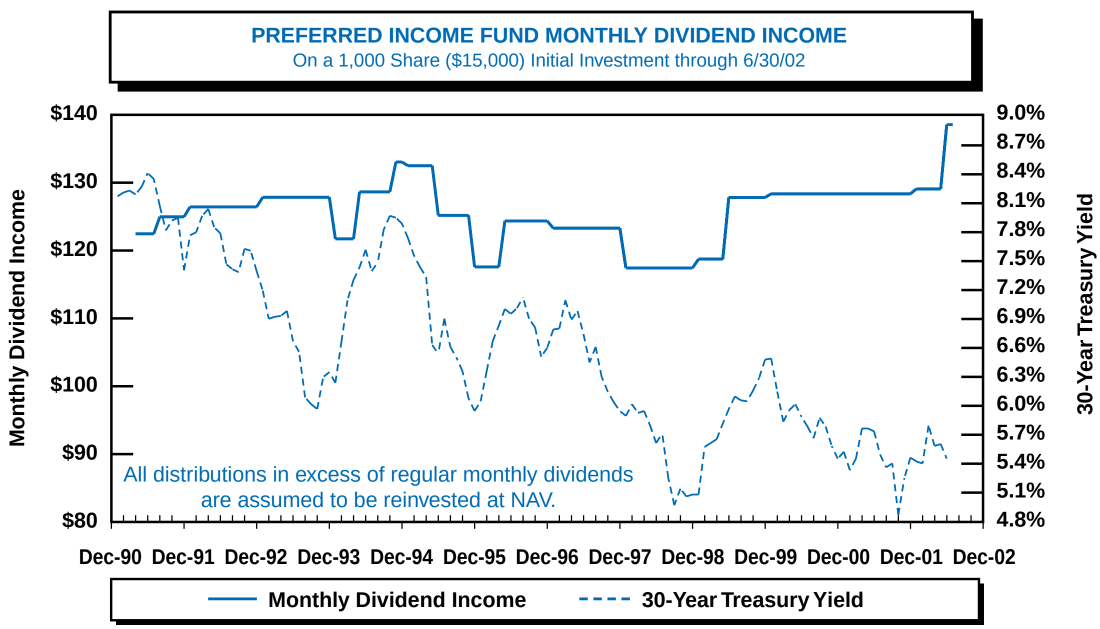
PREFERRED INCOME FUND INCORPORATED

Dear Shareholder:

Sometimes it is good to be boring! Despite the highly unsettled state of the world, financially and otherwise, Preferred Income Fund essentially treaded water in the first half of fiscal 2002. In that six-month period, the Fund earned a total return of -0.4% on the net asset value ("NAV") of its shares. For the twelve months ending May 31, 2002, the return was a more substantial +8.9%.

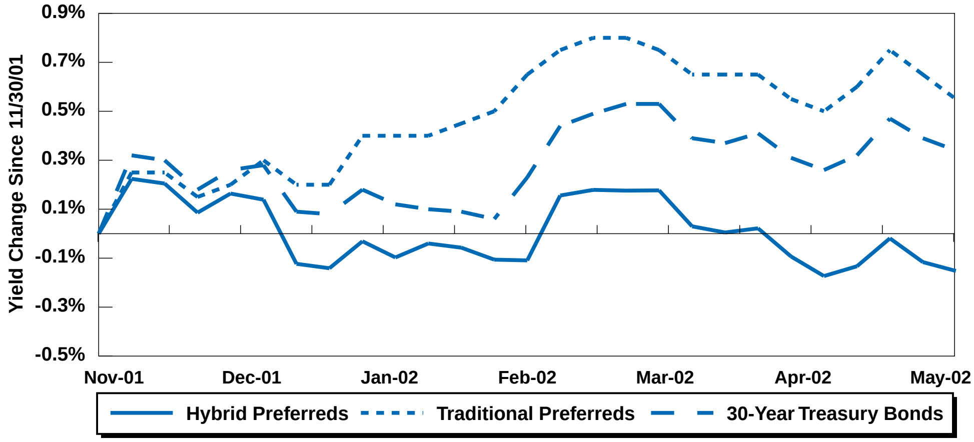
Good news on our dividend rate! The Fund recently raised the dividend rate on its common stock by about 7.3% effective with the dividend payable on June 28, 2002. The new monthly rate will be 8.8 cents per share. The most obvious contributor to the increase has been the low cost of the Fund's leverage caused by very low short-term interest rates. However, there is more to the story than just that, as discussed in the Question & Answer section that follows this letter.



The above graph updates the history of the Fund's dividend income to reflect the increase at the end of June. The Fund's income (represented by the solid line) has performed remarkably well over the years. Income has generally managed to avoid being dragged down in periods of declining interest rates on long-term Treasury bonds (the dotted line). In contrast, when the Treasury interest rates have increased, the Fund's income has typically also increased. This is exactly what we are trying to do.

Market conditions included a little bit of everything in the six months ended May 31st. For example, the two primary preferred market sectors moved in opposite directions. Hybrid preferreds rose in price, causing a slight decline in their yields. In contrast, the prices of traditional fixed-rate preferreds fell, and their yields increased by more than one-half of a percentage point. The chart below illustrates the diverse yield changes produced by these trends since the beginning of fiscal 2002. For reference, it also shows the change in the yields of long-term Treasury bonds.

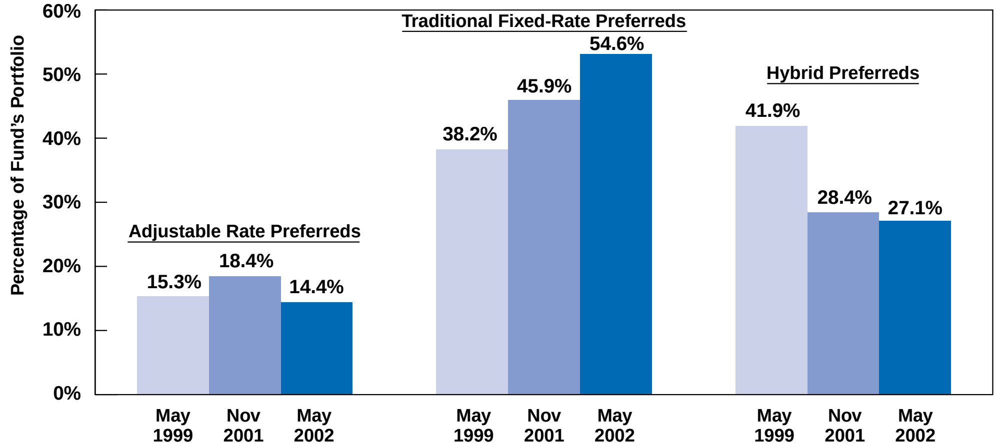
Cumulative Changes In Yields of Preferreds and Treasury Bonds Since 11/30/01



Traditional preferreds typically yield less than hybrid preferreds, and well they should. Traditional preferreds, including both fixed and adjustable rate issues, offer corporate investors the tax benefit of the Dividends Received Deduction ("DRD"), which is not available from hybrids. (The DRD also benefits the Fund through a complicated formula that reduces the cost of its leverage.) Because of this tax advantage, it is entirely possible for traditional preferreds to be very attractive among fixed-rate issues even when they yield somewhat less than hybrids. We believe that traditional fixed-rate preferreds reached that point some time ago and have since become increasingly undervalued.

Not surprisingly, we have continued to sell gradually some of our holdings of hybrids and buy particularly attractive traditional fixed-rate preferreds as opportunities have appeared in the market. By picking our spots carefully and executing the strategy well, we have been able to avoid a significant impact on the Fund's income despite the normally lower yields on traditional issues. As shown by the bar chart on the next page, the change in the composition of the Fund's portfolio has been enough to make a difference, particularly versus three years ago when our position in hybrids was close to its highest level. We think the Fund is in a good position to benefit from the bargains that we see in traditional preferreds now.

PREFERRED INCOME FUND
Comparative Portfolio Weightings, 5/31/99 to 5/31/02

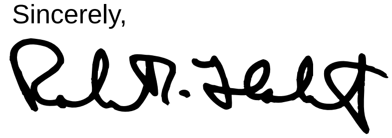


The Fund has now completed on a very satisfactory basis the increase in its leverage discussed in our report to shareholders for the first fiscal quarter. On June 4, 2002, Preferred Income Fund issued $22.5 million of additional shares of Money Market Cumulative Preferred™ stock ("MMP"), as detailed in the Notes to the Financial Statements. The newly issued MMP increased the total face amount of such shares outstanding to $80 million. This seems to be a more appropriate amount of leverage for the Fund in view of the increase in its assets that has occurred since its inception. The goal of this increase is to enhance over time the income available to the holders of the Fund's common stock. Remember, however, that leverage magnifies both good *and* bad news.

As described more fully in Note 6 on page 23, one of Preferred Income Fund's policies was recently revised in order to preserve investment flexibility. In recent years, both Moody's and Standard & Poor's have integrated their rating scales for bonds and preferreds. In the process, the ratings on many preferreds were reduced, although the rating agencies indicated that this was not by itself intended to signal changes in the credit standing of the issuers. The Fund's Board of Directors has taken this into account by increasing from 15% to 25% the limit on the Fund's holdings of securities that meet certain minimum ratings requirements, but are not rated investment grade themselves. As always, all of the Fund's investments must be in companies that, at the time of purchase, have investment grade rated senior debt outstanding or are of comparable quality.

The Question and Answer section provides further important information on the Preferred Income Fund. In addition, please visit our web site at **www.preferredincome.com** to get the most current data on the Fund.

Sincerely,



Robert T. Flaherty
Chairman of the Board

June 19, 2002

QUESTIONS & ANSWERS

WHY WAS THE FUND ABLE TO RAISE ITS DIVIDEND RATE?

The higher dividend is really the net result of several factors. A decline in the cost of leverage was a big help. Ongoing management of the portfolio also helped, mostly by avoiding things that would normally have reduced income. Hedging tended to reduce income.

CAN YOU GIVE US MORE DETAILS ON THE DIVIDEND INCREASE?

The reduction in the cost of the Fund's leverage was the most visible factor. The Fed's easier money policies over the last 1 1/2 years have sharply reduced short-term rates. The rates paid by the Fund on its outstanding Money Market Cumulative Preferred™ stock, which are reset every 49 days through an auction process, have stayed in the range of 1 1/2% to 1 3/4% so far this year. When money was relatively tight about a year and a half ago, we were paying close to 5% for this money.

Day-to-day management of the portfolio also made an important, but less obvious, contribution to income. We have moved a lot of money from hybrid preferreds to traditional DRD eligible preferreds over the last several years. We believe this has created a more attractive portfolio, but it would normally have made a real dent in income and offset a significant part of the savings on our leverage costs. We were able to avoid that by taking advantage of the inefficiencies inherent in the preferred market. This phase of the war was won through "hand-to-hand" combat in the trenches.

Hedging was a negative. The cost of hedging increased significantly in this environment. Furthermore, long-term interest rates declined slightly over the last year and a half. As we would expect under these conditions, our hedges were something of a drag on the Fund's income. Our hedges are designed to cope with upward spurts in long-term interest rates. The only spurt this time was down, not up, and it was in short-term rates, not long rates.

WILL THE FUND PAY AN EXTRA DIVIDEND AGAIN AT YEAR-END?

We try to take a conservative approach in setting the Fund's monthly dividend rate. The new dividend rate leaves a little room for the unexpected, including some increase in leverage costs. That cushion could disappear by the end of this fiscal year on November 30th. Nonetheless, our best guess at the moment is that the Fund will wind up the fiscal year with some income left over. If that happens, we will distribute the extra income to shareholders in December as we have in the past.

WHAT DO YOU MAKE OF THE CURRENT WAVE OF BANKRUPTCIES AND ACCOUNTING PROBLEMS?

Credit analysis has never been more important. A steady stream of financial and accounting problems has surfaced in the wake of the Enron catastrophe, and each new announcement creates rumors of ten more. Clearly, the system is in need of repair. At the moment, the market is punishing the suspects along with the guilty.

We fully expect the headlines to get worse before the problems in the system are fixed. Time will resolve the economic problems left over from the speculative bubble of the late 1990s. Other problems may require an increase in the prison population. We would expect the latter to have an extremely positive influence on the restoration of financial responsibility and business ethics.

HAVE THESE CREDIT PROBLEMS AFFECTED THE FUND?

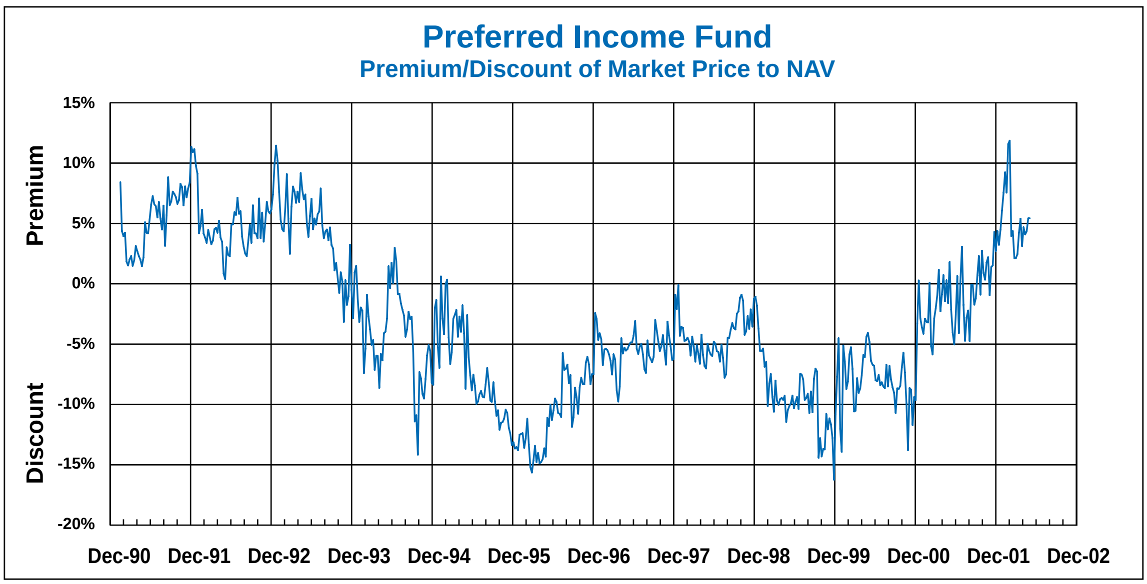
Remember that the Preferred Income Fund only purchases securities of companies that have senior debt rated investment grade by either Moody's or S&P or are of comparable quality. Beyond that, roughly 90% of the Fund's current portfolio is made up of issues that are themselves rated investment grade by at least one of the two agencies. In the current market environment, we think that the lower rated issues in the Fund's portfolio are more of an opportunity than a problem.

Like most investors, we have had a few unpleasant surprises; but the Fund has so far dodged the big bullets. We avoided direct hits from the California energy crisis, Enron and its nefarious colleagues, and the telecom disaster. Furthermore, the indirect exposure to these problems through our utility investments seems manageable. The only holding in the Fund's portfolio that is not up-to-date on its dividends is Farmland Industries, Inc., which recently filed for Chapter 11 bankruptcy. Fortunately, we had sold much of our holding of Farmland's preferred earlier. Our remaining shares of Farmland account for less than 2/10 of 1% of the current market value of the Fund's portfolio.

HOW DOES THE MARKET PRICE OF THE FUND'S SHARES COMPARE TO ITS NET ASSET VALUE?

The following chart shows the evolution of the market price of the Fund's shares from moderate discounts from net asset value last year to moderate premiums this year. This pattern is not unusual among income oriented closed-end funds (although we would naturally like to think that it is more deserved in the case of the Preferred Income Fund).

The emergence of the premium has naturally had a positive effect on returns based on the market price of the Fund's shares. The total returns on market were 6.1% for the first six months of fiscal 2002 and 14.4% for latest twelve months.



We would like to remind our shareholders that the Fund's Dividend Reinvestment Plan (the "DRIP") provides a means of acquiring additional shares of the Fund without paying the full market premium. When the market price is above NAV, DRIP participants reinvest their dividends in new shares acquired directly from the Fund at NAV. The only limitation is the IRS rule that the purchase can not be more than 5% below the market price. If the shares are selling at a discount from NAV, reinvestments are executed in the market to take advantage of the discount.

More information on the DRIP is available. If your shares are held in a brokerage account, ask your broker if his firm is set up to participate. If you hold your shares in certificate form, or if you would just like more information, call the DRIP's agent, PFPC Inc., at 1-800-331-1710.

FINANCIAL DATA

Per Share of Common Stock (Unaudited)

	Dividends Paid	Net Asset Value	NYSE Closing Price	Dividend Reinvestment Price (1)
December 31, 2001	**$0.1640**	$14.46	$14.70	$14.46
January 31, 2002	0.0820	14.40	15.20	14.77
February 28, 2002	0.0820	14.24	15.50	15.20
March 31, 2002	0.0820	14.14	14.44	14.14
April 30, 2002	0.0820	14.11	14.52	14.11
May 31, 2002	0.0820	13.99	14.75	13.99

(1) Whenever the net asset value per share of the Fund's common stock is less than or equal to the market price per share on the payment date, new shares issued will be valued at the higher of net asset value or 95% of the then current market price. Otherwise, the reinvestment shares of common stock will be purchased in the open market.

See Notes to Financial Statements.

Preferred Income Fund Incorporated

PORTFOLIO OF INVESTMENTS

May 31, 2002 (Unaudited)

Shares/$ Par		Value (Note 1)
	PREFERRED SECURITIES — 97.2%	
	ADJUSTABLE RATE PREFERRED SECURITIES — 14.4%	
	BANKING — 14.1%	
	Citigroup Inc.:	
85,250	Series R, Adj. Rate Pfd.	$ 2,077,969*
35,000	Series Q, Adj. Rate Pfd.	853,125*
75,000	Cobank, Adj. Rate Pfd., Pvt. 144A***	3,984,750*
	J.P. Morgan Chase & Co.:	
89,675	Series A, Adj. Rate Pfd.	7,174,000*
24,000	Series L, Adj. Rate Pfd.	2,172,000*
134,200	Series N, Adj. Rate Pfd.	3,027,887*
170,850	Wells Fargo & Company, Series B, Adj. Rate Pfd.	8,525,415*
	TOTAL BANKING ADJUSTABLE RATE PREFERRED SECURITIES	27,815,146
	FINANCIAL SERVICES — 0.3%	
10,500	Bear Stearns Companies, Inc., Series A, Adj. Rate Pfd.	483,000*
	TOTAL ADJUSTABLE RATE PREFERRED SECURITIES	28,298,146
	FIXED RATE PREFERRED SECURITIES — 81.7%	
	BANKING — 18.0%	
20,000	Abbey National Group, 7.375% Pfd., Series B	504,700
700	ABN AMRO North America, Inc., 6.46% Pfd., Pvt., 144A***	662,123*
	BancWest Corporation:	
$4,350,000	First Hawaiian Capital I, 8.343% 7/1/27 Capital Security, Series B	4,600,560
400	BancWest Capital I, 9.50% 12/01/30 QUIPS	10,992
	Bank of America Corporation,	
$ 500,000	NB Capital Trust II, 7.83% 12/15/26 Capital Security	523,285
	Citigroup Inc.:	
13,276	6.213% Pfd., Series G	616,272*
13,750	6.231% Pfd., Series H	643,981*
167,977	5.864% Pfd., Series M	7,403,586*
	Deutsche Bank,	
$1,000,000	BT Preferred Capital Trust II, 7.875% 2/25/27 Capital Security	$ 1,034,285
2,800	Firstar Realty LLC, 8.875% Pfd., REIT, Pvt., 144A***	3,105,018
	GreenPoint Financial Corporation,	
$3,320,000	GreenPoint Capital Trust I, 9.10% 6/1/27 Capital Security	3,364,422
	HSBC USA, Inc.:	
41,700	$2.8575 Pfd.	1,897,975*
$2,635,000	Republic New York Capital II, 7.53% 12/4/26 STOPS	2,624,855
$1,870,000	Keycorp Institutional Capital B, 8.25% 12/15/26 Capital Security	1,937,320
16,500	Regions Financial Trust I, 8.00% 2/28/31 Pfd.	434,527
	Wachovia Corporation:	
$1,750,000	First Union Institutional Capital II, 7.85% 1/1/27 Capital Security	1,825,233
$1,500,000	First Union Capital II, 7.95% 11/15/29 Capital Security	1,602,720
$2,500,000	First Union Institutional Capital I, 8.04% 12/1/26 Capital Security	2,631,538
	TOTAL BANKING FIXED RATE PREFERRED SECURITIES	35,423,392
	FINANCIAL SERVICES — 15.3%	
	Bear Stearns Companies, Inc.:	
201,340	5.49% Pfd., Series G	7,709,308*
13,790	5.72% Pfd., Series F	550,083*
	Household International, Inc.:	
2,860	5.00% Pfd.	95,510*
65,800	7.50% Pfd., Series 2001-A	1,620,654*
100,000	7.60% Pfd.	2,493,000*
10,000	$4.30 Pfd.	579,750*
	Lehman Brothers Holdings, Inc.:	
169,275	5.94% Pfd., Series C	7,040,147*
65,400	5.67% Pfd., Series D	2,597,034*
147,755	SLM Corporation, 6.97% Pfd. Series A	7,435,032*
	TOTAL FINANCIAL SERVICES FIXED RATE PREFERRED SECURITIES	30,120,518

See Notes to Financial Statements.

PORTFOLIO OF INVESTMENTS (Continued)

May 31, 2002 (Unaudited)

Shares/$ Par		Value (Note 1)
	PREFERRED SECURITIES (Continued)	
	FIXED RATE PREFERRED SECURITIES (Continued)	
	INSURANCE — 8.5%	
	AON Corporation,	
$3,120,000	AON Capital Trust A, 8.205% 1/1/27 Capital Security	$ 3,116,474
	Conseco, Inc.:	
29,350	Conseco Financing Trust V, 8.70% TOPrS	221,739
75,000	Conseco Financing Trust VI, 9.00% TOPrS	587,250
14,850	Conseco Financing Trust I, 9.16% TOPrS	116,350
1,250	Fortis Funding Trust, 7.68% Pfd., Pvt. 144A***	1,415,925*
21	Prudential Human Resources Management Company, Inc., 6.30% Sinking Fund Pfd. Series A, Pvt.	2,146,045*
	The St. Paul Companies, Inc.:	
$3,300,000	MMI Capital Trust I, 7.625% 12/15/27 Capital Security, Series B	3,093,255
12,000	St. Paul Capital Trust I, 7.60% Pfd.	294,300
	UnumProvident Corporation,	
$4,000,000	Provident Financing Trust I, 7.405% 3/15/38 Capital Security	3,780,280
2,000	Zurich Financial Reg Caps I, 6.01% Pfd., Pvt. 144A***	2,042,780*
	TOTAL INSURANCE FIXED RATE PREFERRED SECURITIES	16,814,398
	MISCELLANEOUS INDUSTRIES — 3.0%	
17,500	E.I. Du Pont de Nemours and Company, $4.50 Pfd., Series B	1,343,038*
36,200	Farmland Industries, Inc., 8.00% Pfd., Pvt., 144A***	461,369*†
23,250	Ocean Spray Cranberries, Inc., 6.25% Pfd., Pvt., 144A***	1,892,085*
26,000	Touch America Holdings, $6.875 Pfd.	1,637,220*
9,520	Viad Corporation, $4.75 Sinking Fund Pfd.	$ 552,350*
	TOTAL MISCELLANEOUS INDUSTRIES FIXED RATE PREFERRED SECURITIES	5,886,062
	OIL AND GAS — 3.4%	
11,200	Anadarko Petroleum Corporation, 5.46% Pfd.	989,352*
41,300	Apache Corporation, 5.68% Pfd., Series B	3,747,562*
1,860	EOG Resources, Inc., 7.195% Pfd., Series B	1,971,833*
	TOTAL OIL AND GAS FIXED RATE PREFERRED SECURITIES	6,708,747
	UTILITIES — 33.5%	
237,600	Alabama Power Company, 5.20% Pfd.	4,920,696*
16,000	Alabama Power Capital Trust I, 7.375% Pfd., TOPrS	401,040
19,700	Alabama Power Capital Trust II, 7.60% Pfd., TOPrS	496,243
	Appalachian Power Company:	
76,450	8.00% QUIDS, Series B	1,938,772
100	8.25% Pfd. QUIDS, Series A	2,545
25,000	Avista Corporation, $6.95 Sinking Fund Pfd., Series K	2,263,625*
	Baltimore Gas & Electric Company,	
22,675	6.99% Pfd., Series 1995	2,368,630*
26,000	BGE Capital Trust I, 7.16% TOPrS	647,920
10,000	Boston Edison Company, 4.78% Pfd.	729,650*
	Central Hudson Gas & Electric Corporation:	
5,000	4.35% Pfd., Series D, Pvt.	323,500*
750	4.96% Pfd., Series E, Pvt.	55,331*
10,000	Central Illinois Light Company, 4.64% Pfd.	658,600*
12,450	Columbus Southern Power Company, 7.92%, Jr. Sub. Debt., Series B	316,479

See Notes to Financial Statements.

PORTFOLIO OF INVESTMENTS (Continued)

May 31, 2002 (Unaudited)

Shares/$ Par		Value (Note 1)
	PREFERRED SECURITIES (Continued)	
	FIXED RATE PREFERRED SECURITIES (Continued)	
	UTILITIES (Continued)	
	Connecticut Light and Power Company:	
985	$2.06 Pfd.	$ 28,619*
5,323	$3.24 Pfd.	244,778*
2,000	4.50% Pfd.	63,470*
9,300	5.28% Pfd.	348,471*
200	6.56% Pfd., Series 1968	9,252*
6,870	Dayton Power and Light Company, 3.90% Pfd., Series C	400,349*
	Duke Energy Corporation:	
5,550	4.50% Pfd., Series C	384,504*
24,965	6.75% Pfd., Series X, Sinking Fund Pfd.	2,630,312*
519	7.04% Pfd., Series Y	54,700*
10,412	7.85% Pfd., Series S	1,089,147*
5,000	Energy East Capital Trust I, 8.25% TOPrS	126,250
	Entergy Arkansas, Inc.:	
2,800	7.32% Pfd.	255,472*
11,350	7.40% Pfd.	1,046,867*
1,147	7.88% Pfd.	110,663*
4,440	Entergy Gulf States, Inc., 7.56% Pfd.	404,551*
	Entergy Louisiana, Inc.:	
260	7.84% Pfd.	25,559*
106,138	8.00% Pfd., Series 92	2,661,410*
8,500	Entergy Mississippi, Inc., 7.44% Pfd.	788,077*
	Florida Power & Light Company:	
5,350	4.35% Pfd., Series E, Pvt.	342,935*
7,500	6.75% Pfd., Series U	768,450*
2,010	Great Plains Energy, Inc., 4.50% Pfd.	129,886*
5,000	Green Mountain Power Corporation, 7.32% Pfd., Series 1	443,325*
	Hawaiian Electric Company, Inc.,	
20,000	HECO Capital Trust I, 8.05% QUIPS	508,100
2,500	Idaho Power Co., 7.68% Pfd., Series 1	254,988*
10,000	Indiana Michigan Power Company, 8.00% Pfd., Series A, TOPrS	$ 249,500
27,150	Indianapolis Power & Light Company, 5.65% Pfd.	2,028,512*
5,874	Jersey Central Power & Light Company, 7.52% Sinking Fund Pfd., Series K	604,581*
4,500	Kentucky Utilities Company, 6.53% Pfd.	426,443*
22,000	Monongahela Power Company, $7.73 Pfd., Series L	2,293,830*
3,500	Northern Indiana Public Service Company, 7.44% Pfd.	360,028*
11,000	Northern States Power Company, NSP Financing I, 7.875% Pfd.	274,615
6,170	Ohio Edison Company, 4.44% Pfd.	410,891*
	Ohio Power Company:	
15,500	7.92% QUIDS, Series B	394,320
33,600	8.16% Pfd., Series A	855,624
	PECO Energy Company:	
5,000	$4.40 Pfd., Series C	321,675*
7,500	$7.48 Pfd.	784,163*
$1,050,000	Capital Trust III, $7.38 4/6/28, Capital Security, Series D	972,232
5,000	PPL Electric Utilities Corporation, 6.75% Pfd.	475,675*
9,410	PSI Energy, Inc., 4.32% Pfd.	153,101*
	PacifiCorp:	
1,225	$4.56 Pfd.	79,735*
6,468	$4.72 Pfd.	435,782*
3,000	$7.48 Sinking Fund Pfd.	309,360*
86,350	8.25% QUIPS	2,171,703
15,000	Portland General Electric, 7.75%, Sinking Fund Pfd.	1,262,025*
25,500	Public Service Company of Colorado, Capital Trust I, 7.60% TOPrS	632,528
10,000	Public Service Company of New Mexico, 4.58% Pfd., Pvt.	594,250*

See Notes to Financial Statements.

PORTFOLIO OF INVESTMENTS (Continued)

May 31, 2002 (Unaudited)

Shares/$ Par		Value (Note 1)
	PREFERRED SECURITIES (Continued)	
	FIXED RATE PREFERRED SECURITIES (Continued)	
	UTILITIES (Continued)	
	Public Service Enterprise Group, Inc.,	
10,800	Enterprise Capital Trust I,	
	7.44% TOPrS, Series A	$ 261,954
	Puget Sound Energy, Inc.:	
127,900	7.45% Pfd., Series II	3,191,105*
27,430	7.75% Sinking Fund Pfd.	2,709,261*
	Reliant Energy, Inc.:	
45,000	Houston Light & Power,	
	Capital Trust I,	
	8.125% QUIPS	965,700
$3,500,000	Houston Light & Power,	
	Capital Trust II,	
	8.257%, 2/1/37 Capital Security,	
	Series B	3,168,025
60,150	REI Trust I,	
	7.20% TOPrS, Series C	1,120,294
	Rochester Gas & Electric Corporation:	
4,984	4.10% Pfd., Series H	301,682*
10,000	4.55% Pfd. Series M, Pvt.	648,100*
25,000	San Diego Gas & Electric,	
	$1.70 Pfd	618,875*
	South Carolina Electric & Gas Company:	
25,864	5.125% Purchase Fund Pfd., Pvt.	1,033,913*
6,703	6.00% Purchase Fund Pfd., Pvt.	311,120*
	Southern Union Company,	
60,400	Southern Union Financing I,	
	9.48% TOPrS	1,542,314
	TXU US Holding Company,	
$ 750,000	TXU Electric Capital V,	
	8.175% 1/30/37 Capital Security	757,249
6,850	TransCanada PipeLines Ltd.,	
	8.25% Pfd.	177,175
	XCEL Energy, Inc.:	
16,030	$4.08 Pfd., Series B	$ 849,269*
26,200	$4.10 Pfd., Series C	1,394,757*
22,000	$4.11 Pfd., Series D	1,174,030*
17,750	$4.16 Pfd., Series E	958,766*
10,000	$4.56 Pfd., Series G	592,150*
	TOTAL UTILITIES FIXED RATE PREFERRED SECURITIES	66,109,478
	TOTAL FIXED RATE PREFERRED SECURITIES	161,062,595
	INVERSE FLOATING RATE PREFERRED — 1.1%	
18	Premium Assets, Series A,	
	Zurich Financial Reg Caps	2,151,472*
	TOTAL PREFERRED SECURITIES	
	(Cost $187,579,264)	191,512,213
	DEBT SECURITIES — 0.5%	
36,200	Ohio Power Company,	
	7.375% Sr. Notes	897,036
5,000	Telephone & Data Systems, Inc.,	
	7.60% Sr. Unsecured Notes,	
	Series A	124,150
	TOTAL DEBT SECURITIES	
	(Cost $996,325)	1,021,186
	OPTION CONTRACTS — 0.3% (Cost $1,235,714)	
1,209	Put Options on U.S. Treasury	
	Bond Futures,	
	Expiring 08/24/2002	681,938

See Notes to Financial Statements.

Preferred Income Fund Incorporated

PORTFOLIO OF INVESTMENTS (Continued)

May 31, 2002 (Unaudited)

Shares/$ Par			Value (Note 1)
MONEY MARKET FUNDS — 1.5% (Cost $2,860,300)			
$2,860,300	Provident TempFund, 1.81%		$ 2,860,300
TOTAL INVESTMENTS (Cost $192,671,603**)		99.5%	196,075,637
OTHER ASSETS AND LIABILITIES (Net)		0.5	962,634
TOTAL NET ASSETS		100.0%	$197,038,271

* Securities eligible for the Dividends Received Deduction.

** Aggregate cost of securities held.

*** Securities exempt from registration under Rule 144A of the Securities Act of 1933. These securities may by resold in transactions exempt from registration to qualified institutional buyers.

† Non-income producing.

ABBREVIATIONS (Note 6):

CorTS — Corporate Backed Trust Securities
QUIDS — Quarterly Income Debt Securities
QUIPS — Quarterly Income Preferred Securities
STOPS — Semi-Annual Trust Originated Pass Through Securities
TIPS — Trust Issued Preferred Securities
TOPrS — Trust Originated Preferred Securities
Pfd. — Preferred securities
Pvt. — Private placement securities

Capital Securities are treated as debt instruments for financial statement purposes and the amounts shown in the Shares/$ Par column are dollar amounts of par value.

See Notes to Financial Statements.

STATEMENT OF ASSETS AND LIABILITIES

May 31, 2002 (Unaudited)

ASSETS:		
Investments, at value (Cost $192,671,603) (Note 1) See accompanying schedule		$196,075,638
Dividends and interest receivable		1,366,202
Prepaid expenses		150,525
Total Assets		197,592,365
LIABILITIES:		
Dividends payable to Common Shareholders	$152,322	
Investment advisory fee payable (Note 2)	94,191	
Professional fees payable	22,915	
Accrued expenses and other payables	86,661	
Cost of New Securities Issuance (Note 9)	198,005	
Accumulated undeclared distributions to Money Market Cumulative Preferred™ Stock (Note 5)	147,547	
Total Liabilities		701,641
Money Market Cumulative Preferred™ Stock (575 shares outstanding) redemption value (Notes 5 and 9)		57,500,000
NET ASSETS AVAILABLE TO COMMON STOCK		$139,390,724
NET ASSETS AVAILABLE TO COMMON STOCK consist of:		
Undistributed net investment income (Note 1)		$ 282,778
Accumulated net realized loss on investments sold (Note 1)		(7,721,518)
Unrealized appreciation on investments (Note 3)		3,404,034
Par value of Common Stock		99,650
Paid-in capital in excess of par value of Common Stock		143,325,780
Total Net Assets Available to Common Stock		$139,390,724
NET ASSET VALUE PER SHARE OF COMMON STOCK:		
Common Stock (9,964,988 shares outstanding)		$ 13.99

See Notes to Financial Statements.

Preferred Income Fund Incorporated

STATEMENT OF OPERATIONS

For the Six Months Ended May 31, 2002 (Unaudited)

INVESTMENT INCOME:		
Dividends		$ 5,397,907
Interest		1,681,462
Total Investment Income		7,079,369
EXPENSES:		
Investment advisory fee (Note 2)	$558,869	
Administration fee (Note 2)	99,308	
Money Market Cumulative Preferred™ broker commissions and Auction Agent fees	84,976	
Insurance expense	73,419	
Legal and audit fees	60,372	
Directors' fees and expenses (Note 2)	36,078	
Shareholder servicing agent fees and expenses (Note 2)	37,351	
Custodian fees and expenses (Note 2)	14,595	
Other	25,707	
Total Expenses		990,675
NET INVESTMENT INCOME		6,088,694
REALIZED AND UNREALIZED LOSS ON INVESTMENTS (Notes 1 and 3):		
Net realized loss on investments sold during the period		(748,536)
Change in net unrealized depreciation of investments during the period		(5,177,578)
NET REALIZED AND UNREALIZED LOSS ON INVESTMENTS		(5,926,114)
DISTRIBUTIONS TO MONEY MARKET CUMULATIVE PREFERRED™ STOCK SHAREHOLDERS (Note 5):		
From net investment income (including changes in accumulated undeclared distributions)		(494,600)
NET DECREASE IN NET ASSETS TO COMMON STOCK RESULTING FROM OPERATIONS		$ (332,020)

See Notes to Financial Statements.

STATEMENT OF CHANGES IN NET ASSETS

	Six Months Ended May 31, 2002 (Unaudited)	Year Ended November 30, 2001
OPERATIONS:		
Net investment income	$ 6,088,694	$ 12,196,515
Net realized loss on investments sold during the period	(748,536)	(1,300,809)
Change in net unrealized (depreciation) appreciation of investments during the period	(5,177,578)	12,993,581
Distributions to Money Market Cumulative Preferred™ Stock Shareholders from net investment income, including changes in accumulated undeclared distributions (Note 5)	(494,600)	(2,250,954)
Net (decrease) increase in net assets available to common stock resulting from operations	(332,020)	21,638,333
DISTRIBUTIONS:		
Dividends paid from net investment income to Common Stock Shareholders	(5,700,792)	(9,703,430)
Distributions paid from net realized capital gains to Common Stock Shareholders	—	—
FUND SHARE TRANSACTIONS:		
Increase from Common Stock transactions (Note 4)	983,873	823,227
Decrease due to Money Market Cumulative Preferred™ Stock transactions (Note 9)	(210,000)	—
NET (DECREASE) INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK FOR THE PERIOD	(5,258,939)	12,758,130
NET ASSETS AVAILABLE TO COMMON STOCK:		
Beginning of period	144,649,663	131,891,533
End of period (including undistributed net investment income of $282,778 and $389,476, respectively)	$139,390,724	$144,649,663

See Notes to Financial Statements.

Preferred Income Fund Incorporated

FINANCIAL HIGHLIGHTS

For a Common share outstanding throughout each period.

Contained below is per share operating performance data, total investment returns, ratios to average net assets and other supplemental data. This information has been derived from information provided in the financial statements and market price data for the Fund's shares.

	Six Months Ended May 31, 2002 (Unaudited)	Year Ended November 30,				
		2001	2000	1999	1998	1997
PER SHARE OPERATING PERFORMANCE:						
Net asset value, beginning of period	$ 14.62	$ 13.41	$ 14.41	$ 16.43	$ 16.71	$ 16.50
INVESTMENT OPERATIONS:						
Net investment income	0.61	1.23	1.32	1.29	1.28	1.29
Net realized and unrealized gain/(loss) on investments	(0.60)	1.19	(0.56)	(1.35)	0.05	1.00
DISTRIBUTIONS TO MMP* SHAREHOLDERS:						
From net investment income	(0.05)†	(0.23)†	(0.29)†	(0.23)†	(0.19)	(0.22)
From net realized capital gains	—	—	(0.01)	(0.08)	(0.07)	(0.06)
Total from investment operations	(0.04)	2.19	0.46	(0.37)	1.07	2.01
Cost of Issuance of Additional MMP*	(0.02)	—	—	—	—	—
DISTRIBUTIONS TO COMMON SHAREHOLDERS:						
From net investment income	(0.57)	(0.98)	(1.04)	(1.12)	(1.05)	(1.15)
From net realized capital gains	—	—	(0.42)	(0.53)	(0.30)	(0.65)
Total distributions to Common Shareholders	(0.57)	(0.98)	(1.46)	(1.65)	(1.35)	(1.80)
Net asset value, end of period	$ 13.99 †	$ 14.62 †	$ 13.41 †	$ 14.41 †	$ 16.43	$ 16.71
Market value, end of period	$ 14.75	$ 14.47	$ 12.125	$ 12.75	$ 15.938	$ 16.188
Total investment return based on net asset value**	(0.44)%	17.01%	4.55%	(1.81)%	6.91%	13.65%
Total investment return based on market value**	6.05%	28.02%	6.88%	(10.43)%	7.05%	17.20%
RATIOS TO AVERAGE NET ASSETS AVAILABLE TO COMMON STOCK SHAREHOLDERS:						
Operating expenses	1.40%	1.42%	1.41%	1.37%	1.32%	1.34%
Net investment income***	7.92%	7.21%	7.58%	6.66%	6.13%	6.22%
SUPPLEMENTAL DATA:††						
Portfolio turnover rate	15%	39%	66%	65%	87%	74%
Total net assets, end of period (in 000's)	$197,038	$202,412	$189,983	$199,863	$219,398	$221,990
Ratio of operating expenses to total average net assets	1.00%	1.00%	0.98%	0.99%	0.97%	0.99%

* Money Market Cumulative Preferred™ Stock.
** Assumes reinvestment of distributions at the price obtained by the Fund's Dividend Reinvestment Plan.
*** The net investment income ratios reflect income net of operating expenses and payments to MMP* Shareholders.
† Includes effect of additional distribution available to MMP* Shareholders ($0.00 per Common Share at May 2002, $0.02 per Common Share at November 2001, $0.03 per Common Share at November 2000 and $0.05 per Common Share at November 1999). (See Note 5 to the Financial Statements.)
†† Information presented under heading Supplemental Data includes MMP*.

See Notes to Financial Statements.

FINANCIAL HIGHLIGHTS (Continued)

The table below sets out information with respect to Money Market Cumulative Preferred™ Stock currently outstanding.

	Total Shares Outstanding (2)	Asset Coverage Per Share	Involuntary Liquidating Preference Per Share (1)	Average Market Value Per Share (1) & (2)
05/31/02*	575	$342,675	$100,000	$100,000
11/30/01	575	352,021	100,000	100,000
11/30/00	575	330,404	100,000	100,000
11/30/99	575	347,588	100,000	100,000
11/30/98	575	381,562	100,000	100,000
11/30/97	575	386,070	100,000	100,000

(1) Excludes accumulated undeclared dividends.
(2) See Notes 5 and 9.
* Unaudited.

See Notes to Financial Statements.

NOTES TO FINANCIAL STATEMENTS (Unaudited)

1. Significant Accounting Policies

Preferred Income Fund Incorporated (the "Fund") is a diversified, closed-end management investment company organized as a Maryland corporation and is registered with the Securities and Exchange Commission ("SEC") under the Investment Company Act of 1940, as amended. The policies described below are followed consistently by the Fund in the preparation of its financial statements in conformity with accounting principles generally accepted in the United States of America.

Portfolio valuation: The net asset value of the Fund's Common Stock is determined by the Fund's Administrator no less frequently than on the last business day of each week and month. It is determined by dividing the value of the Fund's net assets attributable to common shares by the number of shares of Common Stock outstanding. The value of the Fund's net assets attributable to common shares is deemed to equal the value of the Fund's total assets less (i) the Fund's liabilities, (ii) the aggregate liquidation value of the outstanding Money Market Cumulative Preferred™ Stock, and (iii) accumulated and unpaid dividends on the outstanding Money Market Cumulative Preferred™ Stock.

Securities listed on a national securities exchange are valued on the basis of the last sale on such exchange on the day of valuation, except as described hereafter. In the absence of sales of listed securities and with respect to (a) securities for which the most recent sale prices are not deemed to represent fair market value and (b) unlisted securities (other than money market instruments), securities are valued at the mean between the closing bid and asked prices when quoted prices for investments are readily available. Investments in over-the-counter derivative instruments, such as interest rate swaps and options thereon ("swaptions") are valued at the prices obtained from the broker/dealer or bank that is the counterparty to such instrument, subject to comparison of such valuation with a valuation obtained from a broker/dealer or bank that is not a counterparty to the particular derivative instrument. Investments for which market quotations are not readily available or for which management determines that the prices are not reflective of current market conditions are valued at fair value as determined in good faith by or under the direction of the Board of Directors of the Fund, including reference to valuations of other securities which are comparable in quality, maturity and type. Investments in money market instruments, which mature in 60 days or less, are valued at amortized cost. Investments in Money Market Funds are valued at the net asset value of such funds.

Securities transactions and investment income: Securities transactions are recorded as of the trade date. Realized gains and losses from securities sold are recorded on the identified cost basis. Dividend income is recorded on ex-dividend dates. Interest income is recorded on the accrual basis.

As required, effective December 1, 2001, the Fund has adopted the provisions of the AICPA Audit and Accounting Guide, *Audits of Investment Companies* which require that the Fund amortize premium and accrete discount on all fixed-income securities which trade and are quoted on an "accrued interest" basis. Prior to December 1, 2001, the Fund did not amortize premium and accrete discounts for these securities. Adopting these accounting principles will not affect the Fund's net asset value, but will change the classification of certain amounts between interest income and realized and unrealized

NOTES TO FINANCIAL STATEMENTS (Unaudited) (Continued)

gain/loss in the statement of operations and will change the classification of certain of the components of capital in the statement of assets and liabilities. The adoption of this principle is not material to the financial statements.

At November 30, 2001	For the Six Months Ended May 31, 2002		
Change in Amortized Cost of Securities Held	Change in Undistributed Net Investment Income	Change in Accumulated Net Realized Gain	Change in Net Unrealized Appreciation of Investments
$(76,921)	$(7,536)	$10,498	$(2,962)

Options: Upon the purchase of an option by the Fund, the total purchase price paid is recorded as an investment. The market valuation is determined as set forth in the preceding portfolio valuation section. When the Fund enters into a closing sale transaction, the Fund will record a gain or loss depending on the difference between the purchase and sale price. The risks associated with purchasing options and the maximum loss the Fund would incur are limited to the purchase price originally paid.

Repurchase agreements: The Fund may engage in repurchase agreement transactions. The Fund's Investment Adviser reviews and approves the eligibility of the banks and dealers with which the Fund may enter into repurchase agreement transactions. The value of the collateral underlying such transactions is at least equal at all times to the total amount of the repurchase obligations, including interest. The Fund maintains possession of the collateral through its custodian and, in the event of counterparty default, the Fund has the right to use the collateral to offset losses incurred. There is the possibility of loss to the Fund in the event the Fund is delayed or prevented from exercising its rights to dispose of the collateral securities.

Dividends and distributions to shareholders: The Fund expects to declare dividends on a monthly basis to shareholders of Common Stock. The shareholders of Money Market Cumulative Preferred™ Stock are entitled to receive cumulative cash dividends as declared by the Fund's Board of Directors. Distributions to shareholders are recorded on the ex-dividend date. Any net realized short-term capital gains will be distributed to shareholders at least annually. Any net realized long-term capital gains may be distributed to shareholders at least annually or may be retained by the Fund as determined by the Fund's Board of Directors. Capital gains retained by the Fund are subject to tax at the capital gains corporate tax rate. Subject to the Fund qualifying as a regulated investment company, any taxes paid by the Fund on such net realized long-term gains may be used by the Fund's shareholders as a credit against their own tax liabilities.

Federal income taxes: The Fund intends to continue to qualify as a regulated investment company by complying with the requirements under subchapter M of the Internal Revenue Code of 1986, as amended, applicable to regulated investment companies and intends to distribute substantially all of its taxable net investment income to its shareholders. Therefore, no Federal income tax provision is required.

NOTES TO FINANCIAL STATEMENTS (Unaudited) (Continued)

Income and capital gain distributions are determined and characterized in accordance with income tax regulations which may differ from generally accepted accounting principles. These differences are primarily due to (1) differing treatments of income and gains on various investment securities held by the Fund, including timing differences, (2) the attribution of expenses against certain components of taxable investment income, and (3) federal regulations requiring proportional allocation of income and gains to all classes of shareholders.

The Internal Revenue Code of 1986, as amended, imposes a 4% nondeductible excise tax on the Fund to the extent the Fund does not distribute by the end of any calendar year at least (1) 98% of the sum of its net investment income for that year and its capital gains (both long term and short term) for its fiscal year and (2) certain undistributed amounts from previous years.

Other: The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from those estimates.

2. Investment Advisory Fee, Directors' Fees, Administration Fee and Transfer Agent Fee

Flaherty & Crumrine Incorporated (the "Adviser") serves as the Fund's Investment Adviser. The Fund pays the Adviser a monthly fee at an annual rate of 0.625% of the value of the Fund's average monthly net assets up to $100 million and 0.50% of the value of the Fund's average monthly net assets in excess of $100 million.

The Fund currently pays each Director who is not a director, officer or employee of the Adviser a fee of $9,000 per annum, plus $500 for each in-person meeting of the Board of Directors or any committee and $100 for each telephone meeting. In addition, the Fund will reimburse all Directors for travel and out-of-pocket expenses incurred in connection with such meetings.

PFPC Inc., a member of The PNC Financial Services Group, Inc. ("PNC Financial Services"), serves as the Fund's Administrator and Transfer Agent. As Administrator, PFPC Inc. calculates the net asset value of the Fund's shares and generally assists in all aspects of the Fund's administration and operation. As compensation for PFPC Inc.'s services as Administrator, the Fund pays PFPC Inc. a monthly fee at an annual rate of 0.10% of the Fund's average monthly net assets. PFPC Inc. also serves as the Fund's Common Stock servicing agent (transfer agent), dividend-paying agent and registrar and, as compensation for PFPC Inc.'s services as such, the Fund pays PFPC Inc. a fee at an annual rate of 0.02% of the Fund's average monthly net assets plus certain out-of-pocket expenses.

PFPC Trust Company ("PFPC Trust") serves as the Fund's Custodian. PFPC Trust is an indirect subsidiary of PNC Financial Services. As compensation for PFPC Trust's services as Custodian, the Fund pays PFPC Trust a monthly fee at the annual rate of 0.01% of the Fund's average monthly net assets.

3. Purchase and Sales of Securities

Cost of purchases and proceeds from sales of securities for the period ended May 31, 2002, excluding short-term investments, aggregated $34,117,526 and $29,665,965, respectively.

At May 31, 2002, aggregate gross unrealized appreciation for all securities in which there is an excess of value over tax cost was $8,756,195 and aggregate gross unrealized depreciation for all securities in which there is an excess of tax cost over value was $5,352,161.

4. Common Stock

At May 31, 2002, 240,000,000 shares of $0.01 par value Common Stock were authorized.

Common Stock transactions were as follows:

	Six Months Ended 5/31/02	
	Shares	**Amount**
Issued as reinvestment of dividends under the Dividend Reinvestment and Cash Purchase Plan	68,000	$983,873

5. Money Market Cumulative Preferred™ Stock

The Fund's Articles of Incorporation authorize the issuance of up to 10,000,000 shares of $0.01 par value preferred stock. The Money Market Cumulative Preferred™ Stock is senior to the Common Stock and results in the financial leveraging of the Common Stock. Such leveraging tends to magnify both the risks and opportunities to Common Stock shareholders. Dividends on shares of Money Market Cumulative Preferred™ Stock are cumulative.

The Fund is required to meet certain asset coverage tests with respect to the Money Market Cumulative Preferred™ Stock. If the Fund fails to meet these requirements and does not correct such failure, the Fund may be required to redeem, in part or in full, Money Market Cumulative Preferred™ Stock at a redemption price of $100,000 per share plus an amount equal to the accumulated and unpaid dividends on such shares in order to meet these requirements. Additionally, failure to meet the foregoing asset requirements could restrict the Fund's ability to pay dividends to Common Stock shareholders and could lead to sales of portfolio securities at inopportune times.

Under Emerging Issues Task Force (EITF) promulgating Topic D-98, *Classification and Measurement of Redeemable Securities,* which was issued on July 19, 2001, preferred securities that are redeemable for cash or other assets are to be classified outside of permanent equity to the extent that the redemption is at a fixed or determinable price and at the option of the holder or upon the occurrence of an event that is not solely within the control of the issuer. Subject to the guidance of the EITF, the Fund's Money Market Cumulative Preferred™ Stock, which was previously classified as a

NOTES TO FINANCIAL STATEMENTS (Unaudited) (Continued)

component of net assets, has been reclassified outside of permanent equity (net assets available to common stock) in the accompanying financial statements. Prior year amounts have also been reclassified to conform with this presentation. The impact of this reclassification creates no change to the net assets available to common shareholders.

If the Fund allocates any net gains or income ineligible for the Dividends Received Deduction to shares of the Money Market Cumulative Preferred™ Stock, the Fund is required to make additional distributions to Money Market Cumulative Preferred™ Stock shareholders or to pay a higher dividend rate in amounts needed to provide a return, net of tax, equal to the return had such originally paid distributions been eligible for the Dividends Received Deduction. Prior to November 30, 1999, additional distributions were not reported as available to Money Market Cumulative Preferred™ Stock until declared by the Fund's Board of Directors. The amount of additional distributions payable for any year may be highly uncertain and will not be known until after a fiscal year has been completed.

An auction of the Money Market Cumulative Preferred™ Stock is generally held every 49 days. Existing shareholders may submit an order to hold, bid or sell such shares at par value on each auction date. Money Market Cumulative Preferred™ Stock shareholders may also trade shares in the secondary market between auction dates.

At May 31, 2002, 575 shares of Money Market Cumulative Preferred™ Stock were outstanding at the annual rate of 1.64 %. (See Note 9 – "Subsequent Events.") The dividend rate, as set by the auction process, is generally expected to vary with short-term interest rates. These rates may vary in a manner unrelated to the income received on the Fund's assets, which could have either a beneficial or detrimental impact on net investment income and gains available to Common Stock shareholders. While the Fund expects to structure its portfolio holdings and hedging transactions to lessen such risks to Common Stock shareholders, there can be no assurance that such results will be attained.

6. Portfolio Investments, Concentration and Investment Quality

The Fund invests primarily in traditional DRD-eligible preferred securities (i.e., adjustable rate, fixed rate, and inverse floating rate preferred and preference stocks) and similar hybrid, i.e., fully taxable, preferred securities. Under normal market conditions, at least 80% of the value of the Fund's net assets will be invested in preferred securities. Also, under normal market conditions, the Fund invests at least 25% of its assets in securities issued by utilities and at least 25% of its assets in securities issued by companies in the banking industry. The Fund's portfolio may therefore be subject to greater risk and market fluctuation than a portfolio of securities representing a broader range of investment alternatives. The risks could adversely affect the ability and inclination of companies in these industries to declare and pay dividends or interest and the ability of holders of securities of such companies to realize any value from the assets of the issuer upon liquidation or bankruptcy.

NOTES TO FINANCIAL STATEMENTS (Unaudited) (Continued)

The Fund may invest up to 25% of its assets in holdings of securities rated below investment grade. These securities must be rated at least either “Ba3” by Moody’s Investors Service, Inc. or “BB-” by Standard & Poor’s or judged to be comparable in quality, in either case at the time of purchase; however, these securities must be issued by an issuer having a class of senior debt rated investment grade outstanding. This percentage limitation was raised from 15% by the Fund’s Board of Directors at its regular board meeting on April 19, 2002.

The Fund may invest up to 15% of its assets in common stocks and, under normal market conditions, up to 20% of its assets in debt securities. Certain of its investments in hybrid, i.e., fully taxable, preferred securities, such as TOPrS, TIPS, QUIPS, MIPS, QUIDS, QUICS, QIB’s, STOPS, CorTS, Capital Securities, and other similar or related investments, will be subject to the foregoing 20% limitation to the extent that, in the opinion of the Fund’s investment adviser, such investments are deemed to be debt-like in key characteristics. Typically, a security will not be considered debt-like (a) if an issuer can defer payment of income for eighteen months or more without triggering an event of default and (b) if such issue is a junior and fully subordinated liability of an issuer or its ultimate guarantor.

7. Special Investment Techniques

The Fund may employ certain investment techniques in accordance with its fundamental investment policies. These may include the use of when-issued and delayed delivery transactions. Securities purchased or sold on a when-issued or delayed delivery basis may be settled within 45 days after the date of the transaction. Such transactions may expose the Fund to credit and market valuation risk greater than that associated with regular trade settlement procedures. The Fund may also enter into transactions, in accordance with its fundamental investment policies, involving any or all of the following: lending of portfolio securities, short sales of securities, futures contracts, interest rate swaps, options on futures contracts, options on securities and swaptions. As in the case of when-issued securities, the use of over-the-counter derivatives, such as interest rate swaps and swaptions, may expose the Fund to greater credit, operations, and market value risk than is the case with regulated, exchange traded futures and options. With the exception of purchasing securities on a when-issued or delayed delivery basis or lending portfolio securities, these transactions are used for hedging or other appropriate risk-management purposes or, under certain other circumstances, to increase income. As of May 31, 2002, the Fund owned put options on U.S. Treasury bond futures contracts. No assurance can be given that such transactions will achieve their desired purposes or will result in an overall reduction of risk to the Fund.

8. Significant Shareholders

At May 31, 2002, the Commerce Group, Inc. and its affiliates owned approximately 29.9% of the Fund’s outstanding Common Stock, according to the Commerce Group, Inc. annual report to the Securities and Exchange Commission on Form 10-K for 2001.

NOTES TO FINANCIAL STATEMENTS (Unaudited) (Continued)

9. Subsequent Events

On June 4, 2002, the Fund issued 225 shares of additional Money Market Cumulative Preferred™ Stock with an initial dividend rate equal to 1.64%. These newly issued shares are identical to the previously outstanding 575 shares in all respects on and after their first auction date, which was June 5, 2002. Consequently, the Fund now has 800 shares of Money Market Cumulative Preferred™ Stock outstanding in one series, which represents a par value of $80 million.

The newly issued shares were underwritten by Lehman Brothers Inc. The underwriter's discount of 1.25% of the $22.5 million newly issued face value totaled $281,250 and was immediately charged to common equity capital upon completion of the offering.

Costs of the issue, including legal, printing, registration, rating fees, etc. were estimated at $210,000, all of which had been charged against common equity capital as of May 31, 2002, since substantially all of the costs had been incurred by that date.

ADDITIONAL INFORMATION (Unaudited)

Dividend Reinvestment and Cash Purchase Plan

Under the Fund's Dividend Reinvestment and Cash Purchase Plan (the "Plan"), a shareholder whose Common Stock is registered in his own name will have all distributions reinvested automatically by PFPC Inc. as agent under the Plan, unless the shareholder elects to receive cash. Distributions with respect to shares registered in the name of a broker-dealer or other nominee (that is, in "street name") may be reinvested by the broker or nominee in additional shares under the Plan, but only if the service is provided by the broker or nominee, unless the shareholder elects to receive distributions in cash. A shareholder who holds Common Stock registered in the name of a broker or other nominee may not be able to transfer the Common Stock to another broker or nominee and continue to participate in the Plan. Investors who own Common Stock registered in street name should consult their broker or nominee for details regarding reinvestment.

The number of shares of Common Stock distributed to participants in the Plan in lieu of a cash dividend is determined in the following manner. Whenever the market price per share of the Fund's Common Stock is equal to or exceeds the net asset value per share on the valuation date, participants in the Plan will be issued new shares valued at the higher of net asset value or 95% of the then current market value. Otherwise, PFPC Inc. will buy shares of the Fund's Common Stock in the open market, on the New York Stock Exchange or elsewhere, on or shortly after the payment date of the dividend or distribution and continuing until the ex-dividend date of the Fund's next distribution to holders of the Common Stock or until it has expended for such purchases all of the cash that would otherwise be payable to the participants. The number of purchased shares that will then be credited to the participants' accounts will be based on the average per share purchase price of the shares so purchased, including brokerage commissions. If PFPC Inc. commences purchases in the open market and the then current market price of the shares (plus any estimated brokerage commissions) subsequently exceeds their net asset value most recently determined before the completion of the purchases, PFPC Inc. will attempt to terminate purchases in the open market and cause the Fund to issue the remaining dividend or distribution in shares. In this case, the number of shares received by the participant will be based on the weighted average of prices paid for shares purchased in the open market and the price at which the Fund issues the remaining shares. These remaining shares will be issued by the Fund at the higher of net asset value or 95% of the then current market value.

Plan participants are not subject to any charge for reinvesting dividends or capital gains distributions. Each Plan participant will, however, bear a proportionate share of brokerage commissions incurred with respect to PFPC Inc.'s open market purchases in connection with the reinvestment of dividends or capital gains distributions. For the period ended May 31, 2002, $186 in brokerage commissions were incurred.

The automatic reinvestment of dividends and capital gains distributions will not relieve Plan participants of any income tax that may be payable on the dividends or capital gains distributions. A participant in the Plan will be treated for Federal income tax purposes as having received, on the dividend

ADDITIONAL INFORMATION (Unaudited) (Continued)

payment date, a dividend or distribution in an amount equal to the cash that the participant could have received instead of shares.

In addition to acquiring shares of Common Stock through the reinvestment of cash dividends and distributions, a shareholder may invest any further amounts from $100 to $3,000 semi-annually at the then current market price in shares purchased through the Plan. Such semi-annual investments are subject to any brokerage commission charges incurred.

A shareholder whose Common Stock is registered in his or her own name may terminate participation in the Plan at any time by notifying PFPC Inc. in writing, by completing the form on the back of the Plan account statement and forwarding it to PFPC Inc. or by calling PFPC Inc. directly. A termination will be effective immediately if notice is received by PFPC Inc. not less than 10 days before any dividend or distribution record date. Otherwise, the termination will be effective, and only with respect to any subsequent dividends or distributions, on the first day after the dividend or distribution has been credited to the participant's account in additional shares of the Fund. Upon termination and according to a participant's instructions, PFPC Inc. will either (a) issue certificates for the whole shares credited to the shareholder's Plan account and a check representing any fractional shares or (b) sell the shares in the market. Shareholders who hold Common Stock registered in the name of a broker or other nominee should consult their broker or nominee to terminate participation.

The Plan is described in more detail in the Fund's Plan brochure. Information concerning the Plan may be obtained from PFPC Inc. at 1-800-331-1710.

ADDITIONAL INFORMATION (Unaudited) (Continued)

Meeting of Shareholders

On April 19, 2002, the Fund held its Annual Meeting of Shareholders (the "Meeting") to (1) elect two Directors of the Fund ("Proposal 1"), and (2) ratify the selection of KPMG LLP as independent auditors for the Fund for the fiscal year ending November 30, 2002 ("Proposal 2"). The results of each proposal are as follows:

Proposal 1: Election of Directors.

Name	For	Withheld
Common Stock		
Martin Brody	9,205,288	92,603
David Gale	9,218,069	79,822

Donald F. Crumrine, Robert T. Flaherty, Morgan Gust and Robert F. Wulf continue to serve in their capacities as Directors of the Fund.

Proposal 2: Ratify the selection of KPMG LLP as independent auditors.

	For	Against	Abstained
Common Stock and Preferred Stock (voting together as a single class)			
Voted	9,170,663	39,658	87,869

Directors

Martin Brody
Donald F. Crumrine, CFA
Robert T. Flaherty, CFA
David Gale
Morgan Gust
Robert F. Wulf, CFA

Officers

Robert T. Flaherty, CFA
Chairman of the Board
and President
Donald F. Crumrine, CFA
Vice President
and Secretary
Robert M. Ettinger, CFA
Vice President
Peter C. Stimes, CFA
Vice President
and Treasurer

Investment Adviser

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

Questions concerning your shares of Preferred Income Fund?

- If your shares are held in a Brokerage Account, contact your Broker.
- 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.

Preferred Income Fund

Semi-Annual Report

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web site: www.preferredincome.com