

US Fixed Income

Overview

US Economic Overview

Manufacturing activity, which has thus far led the US economic recovery, continued to accelerate in February. Industrial production posted another strong monthly gain, buoyed by the manufacturing component of the index. Further, the Empire State Manufacturing Survey jumped nine points to 24.9, indicating significant acceleration in the region's manufacturing activity. The Philadelphia Fed Survey, which tracks manufacturing activity in the Philadelphia region, also pointed to accelerating growth in manufacturing.

Home sales were weaker than anticipated in February, likely impacted by harsh weather and the extension of the new home buyer's tax credit to April, thus enabling potential buyers to postpone their purchases. Existing home sales fell 7.2% in January on the heels of December's 16.2% decline. Further, new home sales fell to a much lower-than-expected annual rate of 309,000 in January. The labor market continued to be weak with the February weekly releases of jobless claims coming in much higher than anticipated. Initial claims for unemployment benefits climbed to nearly 500,000 in the week ending February 20, the highest level since November. Reflecting consumers' worries about unemployment, the Conference Board's Consumer Confidence Index retreated to 46, 18% below January's level. Further, both consumers' expectations and their assessments of current economic conditions showed marked signs of deterioration.

Headline inflation remained benign as higher gasoline prices were offset by a decline in shelter costs. The Core CPI (ex food and energy) fell 0.1% for the month. The Fed raised the discount rate, the rate at which it makes loans to banks, by 0.5%. This hike was largely ignored by the market as the Fed reiterated its intent to keep the closely-watched Fed Funds rate at very low levels for an extended period of time.

The broad fixed income market generated muted returns that were driven mostly by monthly coupon income. US Treasury, mortgage, high-grade, and high-yield credit indices all returned less than 0.5% for the month. These markets, however, were more volatile than the numbers revealed. The Barclays Capital High Yield Very Liquid Index was down 3.1% through the first two weeks of February only to rebound by month-end. Separately, stocks were up nearly 3.1% as measured by the S&P 500 Index, taking their cue from overall favorable earnings reports. However, the stock market also exhibited significant

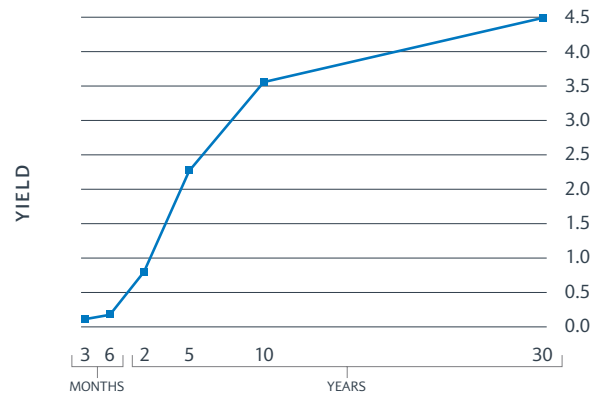
Fixed Income Index Returns by Sector

	FEBRUARY RETURN (%)	YTD RETURN (%)
Barclays Capital US Aggregate	0.37	1.91
Barclays Capital US Treasury	0.40	1.98
Barclays Capital US TIPs	-1.16	0.43
Barclays Capital US Corporate	0.36	1.99
Barclays Capital US Corporate High Yield	0.17	1.44
Barclays Capital US MBS	0.18	1.51
S&P National Municipal Bond	1.02	1.38
J.P. Morgan Emerging Markets Bond	1.48	1.63

Index returns are for illustrative purposes only and do not represent actual iShares Fund performance. Index performance returns do not reflect any management fees, transaction costs or expenses. Indexes are unmanaged and one cannot invest directly in an index. Past performance does not guarantee future results.

Source: BlackRock. As of 02/26/10.

US Treasury Yield Curve



Source: Bloomberg Finance L.P. As of 02/26/10.

volatility, evidenced by a handful of triple-digit point swings in the Dow Jones Industrial Average over the course of the month.

Sector Reviews

The Barclays Capital (BC) US Aggregate Bond Index returned a muted 0.4% in February, matching the return of the BC US Treasury Bond Index and the BC U.S Credit Bond Index as both interest rates and spreads were little changed over the course of the month. Risk aversion continued to be the dominant theme in the market as concerns over Greece's debt predicament escalated.

US Treasuries

US Treasury yields were little changed on a month-over-month basis, belying intra-month volatility that was largely driven by mixed economic data. The 10-year US Treasury yield opened and closed February at 3.6%, but peaked at 3.8% during the month. Signs of continued strength in the manufacturing sector drove yields higher while weak home sales figures, rising unemployment claims and deterioration in consumer sentiment indices weighed on rates later in the month.

Mortgages

Mortgages underperformed duration-matched US Treasuries in February by a modest 7 basis points, as measured by the BC U.S MBS Index. However, this unspectacular headline return masked significant volatility across mortgage sub-sectors and coupon buckets. Announcements by the FHLMC and FNMA regarding plans for their delinquent loan buyout programs had a swift and negative impact on higher coupon mortgages. Delinquent loans that meet stated criteria will be purchased at par, significantly below the dollar prices at which these higher coupons have been trading. Though the FHLMC will complete its program in March, thus affecting current owners of securities only, uncertainty over the timing of FNMA's repurchases had a broader effect on the higher coupon sector. As a result, monthly excess returns were modestly positive for current coupon securities while their higher coupon counterparts significantly underperformed duration-matched Treasuries.

Investment Grade Credit

Investment grade credit produced lackluster performance again this month. The BC U.S Credit Bond Index posted a total return of 0.4% mirroring the return of the US Treasury market as the option-adjusted spread on the BC U.S. Credit Bond Index was a modest 2 basis points wider month-over-month. Within credit, sovereign debt posted the best returns partially rebounding from underperformance in January. In particular, Peru, Mexico and Brazil were strong performers. Financials lagged this month, delivering excess returns of -25 basis. Performance across the quality spectrum was not widely divergent in February.

Municipals

The BC Municipal Bond Index returned 1.0% in February, outperforming most taxable sectors of the fixed income market despite elevated concerns over credit fundamentals. Limited supply and strong demand contributed to the sector's strong relative performance.

High Yield Credit

The high yield credit sector barely scraped out its 12th consecutive month of positive absolute performance in February, returning 0.2% as measured by the BC US Corporate High Yield Bond Index. As in other sectors, this muted return belied significant intra-month volatility. At one point, the sector was down almost 1.5% as heightened concerns over debt woes faced by Greece and profit-taking put pressure on spreads. For the month, the best performing industries were finance-related: finance companies, life insurance, and banks. More cyclical sectors such as gaming and oil refiners were among the worst performing industries. With respect to quality, the trend away from risk was reflected in solid outperformance by the BB segment of the market relative to the lower quality B and CCC sectors.

TIPS

Inflation-linked bonds underperformed in February after strong performance in January. The BC TIPS Bond Index returned -1.2% for the month. Generally weaker economic data and inflation figures as well as heavy supply contributed to the sector's underperformance. The US issued its first 30-year TIPS in eight years, which initially weighed on the market but eventually cleared at a fair level.

Emerging Markets

Emerging markets debt had a strong month in February with solid returns from both external debt and currency. The JPMorgan EMBIG Diversified Index returned 1.4% bringing its year-to-date return to 1.8%. Overall, economic data continued to confirm the recovery in global growth and trade. China implemented further measures to start removing the unprecedented levels of monetary accommodation, but its monetary policy remained loose. Higher quality credits in Latin America performed well, as did Ukraine and Indonesia. The weakest performer was Argentina, with its -3.5% return hurt by the constitutional crisis, as the executive branch battled in the courts with the central bank governor over the control of central bank reserves.

iShares Fixed Income Funds

FIXED INCOME PRODUCT	TICKER	MANAGEMENT FEES (%)*	EFFECTIVE DURATION***
iShares Barclays Aggregate	AGG	0.24**	4.1
iShares Barclays Short Treasury	SHV	0.15	0.38
iShares Barclays 1-3 Year Treasury	SHY	0.15	1.88
iShares Barclays 3-7 Year Treasury	IEI	0.15	4.48
iShares Barclays 7-10 Year Treasury	IEF	0.15	7.25
iShares Barclays 10-20 Year Treasury	TLH	0.15	9.49
iShares Barclays 20+ Year Treasury	TLT	0.15	14.9
iShares Barclays Agency	AGZ	0.20	2.96
iShares Barclays Credit	CFT	0.20	5.91
iShares Barclays 1-3 Year Credit	CSJ	0.20	1.83
iShares Barclays Intermediate Credit	CIU	0.20	4.13
iShares 10+ Year Credit Bond Fund	CLY	0.20	10.99
iShares iBoxx \$ Investment Grade Corporate	LQD	0.15	7.08
iShares Barclays Government/Credit	GBF	0.20	5.09
iShares Barclays Intermediate Government/Credit	GVI	0.20	3.84
iShares 10+ Year Government/Credit Bond Fund	GLJ	0.20	11.18
iShares Barclays MBS MBB	MBB	0.34**	2.38
iShares Barclays TIPS	TIP	0.20	7.53
iShares iBoxx \$ High Yield Corporate	HYG	0.50	4.23
iShares S&P Short Term National AMT-Free Municipal	SUB	0.25	2.15
iShares S&P National AMT-Free Municipal	MUB	0.25	7.49
iShares S&P California National AMT-Free Municipal	CMF	0.25	7.79
iShares S&P New York National AMT-Free Municipal	NYF	0.25	7.17
iShares 2012 S&P AMT-Free Municipal Series	MUAA	0.30	2.24
iShares 2013 S&P AMT-Free Municipal Series	MUAB	0.30	3.07
iShares 2014 S&P AMT-Free Municipal Series	MUAC	0.30	3.91
iShares 2015 S&P AMT-Free Municipal Series	MUAD	0.30	4.68
iShares 2016 S&P AMT-Free Municipal Series	MUAE	0.30	5.43
iShares 2017 S&P AMT-Free Municipal Series	MUAF	0.30	6.1
iShares S&P/Citigroup 1-3 Year International Treasury	ISHG	0.35	1.77
iShares S&P/Citigroup International Treasury	IGOV	0.35	6.24
iShares JPMorgan USD Emerging Markets Bond	EMB	0.60	6.87

Sources: BlackRock, Bloomberg Finance, LP. As of 02/26/10 .

* "Management Fees" are fees paid to BlackRock Fund Advisors, the Fund's investment advisor. A Fund may also incur indirect expenses on its investments, if any, in other investment companies. Please see the Fund's prospectus for more information on such expenses.

** The total annual operating expenses are shown for the iShares Barclays Aggregate Bond Fund and iShares Barclays MBS Bond Fund. In addition to the management fees, the total expenses include "acquired fund fees and expenses" of 0.04% and 0.09%, respectively, which are related to the funds' investments in the BlackRock Cash Funds: Prime (the "money market fund"). "Acquired fund fees and expenses" represent the funds' pro rata share of the fees and expenses charged by the money market fund and may vary based on the funds' allocation of assets to the annualized net expenses of the money market fund. Annual operating expenses do not include the effect of interest earned by investments in the money market fund, which is expected to offset the money market fund's fees and expenses.

*** Effective duration is a measure of the responsiveness of a bond or portfolio's price to changes in interest rates. Effective duration takes into account the possible changes in expected bond cash flows due to interest rate changes.

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