

Morgan Stanley

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PRIVATE WEALTH MANAGEMENT ASIA

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# Best Execution & OTC Order Handling Policy

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November 2022

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## 1. Executive Summary

This document sets out the Best Execution Policy (“Policy”) and approach to providing Best Execution for the Private Wealth Management (“PWM”) Asia business of Morgan Stanley Bank Asia Limited or Morgan Stanley Bank Asia Limited, Singapore Branch (collectively known as “MSBAL”).

Morgan Stanley is committed to treating our clients fairly and to create a suitable trading environment for all clients. We have a duty to provide our clients with “Best Execution” when entering into transactions with them. Our primary objective in handling client orders is to deliver the highest quality executions reasonably available under the circumstances and within the context of applicable markets, seeking to balance often conflicting considerations with a view to providing clients with the best possible result on a consistent basis. This Policy sets forth our approach to achieving the best possible result for our clients when executing their orders.

Morgan Stanley needs to take all reasonable steps to obtain the best possible result for clients, taking into account price, costs, speed and likelihood of execution, likelihood of settlement, size, nature and/or any other relevant order execution consideration, whether we are executing orders on behalf of clients or placing orders with, or passing orders to, others for execution. This overarching obligation to obtain the best possible result for clients is referred to, in this document, as our obligation of ‘Best Execution’.

The PWM Asia Best Execution Committee (“BEC”) shall oversee PWM Asia’s application of the Policy to each order with a view to obtaining the best possible result in accordance with the Policy in order to comply with the overarching Best Execution requirement.

## 2. Scope

This Policy covers the Best Execution obligation & OTC Order Handling Principles PWM Asia will adhere to for their PWM Asia Hong Kong Professional Investor (PI) & Singapore Accreditor Investors (SGAI) clients across all products as further described in the Policy. Please refer to the Policy with detailed information with respect to our approach to Best Execution for the following products:

- (i) Section 8: Execution Principles for Exchange Traded Products
- (ii) Section 9: Execution Principles for Bonds and Fixed Income Instruments Products
- (iii) Section 10: Execution Principles for OTC Derivative, Structured Notes and FX Cash
- (iv) Section 11: Execution Principles for Funds and Alternative Investments

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For products not described in this Policy, Morgan Stanley will at all times be required to treat clients fairly, not disadvantage them and to manage any conflicts of interest that may arise.

### 3. Best Execution Obligation

#### When does Best Execution Apply?

The obligation to provide Best Execution arises when a licensed person is ‘acting for or with a client’, when that licensed person is able to exercise its discretion when executing a client’s instruction or order and where the client is relying on that licensed person to protect their interests in relation to the order. To assess PWM Asia’s role in providing Best Execution, the responsibilities of each Morgan Stanley entity involved in the trade execution flow should be evaluated. The following Morgan Stanley entities are involved in the PWM Asia trade flow:

- MSBAL is a fully licensed bank under the Hong Kong Monetary Authority (“HKMA”), Securities and Futures Commission (“SFC”) and Monetary Authority of Singapore (“MAS”). Investment Representatives (“IRs”) who provide PWM services by taking orders from clients as agents of those clients are employees of MSBAL. IRs do not have execution/ trading capacity.
- Morgan Stanley Asia Limited (“MSAL”) is the licensed execution desk which receives all orders from PWM Asia IRs for execution and remotely books such transactions to MSIP.
- Morgan Stanley & Co. International Plc. (“MSIP”) provides clearing and settlement of transactions and is the custodian for PWM Asia Clients. MSIP is the counterparty in all OTC derivative transactions unless otherwise notified to the client.

MSBAL is the client facing entity and acts in an agency capacity when transmitting PWM Asia’s orders to MSAL for execution – PWM Asia therefore assumes responsibility for and obligation of providing Best Execution to the end client.

As OTC derivative instruments are bilateral contracts, and MSIP acting as counterparty for all OTC derivative transactions, MSIP will be acting as principal and may be trading in the underlying reference asset to hedge itself in relation to its principal position facing the clients.

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## Best Execution Obligation

Best Execution is the requirement to execute a client order on the best available terms for the client. Where PWM Asia has the obligation to provide Best Execution, it will execute a client order taking into consideration the following factors (together, the Best Execution factors):

- **Price:** this refers to the resulting price of the transaction excluding our own execution charges. Price includes execution venue fees, clearing and settlement prices and any other fees if applicable (all fees relating to Morgan Stanley are charged in accordance with our fee schedule).
- **Speed and Likelihood of Execution:** we interpret speed and likelihood of execution as the rate at which we are able to progress the order and the likelihood that we are able to fill the order or at least a substantial part of it, in its entirety. Where client instructions dictate or imply a rate at which we should progress the order, we will follow such instructions unless we see an immediate and substantial conflict with the price. Where the instructions do not refer to speed, we will progress the order at a rate which we believe represents a balance between creating market impact and executing the order in a timely fashion so as to reduce execution risk. This factor increases in importance in situations where access to liquidity in the relevant instrument is constrained in some way. For example, if the security itself is illiquid or if client provides a limit price which is not marketable.
- **Costs:** This refers to the expenses incurred from entering into the transactions and any associated hedging activity.
- **Likelihood of settlement:** we expect transactions that we execute to settle in a timely fashion. If we become aware that a particular execution strategy may compromise likelihood of settlement, we may not pursue that strategy even if it would result in a better price.
- **Order size:** Size of any request for quote may affect the quote price, e.g., exceptionally large market moving orders or with limited counterparties willing to quote.
- **Nature of the order:** Characteristics of a request for quote or resultant order might affect the performance.
- **Any other relevant consideration:** e.g. relevant to the efficient execution of the client's order such as the nature of the relevant market, local regulatory requirements, prevailing market conditions, potential market impact, timing of receipt of orders and what might have been agreed with the client.

Morgan Stanley may also take into consideration the following general criteria when determining how to achieve Best Execution of the order:

- the characteristics of the client (including the regulatory categorization of client);

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- the characteristics and nature of the order, including any specific instructions received;
- the characteristics of the financial products that are the subject of the order; and
- the characteristics of the execution venues or brokers to which the order can be directed.

In relation to the above factors, Morgan Stanley takes into account a high/medium/ low approach as a general indication for evaluating the relative importance of execution factors. These factors will be measured on a collective basis, unless the client has specified otherwise. On a case by case basis and subject to specific client instructions, Morgan Stanley may prioritize one or more of the execution factors above differently and this may result in different permissible approaches being used. Even though Morgan Stanley takes all reasonable steps to achieve the best possible result for the client, taking into account the above-mentioned execution factors, Morgan Stanley cannot guarantee that particularly at an individual transaction level the price obtained by Morgan Stanley will always be the best price available in the market at that point in time. Therefore, the fact that any execution may not have been done at the best price, for example, does not necessarily mean that Best Execution has not been provided.

Where the client gives specific execution instructions, including specifying the characteristics of a bespoke product, either relating to an order or a particular aspect of an order, this may prevent Morgan Stanley from following some or all of the steps in this Policy that are designed to obtain the best available terms for the execution of that order; Morgan Stanley will execute so far as is reasonably possible in accordance with those instructions subject to our legal and regulatory obligations. To the extent that a client's specific instructions are not comprehensive, Morgan Stanley will determine any non-specified components in accordance with this Policy and to execute client orders on the best available terms.

Morgan Stanley reserves the right to intervene in the execution if such orders would result in adverse market movement (e.g. large orders).

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## 4. Execution Venue

In meeting its Best Execution obligation, Morgan Stanley will monitor which venues are likely to provide, on a consistent basis, the best available terms for our clients. Morgan Stanley may, however, not connect to all venues or sources of liquidity.

In certain Financial Instruments there may only be one execution venue available and in executing a trade in such circumstances Morgan Stanley will assume that the selection of that venue satisfies the Best Execution factor dealing with venue selection.

## 5. Affiliates, Third Party Brokers, Counterparties and Note Issuers

In the normal course of business of executing transactions for clients, Morgan Stanley utilizes affiliates, third party brokers, counterparties and note issuers. Where Morgan Stanley uses a third party broker, counterparty or note issuer to execute transactions, it retains an overarching Best Execution obligation.

### Assessment and Periodic Review

PWM Asia perform due diligence when onboarding structured note issuers, OTC counterparties and other execution brokers (the “Counterparties”). Furthermore, on a regular basis PWM Asia will review and update the due diligence and assess the performance of the respective Counterparties to ensure ongoing suitability for PWM Asia and its clients. Continuing assessment factors may include pricing, reliability, quotation, reputation, coverage, trading capabilities, innovation and operational considerations.

## 6. Governance and Management Supervision

Execution staff and their supervisors form an important first line of defence in the trade execution process. Reasonable diligence is demonstrated in handling client instructions, monitoring execution outcomes and, where applicable, taking steps to obtain multiple quotes. In the absence of multiple quotes, execution staff will obtain sufficient pricing information on a best-efforts basis to validate quotes provided to clients.

## 7. Monitoring and Review

PWM Asia will perform monitoring and surveillance on the effectiveness of its Best Execution & OTC Order Handling Principles arrangements and assess on a regular basis if changes are required.

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## 8. Execution Principles for Exchange Traded Products

This section sets out the approach to Best Execution when handling transactions in exchange traded products which includes Cash Equities (including ETFs) and Listed Options & Futures.

### 8.1.1 Execution factors

Unless stated otherwise, across all exchange traded products the ranking of the execution factors are typically as follows:

1. Price
2. Speed and Likelihood of execution

The remaining execution factors – cost, order size, likelihood of settlement, nature of the order and any other consideration relevant to the efficient execution of the client’s order may also be taken into consideration depending on the circumstances of the trade.

### 8.1.2 Order Handling

Once we have accepted the order we will consider the different execution factors in the context of the instructions that clients have provided to form a suitable execution strategy. Under this execution strategy we will take reasonable steps to obtain the best possible result for clients by employing appropriate aspects of our execution arrangements.

Our execution strategy may result in us routing the order to one or more execution venues immediately or working the order over some period of time. The execution strategy employed will take into account any information that clients provide us with, together with our knowledge of the relevant instrument and the market in which clients are seeking to execute.

### 8.1.3 Criteria & Instructions

Subject to client’s specific instructions, our execution strategy may work the order immediately or over a period of time to achieve Best Execution. An example of such instance could be a large order in size and/or an illiquid security, in which case speed would be deprioritized in order to be more passive within the market and to ensure there is not an unacceptable cost or price impact to the client. The execution strategy employed will take into account any information client provides us with, combined with our knowledge and the market that the order needs to be placed in subject to our legal and regulatory obligations.



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This means that to the extent permitted by the specific instruction or instructions, our obligation to achieve the best possible result will be satisfied by executing the order in accordance with client's specific instruction. Where client's specific instruction covers only a portion of an order (for example, as to the choice of venue), and we have discretion over the execution of other elements of the order, then we will continue to owe Best Execution in respect of the elements of the order that are not covered by the specific instruction.

In certain situations, some regulated markets permit the execution of an order outside the central order book based on market specific parameters such as minimum block thresholds and timings of submission.

This could either be block trades or cross trades (submitting matching business accordingly). In such instances, we will look to secure the best possible result, leveraging relationships with liquidity providers/market makers.

## **9. Execution Principles for Bonds and Fixed Income Instruments**

This section sets out the approach to Best Execution when handling transactions in all Bonds and Fixed Income Instruments.

### **9.1.1 Overview of Quotation Process**

Morgan Stanley will take reasonable steps to obtain available quotes for the client, by putting in place a quotation process whereby it reaches out to a prescribed list of pre-approved counterparties when clients request quotes for Bonds and Fixed Income Instruments.

Quotation Process is the process whereby MSAL reaches out to available counterparties to obtain available quotes. Following a reasonable waiting period for available quotes to be returned and a requirement of reaching out to a minimum of 5 counterparties, the best quote is then selected and executed for the client.

### **9.1.2 Execution Factors and Criteria**

Unless stated otherwise, across all Bonds and Fixed Income Instruments the ranking of the Best Execution factors should typically be as follows:

1. Price
2. Speed & Likelihood of Execution are given an equal ranking

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The remaining execution factors – cost, order size, likelihood of settlement, nature of the order and other considerations relevant to the efficient execution of the client’s order may also be taken into consideration depending on the circumstances of the trade.

### 9.1.3 Out of Scope from the Quotation Process

Products that are out of scope from the Quotation Process include:

Primary Issuance of 1) Certificate of Deposits (CDs), 2) Commercial Papers and 3) European Commercial Papers<sup>1</sup>

- Treasury Bills and Treasury Bonds<sup>1</sup>
- Convertible Bonds<sup>1</sup>
- Japanese Government Bonds<sup>1</sup>
- Propriety/Bespoke products that may be a unique offering and difficult to replicate by other counterparties or innovative payoffs that are not widely traded by the street may also reduce the number of counterparties engaged<sup>1</sup>

Notwithstanding the above products which do not follow the Quotation Process, Best Execution will still be applicable and Morgan Stanley will look to achieve this taking into consideration one or more of the execution factors.

<sup>1</sup> For this product type, *nature of order* and the *speed & likelihood of execution* take priority when evaluating Best Execution factors to achieve Best Execution

### 9.1.4 Deviations from the Quotation Process

Unless stipulated in 9.1.3, Morgan Stanley will attempt to follow the Quotation Process. There may be exceptional cases (e.g. exceptional market events or conditions) which would mean that Morgan Stanley would consider other factors/ parameters as more important in determining the best possible Fixed Income execution result.

In the event where there may be deviations from the Quotation Process, a disclosure will be made to the client where practicable. Such disclosure shall be deemed sufficient where it has been disclosed to the client that the Quotation Process has not been followed and that Best Execution will have been achieved considering other factors accordingly.

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## 10. Execution Principles for OTC Derivatives, Structured Notes and FX Cash

This section sets out the approach to Best Execution when handling transactions in OTC Derivatives, Structured Notes and FX Cash.

### 10.1.1 OTC Derivatives and Structured Notes

For OTC derivatives and structured notes covered by this section we set out below certain principles whereby Morgan Stanley sources, determines and passes on a quote to its clients at a price at which Morgan Stanley would be able to enter into a bilateral agreement with such client for OTC derivatives or the price Morgan Stanley is able to source a structured note. Whilst there is no actual execution in passing of a quote to the client the Policy, as required, sets out a process whereby such quotes that are passed to the client, Morgan Stanley would consider as its best available at that time (i.e., the time Morgan Stanley passes the quote to the client) considering factors that would be relevant for Best Execution.

As OTC derivative instruments are bilateral contracts, clients will be entering into a derivative contract directly with MSIP as principal and MSIP may be trading in the underlying reference asset to hedge itself in relation to its principal position facing the clients. MSIP is the counterparty in all OTC derivative transactions unless otherwise notified to the client. MSBAL acts as agent for PWM Asia's clients to transmit instructions to MSIP, or other Morgan Stanley entity as required, and to legally bind clients to transactions in respect of such instructions. PWM Asia has oversight of the process performed by MSIP, or other Morgan Stanley entity as required, to provide pricing to PWM Asia clients for OTC derivative products and structured notes. By passing a request for quote from a client to MSIP, PWM Asia initiates the shopping process, and will monitor the process through to receiving quotes from MSIP and available counterparts and issuers to ensure fair pricing. On review and subject to this Policy, MSBAL relays the best available quote to PWM Asia's client. These Execution Principles for OTC Derivatives and Structured Notes set out a process by which MSIP will take reasonable steps to obtain terms agreeable to the client. OTC derivative instruments and structured notes with FX, Interest Rate and Commodity underlyings will only go through the shopping process for leveraged notionals above USD 10 million.

For some OTC equity derivative instruments (in particular in respect of single stock swaps, equity index swaps, basket swaps and vanilla option warrants) where we owe Best Execution it applies to the execution by us of the equity derivative, but is measured and monitored by reference to the execution of the underlying hedge as the price of the derivatives reflects the price of the hedge. Please refer to the Execution Principles for Exchange Traded Products for Best Execution details on the Morgan Stanley

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underlying hedge in respect of single stock swaps, equity index swaps, basket swaps and vanilla option warrants.

### **10.1.2 FX Cash Related Products (FX Spot, FX Forward and NDF)**

Due to the highly liquid and transparent market, differences in prices for FX Spot, Forward and NDF transactions are negligible amongst counterparties for the G10 and Hong Kong currency markets and the transactions will be executed through a Morgan Stanley affiliate. Intraday volatility in the underlying market prices prescribes that speed and likelihood of execution typically takes highest priority amongst Best Execution factors. For less liquid currency transactions above USD 10 million MSIP will follow the shopping process outlined below while transactions for less than USD 10 million will be executed through a Morgan Stanley affiliate.

### **10.1.3 Overview of Shopping Process**

Morgan Stanley will take reasonable steps to obtain agreed terms for the client, by putting in place a shopping process whereby it reaches out to a prescribed list of pre-approved external counterparties and note issuers when clients request quotes for OTC derivative products, structured notes and FX cash related products. This can be referred to as the “Shopping Process”.

MSIP retains a panel of external counterparties and note issuers (which may be amended from time to time) from which it may obtain indicative pricing for potential transactions. The Shopping Process is where MSIP will reach out to its panel of counterparties and note issuers to obtain available quotes. Following a reasonable waiting period for available quotes to be returned by each counterparty/issuer and a requirement for a minimum of 3, the best quote is then passed to the client to agree the terms for the product. If the client agrees to those terms MSIP will confirm the validity of the indicative prices with the counterparty/issuer and enter into the OTC derivative instrument or FX cash related product directly with the client or obtain the structured note for the client on those terms. For OTC derivative instruments, MSIP retains discretion as to how to hedge. MSIP will first look to see if it can hedge the agreed OTC derivative instrument internally (no names will be shared with the MSIP trading desk), failing which the hedge will likely be executed with an external counterparty.

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## 10.1.4 Execution Factors and Criteria

Unless stated otherwise, for OTC Derivatives, Structured Notes and FX Cash the ranking of the execution factors is typically as follows:

1. Price
2. Speed and Likelihood of execution

The remaining execution factors – cost, order size, likelihood of settlement, nature of the order and any other consideration relevant to the efficient execution of the client's order may also be taken into consideration depending on the circumstances of the trade.

## 10.1.5 Specific Instructions by Clients or Orders Solicitations

Where the client gives specific execution instructions, Morgan Stanley will follow such instructions as far as it is reasonably and commercially possible. This may prevent Morgan Stanley from following the Shopping Process. In the absence of specific instructions Morgan Stanley will exercise its own discretion when following the Shopping Process, having regard to the terms of the order in determining the factors that it needs to take into account for the purpose of providing the client with Best Execution. In situations where Morgan Stanley solicits an order to the client and recommends a price, such price may be inclusive of any premium charged and this fee is disclosed explicitly and charged within our fee schedule.

## 10.1.6 Out of Scope from the Shopping Process

Products that are out of scope in this section from the Shopping Process:

- Equity markets where Morgan Stanley will not be able to follow the Shopping Process for OTC Equity Derivatives due to regulatory, legal and infrastructure constraints, these include: Taiwan, Thailand, Europe, Korea, China A-shares / Stock Connect<sup>2</sup>
- Special Purpose Vehicle issued Delta 1 Warrants / Certificates<sup>2</sup>
- OTC with FX and Commodity underlying when the total leveraged notional of the trade is less than USD 10million<sup>3</sup>
- Dual Currency Notes when the notional of the trade is less than USD 10million and the tenor is less than 3 months<sup>3</sup>
- Limit orders for FX, Interest Rates and Commodity OTC Derivatives, Structured Notes and FX Cash<sup>2</sup>
- FX, Interest Rates and Commodity Structured Notes with issue dates less than 5 business days from trade date<sup>2</sup>
- For G10 and HKD spot, forward and FX swap trades<sup>3</sup>

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- Onshore currency trades (such as MYR, PHP, THB, IDR and TWD)<sup>2</sup>
- Interest Rate Swap, Swaption and Gold<sup>2</sup>
- Secured Cash Notes<sup>2</sup>
- Exotic Options<sup>2</sup>
- Callable Bonus Accumulator and Decumulator<sup>2</sup>
- Continuous Knock Out Accumulator and Decumulator<sup>2</sup>
- Accumulator and Bonus Accumulator with synthetic settlement<sup>2</sup>
- Accumulator and Decumulator with upfront delivery/settlement<sup>2</sup>
- Secondary top-ups of Structured Notes<sup>2</sup>
- Propriety / Bespoke products that may be a unique offering and difficult to replicate by other counterparties or innovative payoffs that are not widely traded by the street may also reduce the number of counterparties engaged<sup>2</sup>
- For single stock swaps, equity index swaps, basket swaps and vanilla option warrants, please refer back to 10.1.1<sup>2</sup>
- Credit Access Notes (CAN)<sup>2</sup>
- Structured Notes and OTC Derivatives quoted and traded after 6pm Hong Kong time<sup>2</sup>
- Bonds executed outside of Asian trading hours by Morgan Stanley & Co. LLC and other local affiliates<sup>2</sup>
- Unwinds and restructurings of existing Structured Notes and / or OTC Derivatives<sup>2</sup>

Notwithstanding the above products which do not follow the Shopping Process, Best Execution will still be applicable and Morgan Stanley will look to achieve this taking into consideration one or more of the execution factors.

<sup>2</sup> For this product type, *nature of order* and the *speed & likelihood of execution* take priority when evaluating Best Execution factors to achieve Best Execution

<sup>3</sup> Due to constraints in the efficiency of the market, trades with less than USD 10million total leveraged notional will not be included in the shopping process. For this product type, *nature of order* and the *speed & likelihood of execution* take priority when evaluating Best Execution factors to achieve Best Execution

## 10.1.7 Deviations from the Shopping Process

Unless stipulated in 10.1.6, Morgan Stanley will attempt follow the Shopping Process. There may be exceptional cases (e.g. exceptional market events) which would mean that Morgan Stanley would consider other factors/ parameters as more important in determining the best possible execution result and in such instances a separate disclosure will be made to the client where practicable.

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In the event where there may be deviations from the Shopping Process, a disclosure will be made to the client where practicable. Such disclosure shall be deemed sufficient where it has been disclosed to the client that the Shopping Process has not been followed and that Best Execution will have been achieved considering other factors accordingly.

Notwithstanding a deviation from the Shopping Process, Morgan Stanley will notify the client of a deviation and endeavor to provide the client with pricing for the OTC derivative instrument so that the client is able to decide whether or not they still wish to enter into a transaction. Where a deviation is not covered below and where Morgan Stanley intends to so deviate, then a separate disclosure will be made to the client prior to order execution.

## **11. Execution Principles for Funds and Alternative Investments**

### **11.1.1 Overview for Mutual Funds, Hedge Funds, Private Equity/ Real Estate Funds**

Dealing in fund products can normally be effected daily on any day that is a dealing day for the relevant funds. Orders for subscription and redemption should be received before the standard fund order time on the relevant dealing day. The price applied will be the daily net asset value and price calculation per unit by the relevant fund, and this price is the same across different investors both in and outside of PWM Asia.

### **11.1.2 Overview for Discretionary Portfolio Management**

There is no separate execution facility for Discretionary Portfolio Management as all orders are passed to various product execution desks for trade execution. In other words, trades that are executed under Discretionary Portfolio Management are no different from other trades, and are subject to the same Best Execution obligations as detailed in other sections in this Policy. In the course of providing Discretionary Portfolio Management services to clients, PWM Asia may give specific execution instructions on behalf of clients, pursuant to the general discretionary authority bestowed on PWM Asia.

### **11.1.3 IMS Fund Onboarding Due Diligence Process**

PWM Asia conducts fund-level due diligence and assessments prior to onboarding any funds to the Morgan Stanley PWM Asia platform for sale.

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PWM Asia conducts ongoing monitoring at least annually or when necessary on the funds that are on the Morgan Stanley PWM Asia Platform.

#### **11.1.4 Out of Scope: Best Execution will not apply**

Mutual Funds are generally out of scope for Best Execution due to the nature of the product where there is limited to no market variance on the available daily price.

Hedge Funds, Private Equity/ Real Estate Funds are out of scope for Best Execution as all of these products are unique offerings and other fund houses would find it difficult to replicate these offerings.