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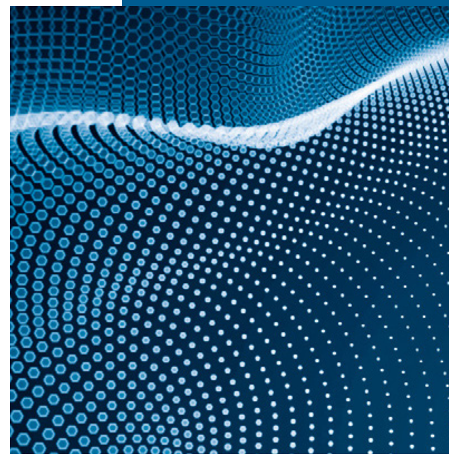

Looking Ahead: Rate Uncertainty and Innovation

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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 U.S. FEDERAL RESERVE'S NEW PLAYBOOK**
- **EU MMF REGULATION UNCHANGED WITH NEW SUPERVISORY GUIDANCE**
- **THE EUROPEAN CENTRAL BANK AND BANK OF ENGLAND NAVIGATE HIGHER ENERGY PRICES**
- **TOKENIZED ASSETS PUSH GAINS MOMENTUM**
- **PORTFOLIO POSITIONING GIVEN ELEVATED INFLATION EXPECTATIONS**
- **EU COMMISSION'S CONSULTATION ON CRYPTO-ASSETS REGULATION**

The U.S. Federal Reserve's New Playbook

- Interest rate volatility increased throughout the summer as markets reassessed the outlook for U.S. Federal Reserve policy amid higher oil prices and rising business investment in AI-related technologies.
- Heading into 2026 investors were expecting the Fed to cut rates multiple times this year, but persistent inflation concerns and a new Fed Chair 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.

The European Central Bank and Bank of England Navigate Higher Energy Prices

European Central Bank

- The European Central Bank (ECB) has highlighted the conflict in the Middle East as a key upside risk to inflation, warning that sustained increases in energy prices could spill over into broader price categories and trigger second-round inflation effects. Given the ECB noted that inflation is set to be "well above target for an extended period," their September rate hike is likely to be followed by further increases, with markets expecting at least one 0.25% hike before year end.
- At the same time, GDP growth has been relatively resilient. However, risks to growth remain to the downside given likely second-round impacts of the energy shock. Given this dynamic, the ECB has emphasized a data-dependent, meeting-by-meeting approach with the goal of returning inflation sustainably to its 2% medium-term target.

Bank of England

- The Bank of England (BoE) remains focused on the inflationary impact of higher energy prices while closely monitoring persistent wage pressures. The BoE has maintained an "active hold" stance – keeping policy unchanged for now, but signaling a willingness to tighten if energy-driven inflation begins to feed through into wages and broader price pressures.
- Monetary policy remains in restrictive territory, with the MPC reinforcing a data-dependent approach. Growth momentum is weak, business confidence has been affected by geopolitical uncertainty, and fiscal headroom remains limited, reinforcing the government's constrained policy backdrop.

Portfolio Positioning Given Elevated Inflation Expectations

USD Prime 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.

USD Treasury Strategies

- With expectations for higher interest rate volatility under Fed Chair Warsh, opportunities in the repo funding markets may become more frequent.
- Given this expected rate volatility and the potential for Fed to remain on hold or hike rates, U.S. Treasury floating-rate securities should remain attractive. Opportunities to lock in longer-dated yields should persist as well.

EUR Strategies

- We have continued to capitalize on duration opportunities across the yield curve as the market priced in additional rate hikes. We continue to maintain high levels of liquidity, providing flexibility to respond to evolving market conditions, and remain focused on country diversification in light of fiscal and geopolitical risks, avoiding credits directly impacted by the Iran conflict.
- With markets anticipating further hikes, our strategy remains focused on balancing fixed-rate investments around key ECB meeting dates while maintaining exposure to floating-rate instruments.

GBP Strategies

- As the Bank of England's monetary policy is still in restrictive territory, they have not yet hiked rates to respond to the inflationary pressures.
- With markets expecting further rate hikes, the extent of market pricing could be somewhat excessive relative to the underlying economic outlook. As a result, we continue to favour selectively extending duration through longer-dated fixed-rate investments where valuations remain attractive.

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% Weekly Liquidity Assets (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 the end of 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.

EU Commission's Consultation on Crypto-Assets Regulation

- The Markets in Crypto-Assets Regulation (MiCA) is the European Union's comprehensive regulatory framework that establishes a harmonized rulebook for the issuance, trading, custody, and provision of crypto-asset services across all EU member states. It covers crypto-asset issuers, stablecoins, and crypto-asset service providers, while establishing requirements for licensing, governance, consumer protection, operational resilience, and oversight.
- In May 2026, the European Commission launched a consultation to assess whether MiCA remains fit for purpose, focusing on areas including stablecoins, tokenization, and its interaction with other EU financial services rules. Following the consultation's close on 30 September 2026, the Commission will review feedback with any legislative amendments expected to be considered in 2027.

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 treasury and cash management strategies, please reach out to your Morgan Stanley relationship manager.

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