflation by tracking the consumer price index (CPI). While the real rate of return is guaranteed, TIPS tend to offer a low return. Because the return of TIPS is linked to inflation, TIPS may significantly underperform versus conventional U.S. Treasuries in times of low inflation.

Asset allocation and diversification do not assure a profit or protect against loss in declining financial markets.

The indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment.

The indices selected by Morgan Stanley Wealth Management to measure performance are representative of broad asset classes. Morgan Stanley Wealth Management retains the right to change representative indices at any time.

REITs investing risks are similar to those associated with direct investments in real estate: property value fluctuations, lack of liquidity, limited diversification and sensitivity to economic factors such as interest rate changes and market recessions.

Investing in commodities entails significant risks. Commodity prices may be affected by a variety of factors at any time, including but not limited to, (i) changes in supply and demand relationships, (ii) governmental programs and policies, (iii) national and international political and economic events, war and terrorist events, (iv) changes in interest and exchange rates, (v) trading activities in commodities and related contracts, (vi) pestilence, technological change and weather, and (vii) the price volatility of a commodity. In addition, the commodities markets are subject to temporary distortions or other disruptions due to various factors, including lack of liquidity, participation of speculators and government intervention.

Because of their narrow focus, sector investments tend to be more volatile than investments that diversify across many sectors and companies.

Asset-backed securities generally decrease in value as a result of interest rate increases, but may benefit less than other fixed-income securities from declining interest rates, principally because of prepayments.

Alternative investments which may be referenced in this report, including private equity funds, real estate funds, hedge funds, managed futures funds, funds of hedge funds, private equity, and managed futures funds, are speculative and entail significant risks that can include losses due to leveraging or other speculative investment practices, lack of liquidity, volatility of returns, restrictions on transferring interests in a fund, potential lack of diversification, absence and/or delay of information regarding valuations and pricing, complex tax structures and delays in tax reporting, less regulation and higher fees than mutual funds and risks associated with the operations, personnel and processes of the advisor.

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