To the Shareholders of Flaherty & Crumrine Preferred Income Fund:

The new fiscal year is off to a fine start—total return on *net asset value*[1] for the first fiscal quarter[2] was +4.1%. Over the same period total return based on income plus change in the Fund's *market price* was +3.6%.

With signs of economic improvement trickling in, prices on intermediate and long-term US Treasury bonds fell as much as five percent in the quarter. In contrast, prices on many preferred securities rose. Conditions in the market for preferred securities have been, and remain, positive; credit quality continues to improve, investor demand is high, and the market is shrinking.

Once again redemptions of preferred securities outpaced issuance. Since December 1, 2012, redemptions[3] totaled $30.1 billion. Over the same period, $16.8 billion of new preferred securities were brought to market. *During the past four months, the preferred securities market has shrunk by $13.3 billion, or 3.7%.*

It's instructive to break these numbers down between bank and non-bank securities. Since December 1, 2012, redemptions of bank preferred securities have totaled $17.6 billion, or 44% of total preferred redemptions. Since mid-March, however, bank calls have spiked and comprise over 70% of total redemptions. The pace quickened immediately after regulators announced results from their annual review of capital at large banks. So far, banks have been slow to replace preferred capital—new bank issues have totaled a paltry $3.9 billion since December 1st of last year.

For non-bank companies the decision to call or issue is driven primarily by economics. In the current low interest rate environment, it is often possible for issuers to achieve substantial savings by refinancing. While banks are concerned about expense reduction as well, their decisions about redemption or issuance have been driven mainly by regulatory requirements. The Dodd-Frank Wall Street Reform and Consumer Protection Act, passed by Congress in 2010, mandated new standards for the amount and form of bank capital. Under the Act, trust preferred securities are being phased out of the calculation of Tier 1 capital. New capital will be either traditional equity or non-cumulative perpetual preferred stock.

As we've discussed in the past, the wave of refinancing negatively impacts income earned from Fund investments. The current combination of high-yielding portfolio assets and low cost of Fund leverage won't last forever; we attempt to set distribution rates that reflect this situation.

As always, we encourage you to visit the Fund's website, www.preferredincome.com, for important information.

Sincerely,

Donald F. Crumrine
Chairman

Robert M. Ettinger
President

March 28, 2013

---

1 Following the methodology required by the SEC, total return includes income and principal change, plus the impact of the Fund's leverage and expenses.

2 December 1, 2012—February 28, 2013

3 Announced or implemented.