

Edgar Filing: PREFERRED INCOME FUND INC - Form N-30D

PREFERRED INCOME FUND INC

Form N-30D

April 23, 2003

PREFERRED INCOME FUND INCORPORATED

Dear Shareholder:

The Preferred Income Fund got off to a terrific start during the first quarter of fiscal 2003. For the three months ending February 28th, the Fund earned 9.8% on Net Asset Value and 12.4% on the market value of its shares. During the same period, the Lipper US Government Fund Index rose 3.9% and the Lipper BBB Rated Corporate Debt Index was up 5.6%. There were several factors underpinning the strong performance of the Fund, but one in particular stands out.

The centerpiece of the Bush Administration's Jobs and Growth Package announced in early January is a proposal to eliminate the double taxation of dividends. Under current law, corporate earnings may be subject to two levels of taxation - one at the corporate level and once again at the shareholder level. The Administration believes that multiple taxation of corporate profits increases the cost of capital and creates "severe economic distortions". Some in Congress, however, have expressed doubt about the wisdom and timing of the President's proposals. In the parlance of Washington, this means there will be some serious horse-trading in the coming months, and the eventual outcome is very much up in the air.

Preferred securities can be divided into two basic types - traditional preferreds, which pay dividends, and taxable or "hybrid" preferreds, which pay interest. If enacted, the Administration's proposal would directly impact holders of traditional preferreds only. Not surprisingly, since the proposal was announced traditional preferreds have turned in the best performance.

As discussed in previous letters, over the past several quarters we have been increasing the portfolio's allocation to traditional preferreds. Some might assume that the shift was in anticipation of what might come out of Washington. Not so! The actual reason for the reallocation was based on the same decision-making process employed consistently throughout the life of the Fund. We have felt that in recent months, the yield levels on traditional preferreds have been more attractive than other segments of the market. We considered this an aberration and therefore a great opportunity to purchase undervalued securities. Regardless of the legislative outcome, traditional preferreds still look attractive by most historical measures, and we are very comfortable with the current composition of the investment portfolio.

The historically low level of interest rates in the United States presents some challenges as we strive to maintain the current level of income produced from the assets in the portfolio. Sustained low levels of rates could ultimately result in issuers refinancing higher yielding securities with lower coupon issues much like homeowners refinance a mortgage.

Two of our basic investment approaches should help ward off this income erosion. First, we always attempt to buy undervalued securities. If we are right, the Fund will have more money to invest in additional income producing securities. Second, we generally avoid those securities that pay a high dividend rate but have a greater likelihood of being redeemed by the issuer in the near future. Such issues provide short-term gratification but long-term pain if the investor is forced to reinvest in a lower interest rate environment.

The strategy has been generally effective thus far, but the challenge will increase if interest rates continue to fall and remain low for an extended period of time. The first quarter will be a tough act to follow, but you can count on us to stick to our strategy and provide you with candid assessments of

Edgar Filing: PREFERRED INCOME FUND INC - Form N-30D

our progress.

Sincerely,

/S/ DONALD F. CRUMRINE

/S/ ROBERT M. ETTINGER

Donald F. Crumrine
CHAIRMAN OF THE BOARD

Robert M. Ettinger
PRESIDENT

March 20, 2003

Preferred Income Fund Incorporated
SUMMARY OF INVESTMENTS
FEBRUARY 28, 2003 (UNAUDITED)

	VALUE (000'S)	PERCENT OF TOTAL NET ASSETS
	-----	-----
ADJUSTABLE RATE PREFERRED SECURITIES		
Utilities	\$ 367	0.2%
Banking	20,625	9.1
Financial Services	520	0.2
	-----	-----
Total Adjustable Rate	21,512	9.5
	-----	-----
FIXED RATE PREFERRED SECURITIES		
Utilities	85,354	37.7
Banking	42,127	18.6
Financial Services	33,779	14.9
Insurance	19,181	8.5
Oil and Gas	7,940	3.5
Miscellaneous Industries	5,651	2.5
	-----	-----
Total Fixed Rate	194,032	85.7
	-----	-----
INVERSE FLOATING RATE PREFERRED SECURITIES	1,852	0.8
TOTAL PREFERRED STOCKS AND SECURITIES	217,396	96.0
DEBT SECURITIES	2,086	0.9
COMMON STOCKS	3,049	1.3
PURCHASED PUT OPTIONS	1,848	0.8
MONEY MARKET FUNDS	1,652	0.7
	-----	-----
TOTAL INVESTMENTS	226,031	99.7
OTHER ASSETS AND LIABILITIES (NET)	716	0.3
	-----	-----
TOTAL NET ASSETS AVAILABLE TO COMMON AND PREFERRED STOCK ...	\$226,747	100.0%
	=====	=====

FINANCIAL DATA
PER SHARE OF COMMON STOCK (UNAUDITED)

Edgar Filing: PREFERRED INCOME FUND INC - Form N-30D

	DIVIDENDS PAID	NET ASSET VALUE	NYSE CLOSING PRICE
	-----	-----	-----
December 31, 2002 - Regular	\$0.0915	\$13.65	\$15.10
December 31, 2002 - Extra	0.1285	13.65	15.10
January 31, 2003	0.0915	14.45	16.70
February 28, 2003	0.0915	14.55	16.42

2

STATEMENT OF CHANGES IN NET ASSETS AVAILABLE TO COMMON STOCK(1)
THREE MONTHS ENDED FEBRUARY 28, 2003 (UNAUDITED)

OPERATIONS:

Net investment income	\$
Net realized loss on investments sold during the period	(
Net unrealized appreciation of investments during the period	1
Distributions to Money Market Cumulative Preferred (TRADE MARK) Stock (MMP (TRADE MARK)) Shareholders from net investment income, including changes in accumulated undeclared distributions	
Decrease due to MMP (TRADE MARK) offering cost adjustment	---
Net increase in net assets from operations	1

DISTRIBUTIONS:

Dividends paid from net investment income to Common Stock Shareholders(2)	(
Distributions paid from net realized capital gains to Common Stock Shareholders	---
Total Distributions	(

FUND SHARES TRANSACTIONS:

Increase from Common Stock Transactions	---
---	-----

NET INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK FOR THE PERIOD

NET ASSETS AVAILABLE TO COMMON STOCK:

Beginning of period	13
End of period	\$14

FINANCIAL HIGHLIGHTS(1)
THREE MONTHS ENDED FEBRUARY 28, 2003 (UNAUDITED)

Edgar Filing: PREFERRED INCOME FUND INC - Form N-30D

FOR A COMMON SHARE OUTSTANDING THROUGHOUT THE PERIOD.

PER SHARE OPERATING PERFORMANCE:

Net asset value, beginning of period \$

INVESTMENT OPERATIONS:

Net investment income

Net realized gain and unrealized appreciation on investments

DISTRIBUTIONS TO MMP (TRADE MARK) SHAREHOLDERS:

From net investment income (including change in accumulated
 undeclared dividends on MMP (TRADE MARK))

From net realized capital gains

Total from investment operations

DISTRIBUTIONS TO COMMON SHAREHOLDERS:

From net investment income

From net realized capital gains

Total distributions to Common Shareholders

Net asset value, end of period \$

Market value, end of period \$

Common shares outstanding, end of period \$10,0

RATIOS TO AVERAGE NET ASSETS AVAILABLE TO COMMON STOCK SHAREHOLDERS:

Net investment income

Operating expenses

SUPPLEMENTAL DATA:++

Portfolio turnover rate fiscal year to date

Total net assets available to Common and Preferred Stock, end of period (in 000's). \$ 2

Ratio of operating expenses to total average net assets including MMP (TRADE MARK)..

DIRECTORS

- Martin Brody
- Donald F. Crumrine, CFA
- Robert M. Ettinger, CFA
- David Gale
- Morgan Gust
- Robert F. Wulf, CFA

OFFICERS

- Donald F. Crumrine, CFA
- Chairman of the Board

Edgar Filing: PREFERRED INCOME FUND INC - Form N-30D

and Chief Executive Officer
Robert M. Ettinger, CFA
President and Secretary
Peter C. Stimes, CFA
Vice President, Treasurer,
Chief Financial and
Accounting Officer
Robert E. Chadwick, CFA
Assistant Treasurer

INVESTMENT ADVISER
Flaherty & Crumrine Incorporated
e-mail: flaherty@fin-mail.com

QUESTIONS CONCERNING YOUR SHARES OF PREFERRED
INCOME FUND?

- o If your shares are held in a brokerage account,
contact your broker.
- o If you have physical possession of your shares in certificate form,
contact the Fund's Transfer Agent & Shareholder Servicing Agent --
PFPC Inc.
P.O. Box 43027
Providence, RI 02940-3027
1-800-331-1710

THIS REPORT IS SENT TO SHAREHOLDERS OF PREFERRED INCOME FUND INCORPORATED FOR
THEIR INFORMATION. IT IS NOT A PROSPECTUS, CIRCULAR OR REPRESENTATION INTENDED
FOR USE IN THE PURCHASE OR SALE OF SHARES OF THE FUND OR OF ANY SECURITIES
MENTIONED IN THIS REPORT.

[LOGO OMITTED - PREFERRED INCOME FUND]

Quarterly
Report

February 28, 2003

web site: www.preferredincome.com