

## **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](mailto:flaherty@fin-mail.com)  
web site: [www.preferredincome.com](http://www.preferredincome.com)

## **Questions concerning your shares of Preferred Income Opportunity 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 —  
First Data Investor Services Group, Inc.  
P.O. Box 1376  
Boston, MA 02104  
1-800-331-1710

**This report is sent to shareholders of Preferred Income Opportunity 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.**



## **Quarterly Report**

**August 31, 1999**

## PREFERRED INCOME OPPORTUNITY FUND INCORPORATED

Dear Shareholder:

The fixed income markets have been fighting an uphill battle lately. This shows up in the Preferred Income Opportunity Fund's total return on net asset value of  $-0.8\%$  for the first three quarters of fiscal 1999.

Interest rates increased significantly in the first nine months of fiscal 1999, reflecting strength in the domestic economy and two recent moves by the Federal Reserve Board to tighten credit. This led to a decline in the market prices of long term Treasury bonds as their yields rose more than a full percentage point. Corporate bonds and preferreds were generally hit even harder by rising interest rates, resulting in bigger price declines and larger yield increases compared to Treasuries.

The sub-par performance of corporate bonds and preferreds was due to a flood of new issues hitting the market in the last few months. This reflected an active economy and, perhaps, a rush to catch up by corporate treasurers who missed the bottom of interest rates earlier. Some financing may also have been accelerated to avoid the risk of the "Y2K" problem impacting the market later in the year. Corporate bonds were particularly affected, but the fall-out also hit preferreds.

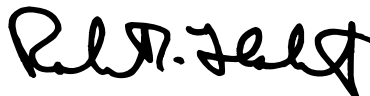
The stars of our portfolio were the put options on Treasury bond futures contracts that the Fund purchased as hedges against rising interest rates. In the first three quarters of fiscal 1999, those puts added approximately \$4.8 million to the Fund's total return. We would have made even more on our hedges if Treasury bonds had declined in price as much as corporate bonds and preferreds.

We are very comfortable with the Fund's portfolio at this time. Present market prices of corporate bonds and preferreds seem quite attractive. In comparison, Treasury bonds appear to be somewhat overvalued, which is good since we make money on our hedges when the prices of Treasuries decline. Furthermore, at current price levels, many individual issues offer better protection against the risk of redemptions by issuers. This typically results in greater upside potential.

We hope that those of you who have access to the Internet will check out our new web site at [www.preferredincome.com](http://www.preferredincome.com). It provides basic information about the Fund, recent news and up-to-date "vital statistics" on the Fund's performance, dividends, net asset value, market discount and the like. We would welcome your comments on it.

As everyone knows, "Y2K" is coming. We have done everything we can to prepare for it, although there are still risks of market disruptions and problems originating elsewhere cascading through the system. Nonetheless, we are sleeping soundly at night and are looking forward to January 1, 2000 when we hope to be able to get on with life as usual.

Sincerely,



Robert T. Flaherty  
*Chairman of the Board*

September 17, 1999

Preferred Income Opportunity Fund Incorporated

**SUMMARY OF INVESTMENTS**

**August 31, 1999 (Unaudited)**

	<u>Value (000's)</u>	<u>Percent of Total Net Assets</u>
<b>Adjustable Rate Preferred Stocks</b>		
Utilities .....	\$ 13,592	6.7%
Banking .....	8,196	4.0
Total Adjustable Rate .....	<u>21,788</u>	<u>10.7</u>
<b>Fixed Rate Preferred Stocks and Securities</b>		
Utilities .....	68,810	33.7
Banking .....	35,597	17.4
Financial Services .....	28,025	13.7
Insurance .....	20,983	10.3
Miscellaneous Industries .....	18,250	9.0
Total Fixed Rate .....	<u>171,665</u>	<u>84.1</u>
<b>TOTAL PREFERRED STOCKS AND SECURITIES</b> .....	193,453	94.8
<b>COMMON STOCKS</b>		
Utilities .....	1,052	0.5
<b>REPURCHASE AGREEMENT</b> .....	4,379	2.1
<b>PURCHASED PUT OPTIONS</b> .....	<u>3,975</u>	<u>2.0</u>
<b>TOTAL INVESTMENTS</b> .....	202,859	99.4
<b>OTHER ASSETS AND LIABILITIES (Net)</b> .....	<u>1,294</u>	<u>0.6</u>
<b>TOTAL NET ASSETS</b> .....	<u>\$204,153</u>	<u>100.0%</u>

**FINANCIAL DATA**

**Per Share of Common Stock (Unaudited)**

	<u>Dividend Paid</u>	<u>Net Asset Value</u>	<u>NYSE Closing Price</u>	<u>Dividend Reinvestment Price (1)</u>
December 31, 1998 .....	\$0.8100	\$12.75	\$12.5000	\$12.53
January 31, 1999 .....	0.0655	12.67	11.9375	11.92
February 28, 1999 .....	0.0655	12.68	11.3125	11.62
March 31, 1999 .....	0.0655	12.61	11.6250	11.57
April 30, 1999 .....	0.0655	12.65	11.1875	11.15
May 31, 1999 .....	0.0655	12.56	11.1875	11.38
June 30, 1999 .....	0.0710	12.41	11.6250	11.57
July 31, 1999 .....	0.0710	12.13	11.1250	11.12
August 31, 1999 .....	0.0710	12.00	10.9375	10.87

(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.

**STATEMENT OF CHANGES IN NET ASSETS<sup>(1)</sup>**  
**Nine Months Ended August 31, 1999 (Unaudited)**

<b>OPERATIONS:</b>	
Net investment income .....	\$ 9,475,465
Net realized gain on investments sold .....	6,600,661
Net unrealized depreciation of investments during the period .....	<u>(15,147,484)</u>
Net increase in net assets from operations .....	928,642
<b>DISTRIBUTIONS:</b>	
Dividends paid from net investment income to MMP* Shareholders .....	(2,157,830)
Distributions paid from net realized capital gains to MMP* Shareholders(3) .....	(247,384)
Dividends paid from net investment income to Common Stock Shareholders(2) .....	(8,370,009)
Distributions paid from net realized capital gains to Common Stock Shareholders(3) .....	<u>(6,689,804)</u>
<b>NET DECREASE IN NET ASSETS:</b> .....	(16,536,385)
<b>NET ASSETS:</b>	
Beginning of period .....	<u>220,689,622</u>
End of period .....	<u><u>\$204,153,237</u></u>

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

**Nine Months Ended August 31, 1999 (Unaudited)**  
**For a Common share outstanding throughout the period.**

<b>OPERATING PERFORMANCE:</b>	
Net asset value, beginning of period .....	\$ 13.50
Net investment income .....	0.85
Net realized gain and unrealized depreciation on investments .....	<u>(0.77)</u>
Net increase in net asset value resulting from investment operations .....	0.08
<b>DISTRIBUTIONS:</b>	
Dividends paid from net investment income to MMP* Shareholders .....	(0.19)
Distributions paid from net realized capital gains to MMP* Shareholders(3) .....	(0.02)
Dividends paid from net investment income to Common Stock Shareholders(2) .....	(0.75)
Distributions paid from net realized capital gains to Common Stock Shareholders(3) .....	(0.60)
Change in accumulated undeclared dividends on MMP* .....	<u>(0.02)</u>
Total distributions .....	(1.58)
Net asset value, end of period .....	<u>\$ 12.00</u>
Market value, end of period .....	<u>\$ 10.9375</u>
Common shares outstanding, end of period .....	<u><u>11,151,287</u></u>
<b>RATIOS TO AVERAGE NET ASSETS AVAILABLE TO COMMON STOCK SHAREHOLDERS:</b>	
Net investment income(4) .....	6.52%**
Operating expenses .....	1.53%**
<b>SUPPLEMENTAL DATA:</b>	
Portfolio turnover rate .....	40%
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Ratio of operating expenses to total average net assets including MMP* .....	1.02%**

(1) These tables summarize the nine months ended August 31, 1999 and should be read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 1998.

(2) Includes dividends earned, but not paid out, in prior fiscal year.

(3) Paid from capital gains realized, but not paid out, in prior fiscal year.

(4) Not necessarily reflective of results on an annual basis due to impact of Fiscal 1998 Additional Distributions to MMP\*, all of which were paid in the first quarter of Fiscal 1999.

\* Money Market Cumulative Preferred™ Stock

\*\* Annualized