

Closed-End Fund Market Update

Auction Rate Preferred Shares — Dutch Auctions

MARCH 2008

BLACKROCK

The credit market issues of recent months are spilling over into the market for auction rate preferred shares (ARPS). The issues in the ARPS market are driven by a liquidity problem due to a greater number of sellers than buyers. ARPS are one of the primary instruments used by many closed-end funds, including BlackRock's closed-end funds, to leverage municipal and taxable fixed income portfolios.

Closed-end funds issue ARPS with the goal of paying higher dividends on the fund's common shares. The fund, in essence, obtains money at short-term interest rates by issuing ARPS and invests the proceeds in longer-dated securities. The fund captures the "spread," if any, between short- and long-term interest rates and then passes the spread along to the owners of common shares as incremental dividend income.

ARPS issued by closed-end funds entitle their owners to receive cash dividends at rates determined through a "Dutch auction" process that typically occurs every 7 to 28 days. In a successful auction, an auction agent matches buyers and sellers brought to the auction by broker-dealers at a "clearing rate."

Closed-end funds historically have had an extremely high rate of successful auctions for these ARPS. However, recent auction market liquidity problems have triggered numerous failed auctions across sponsors of closed-end funds, including BlackRock. A failed auction occurs when there are more sellers of ARPS than buyers.

As the auction process is critical to understanding recent developments in the ARPS market, it is important for investors to understand the different potential outcomes of the auction process.

How Auctions Function

Example 1 illustrates the circumstances that lead to a successful Dutch auction. In a successful Dutch auction, buyers and sellers are efficiently matched where bid/ask interplay determines the clearing rate—the dividend rate at which all ARPS change ownership successfully. Example 2 illustrates the circumstances that lead to a failed auction. In a failed Dutch auction, sellers outnumber buyers, and the supply and demand market mechanism fails to determine a clearing rate, even if there is a minor mismatch between buy and sell orders.

Example 1: A “Successful Auction”

In our example, the number of potential buyers outnumbered the potential sellers and the bid/ask interplay determined a clearing rate of 3.25%; therefore, the auction was successful.

Historically, auctions for closed-end fund ARPS have seen predominantly “hold” orders, as investors chose to continue holding their ARPS from auction to auction at whatever clearing rate the active participants determined. The high level of hold orders kept the amount of shares available for purchase limited as the demand for the ARPS outpaced the available supply, contributing to the high success rate for closed-end fund auctions.

Recent liquidity constraints and apprehension in the auction rate market seem to have caused many investors to move from “hold” to “sell” orders. This shift in investor preference appears to have caused an imbalance in supply and demand for ARPS. Also contributing to the supply and demand imbalance, broker-dealers have determined not to commit increasing amounts of capital to maintain the auction market.

Traditionally, when buyers and sellers were unable to be matched perfectly in the auction process, the broker-dealers would voluntarily step in and make a market to facilitate a fluid and successful auction process. However, the broker-dealers have no direct obligation to step in and “back stop” the auction to prevent failure and this inaction has contributed to the recent level of auction failures.

For more information on the auction rate preferred share market, please refer to our “Closed-End Fund Auction Rate Preferred Shares (ARPS) Q&A,” which can be found at www.blackrock.com.

Example 1: A Hypothetical Successful Auction

Holder	Desired Action	Order
Current Holder A	Owens 500 shares; Wants to sell if auction rate is less than 3.50%	Bid order of 3.50% for 500 shares
Current Holder B	Owens 300 shares; Wants to hold all shares	Hold order to take auction rate
Current Holder C	Owens 200 shares; Wants to sell all shares if auction rate is less than 3.25%	Bid order of 3.25% for 200 shares
Prospective Holder A	Wants to buy 300 shares if auction rate is 3.00% or greater	Bid order of 3.00% or above for 300 shares
Prospective Holder B	Wants to buy 300 shares if auction rate is 3.50% or greater	Bid order of 3.50% or above for 300 shares
Prospective Holder C	Wants to buy 400 shares if auction rate is 3.75% or greater	Bid order of 3.75% or above for 400 shares
Prospective Holder D	Wants to buy 200 shares if auction rate is 3.25% or greater	Bid order of 3.25% or above for 200 shares
Rate necessary to clear the market (for all shares to change hands successfully): 3.25%		
Resulting Actions from the Auction		
Current Holder A will sell its shares, as the clearing rate is less than 3.50%		
Current Holder B will continue to hold its shares at 3.25%		
Current Holder C will continue to hold its shares at 3.25%, as the clearing rate is not less than 3.25%		
Prospective Holder A will buy 300 shares, as the clearing rate is greater than or equal to 3.00%		
Prospective Holder B will not participate in the auction, as the clearing rate is less than 3.50%		
Prospective Holder C will not participate in the auction, as the clearing rate is less than 3.75%		
Prospective Holder D will buy 200 shares, as the rate is greater than or equal to 3.25%		

Example 2: A “Failed Auction”

In the case of a failed auction, there is a supply and demand imbalance and the auction does not reach an interest rate necessary to clear the market. Instead, after an auction fails, closed-end funds pay a dividend rate to ARPS holders which resets to a predetermined, formula driven “maximum reset rate.” For BlackRock’s closed-end funds, the maximum reset rate is calculated based upon a predetermined formula that incorporates an applicable reference rate (e.g., LIBOR, “AA” Commercial Paper), as disclosed in the ARPS prospectus. Some ARPS prospectuses list several reference rates, and in the situation of a failed auction, the maximum reset rate will be calculated based on the highest of the specified reference rates in the prospectus. It is worth noting that depending on the number of potential buyers, ARPS may change hands in a failed auction as sell orders and bid orders are filled pro rata, provided some buyers bid at or below the maximum reset rate.

Because failed auctions generally result in limited liquidity to the ARPS holders, many shareholders continue to hold their ARPS after the failed auction. ARPS holders who continue holding securities after a failed auction receive dividends at the maximum reset rate, which is anticipated to be higher than short-term rates outside the auction process. These ARPS holders may offer their shares at the next scheduled auction. However, the ARPS holders remain subject to the same risk that subsequent auctions may also fail to attract sufficient demand to clear the market.

In the event that the ARPS holders experience sustained liquidity impairment in the auction market because auctions continue to fail from week to week, the maximum reset rate does not increase incrementally with every failure. Instead, the maximum reset rate will only vary as the applicable reference rate fluctuates or the applicable benchmark changes.

For more information on the auction rate preferred share market, please refer to our “Closed-End Fund Auction Rate Preferred Shares (ARPS) Q&A,” which can be found at www.blackrock.com.

Example 2: A Hypothetical Failed Auction

Holder	Desired Action	Order
Current Holder A	Owns 1000 shares; wants to sell all shares	Sell order—will sell no matter what the rate
Current Holder B	Owns 300 shares; wants to hold all shares	Hold order—will take auction rate
Prospective Holder A	Wants to buy 300 shares if auction rate is 3.00% or greater	Bid order at 3.00% or above for 300 shares
Prospective Holder B	Wants to buy 200 shares if auction rate is 3.50% or greater	Bid order at 3.50% or above for 200 shares
Prospective Holder C	Wants to buy 200 shares if auction rate is 3.75% or greater	Bid order at 3.75% or above for 200 shares
Rate necessary to clear the market (for all shares to change hands successfully) is not established: Defaults to “maximum reset rate” (assume 4.00%)		
Resulting Actions from the Auction		
Current Holder A will sell 700 of its shares, as that is the maximum number of shares subject to buy orders at/or below the maximum reset rate*;		
Holder A will continue to hold 300 shares at the maximum reset rate		
Current Holder B will continue to hold its shares at the maximum reset rate		
Prospective Holder A will buy 300 shares, as the maximum reset rate is greater or equal to 3.00%		
Prospective Holder B will buy 200 shares, as the maximum reset rate is greater or equal to 3.50%		
Prospective Holder C will buy 200 shares, as the maximum reset rate is greater or equal to 3.75%		
<i>Maximum Reset Rate Calculation is typically the higher of the (multiplier X reference rate) or (addition factor + reference rate), as applicable</i>		
<i>* Bid orders above the maximum reset rate are void.</i>		

A failed auction is not a default on a dividend payment to ARPS holders. In the example shown above, the failed auction occurred because of liquidity impairment. Under the terms of the ARPS, the fund is required to maintain a minimum asset coverage test of 200% or to redeem the ARPS until that asset coverage level is restored. The fund is also subject to additional requirements imposed by rating agencies in order to ensure that the ARPS are triple-A rated. It is important to note that a failed auction does not automatically impact the fund's coverage ratio, credit quality of the underlying portfolio, or the credit quality of the ARPS.

For more information on the auction rate preferred share market, please refer to our "Closed-End Fund Auction Rate Preferred Shares (ARPS) Q&A," which can be found at www.blackrock.com.

Any opinions expressed herein are those of BlackRock as of February 25, 2008 and are subject to change. This material does not constitute investment advice and is not intended as an endorsement of any specific investment.

FOR MORE INFORMATION
www.blackrock.com

©2008 BlackRock, Inc. All Rights Reserved.

F2436-2/2008

BLACKROCK