

MECHANICS OF TIPS AND TIPS ETFs

What are TIPS?

The market for U.S. Treasury Inflation-Protected Securities (TIPS) has grown steadily since their introduction in 1997. TIPS are government bonds with principals that are adjusted with changes in inflation. The U.S. Treasury has issued over \$1.5 trillion of TIPS outstanding as of 3/31/2026.

How do the TIPS bonds work?

TIPS are designed to protect investors from the risk of higher-than-expected inflation. TIPS will adjust their principal based on changes on U.S. Consumer Price Index (CPI) and pay out a fixed coupon rate on the principal. As the size of the principal is adjusted, the coupon will also change, increasing and decreasing with changes in CPI.

Principal amounts

Like a nominal U.S. Treasury, TIPS are issued with an original face value of \$1,000. To measure inflation, the Treasury uses the CPI-U (Non-Seasonally Adjusted CPI Index for All Urban Consumers) to adjust the principal up or down. At maturity, an investor will receive the greater of the bond's original principal or the inflation-adjusted principal value.

Coupons

TIPS will pay out a fixed percentage of the principal as its coupon biannually until maturity. As the principal is adjusted up or down, the dollar amount of coupon paid out will vary. When TIPS are issued, their initial coupons are set at the prevailing real interest rate, which is the nominal rate of a similar duration Treasury adjusted for market assumptions of future inflation. TIPS's coupons generally yield less than Treasuries.

iShares TIPS ETFs

TIP

iShares TIPS Bond ETF

Expense ratio: 0.18%
Effective duration*: 6.41 years

STIP

iShares 0-5 Year TIPS Bond ETF

Expense ratio: 0.03%
Effective duration: 2.37 years

ICPI

iShares 0-1 Year TIPS Bond ETF

Expense ratio: 0.09%
Index effective duration: 0.56 years

Types of marketable U.S. government debt¹

Type of Treasury bond	Total market value (\$ bn)	% of total
Floating Rate Notes	704	2.28
T-Bills (<1 year)	6,820	22.11
Notes (1-10 years)	15,879	51.48
Bonds (10+ years)	5,439	17.34
TIPS (Inflation-protected)	2,090	6.78
Federal Financing Bank	4	0.01
Total Debt	\$30,846	100.00%

Key differences between TIPS and TIPS ETFs	TIPS ETFs	Individual TIPS Bonds
Diversified	Yes	No
Inflation adjustment	Paid monthly	Paid at maturity
Frequency of income payments	Monthly	Semi-annually
Exchange traded / intra-day prices	Yes	No, OTC
Set maturity date	No	Yes
Phantom income	No	Yes

¹ Source: U.S. Treasury as of 3/31/2026. Totals on marketable securities are provided by the U.S. Treasury in the Monthly Statement of the Public Debt as of 3/31/2026. *Effective duration is a measure of the potential responsiveness of a bond or portfolio price to small parallel shifts in interest rates.

Understanding TIPS ETF income distributions

TIPS ETFs pay out the earned income of the portfolio, including an inflation adjustment based on two months' prior CPI applied to the fund's underlying securities.

For tax purposes, the principal adjustment is classified as Treasury income and is distributed by the fund even though it is not distributed to individual TIPS security holders (known as phantom income). If there is deflation, the TIP ETF might omit or not pay a monthly distribution.

The monthly distribution is equal to:

Accrued Coupon Interest
 - Premium amortization
 +Discount accretion
 - Net expenses
 +/-Inflation adjustment
 =ETF earned income

Timing of inflation adjustment and ETF income distribution

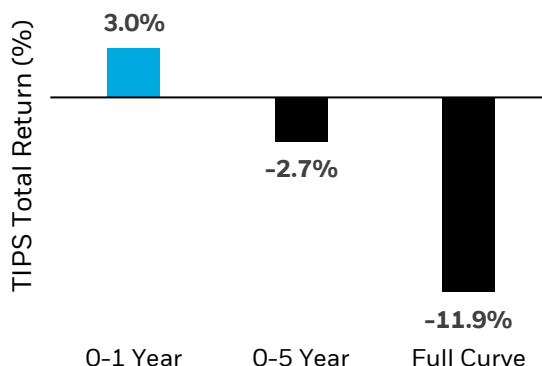
January	February	March	April
January 1-31 CPI measuring period	February 20 January CPI released	March 1-31 Daily rate applied	April 1 ETF distribution paid

Why 0-1-year TIPS?

Just because inflation is rising, doesn't mean TIPS will have positive performance. TIPS have interest rate sensitivity, just like other bonds, and rate moves can de-link TIPS returns from the level of inflation. Investors were reminded about these dynamics in 2022, when the CPI index increased by +6.5% but the TIPS index declined by -12% as the Fed raised interest rates.²

Conversely, 0-1 Year TIPS posted a +3% return in 2022, as their short maturity profile may have helped protect against rising rates.³ Investors can access 0-1 TIPS through ICPI to seek inflation protection and less unwanted duration.

TIPS total return (12/31/2021 - 12/31/2022)⁴



TIPS glossary

- **Inflation adjustments:** The principal amount of TIPS are adjusted by changes in the Consumer Price Index Non-Seasonally Adjusted All Urban Consumers index. This measures the changes in prices paid on a representative basket of goods and services. This metric is published monthly by the Bureau of Labor Statistics.
- **Real yields:** Yield of a nominal bond minus the rate of inflation. $Real\ Yield = Nominal\ Yield - Expected\ Inflation$
- **Breakeven inflation:** The difference between the yield of a nominal bond and an inflation-linked bond of the same maturity. This can be thought of as a market-based measure of inflation expectations, or the level of inflation required for investors to be indifferent (i.e. 'break-even') between holding the nominal bond and an inflation-linked bond.
- **Phantom income:** When TIPS principal value are adjusted upwards, the Internal Revenue Service (IRS) considers this change in value as income paid to the investor and is taxed. However, investors do not receive the cash flow from this income until the maturity of the bond, hence the term 'phantom income'. The ETF pays out the inflation adjustment in monthly income, which provides the cash flow to match the tax consequences.
- **30-Day SEC yield:** A standard calculation developed by the SEC to provide directly comparable values among bond funds. It reflects interest earned by the average investor during the most recent 30-day period, after deducting expenses, annualized. For TIPS ETFs, the SEC yield includes the CPI adjustment on the bonds over the period and is annualized. For months with larger changes in CPI, the fund's SEC yields may be greater than other yield metrics.

² Source: Bloomberg as of 12/31/2022. CPI represented by the US CPI Urban Consumers NSA Index & US TIPS represented by the ICE US Treasury Inflation Linked Bond Index. ³ Source: Bloomberg as of 12/31/2022. ⁴ Source: Bloomberg as of 12/31/2022. 0-1 Year TIPS represented by the ICE BofA 0-1 Year US Inflation-Linked Treasury Index, 0-5 Year TIPS represented by the ICE US Treasury 0-5 Year Inflation Linked Bond Index, Full Curve TIPS represented by the ICE US Treasury Inflation Linked Bond Index. Index performance is for illustrative purposes only. Index performance does not reflect any management fees or expenses. Indexes are unmanaged and one cannot invest directly in an index. Past performance does not guarantee future results.

IMPORTANT INFORMATION

Carefully consider the iShares Funds' investment objectives, risk factors, and charges and expenses before investing. This and other information can be found in the Funds' prospectuses, which may be obtained by calling 1-800-iShares (1-800-474-2737) or by visiting www.iShares.com. Read the prospectus carefully before investing.

Investing involves risk, including possible loss of principal.

Bonds and bond funds will decrease in value as interest rates rise and are subject to credit risk, which refers to the possibility that the debt issuers may not be able to make principal and interest payments or may have their debt downgraded by ratings agencies. Securities with floating or variable interest rates may decline in value if their coupon rates do not keep pace with comparable market interest rates. The Fund's income may decline when interest rates fall because most of the debt instruments held by the Fund will have floating or variable rates.

Fixed income risks include interest-rate and credit risk. Typically, when interest rates rise, there is a corresponding decline in the value of debt securities. Credit risk refers to the possibility that the debt issuer will not be able to make principal and interest payments.

TIPS can provide investors a hedge against inflation, as the inflation adjustment feature helps preserve the purchasing power of the investment. Because of this inflation adjustment feature, inflation protected bonds typically have lower yields than conventional fixed rate bonds and will likely decline in price during periods of deflation, which could result in losses. Government backing applies only to government issued securities, and does not apply to the fund

An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency and its return and yield will fluctuate with market conditions.

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.

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