Inside the market

What's behind the rise in rates?

Interest rates have moved sharply higher, with the 10-year U.S. Treasury yield rising more than 60 bps in a month to its highest level since 2002.[1] As discussed in our recent Fall Investment Directions, strong growth, the AI investment boom, and heavy government borrowing are all competing for capital, and sticky headline inflation, elevated energy prices, and a resilient labor market prompted the Fed's first hike since July 2023.[2] That brings risks, but also an opportunity. Read more about the implications for portfolios here.

3 things to know about the rise in rates

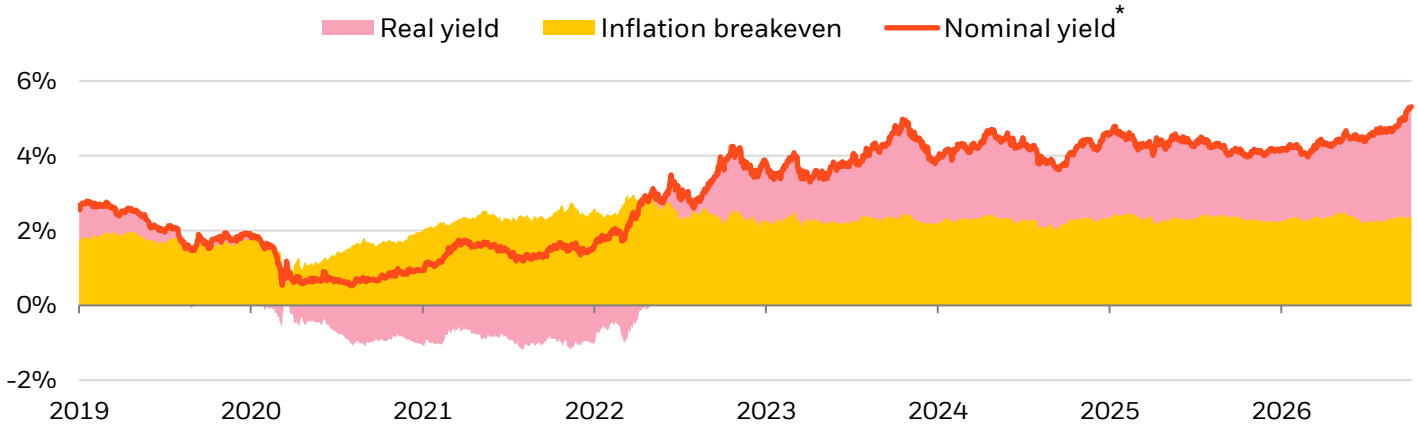
1. **Fed hikes could help contain longer-term rates.** Fed credibility reduces uncertainty about future inflation. After the hot August CPI report, 2-year yields rose another ~15 bps*, but breakevens narrowed and longer rates declined.[3] Chair Warsh cited resilient growth while reaffirming the 2% inflation target. Strong data may call for more hikes, but that doesn't necessarily translate 1:1 to the longer maturities which potentially matters more for stocks.

2. **The rise in rates has been almost entirely a rise in real yields*.** Inflation breakevens* narrowed once the Fed signaled it would act, so higher yields reflect strong growth, heavy demand for capital, and a rising term premium* rather than fears of future inflation. We believe elevated real yields, the return on an investment after accounting for inflation, provide an attractive starting point for fixed income returns.[4]

3. **Demand for long duration* has been relatively limited, despite multi-decade-high yields.**[5] While there have been pockets of demand for long-duration bonds, investors may still see insufficient reward to meaningfully shift allocations from other asset classes, such as AI-linked equities. With lower volatility-adjusted returns* for longer-duration bonds, yields may need to rise further, or the curve steepen*, to encourage broader demand further out along the curve.

The selloff isn't US-only. Read more about the global rise in yields in the BlackRock Investment Institute's report here.

Elevated yields have been driven by real yields, not inflation expectations
Breakdown of U.S. 10-year treasury yield[6]



1: Bloomberg, as of Sept 30, 2026. 2: Federal Reserve. 3: Bloomberg, 2-year Treasury yields and inflation breakevens, September 2026. 4: BlackRock, "First Fed rate hike in years: What it may mean for investor portfolios," Sept 18, 2026. 5: Since the Aug 28 Jackson Hole speech, TLT has seen just $39 million of inflows through Sept 30, 2026. 6: BlackRock, St. Louis Federal Reserve, as of Oct. 5, 2026. *See glossary on page 6.

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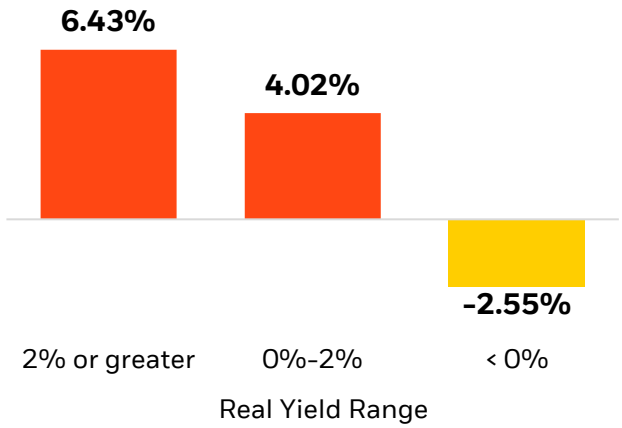
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What could higher rates mean for my portfolio?

Figure 1: Real yields have reached highs not seen since 2008
10-year Treasury Inflation Protected Bond Yield, 1/1/2003 - 9/30/2026



Figure 2: Bonds have historically performed better when real yields were higher
Average annual returns over following 12 months, since 2003



Both stocks and bonds have historically performed well even at elevated rates, with positive average S&P 500 forward returns across every 10-year Treasury yield bucket since 1962 (figure 3). Despite modestly weaker returns with Fed Fund rates between 4-6%, there is no clear yield level where equities consistently break down: even above 6%, 1-year returns averaged 13.5%. What may matter more is *why rates are rising*. Higher real yields driven by stronger growth can coexist with solid returns, while moves driven by tighter policy, higher term premium, or rising inflation expectations can pressure valuations.

Figure 3: Stocks have historically advanced across yield environments
Avg U.S stocks forward return* by 10Y treasury yield bucket* (1/1/1962 – 9/30/2026)

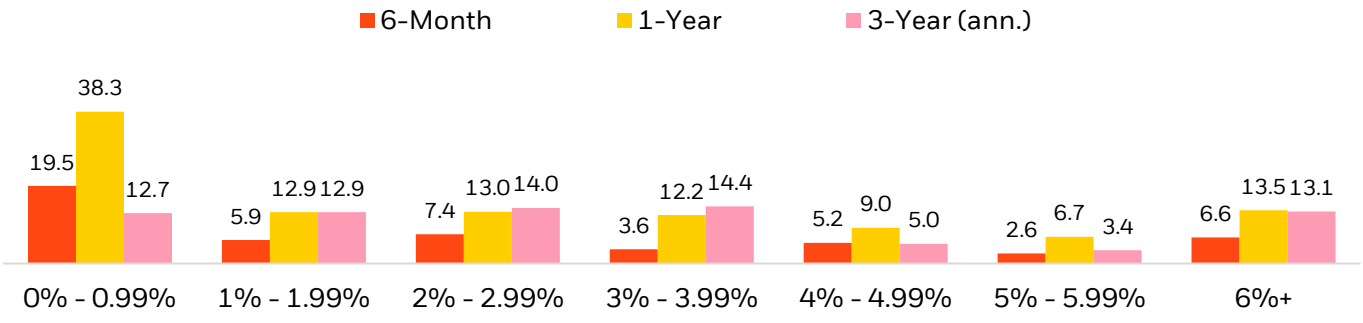


Figure 1,2: Morningstar and the St Louis Federal Reserve as of 9/30/26, U.S. bonds represented by the Bloomberg U.S. Agg Bond Intermediate TR Index. **Past performance does not guarantee or indicate future results. Index performance is for illustrative purposes only. You cannot invest directly in the index.**

Figure 3: Federal Reserve Bank of St. Louis, Morningstar, as of 9/30/2026. Yield levels represented by the Market Yield on U.S. Treasury Securities at 10-Year Constant Maturity, monthly; U.S. stock returns by the IA SBBI U.S. Large Stock Total Return USD Extended Index. Returns shown represent forward total returns measured from each monthly observation: 6-month and 1-year cumulative, 3-year annualized. **Past performance does not guarantee or indicate future results. Index performance is for illustrative purposes only. You cannot invest directly in the index.** *See glossary on page 6.

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Where can investors potentially benefit from higher rates?

We favor carry* and active curve positioning* over directional duration bets. Higher starting yields have restored bonds as a meaningful source of income, with much of today's yield coming from the risk-free rate rather than credit spreads. Short- and medium-term bonds continue to offer attractive income relative to their risk. We remain more cautious on long-term bonds, which could face greater price declines if strong economic growth, heavy bond issuance, and inflation concerns push yields higher.

STEP OUT OF CASH

If overnight interest rates stay higher for longer, investors could consider stepping out of cash into diversified short-duration credit. Short-term bond funds with slightly longer duration than cash are currently yielding nearly a full percentage point more[1], offering a step-up in income without taking on much additional duration or credit risk.

Funds to consider:

SGOV	NEAR	SHY
iShares 0-3 Month Treasury Bond ETF	iShares Short Duration Bond Active ETF	iShares 1-3 Year Treasury Bond ETF

CAPTURE HIGHER RATES

Floating-rate bonds have coupons that reset at regular intervals with short-term rates. That allows investors to potentially capture higher income as rates rise, while limited interest-rate sensitivity can help reduce the price pressure facing traditional fixed-rate bonds.[2]

Funds to consider:

CLOA	USLN
iShares AAA CLO Active ETF	iShares Broad USD Floating Rate Loan ETF

SEEK HIGHER INCOME

Broadening beyond core bonds can help investors seek higher income and diversify their sources of potential return. Opportunities across securitized assets, global bonds, and flexible credit strategies may offer more efficient combinations of yield and risk than relying on the core bond market alone. Additionally, higher yields, strong credit fundamentals, and attractive tax-equivalent income can make municipal bonds a compelling opportunity for investors seeking tax-efficient income, diversification and attractive risk-adjusted returns.

Funds to consider:

SECU	EMB	BINC	HIMU
iShares Securitized Income Active ETF	iShares JPMorgan USD Emerging Markets Bond ETF	iShares Flexible Income Active ETF	iShares High Yield Muni Active ETF

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1: Bloomberg as of 9/30/2026. Cash represented by the Bloomberg U.S. Treasury Bills: 1-3 Months index, short-term bonds by the Bloomberg 1-3 Yr US Gov/Credit Total Return Index Value Unhedged index. 2: The Bloomberg U.S. Aggregate bond index has returned –3.21% from 6/1/26 – 9/30/26. *See glossary on page 6.

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Liquid alternatives can be an alternative to duration

Fixed Income paired with liquid alternatives could offer diversification and independent potential return drivers

A healthy portfolio employs diversifiers to help reduce risk and balance return drivers. Traditional diversifiers such as bonds may provide portfolio risk mitigation, but they can lose effectiveness when correlations with equities rise. In contrast, many alternative strategies are designed to have lower correlation to broad markets by accessing differentiated return potential.

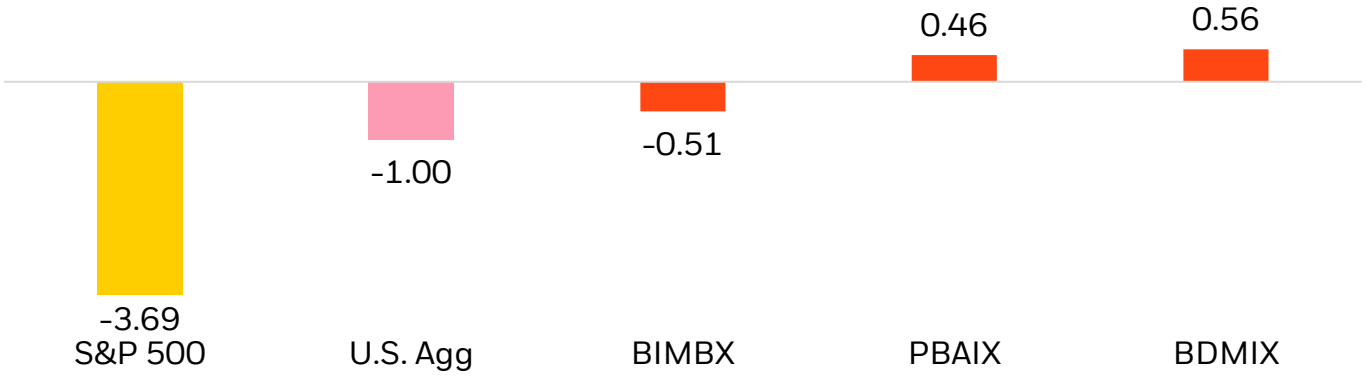
Alternative strategies span a range of approaches that seek to generate returns independent of traditional markets. Market-neutral strategies (**BDMIX**) use quantitative models to take offsetting long and short positions, seeking to isolate stock-specific alpha with minimal market exposure. Learn more about market-neutral investing here. Macro and multi-asset strategies (**PBAIX**) dynamically allocate across equities, rates, currencies, and commodities, often using derivatives to express economic views. Multi-strategy (**BIMBX**) approaches combine several systematic return streams, benefitting from a variety of uncorrelated return drivers. Together, these approaches emphasize flexibility and diversification across market environments.

Funds to consider:

BDMIX	**PBAIX**	**BIMBX**
BlackRock Global Equity Market Neutral Fund	BlackRock Tactical Opportunities Fund	BlackRock Systematic Multi-Strategy Fund

Liquid alternatives have provided ballast when stocks are negative

Average monthly returns when stocks were negative (%, 1/1/2020-9/30/2026)



Source: BlackRock Investment Strategy analysis of data from Morningstar as of 9/30/2026. S&P 500 defined as the S&P 500 TR Index, U.S. Agg by the Bloomberg U.S. Agg Bond TR Index, BIMBX refers to the BlackRock Systematic Multi-Strategy Fund, PBAIX refers to the BlackRock Tactical Opportunities Fund, Gold as the S&P GSCI Gold Spot index, and BDMIX refers to the BlackRock Equity Market Neutral Fund. **The performance quoted represents past performance and does not guarantee future results. Investment returns and principal values may fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. All returns assume reinvestment of all dividend and capital gain distributions. Please click here for most recent standardized performance of BIMBX, PBAIX, and BDMIX.**

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Important Information

Carefully consider the Funds' investment objectives, risk factors, and charges and expenses before investing. This and other information can be found in the Funds' prospectuses or, if available, the summary prospectuses, which may be obtained by visiting the iShares Fund and BlackRock Fund prospectus pages. Read the prospectus carefully before investing.

Investing involves risk, including possible loss of principal.

Funds that concentrate investments in specific industries, sectors, markets or asset classes may underperform or be more volatile than other industries, sectors, markets or asset classes and the general securities market.

Actively managed funds do not seek to replicate the performance of a specified index, may have higher portfolio turnover, and may charge higher fees than index funds due to increased trading and research expenses. There is no guarantee that an active fund will meet its investment objective.

Convertible securities are subject to the market and issuer risks that apply to the underlying common stock. Preferred stocks are not necessarily correlated with securities markets generally. Rising interest rates may cause the value of the Fund's investments to decline significantly. Removal of stocks from the index due to maturity, redemption, call features or conversion may cause a decrease in the yield of the index and the Fund.

International investing involves risks, including risks related to foreign currency, limited liquidity, less government regulation and the possibility of substantial volatility due to adverse political, economic or other developments. These risks often are heightened for investments in emerging/developing markets or in concentrations of single countries.

The Fund's use of derivatives may reduce the Fund's returns and/or increase volatility and subject the Fund to counterparty risk, which is the risk that the other party in the transaction will not fulfill its contractual obligation. The Fund could suffer losses related to its derivative positions because of a possible lack of liquidity in the secondary market and as a result of unanticipated market movements, which losses are potentially unlimited. There can be no assurance that the Fund's hedging transactions will be effective.

AI technology relies on large data sets, which can lead to inaccuracies. Companies in AI face competition, rapid obsolescence, and depend on demand from various industries. Regulatory scrutiny could limit AI development, with data collection facing closer examination and potential fines. Country-specific regulations could also impact AI and big data companies. Securities issued in IPOs have no trading history, and information about the companies may be available for very limited periods. In addition, the prices of securities sold in IPOs may be highly volatile or may decline shortly after the IPO. Technology companies may be subject to severe competition and product obsolescence.

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Glossary

- **Active curve positioning**: Adjusting investments across different bond maturities to take advantage of changes in the yield curve.
- **Bps (basis points):** A measure of changes in yields, with 100 bps equal to 1 percentage point.
- **Carry**: The income earned from holding an investment, such as interest payments from a bond.
- **Curve steepening**: When the difference between long-term and short-term bond yields widens.
- **Duration**: A measure of a bond's sensitivity to changes in interest rates.
- **Forward returns**: The investment returns earned over a future period, typically measured from a specific starting date.
- **Inflation breakevens**: The difference between nominal and inflation-adjusted Treasury yields, reflecting market-implied inflation expectations.
- **Nominal yield**: A bond's yield before accounting for inflation.
- **Real yield**: A bond's yield after adjusting for inflation, reflecting its inflation-adjusted return.
- **Term premium**: The additional yield investors require to hold longer-term bonds instead of shorter-term bonds.
- **Volatility-adjusted returns**: Investment returns measured relative to the level of price fluctuations or risk taken.
- **Yield bucket**: A defined range of yields used to group and compare yield levels observed at different points in time.

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