

## FLAHERTY & CRUMRINE PREFERRED INCOME FUND

To the Shareholders of the Flaherty & Crumrine Preferred Income Fund (“PFD”):

During the Fund’s first fiscal quarter ended February 28, 2007, the Fund performed well in choppy, but ultimately little-changed, fixed-income markets by earning a total return of 1.7% on its net asset value (NAV). These three months saw the Fund continue its recent strong performance.

Interest rates were unchanged to slightly higher over the quarter, as the Federal Reserve left the federal funds rate unchanged and long-term Treasury rates rose only slightly. Corporate credit spreads also ended the quarter little changed, while the Fund’s interest-rate hedge had only a minimal impact. Both the recent quarter and trailing twelve-month periods delivered what the Fund is intended to produce – current income and stability of principal.

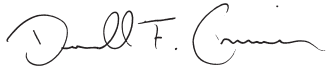
As you can see on the following pages detailing actual holdings in the Fund’s portfolio, the Fund invests in a relatively small number of industries, including utilities and insurers, banks and other finance companies. In fact, the Fund has an investment mandate to concentrate at least 25% of its assets in each of the banking and utilities industries. In terms of the industries the Fund’s assets are in, its portfolio is no different than the overall preferred securities market. Because of the preferred securities market’s overall emphasis in financial services, a portfolio of preferred securities, including the Fund’s, can be at risk if the U.S. economy goes into recession.

One important area of recent concern for the U.S. economy in general, and U.S. credit markets in particular, is subprime mortgage lending, which has experienced increasing default and delinquency rates in recent months. The numbers here are large in an absolute sense, but they are small relative to a \$13 trillion U.S. economy and to the mortgage market as a whole. Because of this, while we cannot entirely rule it out, we currently do not believe that problems in subprime mortgages will push the economy into recession.

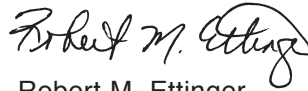
The Fund holds no positions in securities issued by mortgage brokers or subprime specialty lenders. Nonetheless, many of the banks and insurance companies in which we have invested do have some exposure to subprime mortgages in their lending or investment portfolios. While we are examining these companies very closely, the lack of detailed disclosure about subprime mortgages makes it impossible for us to make definitive statements about the Fund’s potential exposure to the problem. However, given what we now know and can infer about the companies in which we invest, we expect that *earnings* (which flow to the companies’ common shareholders) will be reduced at some of the companies we hold as a result of the problems in subprime lending. However, we currently do not expect that they will suffer losses large enough to cut meaningfully into *capital* (which support the debt and preferred securities owned by the Fund). Although we cannot rule out the possibility – despite our best judgment to the contrary – that some of the Fund’s investments could be seriously affected, we do not currently see any serious subprime credit problems in the holdings of the Fund.

The Fund's website at [www.preferredincome.com](http://www.preferredincome.com) has more information about Fund performance and a more complete discussion of the state of the economy (in our First Quarter Economic Update) and of subprime mortgages and their potential impact on the economy and the Fund's portfolio (in the "Frequently Asked Questions" section). We encourage you to explore the website for a wide range of additional information about your Fund.

Sincerely,



Donald F. Crumrine  
Chairman of the Board



Robert M. Ettinger  
President

April 20, 2007

**PORTFOLIO OVERVIEW**

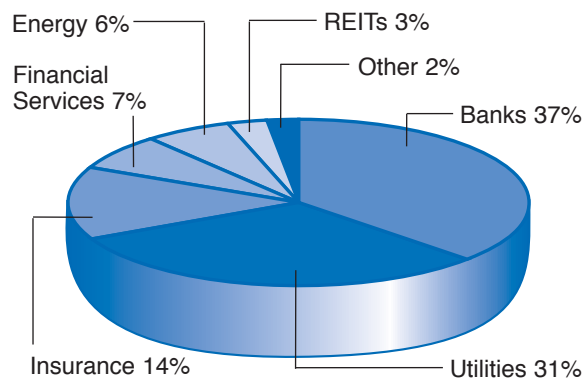
**February 28, 2007 (Unaudited)**

**Fund Statistics on 02/28/07**

Net Asset Value	\$	15.80
Market Price	\$	17.25
Premium		9.18%
Yield on Market Price		5.98%
Common Stock Shares Outstanding		10,488,187

**Industry Categories**

**% of Portfolio**



**Moody's Ratings % of Portfolio**

AAA	0.0%
AA	4.6%
A	19.9%
BBB	52.2%
BB	11.7%
Not Rated	10.3%
Below Investment Grade*	15.1%

\* Below investment grade by both Moody's and S&P.

**Top 10 Holdings by Issuer**

**% of Portfolio**

Interstate Power & Light	5.0%
Capital One Financial	4.3%
Liberty Mutual Group	4.1%
FBOP Corporation	3.8%
Banco Santander	3.8%
HSBC	3.7%
First Republic Bank	3.4%
RenaissanceRe Holdings	3.2%
SLM Corp	3.1%
Xcel Energy	3.1%

**% of Portfolio\*\***

Holdings Generating Qualified Dividend Income (QDI) for Individuals	63%
Holdings Generating Income Eligible for the Corporate Dividend Received Deduction (DRD)	53%

\*\* This does not reflect year-end results or actual tax categorization of Fund distributions. These percentages can, and do, change, perhaps significantly, depending on market conditions. Investors should consult their tax advisor regarding their personal situation.

## PORTFOLIO OF INVESTMENTS

February 28, 2007 (Unaudited)

<u>Shares/\$ Par</u>		<u>Value</u>
<b>Preferred Securities — 94.5%</b>		
<b>Banking — 36.8%</b>		
\$ 3,000,000	Astoria Capital Trust I, 9.75% 11/01/29 Capital Security, Series B .....	\$ 3,451,992
	Auction Pass-Through Trust, Cl. B:	
11	Series 2006-5, Variable Rate Pfd., 144A**** .....	360,800*
11	Series 2006-6, Variable Rate Pfd., 144A**** .....	360,800*
54,700	BAC Capital Trust I, 7.00% Pfd. 12/15/31 .....	1,393,143
7,700	BAC Capital Trust II, 7.00% Pfd. 02/01/32 .....	194,185
	Banco Santander:	
295,000	6.50% Pfd., 144A**** .....	7,522,500**(1)
69,400	6.80% Pfd., 144A**** .....	1,781,498**(1)
\$ 1,500,000	Barclays Bank PLC, 6.278% Pfd. ....	1,509,300**(1)
\$ 800,000	Barnett Capital II, 7.95% 12/01/26 Capital Security .....	832,419
\$ 2,000,000	Capital One Capital III, 7.686% Pfd. ....	2,264,300
71,300	Citigroup Capital VIII, 6.95% Pfd. 09/15/31 .....	1,813,694
19,648	Citizens Funding Trust I, 7.50% Pfd. 09/15/66 .....	512,076
	Cobank, ACB:	
50,000	7.00% Pfd., 144A**** .....	2,644,100*
75,000	7.814% Pfd., 144A**** .....	4,020,075*
	Comerica (Imperial) Capital Trust I:	
5,000	7.60% Pfd. 07/01/50 .....	126,875
\$ 500,000	9.98% 12/31/26 Capital Security, Series B .....	531,130
\$ 1,500,000	Dime Capital Trust I, 9.33% 05/06/27 Capital Security, Series A .....	1,578,522
9,000	FBOP Corporation, Adj. Rate Pfd., 144A**** .....	9,337,500*
\$ 2,250,000	First Hawaiian Capital I, 8.343% 07/01/27 Capital Security, Series B .....	2,356,879(1)
	First Republic Bank:	
200,000	6.25% Pfd. ....	5,181,260*
53,700	6.70% Pfd. ....	1,401,237*
1,000	First Republic Preferred Capital Corporation, 10.50% Pfd., 144A**** .....	1,107,940
22,500	First Republic Preferred Capital Corporation II, 8.75% Pfd., Series B, 144A**** ..	607,050
\$ 1,500,000	First Union Capital II, 7.95% 11/15/29 Capital Security .....	1,889,211
5,000	Fleet Capital Trust VIII, 7.20% Pfd. 03/15/32 .....	127,188
\$ 7,820,000	GreenPoint Capital Trust I, 9.10% 06/01/27 Capital Security .....	8,217,201
	HBOS Capital Funding LP:	
\$ 3,000,000	6.85% Pfd. ....	3,038,700(1)
\$ 2,000,000	6.413% Pfd., 144A**** .....	2,079,634**(1)
5,000	HSBC Series II, Variable Inverse Pfd., Pvt. ....	5,695,000*

**PORTFOLIO OF INVESTMENTS (Continued)****February 28, 2007 (Unaudited)**

<u>Shares/\$ Par</u>		<u>Value</u>
<b>Preferred Securities — (continued)</b>		
<b>Banking — (continued)</b>		
	HSBC USA, Inc.:	
120,000	6.50% Pfd., Series H .....	\$ 3,266,256*
2,500	\$2.8575 Pfd. ....	125,825*
100,000	Keycorp Capital IX, 6.75% Pfd. 12/15/66 .....	2,590,630
\$ 1,000,000	Lloyds TSB Group PLC, 6.267%, Capital Security, 144A**** .....	1,010,059**(1)
15,000	National City Capital Trust II, 6.625% Pfd. 11/15/36 .....	380,157
\$ 674,000	NB Capital Trust II, 7.83% 12/15/26 Capital Security .....	701,079
16,000	PFGI Capital Corporation, 7.75% Pfd. ....	416,320
\$ 650,000	RBS Capital Trust B, 6.80% Pfd. ....	669,500**(1)
10	Roslyn Real Estate, 8.95% Pfd., Series C, 144A**** .....	1,104,156
77,600	Sovereign Bancorp, 7.30% Pfd., Series C .....	2,160,679*
30,600	Sovereign Capital Trust V, 7.75% Pfd. 05/22/36 .....	816,638
\$ 1,000,000	Sovereign Capital Trust VI, 7.908% 06/13/36 Capital Security .....	1,140,467
16,000	USB Capital VII, 5.875% Pfd. 08/15/35 .....	380,160
96,700	USB Capital VIII, 6.35% Pfd. 12/29/65 .....	2,450,745
7,300	USB Capital XI, 6.60% Pfd. 09/15/66 .....	186,953
40,000	Zions Capital Trust B, 8.00% Pfd. 09/01/32 .....	1,017,500
		<u>90,353,333</u>
<b>Financial Services — 7.2%</b>		
35,000	Cabco Trust For Goldman Sachs Capital I, Adj. Rate Pfd. 02/15/34, Series GS ...	836,721
	Goldman Sachs Group, Inc.:	
25	Pass-Through Certificates, Class B, 144A**** .....	2,905,000*
2,500	STRIPES Custodial Receipts, Pvt. ....	2,885,000*
3,000	Merrill Lynch Series II STRIPES Custodial Receipts, Pvt. ....	3,369,000*
5,870	Morgan Stanley Capital Trust VI, 6.60% Pfd. ....	149,758
136,855	SLM Corporation, 6.97% Pfd., Series A .....	7,577,661*
		<u>17,723,140</u>
<b>Insurance — 11.7%</b>		
15,000	ACE Ltd., 7.80% Pfd., Series C .....	386,437**(1)
\$ 500,000	AMBAC Financial Group Inc, 6.15% Pfd., 02/15/37 .....	496,300
\$ 2,500,000	AON Capital Trust A, 8.205% 01/01/27 Capital Security .....	2,944,070
10,000	Arch Capital Group Ltd., 7.875% Pfd., Series B .....	261,875**(1)
\$ 2,500,000	AXA 6.463% 12/14/18 Capital Security, 144A**** .....	2,488,767**(1)

**PORTFOLIO OF INVESTMENTS (Continued)****February 28, 2007 (Unaudited)**

<u>Shares/\$ Par</u>		<u>Value</u>
<b>Preferred Securities — (continued)</b>		
<b>Insurance — (continued)</b>		
	Axis Capital Holdings:	
20,750	7.25% Pfd., Series A .....	\$ 541,446** <sup>(1)</sup>
14,400	7.50% Pfd., Series B .....	1,531,872 <sup>(1)</sup>
27,000	Berkley W.R. Capital Trust II, 6.75% Pfd. 07/26/45 .....	686,812
35,200	Endurance Specialty Holdings, 7.75% Pfd. ....	930,600** <sup>(1)</sup>
18,250	Everest Re Capital Trust II, 6.20% Pfd., Series B .....	440,281 <sup>(1)</sup>
\$ 1,250,000	Glen Meadow Pass Through, 6.505% Capital Security 144A**** .....	1,286,500
\$ 5,000,000	Liberty Mutual Group, 7.80% 03/15/37 Capital Security, 144A**** .....	4,990,050
21,800	Principal Financial Group, 6.518% Pfd. ....	622,663*
\$ 357,000	Provident Financing Trust I, 7.405% 03/15/38 Capital Security .....	376,798 <sup>(2)</sup>
\$ 4,500,000	Renaissancere Capital Trust, 8.54% 03/01/27 Capital Security, Series B .....	4,691,858 <sup>(1)</sup>
	Renaissancere Holdings Ltd.:	
25,200	6.08% Pfd., Series C .....	608,328** <sup>(1)</sup>
100,000	6.60% Pfd., Series D .....	2,473,000** <sup>(1)</sup>
119,500	Scottish Re Group Ltd., 7.25% Pfd. ....	2,452,140** <sup>(1)</sup>
22,850	XL Capital Ltd., 8.00% Pfd., Series A .....	586,959** <sup>(1)</sup>
		<u>28,796,756</u>
<b>Utilities — 29.5%</b>		
	Alabama Power Company:	
300	4.52% Pfd. ....	26,040*
5,734	4.72% Pfd. ....	519,787*
10,000	Baltimore Gas & Electric Company, 6.70% Pfd., Series 1993 .....	1,048,438*
10,000	Calenergy Capital Trust III, 6.50% Pfd. 09/01/27 .....	483,750
	Central Hudson Gas & Electric Corporation:	
5,000	4.35% Pfd., Series D, Pvt. ....	408,500*
900	4.96% Pfd., Series E, Pvt. ....	80,874*
8,340	Central Vermont Public Service Corporation, 8.30% Sinking Fund Pfd., Pvt. ....	866,109*
	Connecticut Light & Power Company:	
12,124	4.50% Pfd., Series 1963, Pvt. ....	483,141*
34,300	5.28% Pfd., Series 1967 .....	1,633,366*
1,905	6.56% Pfd., Series 1968 .....	98,546*
15,778	\$3.24 Pfd. ....	826,136*
2,100	Consolidated Edison Company of New York, 4.65% Pfd., Series C .....	178,458*
2,886	Dayton Power and Light Company, 3.90% Pfd., Series C .....	183,088*
\$ 1,500,000	Dominion Resources Capital Trust III, 8.40% 01/15/31 Capital Security .....	1,878,136

**PORTFOLIO OF INVESTMENTS (Continued)****February 28, 2007 (Unaudited)**

<u>Shares/\$ Par</u>		<u>Value</u>
<b>Preferred Securities — (continued)</b>		
<b>Utilities — (continued)</b>		
	Duquesne Light Company:	
7,675	4.10% Pfd. ....	\$ 271,849*
9,190	4.15% Pfd. ....	329,462*
910	4.20% Pfd. ....	33,015*
5,490	\$2.10 Pfd., Series A ....	199,177*
100,000	Entergy Arkansas, Inc., 6.45% Pfd. ....	2,604,000*
4,555	Entergy Gulf States, Inc., 7.56% Pfd. ....	456,365*
36,000	Entergy Louisiana, Inc., 6.95% Pfd. ....	3,707,640*
5,000	Entergy Mississippi, Inc., 4.92% Pfd. ....	411,850*
	Florida Power Company:	
5,157	4.60% Pfd. ....	444,069*
18,535	4.75% Pfd. ....	1,648,132*
18,300	FPC Capital I, 7.10% Pfd., Series A ....	458,073
101,000	FPL Group Capital, Inc., 6.60% Pfd. 10/01/66, Series A ....	2,613,375
13,100	Georgia Power Capital Trust, 6.125% Pfd. ....	343,056*
50,000	Georgia Power Capital Trust V, 7.125% Pfd. 03/31/42 ....	1,271,875
2,010	Great Plains Energy, Inc., 4.50% Pfd. ....	170,770*
50,000	Hawaiian Electric Company, Inc., 5.25% Pfd., Series H, Pvt. ....	935,000*
32,650	Indianapolis Power & Light Company, 5.65% Pfd. ....	3,131,135*
384,000	Interstate Power & Light Company, 8.375% Pfd., Series B ....	12,168,000*
	Pacific Enterprises:	
27,430	\$4.50 Pfd. ....	2,368,306*
10,000	\$4.75 Pfd., Series 53 ....	911,400*
	Pacific Gas & Electric Co.:	
7,600	4.50% Pfd., Series H ....	158,612*
41,500	5.00% Pfd., Series D ....	919,640*
79,086	5.00% Pfd., Series E ....	1,799,997*
	PacifiCorp:	
1,095	5.40% Pfd. ....	110,858*
1,225	\$4.56 Pfd. ....	100,989*
14,542	\$4.72 Pfd. ....	1,241,014*
10,278	\$7.48 Sinking Fund Pfd. ....	1,045,787*
\$ 500,000	PECO Energy Capital Trust III, 7.38% 04/06/28 Capital Security, Series D ....	546,200
8,137	Portland General Electric, 7.75% Sinking Fund Pfd. ....	824,685*
5,000	PPL Electric Utilities Corporation, 6.75% Pfd. ....	525,000*
10,000	Public Service Company of New Mexico, 4.58% Pfd., Series 1965 ....	795,400*

**PORTFOLIO OF INVESTMENTS (Continued)**

February 28, 2007 (Unaudited)

<u>Shares/\$ Par</u>		<u>Value</u>
<b>Preferred Securities — (continued)</b>		
<b>Utilities — (continued)</b>		
	San Diego Gas & Electric Company:	
1,200	4.40% Pfd. ....	\$ 19,980*
700	4.50% Pfd. ....	11,921*
77,000	\$1.70 Pfd. ....	2,011,625*
	South Carolina Electric & Gas Company:	
24,924	5.125% Purchase Fund Pfd., Pvt. ....	1,280,595*
6,703	6.00% Purchase Fund Pfd., Pvt. ....	341,183*
10,600	Southern California Edison, 6.00% Pfd. ....	1,092,463*
	Southern Union Company:	
\$ 200,000	7.20% Pfd. 11/01/66, Capital Security ....	201,566
64,800	7.55% Pfd. ....	1,687,392*
\$ 750,000	TXU Electric Capital V, 8.175% 01/30/37 Capital Security ....	766,018
	Union Electric Company:	
14,150	4.56% Pfd. ....	1,198,930*
18,800	\$7.64 Pfd. ....	1,946,176*
12,500	Virginia Electric & Power Company, \$7.05 Pfd. ....	1,295,313*
13,500	Virginia Power Capital Trust, 7.375% Pfd. 07/30/42 ....	343,609
	Wisconsin Power & Light Company:	
1,220	4.50% Pfd. ....	105,310*
546	4.80% Pfd. ....	50,276*
13,000	6.20% Pfd. ....	1,334,532*
	Xcel Energy, Inc.:	
16,030	\$4.08 Pfd., Series B ....	1,284,003*
26,200	\$4.10 Pfd., Series C ....	2,109,100*
22,000	\$4.11 Pfd., Series D ....	1,775,180*
17,750	\$4.16 Pfd., Series E ....	1,449,643*
10,000	\$4.56 Pfd., Series G ....	886,700*
		<u>72,450,615</u>
<b>Oil and Gas — 4.5%</b>		
8,000	Devon Energy Corporation, 6.49% Pfd., Series A ....	815,500*
\$ 1,500,000	Enterprise Products Partners, 8.375% Pfd. ....	1,673,415
5,985	EOG Resources, Inc., 7.195% Pfd., Series B ....	6,416,698*
\$ 1,225,000	KN Capital Trust III, 7.63% 04/15/28 Capital Security ....	1,195,600
10,000	Lasmo America Limited, 8.15% Pfd., 144A**** ....	1,055,400*(1)
		<u>11,156,613</u>



**PORTFOLIO OF INVESTMENTS (Continued)****February 28, 2007 (Unaudited)**

<u>Shares/\$ Par</u>		<u>Value</u>
<b>Preferred Securities — (continued)</b>		
<b>Real Estate Investment Trust (REIT) — 2.7%</b>		
21,400	BRE Properties, Inc., 8.08% Pfd., Series B .....	\$ 547,707
10,000	Equity Office Property Trust, 7.75% Pfd., Series G .....	250,938
1,000	Equity Residential Properties, 8.29% Pfd., Series K .....	60,440
	Public Storage, Inc.:	
153,770	6.45% Pfd., Series F .....	3,825,029
44,000	6.625% Pfd., Series M .....	1,094,500
2,800	6.75% Pfd., Series E .....	71,050
10,000	6.75% Pfd., Series L .....	254,063
10,000	7.25% Pfd., Series K .....	261,563
10,000	Realty Income Corp., 6.75% Pfd., Series E .....	251,563
		<u>6,616,853</u>
<b>Miscellaneous Industries — 1.9%</b>		
13,600	E.I. Du Pont de Nemours and Company, \$4.50 Pfd., Series B .....	1,166,626*
40,000	Ocean Spray Cranberries, Inc., 6.25% Pfd., 144A**** .....	3,600,000*
26,000	Touch America Holdings, \$6.875 Pfd. ....	—†
		<u>4,766,626</u>
<b>U.S. Government Securities — 0.2%</b>		
11,000	Federal Home Loan Mortgage, Adj. Rate Pfd., Series B .....	496,320*
		<u>496,320</u>
<b>Total Preferred Securities</b>		
	(Cost \$218,981,849) .....	<u>232,360,256</u>
<b>Corporate Debt Securities — 5.2%</b>		
<b>Insurance — 2.5%</b>		
\$ 900,000	Farmers Exchange Capital, 7.20% 07/15/48, 144A**** .....	954,071
\$ 4,729,000	Liberty Mutual Insurance, 7.697% 10/15/97, 144A**** .....	5,093,161
		<u>6,047,232</u>
<b>Utilities — 1.5%</b>		
\$ 1,000,000	Duquesne Light Holdings, 6.25% 08/15/35 .....	917,571
5,000	Entergy Louisiana LLC, 7.60% 04/01/32 .....	127,188
45,000	Northern States Power Company, 8.00% .....	1,170,000
	Southern Union Company:	
\$ 850,000	7.60% 02/01/24, Senior Notes .....	916,201
\$ 500,000	8.25% 11/15/29, Senior Notes .....	578,924
		<u>3,709,884</u>

**PORTFOLIO OF INVESTMENTS (Continued)**

**February 28, 2007 (Unaudited)**

<u>Shares/\$ Par</u>	<u>Value</u>
<b>Corporate Debt Securities — (continued)</b>	
<b>Oil and Gas — 1.1%</b>	
\$ 2,450,000 KN Energy, Inc., 7.45% 03/01/98 .....	\$ 2,402,926
15,000 Nexen, Inc., 7.35% Subordinated Notes .....	385,782 <sup>(1)</sup>
	<u>2,788,708</u>
<b>Miscellaneous — 0.1%</b>	
15,000 AT&T Inc, 6.375% 02/15/56 .....	374,062
	<u>374,062</u>
<b>Total Corporate Debt Securities</b>	
(Cost \$12,093,470) .....	<u>12,919,886</u>
<b>Common Stock — 0.5%</b>	
<b>Banking — 0.5%</b>	
68,921 New York Community Bancorp, Inc. ....	1,153,738*
	<u>1,153,738</u>
<b>Total Common Stock</b>	
(Cost \$1,135,835) .....	<u>1,153,738</u>
<b>Option Contracts — 0.1%</b>	
1,540 June Put Options on June U.S. Treasury Bond Futures, Expiring 05/25/07 .....	157,438†
	<u>157,438</u>
<b>Total Option Contracts</b>	
(Cost \$662,442) .....	<u>157,438</u>

**PORTFOLIO OF INVESTMENTS (Continued)****February 28, 2007 (Unaudited)**

<u>Shares/\$ Par</u>	<u>Value</u>
<b>Money Market Fund — 0.1%</b>	
241,644 BlackRock Provident Institutional, TempFund .....	\$ 241,644
<hr/>	
<b>Total Money Market Fund</b> (Cost \$241,644) .....	<u>241,644</u>
<b>Total Investments</b> (Cost \$233,115,240***) .....	100.4% 246,832,962
<b>Other Assets And Liabilities</b> (Net) .....	<u>(0.4)% (1,070,461)</u>
<b>Total Net Assets Available to Common and Preferred Stock</b> .....	<u>100.0%† \$ 245,762,501</u>
<b>Money Market Cumulative Preferred™ Stock (MMP®) Redemption Value</b> .....	<u>(80,000,000)</u>
<b>Total Net Assets Available To Common Stock</b> .....	<u>\$ 165,762,501</u>

\* Securities eligible for the Dividends Received Deduction and distributing Qualified Dividend Income.

\*\* Securities distributing Qualified Dividend Income only.

\*\*\* Aggregate cost of securities held.

\*\*\*\* Securities exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration to qualified institutional buyers. These securities have been determined to be liquid under the guidelines established by the Board of Directors.

(1) Foreign Issuer.

(2) A portion of the security is on loan.

† Non-income producing.

‡ The percentage shown for each investment category is the total value of that category as a percentage of net assets available to Common and Preferred Stock.

**ABBREVIATIONS:**

**Pfd.** — Preferred Securities

**Pvt.** — Private Placement Securities

**STATEMENT OF CHANGES IN NET ASSETS AVAILABLE TO COMMON STOCK<sup>(1)</sup>**  
**For the period from December 1, 2006 through February 28, 2007 (Unaudited)**

	<u>Value</u>
<b>OPERATIONS:</b>	
Net investment income . . . . .	\$ 3,447,715
Net realized gain/(loss) on investments sold during the period . . . . .	2,390,183
Change in net unrealized appreciation/depreciation of investments held during the period. . . . .	(2,191,055)
Distributions to MMP <sup>®*</sup> Shareholders from net investment income, including changes in accumulated undeclared distributions . . . . .	<u>(883,992)</u>
<b>Net increase in net assets resulting from operations . . . . .</b>	<b>2,762,851</b>
<b>DISTRIBUTIONS:</b>	
Dividends paid from net investment income to Common Stock Shareholders <sup>(2)</sup> . . . . .	<u>(2,704,137)</u>
<b>Total Distributions to Common Stock Shareholders . . . . .</b>	<b>(2,704,137)</b>
<b>FUND SHARE TRANSACTIONS:</b>	
Increase from shares issued under the Dividend Reinvestment and Cash Purchase Plan . . . . .	<u>228,702</u>
<b>Net increase in net assets available to Common Stock resulting from Fund share transactions . . . . .</b>	<b>228,702</b>
<b>NET INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK FOR THE PERIOD . . . . .</b>	<b><u><u>\$ 287,416</u></u></b>

**NET ASSETS AVAILABLE TO COMMON STOCK:**

Beginning of period . . . . .	\$ 165,475,085
Net increase in net assets during the period . . . . .	<u>287,416</u>
End of period . . . . .	<u><u>\$ 165,762,501</u></u>

\* Money Market Cumulative Preferred™ Stock.

<sup>(1)</sup> These tables summarize the three months ended February 28, 2007 and should be read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 2006.

<sup>(2)</sup> May include income earned, but not paid out, in prior fiscal year.

**FINANCIAL HIGHLIGHTS<sup>(1)</sup>**

**For the period from December 1, 2006 through February 28, 2007 (Unaudited)  
For a Common Stock share outstanding throughout the period.**

**PER SHARE OPERATING PERFORMANCE:**

Net asset value, beginning of period . . . . .	\$ 15.80
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**INVESTMENT OPERATIONS:**

Net investment income . . . . .	0.33
Net realized and unrealized gain/(loss) on investments . . . . .	0.01

**DISTRIBUTIONS TO MMP<sup>®\*</sup> SHAREHOLDERS:**

From net investment income . . . . .	(0.08)
From net realized capital gains . . . . .	<u>—</u>
Total from investment operations . . . . .	<u>0.26</u>

**DISTRIBUTIONS TO COMMON STOCK SHAREHOLDERS:**

From net investment income . . . . .	(0.26)
From net realized capital gains . . . . .	<u>—</u>
Total distributions to Common Stock Shareholders . . . . .	<u>(0.26)</u>

Net asset value, end of period . . . . .	<u>\$ 15.80</u>
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Market value, end of period . . . . .	<u>\$ 17.25</u>
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Common Stock shares outstanding, end of period . . . . .	<u>10,488,187</u>
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**RATIOS TO AVERAGE NET ASSETS AVAILABLE TO COMMON STOCK SHAREHOLDERS:**

Net investment income† . . . . .	6.25%**
Operating expenses . . . . .	1.46%**

**SUPPLEMENTAL DATA:††**

Portfolio turnover rate . . . . .	15%***
Total net assets available to Common and Preferred Stock, end of period (in 000's) . . .	\$ 245,763
Ratio of operating expenses to total average net assets available to Common and Preferred Stock . . . . .	0.98%**

<sup>(1)</sup> These tables summarize the three months ended February 28, 2007 and should be read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 2006.

\* Money Market Cumulative Preferred<sup>™</sup> Stock.

\*\* Annualized.

\*\*\* Not Annualized.

† The net investment income ratios reflect income net of operating expenses and payments to MMP<sup>®\*</sup> Shareholders.

†† Information presented under heading Supplemental Data includes MMP<sup>®\*</sup>.

**FINANCIAL HIGHLIGHTS (Continued)**  
**Per Share of Common Stock (Unaudited)**

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	<u>Total Dividends Paid</u>	<u>Net Asset Value</u>	<u>NYSE Closing Price</u>	<u>Dividend Reinvestment Price<sup>(1)</sup></u>
December 31, 2006 .....	\$0.0860	\$15.56	\$16.86	\$16.02
January 31, 2007 .....	0.0860	15.61	17.20	16.34
February 28, 2007 .....	0.0860	15.80	17.25	16.39

<sup>(1)</sup> 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.

**NOTES TO FINANCIAL STATEMENTS (Unaudited)**

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**1. Aggregate Information for Federal Income Tax Purposes**

At February 28, 2007, the aggregate cost of securities for federal income tax purposes was \$233,362,589, the aggregate gross unrealized appreciation for all securities in which there is an excess of value over tax cost was \$17,667,381 and the aggregate gross unrealized depreciation for all securities in which there is an excess of tax cost over value was \$4,197,008.

## Directors

Donald F. Crumrine, CFA  
Chairman of the Board  
David Gale  
Morgan Gust  
Karen H. Hogan  
Robert F. Wulf, CFA

## Officers

Donald F. Crumrine, CFA  
Chief Executive Officer  
Robert M. Ettinger, CFA  
President  
R. Eric Chadwick, CFA  
Chief Financial Officer,  
Vice President and Treasurer  
Chad C. Conwell  
Chief Compliance Officer,  
Vice President and Secretary  
Bradford S. Stone  
Vice President and  
Assistant Treasurer  
Laurie C. Lodolo  
Assistant Compliance Officer,  
Assistant Treasurer and  
Assistant Secretary

## Investment Adviser

Flaherty & Crumrine Incorporated  
e-mail: [flaherty@pfdincome.com](mailto:flaherty@pfdincome.com)

## Questions concerning your shares of Flaherty & Crumrine 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 Flaherty & Crumrine 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.**



**Flaherty & Crumrine**  
**PREFERRED INCOME FUND**

# Quarterly Report

February 28, 2007

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