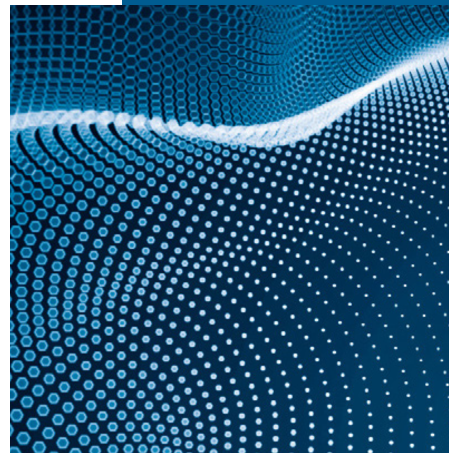
Morgan Stanley

INVESTMENT MANAGEMENT



Looking Ahead: Rate Uncertainty and Innovation

GLOBAL LIQUIDITY TEAM | July 2026

Elevated inflation, heightened geopolitical and economic volatility, and rapidly evolving technologies continue to present both opportunities and challenges. Below is a brief update on six key themes that are likely to remain in the headlines and shape your strategic thinking throughout the remainder of the year.

- THE FEDERAL RESERVE'S NEW PLAYBOOK
- PORTFOLIO POSITIONING GIVEN HIGHER INFLATION EXPECTATIONS
- ULTRA-SHORT STRATEGIES CONTINUED GROWTH
- EU MMF REGULATION UNCHANGED WITH NEW SUPERVISORY GUIDANCE
- TOKENIZED ASSETS PUSH GAINS MOMENTUM
- DIGITAL ASSETS REGULATORY PROGRESS HITS AN IMPASSE

THE FEDERAL RESERVE'S NEW PLAYBOOK

- Interest rate volatility increased in 2Q as markets reassessed the outlook for Federal Reserve policy amid higher oil prices and rising business investment in AI-related technologies.
- While investors had expected the Fed to cut rates multiple times this year, persistent inflation concerns have shifted market expectations toward the possibility of rate hikes.
- Given the future path of interest rates remains uncertain, interest rate volatility is expected to increase as the Federal Reserve moves away from the forward guidance that has historically anchored front-end rates. Under Fed Chair Warsh, the likelihood of policy surprises in either direction could rise, as markets—rather than explicit Fed guidance—play a greater role in determining short-term interest rates and the shape of the yield curve.

PORTFOLIO POSITIONING GIVEN HIGHER INFLATION EXPECTATIONS

GOVERNMENT/TREASURY STRATEGIES

- Approaching quarter-end, we allowed the portfolios to roll down modestly building liquidity for expected quarter-end flow dynamics. With expectations for higher interest rate volatility under Fed Chair Warsh, opportunities in the repo funding markets may become more frequent.
- Given the expected rate volatility and potential for the Fed to remain on hold or raise rates, U.S. Treasury and U.S. Government Agency floating-rate securities should remain attractive. Opportunities to lock in longer-dated yields should persist as well.

CREDIT STRATEGIES

- The relative value of floating-rate securities has become more compelling providing investors with the chance to benefit from funding market volatility and the possibility of higher interest rates.
- Credit spreads are likely to remain rangebound, and we continue to look at relative value opportunities for portfolios across security and coupon types.

ULTRA-SHORT STRATEGIES CONTINUED GROWTH

- Ultra-short fixed income strategies have remained popular with investors seeking to generate yield while preserving capital, particularly amid ongoing economic uncertainty. Through May 2026, the Ultra-Short Bond fund category attracted $54 billion in net new assets, second only to the Intermediate Core Bond category, which gathered $78 billion year-to-date.[1]
- We continue to see strong growth across our ultra-short franchise, spanning both mutual funds and separately managed accounts. The asset class's compelling risk-adjusted return profile and resilience in a range of market environments continue to resonate with investors.

EUROPEAN MMF REGULATION UNCHANGED WITH NEW SUPERVISORY GUIDANCE

- In May 2026, the European Commission issued its report on the adequacy of the current EU Money Market Fund Regulation (MMFR), concluding that the existing regulatory framework continues to function well overall.
- Importantly, the Commission did not recommend any changes to the current EU MMFR Level 1 legislation, meaning that European MMF regulatory requirements and product structures will remain unchanged.
- While no new regulations were proposed, the Commission suggested that national competent authorities (NCAs) should increase their level of supervisory engagement with MMF managers when MMFs fall below 40% WLAs for PDCNAV and LVNAV MMFs and below 20% WLAs for VNAV MMFs to bolster additional resilience in the sector. NCAs are expected to publish final guidance on how these WLA levels will be supervised by late Q3 or Q4 2026.

TOKENIZED ASSETS PUSH GAINS MOMENTUM

- Digital assets are evolving at an accelerating pace with government support and greater regulatory clarity helping to spur growth and interest in products such as stablecoins, tokenized MMFs, and tokenized deposits.
- As market infrastructure continues to develop and interoperability improves, tokenization has the potential to enhance operational efficiency, increase transparency, enable near real-time settlement, and broaden investor access to traditional financial products.
- In line with these developments, we've launched the Morgan Stanley Institutional Liquidity Funds (MSILF) Stablecoin Reserves Portfolio, which is a new government money market fund designed to align with the stablecoin reserves investment requirements of the GENIUS Act. This fund offers payment stablecoin issuers an eligible money market fund option where they can invest required reserves that back their outstanding payment stablecoins.

DIGITAL ASSETS REGULATORY PROGRESS HITS AN IMPASSE

- The Digital Asset Market CLARITY Act is proposed legislation designed to establish a clear regulatory framework for digital assets, including when assets fall under SEC jurisdiction versus CFTC oversight. The Senate Banking Committee approved the CLARITY Act with bipartisan support in May 2026, but further legislative momentum in the Senate has slowed with the debate over stablecoin rewards being a key issue.
- There have been concerns among politicians and within the banking industry that allowing payment stablecoin issuers to offer rewards to stablecoin holders could lead to a migration of deposits away from banks, reducing their capacity to extend loans.

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[1] Morningstar, as of May 31, 2026.

We will continue to monitor these themes as they evolve over the coming months. If you would like to discuss them in more detail or evaluate how they may influence your treasury and cash management strategies, please reach out to your Morgan Stanley relationship manager.

Risk Considerations

There is no assurance that a portfolio will achieve its investment objective. Portfolios are subject to market risk, which is the possibility that the market values of securities owned by the portfolio will decline and that the value of portfolio shares may therefore be less than what you paid for them. Market values can change daily due to economic and other events (e.g. natural disasters, health crises, terrorism, conflicts and social unrest) that affect markets, countries, companies or governments. It is difficult to predict the timing, duration, and potential adverse effects (e.g. portfolio liquidity) of events. **Fixed income securities** are subject to the ability of an issuer to make timely principal and interest payments (credit risk), changes in interest rates (interest-rate risk), the creditworthiness of the issuer and general market liquidity (market risk). In a rising interest-rate environment, bond prices may fall and may result in periods of volatility and increased portfolio redemptions. In a declining interest-rate environment, the portfolio may generate less income. Longer-term securities may be more sensitive to interest rate changes. See prospectus for details.

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