

GNMA FUND

BLACKROCK®

4Q
2018
COMMENTARYInst: BGNIX¹ • A: BGPAX • C: BGPCX • Class K: BBGPX

- ▶ The fund posted returns of 1.45% (Institutional shares) and 1.39% (Investor A shares, without sales charge) for the fourth quarter of 2018.
- ▶ The main drivers of outperformance were allocations to agency collateralized mortgage obligations (CMOs), allocations to agency commercial mortgage-backed securities (CMBS), and underweight exposure to 15-year agency mortgage-backed securities (MBS). Detractors included underperformance of the fund's 30-year holdings in specified pools; duration (sensitivity to interest rates); yield-curve positioning; an overweight to 30-year agency MBS; and an allocation to Treasury inflation-protected securities (TIPS).
- ▶ The fund closed the quarter overweight in agency mortgages. The overweight was concentrated in higher-coupon securities from the Government National Mortgage Association, and deeply seasoned, higher-coupon conventional 30-year securities. The fund continued to hold allocations to agency CMOs (that use prepayment-protected, seasoned collateral) as well as out-of-benchmark allocations to government-guaranteed, AAA rated CMBS.

Contributors	Detractors
The main contributor to performance was an allocation to well-structured agency CMOs. Out-of-benchmark allocations to government-guaranteed agency CMBS contributed too, along with an overweight exposure to 15-year MBS relative to the benchmark.	The main detractor from returns was security selection within 30-year agency MBS, driven by underperformance of the fund's specified pool holdings. The fund's tactical duration and yield-curve positioning also detracted. An overweight exposure to 30-year agency MBS, as well as an allocation to five-year TIPS breakevens (the difference in yield between nominal Treasuries and TIPS with comparable maturities), detracted slightly too.

Further Insight

We maintained our overweight in agency mortgages, with the overweight concentrated in higher-coupon GNMA MBS and deeply seasoned, higher-coupon 30-year conventional securities. The fund continues to hold allocations to agency CMOs that use prepayment-protected, seasoned collateral, as well as out-of-benchmark allocations to government-guaranteed, AAA rated CMBS. Within CMBS, the fund continues to favor agency interest-only CMBS. We have been pursuing an increased allocation to agency CMBS, owing to valuations that have reached attractive levels versus low-coupon MBS. Finally, we are modestly short duration relative to the benchmark.

Overall Morningstar Rating®:
Institutional

Rated against 209 Intermediate Government Funds, as of 12/31/18, based on risk-adjusted total return. Ratings are determined monthly and subject to change. The Overall Morningstar Rating for a fund is derived from a weighted average of the performance figures associated with its 3-, 5- and 10-year (if applicable) Morningstar Rating metrics.^{††}

Portfolio Management

Matthew Kraeger, Siddharth Mehta

TOP 10 HOLDINGS

(% of Net Assets as of 12/31/18)

1. GNMA II	92.6
2. GNMA I	23.9
3. Federal National Mortgage	5.3
4. Gnma_15-187-C	2.9
5. Gnma_15-55-A	2.7
6. Gnma_17-186-Dt	2.4
7. Gnma_18-51a-Qa	2.2
8. Gnma_15-103-B	1.8
9. Federal Home Loan Mortgage Corporation -Gold	1.6
10. United States Treasury	1.0

Invests primarily in securities issued by the Government National Mortgage Association (GNMA) as well as other U.S. government securities. The Fund seeks to maintain an average portfolio duration that is within +/- 1 year of the duration of the benchmark. The fund normally invests at least 80% of its assets in GNMA securities.

% AVERAGE ANNUAL TOTAL RETURNS AS OF 12/31/18

	4Q18 (not annualized)	YTD (not annualized)	1 Year	3 Year	5 Years	10 Years	Since Inception ²
Institutional	1.45	0.47	0.47	1.11	2.11	3.24	4.69
Investor A (Without Sales Charge)	1.39	0.23	0.23	0.85	1.80	2.90	4.31
Investor A (With Sales Charge)	-2.67	-3.78	-3.78	-0.52	0.97	2.48	4.10
Morningstar Intermediate Government Category Avg.	1.95	0.51	0.51	1.05	1.76	2.46	—
BBG Barc GNMA MBS ⁴	1.95	1.02	1.02	1.48	2.35	3.16	—

Expenses for Institutional shares: Total 0.71%; Net, Including Investment Related Expenses (dividend expense, interest expense, acquired fund fees and expenses and certain other fund expenses) 0.53%. For Investor A shares: Total 0.98%; Net, Including Investment Related Expenses 0.78%. Institutional and Investor A shares have contractual waivers with an end date of 1/31/19 terminable upon 90 days' notice. For certain share classes, BlackRock may voluntarily agree to waive certain fees and expenses in which the adviser may discontinue at any time without notice. Expenses stated as of the fund's most recent prospectus. Data represents past performance and is no guarantee of 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. All returns assume reinvestment of dividends and capital gains. Current performance may be lower or higher than that shown. Refer to blackrock.com for most recent month-end performance. Investment returns reflect total fund operating expenses, net of all fees, waivers and/or expense reimbursements. Index performance is shown for illustrative purposes only. It is not possible to invest directly in an unmanaged index. Share classes have different fees and other features. Returns with sales charge reflect deduction of current maximum initial sales charge of 4% for Investor A shares. Institutional shares have no front- or back-end load. Institutional shares have limited availability and may be purchased at various minimums. See prospectus for details. Net Expenses Excluding Investment Related Expenses for Institutional shares: 0.42%; for Investor A shares: 0.67%.

Important Risks: The fund is actively managed and its characteristics will vary. Holdings shown should not be deemed as a recommendation to buy or sell securities. Bond values fluctuate in price so the value of your investment can go down depending on market conditions. Fixed income risks include interest-rate and credit risk. Typically, when interest rates rise, there is a corresponding decline in bond values. Credit risk refers to the possibility that the bond issuer will not be able to make principal and interest payments. Principal of mortgage- or asset-backed securities normally may be prepaid at any time, reducing the yield and market value of those securities. The fund may use derivatives to hedge its investments or to seek to enhance returns. Derivatives entail risks relating to liquidity, leverage and credit that may reduce returns and increase volatility.

The opinions expressed are those of the fund's portfolio management team as of December 31, 2018, and may change as subsequent conditions vary. Information and opinions are derived from proprietary and nonproprietary sources deemed by BlackRock to be reliable, are not necessarily all-inclusive and are not guaranteed as to accuracy. Past performance is no guarantee of future results. There is no guarantee that any forecasts made will come to pass. This material does not constitute investment advice and is not intended as an endorsement of any specific investment. Investment involves risk. Reliance upon information in this material is at the sole discretion of the reader.

1 The share classes have different sales charges, fees and other features. 2 Fund inception: 5/18/98. 3 Lipper category is as of 12/31/18 and may not accurately represent the current composition of the portfolio. 4 The Barclays GNMA MBS Index comprises GNMA mortgage-backed pass-through securities. †† The Morningstar Rating™ for funds, or "star rating", is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics. The weights are: 100% three-year rating for 36-59 months of total returns, 60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10-year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods. The fund was rated against the following numbers of U.S.-domiciled Intermediate Government funds over the following time periods: 209 in the last 3 years, 194 in the last 5 years and 150 in the last 10 years. With respect to these Intermediate Government funds, the fund received a Morningstar Rating of 3, 4 and 4 stars for the 3-, 5- and 10-year periods, respectively. Other classes may have different performance characteristics.

You should consider the investment objectives, risks, charges and expenses of the fund carefully before investing. The prospectus and, if available, the summary prospectus contain this and other information about the fund and are available, along with information on other BlackRock funds, by calling 800-882-0052 or from your financial professional. The prospectus should be read carefully before investing.

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01/19 — GNMA Fund

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