Morgan Stanley Australian Equity Fund

ARSN 133 738 904

Annual report - 30 June 2010

Morgan Stanley Australian Equity Fund
ARSN 133 738 904
Annual report - 30 June 2010

Contents

This financial report covers Morgan Stanley Australian Equity Fund as an individual entity.

The Responsible Entity of Morgan Stanley Australian Equity Fund is Macquarie Investment Management Limited (ABN 66 002 867 003). The Responsible Entity's registered office is Mezzanine Level, No. 1 Martin Place, Sydney, NSW 2000.

Directors' Report

The directors of Macquarie Investment Management Limited, a wholly owned subsidiary of Macquarie Group Limited, the Responsible Entity of Morgan Stanley Australian Equity Fund, present their report together with the financial report of Morgan Stanley Australian Equity Fund ("the Trust") for the year ended 30 June 2010.

Principal activities

The Trust invests in listed equities in accordance with the provisions of the Trust Constitution.

The Trust did not have any employees during the year.

There were no significant changes in the nature of the Trust's activities during the year, until it ceased trading on 17 March 2010.

Directors

The following persons held office as directors of Macquarie Investment Management Limited during the year or since the end of the year and up to the date of this report:

B N Terry
N Roderick (resigned 29/03/2010)
R Cartwright
V Malley
C Vignes
M Rady (resigned 01/02/2010)
C Swanger (appointed 08/02/2010)
T Graham (appointed 29/03/2010)

Review and results of operations

During the year, the Trust continued to invest funds in accordance with target asset allocations as set out in the governing documents of the Trust and in accordance with the provisions of the Trust Constitution.

Results

The performance of the Trust, as represented by the results of its operations, was as follows:

	30 June 2010	30 June 2009
Operating profit before finance costs attributable to unitholders ($)	**107,003**	822
Distributions		
Distribution paid and payable ($)	**106,460**	1,325
Distribution (cents per unit)	**23.64**	0.40

Significant changes in state of affairs

The Trust ceased trading on 17 March 2010.

In the opinion of the directors, there were no other significant changes in the state of affairs of the Trust that occurred during the financial year under review.

Matters subsequent to the end of the financial year

As at the date of this report the Directors are not aware of nay matters or circumstances which have arisen since the end of the financial period which may significantly affect the future state of affairs of the Trust.

Directors' Report (continued)

Indemnification and insurance of officers and auditors

No insurance premiums are paid for out of the assets of the Trust in regards to insurance cover provided to either the officers of Macquarie Investment Management Limited or the auditors of the Trust. So long as the officers of Macquarie Investment Management Limited act in accordance with the Trust Constitution and the Law, the officers remain indemnified out of the assets of the Trust against losses incurred while acting on behalf of the Trust. The auditors of the Trust are in no way indemnified out of the assets of the Trust.

Fees paid to and interests held in the Trust by the Responsible Entity or its associates

Fees paid to the Responsible Entity and its associates out of Trust property during the year are disclosed in note 9 of the financial statements.

No fees were paid out of Trust property to the directors of the Responsible Entity during the year.

The number of interests in the Trust held by the Responsible Entity or its associates as at the end of the financial year are disclosed in note 9 of the financial statements.

Interests in the Trust

The movement in units on issue in the Trust during the year is disclosed in note 6 of the financial statements.

The value of the Trust's assets and liabilities is disclosed on the statement of financial position and derived using the basis set out in note 2 of the financial statements.

Environmental regulation

The operations of the Trust are not subject to any particular or significant environmental regulations under a Commonwealth, State or Territory law.

Auditor's independence declaration

A copy of the Auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 4.

This report is made in accordance with a resolution of the directors.

R Cartwright
Director

Sydney
30 August 2010

Ernst & Young Centre
680 George Street
Sydney NSW 2000 Australia
GPO Box 2646 Sydney NSW 2001

Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
www.ey.com/au

Auditor's Independence Declaration to the Directors of Macquarie Investment Management Limited, as Responsible Entity for Morgan Stanley Australian Equity Fund

In relation to our audit of the financial report of Morgan Stanley Australian Equity Fund for the financial year ended 30 June 2010, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the *Corporations Act 2001* or any applicable code of professional conduct.

Ernst & Young

Ernst & Young

Graeme McKenzie
Partner
30 August 2010

Statement of comprehensive income

	Notes	30 June 2010 $	30 June 2009 $
Investment income			
Interest income		**137**	13
Dividend income		**11,483**	3,328
Net gains/(losses) on financial instruments held at fair value through profit or loss	5	**98,905**	(1,320)
Total net investment income		**110,525**	2,021
Expenses			
Responsible entity's fees	9	**3,133**	683
Other operating expenses		**389**	516
Total operating expenses		**3,522**	1,199
Operating profit		**107,003**	822
Finance costs attributable to unitholders			
Distributions to unitholders		**(106,460)**	(1,325)
(Increase)/decrease in net assets attributable to unitholders	6	**(543)**	503
Profit for the year		**-**	-
Total comprehensive income for the year		**-**	-

The above statement of comprehensive income should be read in conjunction with the accompanying notes.

Statement of financial position

	Notes	**30 June 2010 $**	30 June 2009 $
Assets			
Cash and cash equivalents	7	**26,458**	3,874
Receivables		**2,288**	2,060
Financial assets held at fair value through profit or loss	8	**-**	340,924
Total assets		**28,746**	346,858
Liabilities			
Witholding tax payables		**22**	-
Other payables		**-**	765
Responsible Entity fees payable	9	**17,757**	325
Total liabilities (excluding net assets attributable to unitholders)		**17,779**	1,090
Net assets attributable to unitholders - liability	6	**10,967**	345,768

The above statement of financial position should be read in conjunction with the accompanying notes.

Statement of changes in equity

	30 June 2010 $	30 June 2009 $
Total equity at the beginning of the year	-	-
Total comprehensive income for the year	-	-
Transactions with owners in their capacity as owners	-	-
Total equity at the end of the year	-	-

Under Australian Accounting Standards, net assets attributable to unitholders are classified as a liability rather than equity. As a result there was no equity at the start or end of the year.

The above statement of changes in equity should be read in conjunction with the accompanying notes

Statement of cash flows

	Notes	30 June 2010 $	30 June 2009 $
Cash flows from operating activities			
Proceeds from sale of financial instruments held at fair value through profit or loss		**698,240**	52,434
Purchase of financial instruments held at fair value through profit or loss		**(258,410)**	(394,679)
Dividends received		**12,285**	2,526
Interest received		**137**	12
Other income received		**122,047**	-
Responsible Entity's fees paid		**(109,471)**	(358)
Payment of other expenses		**(427)**	(1,030)
Net cash inflow/(outflow) from operating activities	10(a)	**464,401**	(341,095)
Cash flows from financing activities			
Proceeds from applications by unitholders		**150,000**	344,969
Payments for redemptions by unitholders		**(490,198)**	-
Distributions paid		**(101,619)**	-
Net cash (outflow)/inflow from financing activities		**(441,817)**	344,969
Net increase in cash and cash equivalents		**22,584**	3,874
Cash and cash equivalents at the beginning of the year		**3,874**	-
Cash and cash equivalents at the end of the year	7	**26,458**	3,874
Non-cash financing activities	10(b)	**4,506**	1,302

The above statement of cash flows should be read in conjunction with the accompanying notes.

1 General information

This financial report covers Morgan Stanley Australian Equity Fund ("the Trust") as an individual entity. The Trust was constituted on 29 October 2008 and it ceased trading on 17 March 2010.

The Responsible Entity of the Trust is Macquarie Investment Management Limited (the "Responsible Entity"). The Responsible Entity's registered office is Mezzanine Level, No. 1 Martin Place, Sydney, NSW 2000. The financial report is presented in Australian currency.

During the year, the Trust continued to invest funds in accordance with target asset allocations as set out in the current offer document and in accordance with the provisions of the Trust Constitution.

The financial statements were authorised for issue by the directors on 30 August 2010. The directors of the Responsible Entity have the power to amend and reissue the financial report.

2 Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated in the following text.

(a) Basis of preparation

This general purpose financial report has been prepared in accordance with Australian Accounting Standards, other authoritative pronouncements of the Australian Accounting Standards Board and the *Corporations Act 2001* in Australia.

The financial report is prepared on the basis of fair value measurement of assets and liabilities except where otherwise stated.

Compliance with International Financial Reporting Standards (IFRS)

The financial statements have been prepared in accordance with Australian Accounting Standards as issued by the Australian Accounting Standards Board and International Financial Reporting Standards as issued by the International Accounting Standards Board.

(b) Financial instruments

(i) Classification

The Trust's investments are categorised as at fair value through profit or loss. They comprise:

- Financial instruments designated at fair value through profit or loss upon initial recognition

  These include financial assets that are not held for trading purposes and which may be sold. These are investments in exchange traded equity instruments.

  Financial assets and financial liabilities designated at fair value through profit or loss at inception are those that are managed and their performance evaluated on a fair value basis in accordance with the Trust's documented investment strategy. The Trust's policy is for the Responsible Entity to evaluate the information about these financial assets on a fair value basis together with other related financial information.

Loans and receivables/payables comprise amounts due to or from the Trust.

(ii) Recognition/derecognition

The Trust recognises financial assets and financial liabilities on the date it becomes party to the contractual agreement (trade date) and recognises changes in fair value of the financial assets or financial liabilities from this date.

Investments are derecognised when the right to receive cashflows from the investments has expired or the Trust has transferred substantially all risks and rewards of ownership.

2 Summary of significant accounting policies (continued)

(b) Financial instruments (continued)

(iii) Measurement

(a) Financial assets and liabilities held at fair value through profit or loss

Financial assets and liabilities held at fair value through profit or loss are measured initially at fair value excluding any transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. Transaction costs on financial assets and financial liabilities at fair value through profit or loss are expensed immediately. Subsequent to initial recognition, all instruments held at fair value through profit or loss are measured at fair value with changes in their fair value recognised in the statement of comprehensive income.

- Fair value in an active market

  The fair value of financial assets and liabilities traded in active markets is based on their quoted market prices at the statement of financial position date without any deduction for estimated future selling costs. Financial assets are priced at current bid prices, while financial liabilities are priced at current asking prices.

(b) Loans and receivables

Loan assets are measured initially at fair value plus transaction costs and subsequently amortised using the effective interest rate method, less impairment losses if any. Such assets are reviewed at each statement of financial position date to determine whether there is objective evidence of impairment, such as a significant or prolonged decline in the fair value below carrying amount.

If any such indication of impairment exists, an impairment calculation is undertaken and any impairment loss is recognised in the statement of comprehensive income as the difference between the asset's carrying amount and the present value of the revised estimated future cash flows discounted at the original effective interest rate.

If in a subsequent period the amount of an impairment loss recognised on a financial asset carried at amortised cost decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through the statement of comprehensive income.

(c) Net assets attributable to unitholders

Units are redeemable at the unitholders' option and are therefore classified as financial liabilities. The units can be put back to the Trust at any time for cash based on the redemption price. The fair value of redeemable units is measured at the redemption amount that is payable (based on the redemption unit price) at the statement of financial position date if unitholders exercised their right to put the units back to the Trust.

(d) Cash and cash equivalents

For the purpose of presentation in the statement of cash flows, cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short term, highly liquid investments with original maturities of three months or less from the date of acquisition that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts. Bank overdrafts, if any, are shown separately in the statement of financial position.

Payments and receipts relating to the purchase and sale of investment securities are classified as cash flows from operating activities, as movements in the fair value of these securities represent the Trust's main income generating activity.

2 Summary of significant accounting policies (continued)

(e) Investment income

Interest income is recognised in the statement of comprehensive income for all financial instruments that are not held at fair value through profit or loss using the effective interest method.

Dividend income is recognised on the ex-dividend date.

(f) Expenses

All expenses, including Responsible Entity's fees, are recognised in the statement of comprehensive income on an accruals basis.

(g) Income tax

Under current legislation, the Trust is not subject to income tax provided the taxable income of the Trust is fully distributed either by way of cash or reinvestment (i.e. unitholders are presently entitled to the income of the Trust).

Financial instruments held at fair value may include unrealised capital gains. Should such a gain be realised, that portion of the gain that is subject to capital gains tax will be distributed so that the Trust is not subject to capital gains tax.

Realised capital losses are not distributed to unitholders but are retained in the Trust to be offset against any realised capital gains. If realised capital gains exceed realised capital losses, the excess is distributed to unitholders.

The benefits of imputation credits and foreign tax paid are passed on to unitholders.

The Trust currently incurs withholding tax imposed by certain countries on investment income. Such income is recorded gross of withholding tax in the statement of comprehensive income.

(h) Distributions

In accordance with the Trust Constitution, the Trust distributes its distributable (taxable) income, and any other amounts determined by the Responsible Entity, to unitholders by cash or reinvestment. The distributions are recognised in the statement of comprehensive income as finance costs attributable to unitholders.

(i) Increase/decrease in net assets attributable to unitholders

Income not distributed is included in net assets attributable to unitholders. Movements in net assets attributable to unitholders are recognised in the profit or loss as finance costs.

(j) Receivables

Receivables may include amounts for dividends and interest. Dividends are accrued when the right to receive payment is established. Interest is accrued at the reporting date from the time of last payment in accordance with the policy set out in note 2(e) above. Amounts are generally received within 30 days of being recorded as receivables.

Receivables include such items as Reduced Input Tax Credit (RITC) and application monies receivable from unitholders.

(k) Payables

Payables includes liabilities and accrued expenses owing by the Trust which are unpaid as at year end.

The distribution amount payable to unitholders as at the reporting date is recognised separately on the statement of financial position when unitholders are presently entitled to the distributable income under the Trust's Constitution.

2 Summary of significant accounting policies (continued)

(l) Applications and redemptions

Applications received for units in the Trust are recorded net of any entry fees payable prior to the issue of units in the Trust. Redemptions from the Trust are recorded gross of any exit fees payable after the cancellation of units redeemed.

(m) Goods and Services Tax (GST)

The GST incurred on the costs of various services provided to the Trust by third parties such as investment management fees have been passed onto the Trust. The Trust qualifies for RITC at a rate of 75% hence investment management fees and other expenses have been recognised in the statement of comprehensive income net of the amount of GST recoverable from the Australian Taxation Office (ATO). Accounts payable are inclusive of GST. The net amount of GST recoverable from the ATO is included in receivables in the statement of financial position. Cash flows relating to GST are included in the statement of cash flows on a gross basis.

(n) Use of estimates

The Trust makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

For the majority of the Trust's financial instruments, quoted market prices are readily available. However, certain financial instruments, for example, over-the-counter derivatives or unquoted securities are fair valued using valuation techniques. Where valuation techniques (for example, pricing models) are used to determine fair values, they are validated and periodically reviewed by experienced personnel of the Responsible Entity, independent of the area that created them. Models are calibrated by back-testing to actual transactions to ensure that outputs are reliable.

Models use observable data to the extent practicable. However, areas such as credit risk (both own and counterparty), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

For certain other financial instruments, including amounts due from/to brokers and accounts payable, the carrying amounts approximate fair value due to the immediate or short-term nature of these financial instruments.

(o) New accounting standards and interpretations

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2010 reporting periods. The directors' assessment of the impact of these new standards (to the extent relevant to the Trust) and interpretations is set out below:

(i) AASB 9 *Financial Instruments* and related amendment AASB 2009-11 replacing AASB 139 *Financial Instruments: Recognition and Measurement*

The Australian Accounting Standards Board has now issued AASB 9 Financial Instruments which altered the classification and measurement of financial instruments. Under the new standard only two possible classifications arise, rather than the four existing classifications currently available under AASB 139 Financial Instruments: Recognition and Measurement, and will result in all financial assets being measured at amortised cost or fair value through profit and loss or through other comprehensive income. Financial liabilities are currently excluded from the scope of this standard. The standard is mandatorily applicable for annual reporting periods beginning on or after 1 January 2013. The Trust has not adopted this standard early and is still assessing the full impact of this standard.

3 Financial risk management

(a) Strategy in using financial instruments

The Trust's activities expose it to a variety of financial risks: market risk (including price risk), credit risk and liquidity risk.

The Trust's overall risk management programme focuses on ensuring compliance with the Trust's governing documents and the law and seeks to maximise the returns derived for the level of risk to which the Trust is exposed. The Trust uses derivative financial instruments to alter certain risk exposures.

Financial risk management is carried out by the Responsible Entity's risk management team under policies approved by Responsible Entity's senior managers or by the board of directors of the Responsible Entity (the Board).

(b) Market risk

(i) Price risk

The Trust trades in financial instruments by taking positions listed equities. At 30 June 2010, the Trust's market risk is not affected by changes in market prices as the Trust ceased trading on 17 March 2010.

All securities investments present a risk of loss of capital. The Investment Manager moderates this risk through a careful selection of securities and other financial instruments within specified limits. The maximum risk resulting from financial instruments is determined by the fair value of the financial instruments. The Trust's overall market positions are monitored on a daily basis by the Trust's Investment Manager.

In accordance with the Trust's policy, the risk management department of the Trust's Investment Manager monitors the Trust's overall market price sensitivity on a daily basis. This risk is managed by:

- seeking to ensure the portfolio is fully invested to minimise cash drag

- managing exposure to non index stocks seeking to ensure the Trust is tracking its benchmark within permitted limits

- managing number of securities seeking to ensure diversification across multiple stocks

- managing exposure to any single sector and any single stock seeking to ensure diversification across all sectors

At 30 June 2010 the Trust was not sensitive to price risk as the Trust did not hold any financial instruments. If the S&P/ASX 200 Index at 30 June 2009 had increased by 15% with all other variables held constant, this would have increased net assets attributable to unitholders by approximately $51,139. Conversely, if the S&P/ASX 200 Index at 30 June 2009 had decreased by 15% with all other variables held constant, this would have decreased net assets attributable to unitholders by approximately $51,139.

(ii) Foreign exchange risk

The Trust is not exposed to foreign exchange risk as all assets are denominated in Australian dollars.

(iii) Interest rate risk

The majority of the Trust's financial assets and liabilities are non-interest bearing. As a result, the Trust is not subject to significant amounts of risk due to fluctuations in the prevailing levels of market interest rates. Any excess cash and cash equivalents are invested at short-term market interest rates.

(c) Credit risk

Credit risk (other than that incorporated into price risk) arises from cash and cash equivalents, deposits with banks and other financial institutions and amounts due from brokers. None of these assets are impaired nor past due but not impaired.

The Trust restricts its exposure to credit losses on cash and cash equivalents by managing exposures to single issuers and only investing in banks.

3 Financial risk management (continued)

(c) Credit risk (continued)

In accordance with the Trust's policy, the risk management area of the Investment Manager monitors the Trust's credit position on a daily basis. The Compliance Committee of the Responsible Entity reviews any identified exceptions to internal risk policies and procedures on a quarterly basis.

(d) Liquidity Risk

The Trust is exposed to daily cash redemptions of redeemable units. It therefore invests the majority of its assets in investments that are traded in an active market and can be readily disposed of.

The Trust may, from time to time, invest in derivative contracts traded over the counter, which are not traded in an organised market and may be illiquid. As a result, the Trust may not be able to liquidate quickly its investments in these instruments at an amount close to their fair value to meet its liquidity requirements or to respond to specific events such as a deterioration in the creditworthiness of any particular issuer. No such investments were held at the end of reporting period.

In accordance with the Trust's policy, the risk management area of the Investment Manager monitors the Trust's liquidity position on a daily basis. This is mananaged by:

- monitoring liquidity with respect to liquid assets and large single client holdings

- restricting exposure to illiquid, long-dated stock floats

The Compliance Committee of the Responsible Entity reviews any identified exceptions to internal risk policies and procedures on a quarterly basis.

Subject to the Corporations Act 2001 and the Trust's Constitution, redeemable units are redeemed on demand at the unitholder's option. All other liabilities are payable within 30 days.

4 Auditor's remuneration

During the year the following fees were paid or payable for services provided by the auditor of the Trust:

	30 June 2010 $	30 June 2009 $
Audit services		
Audit and review of financial reports	4,300	7,358
Other audit work under the *Corporations Act 2001*	290	1,400
Total remuneration for audit services	4,590	8,758

Audit fees are paid out of the Responsible Entity's own resources.

5 Net gains/(losses) on financial instruments held at fair value through profit or loss

Net gains/(losses) recognised in relation to financial instruments held at fair value through profit or loss:

	30 June 2010 $	30 June 2009 $
Net gains/(losses) on financial instruments designated as at fair value through profit or loss	98,905	(1,320)
Net gains/(losses) on financial instruments held at fair value through profit or loss	98,905	(1,320)

6 Net assets attributable to unitholders

Movements in number of units and net assets attributable to unitholders during the year were as follows:

As stipulated within the Trust Constitution, each unit represents a right to an individual share in the Trust and does not extend to a right to the underlying assets of the Trust. There are no separate classes of units and each unit has the same rights attaching to it as all other units of the Trust.

	30 June 2010 No.	30 June 2009 No.	30 June 2010 $	30 June 2009 $
Opening balance	329,078	-	345,768	-
Applications	117,621	327,841	150,000	344,969
Redemptions	(439,056)	-	(489,850)	-
Units issued upon reinvestment of distributions	3,353	1,236	4,506	1,302
Increase/(decrease) in net assets attributable to unitholders	-	-	543	(503)
Closing balance	10,996	329,078	10,967	345,768

Capital risk management

The Trust manages its net assets attributable to unitholders as capital, notwithstanding net assets attributable to unitholders are classified as a liability. The amount of net assets attributable to unitholders can change significantly on a daily basis as the Trust is subject to daily applications and redemptions at the discretion of unitholders.

The Trust monitors the level of daily applications and redemptions relative to the liquid assets in the Trust.

7 Cash and cash equivalents

	30 June 2010 $	30 June 2009 $
Cash at bank	**26,458**	3,874

8 Financial assets held at fair value through profit or loss

	30 June 2010 Fair value $	30 June 2009 Fair value $
Designated at fair value through profit or loss		
Equity securities	-	340,924
Total designated at fair value through profit or loss	-	340,924
Total financial assets held at fair value through profit or loss	-	**340,924**

	30 June 2010 Fair value $	30 June 2009 Fair value $
Comprising:		
Equity securities		
Australian equity securities listed on a prescribed stock exchange	-	340,924
Total equity securities	-	340,924
Total financial assets held at fair value through profit or loss	-	**340,924**

An overview of the risk exposures relating to financial assets at fair value through profit or loss is included in note 3.

9 Related party transactions

Responsible Entity

The Responsible Entity of Morgan Stanley Australian Equity Fund is MIML, a wholly owned subsidiary of Macquarie Group Limited.

9 Related party transactions (continued)

Key management personnel

The following persons held office as directors of Macquarie Investment Management Limited during the year or since the end of the year and up to the date of this report:

B N Terry
N Roderick (resigned 29/03/2010)
R Cartwright
V Malley
C Vignes
M Rady (resigned 01/02/2010)
C Swanger (appointed 08/02/2010)
T Graham (appointed 29/03/2010)

No amount is paid by the Trust directly to the directors of the Responsible Entity. Consequently, no compensation as defined in AASB 124 "Related Party Disclosures" is paid by the Scheme to the directors as key management personnel.

Key management personnel unitholdings

At 30 June 2010 no key management personnel held units in the Trust (2009: Nil).

Key management personnel loan disclosures

The Trust has not made, guaranteed or secured, directly or indirectly, any loans to the key management personnel or their personally related entities at any time during the reporting period.

Responsible Entity's fees and other transactions

For the year ended 30 June 2010, in accordance with the Trust Constitution, the Responsible Entity received a total fee of 0.90% of net asset value (inclusive of GST, net of RITC available to the Trust) per annum (2009: 0.90%).

All expenses in connection with the preparation of accounting records and the maintenance of the unit register have been fully borne by the Responsible Entity.

All related party transactions are conducted on normal commercial terms and conditions. The transactions during the year and amounts payable at year end between the Trust and the Responsible Entity were as follows:

	30 June 2010 $	30 June 2009 $
Management fees for the year paid by the Trust to the Responsible Entity	**3,133**	683
Aggregate amounts payable to the Responsible Entity at the reporting date*	**17,757**	325

* The payable to the Responsible Entity relates to amounts paid into the Trust by Morgan Stanley as Investment Manager which are recoverable by MIML as the Responsible Entity. These amounts relate to fees that MIML charges Morgan Stanley directly for the Responsible Entity services and therefore are not reflected in the expenses of the Trust.

Related party schemes' unitholdings

Parties related to the Trust (including MIML, its related parties and other schemes managed by MIML), hold no units in the Trust.

9 Related party transactions (continued)

Investments

At 30 June 2010 the Trust held no investments in any schemes which are also managed by MIML or its related parties (2009: Nil).

No distributions receivable remain unpaid as at 30 June 2010 (2009: Nil).

Other transactions within the Trust

Apart from those details disclosed in this note, no directors of the Responsible Entity have entered into a material contract with the Trust since the end of the previous financial year and there were no material contracts involving directors' interests subsisting at year end.

The bank account for the Trust are held with Macquarie Bank Limited. The Trust may use Macquarie Securities Limited and Macquarie Futures Limited (both Macquarie Group entities), for broking and clearing services respectively. Fees and expenses are negotiated on an arm's length basis for all transactions with related parties.

Bond Street Custodians Limited, a wholly owned subsidiary of Macquarie Group Limited, is the custodian of the Trust.

10 Reconciliation of profit/(loss) to net cash inflow/(outflow) from operating activities

	30 June 2010 $	30 June 2009 $
(a) Reconciliation of profit/(loss) to net cash inflow/(outflow) from operating activities		
Profit/loss for the year	**-**	-
Increase/(decrease) in net assets attributable to unitholders	**543**	(503)
Distributions reinvested	**-**	-
Net (gains)/losses on financial instruments designated as fair value through profit or loss	**(98,905)**	1,320
Proceeds from sale of financial instruments designated as fair value through profit or loss	**698,240**	52,434
Purchase of financial instruments designated as fair value through profit or loss	**(258,410)**	(394,679)
Distributions to unitholders	**106,460**	1,302
Net change in receivables and other assets	**(1,485)**	(2,060)
Net change in payables and other liabilities	**17,958**	1,091
Net cash inflow/(outflow) from operating activities	**464,401**	(341,095)
(b) Non-cash financing and investing activities		
During the year, the following distribution payments were satisfied by the issue of units under the distribution reinvestment plan	**4,506**	1,302
	4,506	1,302

As described in note 2(i), income not distributed is included in net assets attributable to unitholders. The change in this amount each year (as reported in (a) above) represents a non-cash financing cost as it is not settled in cash until such time as it becomes distributable (i.e. taxable).

11 Events occurring after year end

No significant events have occurred since year end which would impact on the financial position of the Trust disclosed in the statement of financial position as at 30 June 2010 or on the results and cash flows of the Trust for the year ended on that date.

12 Contingent assets and liabilities and commitments

There are no outstanding contingent assets and liabilities as at 30 June 2010 and 30 June 2009.

Directors' declaration

In the opinion of the directors of the Responsible Entity:

(a) the financial statements and notes set out on pages 5 to 19 are in accordance with the *Corporations Act 2001*, including:

(i) complying with Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements; and

(ii) giving a true and fair view of the Trust's financial position as at 30 June 2010 and of its performance for the financial year ended on that date; and

(b) there are reasonable grounds to believe that the Trust will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the directors.

R Cartwright
Director

Sydney
30 August 2010

Ernst & Young

Ernst & Young Centre
680 George Street
Sydney NSW 2000 Australia
GPO Box 2646 Sydney NSW 2001

Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
www.ey.com/au

Independent auditor's report to the unitholders of Morgan Stanley Australian Equity Fund

We have audited the accompanying financial report of Morgan Stanley Australian Equity Fund, ("the Fund") which comprises the statement of financial position as at 30 June 2010, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration.

Directors' Responsibility for the Financial Report

The directors of the Responsible Entity, Macquarie Investment Management Limited, are responsible for the preparation and fair presentation of the financial report in accordance with the Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In Note 2(a), the directors also state that the financial report, comprising the financial statements and notes, complies with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, we consider internal controls relevant to the fund's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the fund's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Independence

In conducting our audit we have met the independence requirements of the *Corporations Act 2001*. We have given to the directors of the Responsible Entity a written Auditor's Independence Declaration, a copy of which is included in the directors' report.

Auditor's Opinion

In our opinion:

1. the financial report of Morgan Stanley Australian Equity Fund is in accordance with the *Corporations Act 2001*, including:

   (i) giving a true and fair view of the financial position of Morgan Stanley Australian Equity Fund at 30 June 2010 and of its performance for the year ended on that date; and

   (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*.

Ernst & Young.

Ernst & Young

Graeme McKenzie
Partner
Sydney
30 August 2010