

PIMCO INCOME STRATEGY FUND
Form N-CSR
October 01, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM N-CSR

**CERTIFIED SHAREHOLDER REPORT OF REGISTERED
MANAGEMENT INVESTMENT COMPANIES**

Investment Company Act file number 811-21374

PIMCO Income Strategy Fund
(Exact name of registrant as specified in charter)

1633 Broadway, New York, New York
(Address of principal executive offices)

10019
(Zip code)

Lawrence G. Altadonna -1633 Broadway, New York, New York 10019
(Name and address of agent for service)

Registrant's telephone number, including area code: 212-739-3371

Date of fiscal year July 31, 2012
end:

Date of reporting period: July 31, 2012

Item 1: Report to Shareholders

July 31, 2012

PIMCO Income Strategy Fund

PIMCO Income Strategy Fund II

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Dear Shareholder:

The U.S. economy slowed during the twelve-month fiscal reporting period ended July 31, 2012. Growth was deterred by a variety of economic and geopolitical problems, notably Europe's deepening sovereign debt crisis, a tepid U.S. labor market and increasing gasoline prices. In response, investors shifted assets into the perceived safe haven of U.S. Treasury bonds triggering yields to fall to record lows.

Twelve-Month Period in Review through July 31, 2012

For the twelve-month period ended July 31, 2012:

- PIMCO Income Strategy Fund returned 10.78% on net asset value (NAV) and 12.02% on market price.
- PIMCO Income Strategy Fund II returned 11.16% on NAV and 16.33% on market price.

The Barclays U.S. Credit Index, a measure of high quality corporate bond performance, advanced 9.87% and the Barclays U.S. Corporate High Yield Bond Index, a measure of below investment-grade corporate bond performance, rose 8.06% during the reporting period. Government bonds, as represented by the Barclays Long Term Treasury Index, returned 16.77%. The Barclays U.S. Aggregate Bond Index, a broad credit market measure of government and corporate securities, rose 7.25%, and mortgage-backed securities, reflected by the Barclays Fixed Rate MBS Index, advanced 4.91%. As for stocks, the Standard & Poor's 500 Index increased 9.13% during the twelve-month fiscal period.

U.S. gross domestic product (GDP), the value of goods and services produced in the country, the broadest measure of economic activity and the principal indicator of economic performance, expanded at an annual rate of 1.8% between July and September 2011, and at a robust 4.1% annual rate between October and December 2011. Growth slowed to a 2.0% annual rate between January and March 2012, and to 1.5% (preliminary estimate) between April and June, 2012.

Signs of a slowdown were abundant with dismal U.S. consumer spending and the manufacturing sector contracting for the first time in nearly three years. The period opened with robust private sector hiring; however, hiring diminished throughout the period. U.S. unemployment fell from 9.1% to 8.3%, although the majority of the decline occurred during the first six months of the reporting period.

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Outlook

There is growing uncertainty over future levels of federal taxes and spending. A series of tax cuts are scheduled to expire on December 31, 2012 and major spending reductions are planned to begin in January 2013. The prospect of higher taxes, reduced spending, or both, would likely have an adverse impact on the economy in 2013.

Troubles abroad also contributed to the U.S. economic slowdown. Eurozone unemployment reached 11.2% as a combination of sovereign debt woes, austerity measures, and tax increases took a toll. China's growth rate has also contracted.

Corporate earnings growth also declined on these concerns. The U.S. Federal Reserve (the Fed) indicated that it would maintain low interest rates at least through late 2014 and suggested that it may unveil a new round of quantitative easing to stimulate the economy. In testimony to Congress, Fed chairman Ben Bernanke warned of significant downside risks to the economic outlook, including strains in global financial markets.

For specific information on the Funds and their performance, please review the following pages. If you have any questions regarding the information provided, we encourage you to contact your financial advisor or call the Funds' shareholder servicing agent at (800) 254-5197. In addition, a wide range of information and resources is available on our website, www.allianzinvestors.com/closedendfunds.

Together with Allianz Global Investors Fund Management LLC, the Funds' investment manager, and Pacific Investment Management Company LLC (PIMCO), the Funds' sub-adviser, we thank you for investing with us.

We remain dedicated to serving your investment needs.

Sincerely,

Hans W. Kertess
Chairman

Brian S. Shlissel
President & CEO

Receive this report electronically and eliminate paper mailings. To enroll, go to www.allianzinvestors.com/edelivery.

**PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Fund Insights**

July 31, 2012 (unaudited)

For the twelve months ended July 31, 2012, PIMCO Income Strategy Fund returned 10.78% on net asset value (NAV) and 12.02% on market price.

For the twelve months ended July 31, 2012, PIMCO Income Strategy Fund II returned 11.16% on NAV and 16.33% on market price.

The unmanaged Barclays U.S. Aggregate Bond Index and Barclays U.S. Credit Index returned 7.25% and 9.87%, respectively, during the reporting period.

The overall U.S. fixed income market experienced periods of volatility, but ultimately generated solid returns. During the first two months of the period, the spread sectors (non-U.S. Treasuries) performed poorly as a result of Standard & Poor's downgrade of U.S. government securities, the ongoing European sovereign debt crisis and signs that global economic growth was decelerating. However, during the next six months, investor risk appetite was generally robust. This reversal in investor sentiment was triggered by signs that the U.S. economy was gaining some traction and hopes for progress in Europe. Risk aversion returned in April and May 2012 as a result of fears of contagion from the European sovereign debt crisis and concerns that the U.S. economy may be hitting a soft patch. This resulted in increased risk aversion and falling Treasury yields. The spread sectors rallied in June and July 2012 providing some signs of progress in Europe. There were also expectations of another round of quantitative easing by the Federal Reserve (the Fed) after it extended Operation Twist (a program whereby the Fed purchases longer-term Treasuries and sells an equal amount of shorter-term Treasuries in an attempt to place downward pressure on interest rates and stimulate the economy) until the end of 2012. All told, during the twelve months ended July 31, 2012, both short- and long-term Treasuries declined and the yield curve flattened.

While there were several periods of weakness as a result of increased risk aversion, these were generally temporary setbacks and the U.S. corporate bond market posted strong returns during the reporting period. Supporting

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**PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Fund Insights**

July 31, 2012 (unaudited) (continued)

the corporate bond market were corporate profits that exceeded expectations, strengthening corporate balance sheets that were flush with cash and overall solid demand from investors seeking to generate incremental yield in a low interest rate environment.

Sector exposures largely contributed to the Funds' performance

During the reporting period, the Funds outperformed the broad U.S. fixed income market (as measured by the Barclays U.S. Aggregate Bond Index) as well as the U.S. credit market (as measured by the Barclays U.S. Credit Index).

An allocation to Build America Bonds was rewarded, as these subsidized taxable municipal securities generally outperformed the broader market. An allocation to non-agency mortgage-backed securities helped performance, as these bonds outperformed the broader market, supported by positive supply/demand technicals. Although the financial sector underperformed the broad credit market during the past twelve months, the Funds' emphasis on select high quality financial issues helped performance, as those bonds performed relatively well during the reporting period. Security selection within the insurance sector was also additive to performance. Finally, the Funds' overweight duration positioning was beneficial for performance as rates trended lower during the fiscal annual period ended July 31, 2012.

On the downside, an underweighting to utilities detracted from results as this sector outperformed the overall credit market. Security selection, however, within the sector helped to partially offset the negative impact from the underweight exposure to utilities.

**PIMCO Income Strategy Fund
Performance & Statistics**

July 31, 2012 (unaudited)

Total Return(1):	Market Price	NAV
1 Year	12.02%	10.78%
5 Year	5.92%	4.97%
Commencement of Operations (8/29/03) to 7/31/12	5.45%	4.98%

Market Price/NAV Performance:

Commencement of Operations (8/29/03) to 7/31/12

Market Price/NAV:

Market Price	\$12.52
NAV	\$11.35
Premium to NAV	10.31%
Market Price Yield(2)	8.63%
Leverage Ratio(3)	32.47%

Market Price
NAV

Moody's Ratings

(as a % of total investments)

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**PIMCO Income Strategy Fund II
Performance & Statistics**

July 31, 2012 (unaudited)

Total Return(1):	Market Price	NAV
1 Year	16.33%	11.16%
5 Year	2.85%	2.15%
Commencement of Operations (10/29/04) to 7/31/12	3.06%	2.79%

Market Price/NAV Performance:

Commencement of Operations (10/29/04) to 7/31/12

Market Price/NAV:

Market Price	\$10.96
NAV	\$10.23
Premium to NAV	7.14%
Market Price Yield(2)	8.76%
Leverage Ratio(3)	26.78%

Moody's Ratings

(as a % of total investments)

(1) **Past performance is no guarantee of future results.** Total return is calculated by determining the percentage change in NAV or market price (as applicable) in the specified period. The calculation assumes that all income dividends, capital gain and return of capital distributions, if any, have been reinvested. Total return does not reflect broker commissions or sales charges in connection with the purchase or sale of Fund shares. Total return for a period of more than one year represents the average annual total return.

Performance at market price will differ from results at NAV. Although market price returns typically reflect investment results over time, during shorter periods returns at market price can also be influenced by factors such as changing views about the Funds, market conditions, supply and demand for each Fund's shares, or changes in each Fund's dividends.

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An investment in the Funds involves risk, including the loss of principal. Total return, market price, market price yield and NAV will fluctuate with changes in market conditions. This data is provided for information purposes only and is not intended for trading purposes. Closed-end funds, unlike open-end funds, are not continuously offered. There is a one time public offering and once issued, shares of closed-end funds are traded in the open market through a stock exchange. NAV is equal to total assets attributable to common shareholders less total liabilities divided by the number of common shares outstanding. Holdings are subject to change daily.

(2) Market Price Yield is determined by dividing the annualized current monthly dividend per common share (comprised of net investment income) by the market price per common share at July 31, 2012.

(3) Represents Preferred Shares and Reverse Repurchase Agreements (collectively Leverage) outstanding, as a percentage of total managed assets. Total managed assets refer to total assets (including assets attributable to Leverage) minus accrued liabilities (other than liabilities representing Leverage).

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PIMCO Income Strategy Fund Schedule of Investments

July 31, 2012

Principal Amount (000s)		Value
CORPORATE BONDS & NOTES	54.7%	
Airlines	1.2%	
\$900	American Airlines, Inc., 10.50%, 10/15/12 (d)	\$990,000
3,774	American Airlines Pass Through Trust (d), 9.73%, 9/29/14	2,641,380
1,861	10.18%, 1/2/13 (b)	1,712,391
		5,343,771
Banking	10.3%	
2,600	AgFirst Farm Credit Bank, 7.30%, 8/30/12 (a)(b)(c)(e)(i) (acquisition cost-\$2,225,000; purchased 2/26/10-4/15/10)	2,596,854
£10,400	Barclays Bank PLC, 14.00%, 6/15/19 (e)	19,237,071
3,000	Cooperatieve Centrale Raiffeisen-Boerenleenbank BA, 6.875%, 3/19/20	3,691,937
\$9,400	11.00%, 6/30/19 (a)(c)(e)	12,072,815
600	HBOS PLC, 6.75%, 5/21/18 (a)(c)	581,349
800	Regions Financial Corp., 7.375%, 12/10/37	808,000
1,500	7.75%, 9/15/24	1,544,625
£2,000	Santander Issuances S.A. Unipersonal, 7.30%, 7/27/19, (converts to FRN on 9/27/14)	2,703,915
		43,236,566
Consumer Products	0.2%	
\$800	Reynolds Group Issuer, Inc., 9.00%, 4/15/19	818,000
Energy	0.2%	
1,100	Dynegy Roseton LLC/ Danskammer Pass Through Trust, 7.67%, 11/8/16, Series B (b)(d)	709,500
Financial Services	22.7%	
304	Ally Financial, Inc., 5.90%, 1/15/19	281,927
171	5.90%, 10/15/19	158,856
55	6.00%, 2/15/19	51,097
90	6.00%, 3/15/19	84,404
8	6.00%, 4/15/19	7,468
382	6.00%, 9/15/19	356,359
95	6.05%, 8/15/19	89,181
443	6.05%, 10/15/19	412,331
20	6.10%, 9/15/19	18,852
31	6.125%, 10/15/19	28,672
1,318	6.15%, 8/15/19	1,255,086
27	6.15%, 10/15/19	25,109
22	6.20%, 4/15/19	21,222
1,371	6.25%, 2/15/16	1,343,178
25	6.25%, 1/15/19	23,631
10	6.25%, 7/15/19	9,536
120	6.30%, 8/15/19	114,300
1,168	6.35%, 2/15/16	1,130,446
285	6.35%, 4/15/16	275,819
15	6.35%, 4/15/19	14,176
216	6.40%, 3/15/16	212,196
413	6.40%, 11/15/19	390,009

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1,357
20

6.50%, 2/15/16
6.50%, 9/15/16

1,325,474
19,489

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PIMCO Income Strategy Fund Schedule of Investments

July 31, 2012 (continued)

Principal Amount (000s)		Value
Financial Services (continued)		
\$442	6.50%, 10/15/16	\$429,870
10	6.50%, 6/15/18	9,649
170	6.50%, 12/15/18	162,580
22	6.50%, 5/15/19	21,111
383	6.55%, 12/15/19	369,316
14	6.60%, 5/15/18	13,415
10	6.60%, 6/15/19	9,653
51	6.65%, 6/15/18	49,586
20	6.65%, 10/15/18	19,132
60	6.70%, 6/15/18	57,485
137	6.70%, 6/15/19	132,977
3	6.75%, 8/15/16	2,963
13	6.75%, 6/15/17	12,673
89	6.75%, 5/15/19	86,365
30	6.75%, 6/15/19	28,923
205	6.80%, 9/15/16	201,631
3	6.80%, 10/15/18	2,906
938	6.85%, 4/15/16	916,709
30	6.85%, 5/15/18	28,842
336	6.875%, 8/15/16	330,205
5	6.875%, 7/15/18	4,854
150	6.90%, 6/15/17	145,445
32	6.90%, 8/15/18	31,420
151	6.95%, 6/15/17	148,511
25	7.00%, 12/15/16	24,533
27	7.00%, 6/15/17	26,119
130	7.00%, 7/15/17	126,533
367	7.00%, 2/15/18	356,717
12	7.00%, 3/15/18	11,794
155	7.00%, 8/15/18	152,491
5	7.00%, 9/15/18	4,886
42	7.05%, 3/15/18	40,518
39	7.05%, 4/15/18	38,093
160	7.125%, 10/15/17	157,381
40	7.15%, 3/15/25	39,038
75	7.20%, 10/15/17	74,036
288	7.25%, 6/15/16	284,582
293	7.25%, 9/15/17	288,951
10	7.25%, 4/15/18	9,928
10	7.25%, 8/15/18	9,809
328	7.25%, 9/15/18	325,006
25	7.30%, 1/15/18	24,540
396	7.35%, 4/15/18	393,835
57	7.50%, 6/15/16	56,513
45	7.55%, 5/15/16	44,911
47	7.75%, 10/15/17	46,708
110	8.125%, 11/15/17	109,197
110	9.00%, 7/15/20	110,145
750	Bank of America Corp., 6.00%, 9/1/17 (h)	837,769

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1,400	Capital One Capital VI, 8.875%, 5/15/40	1,431,571
11,300	Ford Motor Credit Co. LLC, 8.00%, 12/15/16	13,387,426
4,600	8.125%, 1/15/20	5,647,590

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July 31, 2012 (continued)

Principal Amount (000s)		Value
Financial Services (continued)		
\$7,000	ILFC E-Capital Trust I, 4.28%, 12/21/65 (a)(c)(f)	\$4,865,000
	LBG Capital No.1 PLC,	
500	6.439%, 5/23/20	506,026
200	7.375%, 3/12/20	209,734
£300	7.588%, 5/12/20	408,033
£4,800	7.867%, 12/17/19	6,597,765
£700	7.869%, 8/25/20	964,150
\$2,500	7.875%, 11/1/20 (a)(c)	2,369,835
1,400	8.00%, 6/15/20 (a)(c)(e)	1,249,500
2,000	8.50%, 12/17/21 (a)(c)(e)	1,860,000
£900	11.04%, 3/19/20	1,434,701
	LBG Capital No.2 PLC,	
£534	9.125%, 7/15/20	760,374
£2,500	11.25%, 9/14/23	3,790,670
\$1,500	National City Preferred Capital Trust I, 12.00%, 12/10/12 (e)(h)	1,547,451
5,000	PNC Financial Services Group, Inc., 6.75%, 8/1/21 (e)	5,438,345
3,700	Royal Bank of Scotland Group PLC, 7.648%, 9/30/31 (e)(h)	3,256,000
	SLM Corp.,	
400	6.25%, 1/25/16	426,000
6,200	8.00%, 3/25/20 (h)	6,990,500
6,400	8.45%, 6/15/18 (h)	7,328,000
2,168	SMFG Preferred Capital USD 3 Ltd., 9.50%, 7/25/18 (a)(c)(e)	2,798,563
8,200	Springleaf Finance Corp., 6.50%, 9/15/17	6,703,500
900	State Street Capital Trust III, 5.458%, 8/30/12 (e)(h)	905,400
500	USB Capital IX, 3.50%, 8/30/12 (e)(h)	413,665
		95,748,871
Insurance 16.8%		
10,000	American General Capital II, 8.50%, 7/1/30 (h)	11,019,320
2,000	American General Institutional Capital A, 7.57%, 12/1/45 (a)(c)	2,110,000
2,000	American General Institutional Capital B, 8.125%, 3/15/46 (a)(c)	2,125,000
	American International Group, Inc.,	
4,000	6.25%, 3/15/87, (converts to FRN on 3/15/37) (h)	3,920,000
£591	6.765%, 11/15/17 (a)(c)	1,044,101
1,995	6.797%, 11/15/17 (a)(b)(c)(i)	
	(acquisition cost-\$1,829,737; purchased 5/21/10)	2,796,960
MXN8,000	7.98%, 6/15/17	588,770
1,000	8.00%, 5/22/68, (converts to FRN on 5/22/18)	1,267,312
4,700	8.00%, 5/22/68, (converts to FRN on 5/22/18) (a)(c)	5,956,365
\$11,000	8.175%, 5/15/68, (converts to FRN on 5/15/38) (h)	12,595,000
£1,350	8.625%, 5/22/68, (converts to FRN on 5/22/18)	2,218,322
£3,500	8.625%, 5/22/68, (converts to FRN on 5/22/18) (a)(c)	5,751,204
\$2,200	Dai-ichi Life Insurance Co., Ltd., 7.25%, 7/25/21 (a)(c)(e)(h)	2,362,248
2,300	Hartford Financial Services Group, Inc., 8.125%, 6/15/68,	
	(converts to FRN on 6/15/18)	2,538,625
2,000	MetLife Capital Trust IV, 7.875%, 12/15/67, (converts to FRN on 12/15/37) (a)(c)(h)	2,290,000
3,300	MetLife Capital Trust X, 9.25%, 4/8/68 (converts to FRN on 4/8/38) (a)(c)(h)	4,125,000
2,440		2,601,299

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	Progressive Corp., 6.70%, 6/15/67, (converts to FRN on 6/15/17) (h)	
5,000	Validus Holdings Ltd., 8.875%, 1/26/40	5,776,445
		71,085,971

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PIMCO Income Strategy Fund Schedule of Investments

July 31, 2012 (continued)

Principal Amount (000s)		Value
Oil & Gas 2.5%		
\$5,000	NGPL PipeCo LLC (a)(c), 7.119%, 12/15/17	\$5,162,500
5,000	7.768%, 12/15/37	4,925,000
600	SandRidge Energy, Inc., 8.00%, 6/1/18 (a)(c)	627,000
		10,714,500
Telecommunications 0.2%		
800	CenturyLink, Inc., 6.00%, 4/1/17	870,353
Utilities 0.6%		
1,900	AES Andres Dominicana Ltd., 9.50%, 11/12/20 (a)(c)(h)	2,002,125
400	PPL Capital Funding, Inc., 6.70%, 3/30/67, (converts to FRN on 3/30/17)	409,406
		2,411,531
Total Corporate Bonds & Notes (cost-\$218,441,367)		230,939,063
MUNICIPAL BONDS 22.5%		
California 9.6%		
9,200	Alameda Cnty. Joint Powers Auth. Rev., 7.046%, 12/1/44, Ser. A	11,979,872
3,000	Fresno Cnty. Rev., zero coupon, 8/15/24, Ser. A (FGIC-NPFGC)	1,707,240
5,000	Golden State Tobacco Securitization Corp. Rev., 5.125%, 6/1/47, Ser. A-1	3,813,350
900	Long Beach Redev. Agcy., Tax Allocation, 8.36%, 8/1/40	1,007,262
7,600	Los Angeles Cnty. Public Works Financing Auth. Rev., 7.618%, 8/1/40	9,993,620
1,100	Oakland Unified School Dist., Alameda Cnty., GO, 9.50%, 8/1/34	1,332,705
600	Riverside Cnty. Dev. Agcy., Tax Allocation, 7.50%, 10/1/30, Ser. A-T	634,740
1,000	Riverside Electric Rev., 7.605%, 10/1/40	1,435,300
2,000	San Luis Obispo Cnty. Rev., zero coupon, 9/1/27, Ser. C (NPFGC)	918,240
4,000	State Public Works Board Rev., 7.804%, 3/1/35, Ser. B-2	4,737,360
3,600	Stockton Public Financing Auth. Rev., 7.942%, 10/1/38, Ser. B	3,022,128
		40,581,817
Colorado 1.3%		
4,000	City & Cnty. of Denver School Dist. No. 1, CP, 7.017%, 12/15/37, Ser. B	5,407,160
District of Columbia 2.2%		
7,500	Metropolitan Airports Auth. Rev., 7.462%, 10/1/46	9,140,100
Nevada 2.8%		
10,000	Las Vegas Valley Water Dist., GO, 7.263%, 6/1/34	11,723,300
New Jersey 0.6%		
1,935	Middlesex Cnty. Improvement Auth. Rev. (AGM-GTD), zero coupon, 10/1/22	1,191,438
2,455	zero coupon, 10/1/23	1,422,451
		2,613,889
Ohio 2.8%		
8,000	American Municipal Power-Ohio, Inc. Rev., Comb Hydroelectric Projects, 8.084%, 2/15/50, Ser. B	12,060,960
Pennsylvania 0.1%		
1,000		419,080

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Philadelphia Auth. for Industrial Dev. Rev.,
zero coupon, 4/15/26, Ser. B (AMBAC)

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PIMCO Income Strategy Fund Schedule of Investments

July 31, 2012 (continued)

Principal Amount (000s)		Value
Texas 3.1%		
\$1,900	Dallas Convention Center Hotel Dev. Corp. Rev., 7.088%, 1/1/42	\$2,321,895
9,000	North Texas Tollway Auth. Rev., 8.91%, 2/1/30	10,562,310
		12,884,205
Total Municipal Bonds (cost-\$77,651,360)		94,830,511
MORTGAGE-BACKED SECURITIES 12.8%		
139	Banc of America Alternative Loan Trust, 6.00%, 1/25/36, CMO	100,197
	Banc of America Funding Corp., CMO,	
4,663	6.00%, 8/25/36	4,537,816
3,030	6.00%, 3/25/37	2,443,341
	BCAP LLC Trust, CMO (a)(c)(f),	
1,200	5.539%, 3/26/37	133,320
760	11.329%, 6/26/36	136,790
	Bear Stearns Alt-A Trust, CMO (f),	
374	2.811%, 11/25/36	206,202
976	3.071%, 9/25/35	615,961
	Chase Mortgage Finance Corp., CMO,	
13	2.734%, 12/25/35 (f)	11,556
1,478	6.00%, 2/25/37	1,334,417
1,058	6.00%, 7/25/37	901,306
2,383	6.25%, 10/25/36	1,938,661
310	Citicorp Mortgage Securities, Inc., 5.50%, 4/25/37, CMO	307,556
	Countrywide Alternative Loan Trust, CMO,	
405	5.50%, 3/25/35	318,319
196	5.50%, 3/25/36	128,201
523	6.00%, 2/25/35	467,529
3,388	6.00%, 5/25/36	2,142,449
1,296	6.00%, 8/25/37	853,800
2,198	6.071%, 4/25/36 (f)	1,420,765
1,074	6.25%, 11/25/36	848,273
589	6.50%, 8/25/36	360,790
	Countrywide Home Loan Mortgage Pass Through Trust, CMO,	
103	2.714%, 2/20/35 (f)	87,001
1,016	5.50%, 10/25/35	983,434
1,035	5.75%, 3/25/37	863,112
680	6.00%, 5/25/36	544,405
841	6.00%, 2/25/37	707,042
200	6.00%, 4/25/37	171,197
1,190	6.25%, 9/25/36	917,227
606	Credit Suisse Mortgage Capital Certificates, 6.00%, 2/25/37, CMO	485,194
	GSR Mortgage Loan Trust, CMO,	
256	5.50%, 5/25/36	212,284
6,640	6.00%, 2/25/36	6,105,919
69	Harborview Mortgage Loan Trust, 3.09%, 7/19/35, CMO (f)	51,280
1,200	JPMorgan Alternative Loan Trust, 6.31%, 8/25/36, CMO	811,729
	JPMorgan Mortgage Trust, CMO,	
1,591	5.00%, 3/25/37	1,248,727
770	5.419%, 1/25/37 (f)	626,451

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406	6.00%, 8/25/37	352,393
4,715	New Century Alternative Mortgage Loan Trust, 6.173%, 7/25/36, CMO (f)	3,232,427

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PIMCO Income Strategy Fund Schedule of Investments

July 31, 2012 (continued)

Principal Amount (000s)		Value
	Residential Asset Securitization Trust, CMO,	
\$1,277	5.75%, 2/25/36	\$954,339
505	6.00%, 9/25/36	285,470
1,323	6.00%, 7/25/37	975,465
	Residential Funding Mortgage Securities I, CMO,	
413	6.00%, 9/25/36	358,101
1,011	6.00%, 1/25/37	839,968
5,133	6.00%, 6/25/37	4,221,344
	Suntrust Adjustable Rate Mortgage Loan Trust, CMO (f),	
2,952	5.49%, 4/25/37	2,306,327
481	5.812%, 2/25/37	355,320
	WaMu Mortgage Pass Through Certificates, CMO (f),	
279	2.512%, 9/25/36	195,145
972	5.315%, 2/25/37	868,778
	Wells Fargo Mortgage-Backed Securities Trust, CMO,	
4,644	2.613%, 7/25/36 (f)	3,712,956
512	2.618%, 7/25/36 (f)	396,591
247	2.666%, 4/25/36 (f)	206,217
715	5.75%, 3/25/37	660,731
445	6.00%, 6/25/37	415,529
645	6.00%, 7/25/37	646,657
	Total Mortgage-Backed Securities (cost-\$52,023,124)	54,006,009
	Shares	
	PREFERRED STOCK 4.6%	
	Banking 1.1%	
90,200	CoBank Acb, 11.00%, 7/1/13, Ser. C (a)(b)(c)(e)(i)(j) (acquisition cost-\$4,973,200; purchased 8/31/10-2/1/11)	4,654,320
	Financial Services 1.4%	
100,000	Ally Financial, Inc., 8.50%, 5/15/16, Ser. A (e)(j)	2,325,000
120,000	Citigroup Capital XIII, 7.875%, 10/30/15 (j)	3,286,800
		5,611,800
	Real Estate Investment Trust 2.1%	
8,000	Sovereign Real Estate Investment Trust, 12.00%, 5/16/20 (a)(c)(e)	8,984,048
	Total Preferred Stock (cost-\$19,538,200)	19,250,168
	CONVERTIBLE PREFERRED STOCK 2.0%	
	Financial Services 0.7%	
2,700	Wells Fargo & Co., 7.50%, 3/15/13, Ser. L (e)	3,123,900
	Utilities 1.3%	
98,000	PPL Corp., 9.50%, 7/1/13	5,326,300
	Total Convertible Preferred Stock (cost-\$7,163,145)	8,450,200

PIMCO Income Strategy Fund Schedule of Investments

July 31, 2012 (continued)

Principal Amount (000s)		Value
ASSET-BACKED SECURITIES	0.8%	
\$1,235	Asset-Backed Funding Certificates, 0.466%, 5/25/37 (a)(c)(f)	\$949,865
1,056	GSAA Trust, 6.295%, 6/25/36	610,200
649	MASTR Asset-Backed Securities Trust, 5.233%, 11/25/35	651,113
860	Mid-State Trust, 6.34%, 10/15/36	847,516
690	Morgan Stanley Mortgage Loan Trust, 6.25%, 7/25/47	467,363
Total Asset-Backed Securities (cost-\$3,453,849)		3,526,057
SHORT-TERM INVESTMENTS	2.6%	
Corporate Notes	1.3%	
Financial Services	1.3%	
329	Ally Financial, Inc., 6.75%, 4/15/13	328,773
3,812	7.10%, 9/15/12	3,828,350
100	7.125%, 8/15/12	100,002
900	Springleaf Finance Corp., 3.25%, 1/16/13	1,057,234
Total Corporate Notes (cost-\$5,498,365)		5,314,359
Repurchase Agreements	1.3%	
\$4,800	Credit Suisse Securities (USA) LLC, dated 7/31/12, 0.20%, due 8/1/12, proceeds \$4,800,027; collateralized by U.S. Treasury Notes, 3.125%, due 1/31/17, valued at \$4,913,159 including accrued interest	4,800,000
892	State Street Bank & Trust Co., dated 7/31/12, 0.01%, due 8/1/12, proceeds \$892,000; collateralized Fannie Mae, 1.75%, due 2/22/13, valued at \$914,741 including accrued interest	892,000
Total Repurchase Agreements (cost-\$5,692,000)		5,692,000
Total Short-Term Investments (cost-\$11,190,365)		11,006,359
Total Investments (cost-\$389,461,410) 100.0%		\$422,008,367

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PIMCO Income Strategy Fund II Schedule of Investments

July 31, 2012

Principal Amount (000s)		Value
CORPORATE BONDS & NOTES 54.3%		
Airlines 1.2%		
\$7,686	American Airlines Pass Through Trust, (d), 9.73%, 9/29/14	\$5,380,197
3,834	10.18%, 1/2/13 (b)	3,527,273
712	United Air Lines Pass Through Trust, 10.40%, 5/1/18	812,871
		9,720,341
Banking 8.3%		
5,500	AgFirst Farm Credit Bank, 7.30%, 8/30/12 (a)(b)(c)(e)(i) (acquisition cost-\$4,709,000; purchased 2/26/10-4/15/10)	5,493,345
£16,700	Barclays Bank PLC, 14.00%, 6/15/19 (e)	30,890,297
\$6,700	BBVA Bancomer S.A., 7.25%, 4/22/20 (a)(c)	7,068,500
16,000	Cooperatieve Centrale Raiffeisen-Boerenleenbank BA, 6.875%, 3/19/20	19,690,333
\$1,400	HBOS PLC, 6.75%, 5/21/18 (a)(c)	1,356,481
1,675	Regions Financial Corp., 7.375%, 12/10/37	1,691,750
£800	Santander Finance Preferred S.A. Unipersonal, 11.30%, 7/27/14 (e)	1,117,815
		67,308,521
Consumer Products 0.2%		
\$1,700	Reynolds Group Issuer, Inc., 9.00%, 4/15/19	1,738,250
Energy 1.3%		
9,003	AES Red Oak LLC, 8.54%, 11/30/19	9,565,955
2,300	Dynegy Roseton LLC/ Danskammer Pass Through Trust, 7.67%, 11/8/16, Series B (b)(d)	1,483,500
		11,049,455
Financial Services 23.3%		
1,800	AGFC Capital Trust I, 6.00%, 1/15/67, (converts to FRN on 1/15/17) (a)(c)	936,000
416	Ally Financial, Inc., 5.25%, 1/15/14	407,534
315	5.35%, 1/15/14	314,256
561	5.75%, 1/15/14	549,332
565	5.90%, 1/15/19	528,298
3	5.90%, 2/15/19	2,765
585	6.00%, 12/15/13	577,933
1,437	6.00%, 2/15/19	1,347,313
119	6.00%, 3/15/19	111,741
9	6.00%, 9/15/19	8,396
486	6.10%, 9/15/19	458,105
159	6.125%, 10/15/19	147,059
394	6.15%, 8/15/19	375,193
454	6.15%, 10/15/19	422,196
675	6.20%, 4/15/19	651,133
500	6.25%, 12/15/18	471,504
47	6.25%, 7/15/19	44,818
7	6.35%, 4/15/16	6,774
792	6.35%, 10/15/16	766,032
303	6.35%, 4/15/19	286,356
1,142	6.35%, 7/15/19	1,074,312
463	6.375%, 1/15/14	457,283

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249	6.50%, 9/15/16	242,635
608	6.50%, 10/15/16	591,314
5	6.50%, 6/15/18	4,824
449	6.50%, 11/15/18	429,049

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July 31, 2012 (continued)

Principal Amount (000s)		Value
Financial Services (continued)		
\$190	6.50%, 12/15/18	\$181,540
15	6.50%, 5/15/19	14,394
208	6.60%, 8/15/16	204,678
864	6.60%, 5/15/18	827,925
100	6.60%, 6/15/19	96,530
132	6.65%, 10/15/18	127,598
190	6.70%, 5/15/14	188,926
256	6.70%, 6/15/18	246,672
335	6.70%, 12/15/19	324,013
555	6.75%, 6/15/14	552,128
215	6.75%, 8/15/16	210,807
1,136	6.75%, 11/15/16	1,121,497
210	6.75%, 6/15/17	204,722
831	6.75%, 7/15/18	805,487
3	6.75%, 9/15/18	2,901
612	6.75%, 10/15/18	604,747
107	6.75%, 11/15/18	103,602
27	6.75%, 5/15/19	26,378
92	6.80%, 9/15/16	90,488
12	6.80%, 9/15/18	11,521
207	6.85%, 4/15/16	203,630
7	6.875%, 7/15/18	6,795
319	6.90%, 7/15/18	313,122
326	6.90%, 8/15/18	320,087
135	6.95%, 6/15/17	132,775
201	7.00%, 8/15/16	198,739
1,729	7.00%, 11/15/16	1,687,955
580	7.00%, 12/15/16	569,424
1,729	7.00%, 1/15/17	1,692,700
601	7.00%, 2/15/17	583,397
1,087	7.00%, 6/15/17	1,051,516
1,073	7.00%, 7/15/17	1,044,383
43	7.00%, 2/15/18	41,615
506	7.00%, 3/15/18	497,321
15	7.00%, 5/15/18	14,640
400	7.00%, 9/15/18	390,868
134	7.00%, 6/15/22	131,458
2,035	7.00%, 11/15/24	1,993,614
325	7.05%, 3/15/18	313,531
4	7.05%, 4/15/18	3,907
6	7.15%, 9/15/18	5,905
477	7.20%, 10/15/17	471,340
55	7.25%, 6/15/16	54,347
653	7.25%, 9/15/17	643,455
329	7.25%, 1/15/18	323,404
255	7.25%, 4/15/18	253,057
39	7.30%, 12/15/17	38,238
503	7.30%, 1/15/18	493,808
165	7.35%, 1/15/17	162,327

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58	7.35%, 4/15/18	57,683
25	7.375%, 11/15/16	24,678
55	7.375%, 4/15/18	54,238
166	7.40%, 12/15/17	163,989

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July 31, 2012 (continued)

Principal Amount (000s)		Value
Financial Services (continued)		
\$1,828	7.50%, 11/15/16	\$1,813,310
15	7.50%, 8/15/17	14,781
559	7.50%, 11/15/17	547,081
290	7.50%, 12/15/17	286,118
40	8.00%, 3/15/17	39,985
3	8.125%, 11/15/17	2,978
25	8.20%, 3/15/17	24,998
24	8.40%, 8/15/15	23,652
224	9.00%, 7/15/20	224,294
3,100	Bank of America Corp., 6.00%, 9/1/17 (h)	3,462,778
2,900	Capital One Capital VI, 8.875%, 5/15/40	2,965,398
£2,000	Credit Agricole S.A., 8.125%, 10/26/19 (e)	2,321,140
\$8,000	Ford Motor Credit Co. LLC, 8.00%, 12/15/16	9,477,824
1,100	HSBC Finance Capital Trust IX, 5.911%, 11/30/35, (converts to FRN on 11/30/15)	1,061,500
11,000	ILFC E-Capital Trust II, 6.25%, 12/21/65, (converts to FRN on 12/21/15) (a)(c)	8,305,000
	LBG Capital No.1 PLC,	
500	6.439%, 5/23/20	506,026
500	7.375%, 3/12/20	524,335
£300	7.588%, 5/12/20	408,033
£10,200	7.867%, 12/17/19	14,020,250
£1,000	7.869%, 8/25/20	1,377,356
\$4,500	7.875%, 11/1/20 (a)(c)	4,265,703
£4,700	11.04%, 3/19/20	7,492,325
	LBG Capital No.2 PLC,	
8,900	8.875%, 2/7/20	10,245,342
£300	12.75%, 8/10/20	484,419
1,100	15.00%, 12/21/19	1,670,821
\$25,500	National City Preferred Capital Trust I, 12.00%, 12/10/12 (e)(h)	26,306,667
5,965	NSG Holdings LLC, 7.75%, 12/15/25 (a)(c)	6,084,300
	SLM Corp.,	
5,000	5.625%, 8/1/33	4,387,500
10,700	8.00%, 3/25/20	12,064,250
1,700	8.45%, 6/15/18	1,946,500
	Springleaf Finance Corp.,	
3,200	4.125%, 11/29/13	3,710,886
\$11,800	6.50%, 9/15/17	9,646,500
1,596	State Street Capital Trust III, 5.458%, 8/30/12 (e)(h)	1,605,576
800	USB Capital IX, 3.50%, 8/30/12 (e)	661,864
17,550	Wells Fargo & Co., 7.98%, 3/15/18 (e)	19,743,750
		188,819,895
Insurance 18.7%		
3,000	American General Institutional Capital A, 7.57%, 12/1/45 (a)(c)	3,165,000
5,000	American General Institutional Capital B, 8.125%, 3/15/46 (a)(c)	5,312,500
	American International Group, Inc.,	
1,900	6.25%, 3/15/87, (converts to FRN on 3/15/37)	1,862,000
£10,545	6.765%, 11/15/17 (a)(c)	18,629,512
12,540		17,580,894

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	6.797%, 11/15/17 (a)(b)(c)(i) (acquisition cost-\$11,931,071; purchased 5/20/10-5/21/10)	
MXN16,000	7.98%, 6/15/17	1,177,541
2,000	8.00%, 5/22/68, (converts to FRN on 5/22/18)	2,534,624

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July 31, 2012 (continued)

Principal Amount (000s)		Value
Insurance (continued)		
12,800	8.00%, 5/22/68, (converts to FRN on 5/22/18) (a)(c)	\$16,221,590
\$31,750	8.175%, 5/15/68, (converts to FRN on 5/15/38) (h)	36,353,750
£1,600	8.625%, 5/22/68, (converts to FRN on 5/22/18) (a)(c)	2,629,122
£8,050	8.625%, 5/22/68, (converts to FRN on 5/22/18)	13,227,769
\$1,700	AXA S.A., 6.463%, 12/14/18 (a)(c)(e)(h)	1,489,625
6,500	Dai-ichi Life Insurance Co., Ltd., 7.25%, 7/25/21 (a)(c)(e)(h)	6,979,369
4,700	Hartford Financial Services Group, Inc., 8.125%, 6/15/68, (converts to FRN on 6/15/18)	5,187,625
15,000	MetLife Capital Trust IV, 7.875%, 12/15/67, (converts to FRN on 12/15/37) (a)(c)	17,175,000
2,500	Validus Holdings Ltd., 8.875%, 1/26/40	2,888,222
		152,414,143
Telecommunications 0.4%		
1,400	CenturyLink, Inc., 6.00%, 4/1/17	1,523,119
1,500	7.60%, 9/15/39	1,547,404
		3,070,523
Utilities 0.9%		
3,900	AES Andres Dominicana Ltd., 9.50%, 11/12/20 (a)(c)	4,109,625
4,500	Ameren Energy Generating Co., 7.95%, 6/1/32	3,577,500
		7,687,125
Total Corporate Bonds & Notes (cost-\$405,215,302)		441,808,253
MUNICIPAL BONDS 21.2%		
California 12.3%		
13,100	Alameda Cnty. Joint Powers Auth. Rev., 7.046%, 12/1/44, Ser. A	17,058,296
1,650	City & Cnty. of San Francisco Redev. Agcy., Tax Allocation, 8.406%, 8/1/39	1,933,454
3,000	La Quinta Financing Auth., Tax Allocation, 8.07%, 9/1/36, Ser. A	3,321,930
4,000	Long Beach Redev. Agcy., Tax Allocation, 8.11%, 8/1/30	4,433,400
10,800	Los Angeles Cnty. Public Works Financing Auth. Rev., 7.618%, 8/1/40	14,201,460
20,000	Northern California Power Agcy. Rev., 7.311%, 6/1/40	24,349,800
11,600	Oakland Unified School Dist., Alameda Cnty., GO, 9.50%, 8/1/34	14,053,980
1,200	Riverside Cnty. Dev. Agcy., Tax Allocation, 7.50%, 10/1/30, Ser. A-T	1,269,480
5,100	San Luis Obispo Cnty. Rev., zero coupon, 9/1/27, Ser. C (NPFGC)	2,341,512
9,200	State Public Works Board Rev., 7.804%, 3/1/35, Ser. B-2	10,895,928
7,500	Stockton Public Financing Auth. Rev., 7.942%, 10/1/38, Ser. B	6,296,100
		100,155,340
Colorado 0.8%		
5,000	City & Cnty. of Denver School Dist. No. 1, CP, 7.017%, 12/15/37, Ser. B	6,758,950
District of Columbia 2.0%		
13,000	Metropolitan Airports Auth. Rev., 7.462%, 10/1/46	15,842,840
Ohio 2.4%		
13,000	American Municipal Power-Ohio, Inc. Rev., Comb Hydroelectric Projects, 8.084%, 2/15/50, Ser. B	19,599,060

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July 31, 2012 (continued)

Principal Amount (000s)		Value
Texas 3.7%		
	\$4,000	Dallas Convention Center Hotel Dev. Corp. Rev., 7.088%, 1/1/42
	21,500	North Texas Tollway Auth. Rev., 8.91%, 2/1/30
		\$4,888,200
		25,232,185
		30,120,385
Total Municipal Bonds (cost-\$146,203,313)		172,476,575

MORTGAGE-BACKED SECURITIES 12.3%

324	Banc of America Alternative Loan Trust, 6.00%, 1/25/36, CMO	233,794
92	Banc of America Funding Corp., CMO, 5.696%, 1/20/47 (f)	57,840
14,269	6.00%, 3/25/37	11,507,347
2,209	BCAP LLC Trust, CMO (a)(c)(f), 2.94%, 5/26/36	40,375
2,500	5.539%, 3/26/37	277,751
3,627	8.819%, 5/26/37	534,939
1,520	11.329%, 6/26/36	273,581
608	Bear Stearns Alt-A Trust, CMO (f), 2.811%, 11/25/36	335,078
2,041	3.071%, 9/25/35	1,287,919
27	Chase Mortgage Finance Corp., CMO, 2.734%, 12/25/35 (f)	23,112
459	5.50%, 5/25/36	429,593
620	Citicorp Mortgage Securities, Inc., CMO, 5.50%, 4/25/37	615,112
5,092	6.00%, 9/25/37	5,197,964
833	Countrywide Alternative Loan Trust, CMO, 5.50%, 3/25/35	655,363
2,232	5.50%, 1/25/36	1,603,162
318	5.50%, 3/25/36	208,327
1,888	5.75%, 12/25/36	1,350,300
1,088	6.00%, 2/25/35	972,965
6,957	6.00%, 5/25/36	4,399,380
1,432	6.00%, 4/25/37	896,019
2,699	6.00%, 8/25/37	1,778,750
4,536	6.071%, 4/25/36 (f)	2,931,066
2,207	6.25%, 11/25/36	1,743,672
1,179	6.50%, 8/25/36	721,579
2,164	Countrywide Home Loan Mortgage Pass Through Trust, CMO, 5.75%, 3/25/37	1,804,688
1,380	6.00%, 5/25/36	1,105,308
1,682	6.00%, 2/25/37	1,414,084
7,280	6.00%, 3/25/37	6,126,045
2,446	6.25%, 9/25/36	1,885,410
3,185	First Horizon Asset Securities, Inc., 2.625%, 11/25/35, CMO (f)	2,493,457
	JPMorgan Alternative Loan Trust, CMO,	

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4,393	2.852%, 5/25/36 (f)	2,696,171
2,500	6.31%, 8/25/36	1,691,101
	JPMorgan Mortgage Trust,	
1,294	5.235%, 10/25/35 (f)	1,269,231
711	6.00%, 8/25/37	616,687
276	6.50%, 9/25/35	279,796
1,644	MASTR Asset Securitization Trust, 6.50%, 11/25/37, CMO	1,450,829

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PIMCO Income Strategy Fund II Schedule of Investments

July 31, 2012 (continued)

Principal Amount (000s)		Value
\$9,998	New Century Alternative Mortgage Loan Trust, 6.173%, 7/25/36, CMO (f)	\$6,854,974
73	Nomura Asset Acceptance Corp., 4.976%, 5/25/35, CMO Residential Asset Securitization Trust, CMO,	63,998
2,640	5.75%, 2/25/36	1,973,573
1,011	6.00%, 9/25/36	570,940
2,811	6.00%, 7/25/37	2,072,862
5,106	Residential Funding Mortgage Securities I, CMO, 5.31%, 9/25/35 (f)	4,195,913
10,540	6.00%, 6/25/37	8,668,257
2,283	6.25%, 8/25/36, CMO	1,967,795
962	Suntrust Adjustable Rate Mortgage Loan Trust, 5.812%, 2/25/37, CMO (f)	710,641
597	WaMu Mortgage Pass Through Certificates, CMO (f), 2.512%, 9/25/36	418,167
1,944	5.315%, 2/25/37	1,737,556
9,448	Wells Fargo Mortgage-Backed Securities Trust, CMO, 2.613%, 7/25/36 (f)	7,554,462
1,070	2.618%, 7/25/36 (f)	829,236
493	2.666%, 4/25/36 (f)	412,434
1,429	5.75%, 3/25/37	1,321,462
Total Mortgage-Backed Securities (cost-\$96,784,335)		100,260,065
Shares		
PREFERRED STOCK 6.4%		
Banking 2.5%		
397,300	CoBank Acb, 11.00%, 7/1/13, Ser. C (a)(b)(c)(e)(i)(j) (acquisition cost-\$21,899,400; purchased 2/26/10-3/23/11)	20,500,680
Financial Services 3.1%		
248,000	Ally Financial, Inc., 7.30%, 8/29/12 (e)	5,979,280
260,000	Citigroup Capital XIII, 7.875%, 10/30/15 (j)	7,121,400
5,000	Farm Credit Bank, 10.00%, 12/15/20, Ser. 1 (e)	5,810,937
255,400	GMAC Capital Trust I, 8.125%, 2/15/16, Ser. 2 (j)	6,226,652
		25,138,269
Real Estate Investment Trust 0.8%		
5,600	Sovereign Real Estate Investment Trust, 12.00%, 5/16/20 (a)(c)(e)	6,288,834
Total Preferred Stock (cost-\$51,006,628)		51,927,783
CONVERTIBLE PREFERRED STOCK 3.7%		
Financial Services 0.5%		
3,500	Wells Fargo & Co., 7.50%, 3/15/13, Ser. L (e)	4,049,500
Utilities 3.2%		
104,000	PPL Corp., 8.75%, 5/1/14	5,601,440

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	374,000	9.50%, 7/1/13	20,326,900
			25,928,340
Total Convertible Preferred Stock (cost-\$27,930,180)			29,977,840

PIMCO Income Strategy Fund
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PIMCO Income Strategy Fund II Schedule of Investments

July 31, 2012 (continued)

Principal Amount (000s)		Value
ASSET-BACKED SECURITIES	1.3%	
\$2,599	Asset-Backed Funding Certificates, 0.466%, 5/25/37 (a)(c)(f)	\$1,999,717
2,200	GSAA Trust, 6.295%, 6/25/36	1,271,251
5,511	Indymac Residential Asset-Backed Trust, 0.406%, 7/25/37 (f)	3,002,365
1,325	MASTR Asset-Backed Securities Trust, 5.233%, 11/25/35	1,329,355
1,803	Mid-State Trust, 6.34%, 10/15/36	1,777,050
1,381	Morgan Stanley Mortgage Loan Trust, 6.25%, 7/25/47	934,727
Total Asset-Backed Securities (cost-\$10,768,736)		10,314,465
SHORT-TERM INVESTMENTS	0.8%	
Corporate Notes	0.5%	
Financial Services	0.5%	
130	Ally Financial, Inc., 5.70%, 6/15/13	128,959
160	6.75%, 9/15/12	160,039
844	6.75%, 10/15/12	840,999
837	7.10%, 9/15/12	840,188
28	7.15%, 11/15/12	27,986
339	7.25%, 8/15/12	338,869
1,998	7.25%, 12/15/12	2,003,099
Total Corporate Notes (cost-\$4,327,478)		4,340,139
U.S. Treasury Obligations (g)(k)	0.1%	
440	U.S. Treasury Bills, 0.074%-0.076%, 8/2/12-8/23/12 (cost-\$439,982)	439,982
Repurchase Agreements	0.2%	
700	Credit Suisse Securities (USA) LLC, dated 7/31/12, 0.13%, due 8/1/12, proceeds \$700,003; collateralized by U.S. Treasury Notes, 0.125%, due 7/31/14, valued at \$716,544 including accrued interest	700,000
567	State Street Bank & Trust Co., dated 7/31/12, 0.01%, due 8/1/12, proceeds \$567,000; collateralized by Fannie Mae, 1.75%, due 2/22/13, valued at \$579,336 including accrued interest	567,000
Total Repurchase Agreements (cost-\$1,267,000)		1,267,000
Total Short-Term Investments (cost-\$6,034,460)		6,047,121
Total Investments (cost-\$743,942,954)		\$812,812,102

PIMCO Income Strategy Fund	
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PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Notes to Schedules of Investments

July 31, 2012

- (a) Private Placement Restricted as to resale and may not have a readily available market. Securities with an aggregate value of \$84,529,762 and \$156,717,443, representing 20.0% and 19.3% of total investments in Income Strategy and Income Strategy II, respectively.
- (b) Illiquid.
- (c) 144A Exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration, typically only to qualified institutional buyers. Unless otherwise indicated, these securities are not considered to be illiquid.
- (d) In default.
- (e) Perpetual maturity. The date shown is the next call date. For Corporate Bonds & Notes, the interest rate is fixed until the first call date and variable thereafter.
- (f) Variable or Floating Rate Security Security with an interest rate that changes periodically. The interest rate disclosed reflects the rate in effect on July 31, 2012.
- (g) All or partial amount segregated for the benefit of the counterparty as collateral for derivatives.
- (h) All or partial amount transferred for the benefit of the counterparty as collateral for reverse repurchase agreements.
- (i) Restricted. The aggregate acquisition cost of such securities is \$9,027,937 and \$38,539,471 for Income Strategy and Income Strategy II, respectively. The aggregate market value is \$10,048,134 and \$43,574,919, representing 2.4% and 5.4% of total investments in Income Strategy and Income Strategy II, respectively.
- (j) Dividend rate is fixed until the first call date and variable thereafter.
- (k) Rates reflect the effective yields at purchase date.

Glossary:

AGM	- insured by Assured Guaranty Municipal Corp.
AMBAC	- insured by American Municipal Bond Assurance Corp.
£	- British Pound
CMO	- Collateralized Mortgage Obligation
CP	- Certificates of Participation
	- Euro
FGIC	- insured by Financial Guaranty Insurance Co.
FRN	- Floating Rate Note
GO	- General Obligation Bond
GTD	- Guaranteed
MXN	- Mexican Peso
NPFGC	- insured by National Public Finance Guarantee Corp.

PIMCO Income Strategy Fund
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PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Statements of Assets and Liabilities

July 31, 2012

	Income Strategy	Income Strategy II
Assets:		
Investments, at value (cost-\$389,461,410 and \$743,942,954, respectively)	\$422,008,367	\$812,812,102
Cash (including foreign currency, at value of \$84,802 and \$15,359 with a cost of \$84,060 and \$13,946, respectively)	661,257	17,184
Unsettled reverse repurchase agreements	12,452,000	9,162,000
Interest and dividends receivable	5,986,783	12,914,136
Unrealized appreciation of OTC swaps	1,293,098	2,653,139
Swap premiums paid	1,040,841	2,187,694
Unrealized appreciation of forward foreign currency contracts	244,879	1,310,801
Prepaid expenses	21,495	42,429
Total Assets	443,708,720	841,099,485
Liabilities:		
Payable for reverse repurchase agreements	57,226,000	57,592,000
Payable for investments purchased	18,735,573	13,218,232
Payable to brokers for cash collateral received	2,295,000	5,230,000
Dividends payable to common and preferred shareholders	2,264,882	4,701,373
Unrealized depreciation of forward foreign currency contracts	333,170	675,651
Investment management fees payable	262,292	509,956
Interest payable for reverse repurchase agreements	53,099	116,846
Payable to broker		42,340
Accrued expenses and other liabilities	278,391	330,407
Total Liabilities	81,448,407	82,416,805
Preferred Shares (\$0.00001 par value and \$25,000 liquidation preference per share applicable to an aggregate of 3,159 and 6,440 shares issued and outstanding, respectively)	78,975,000	161,000,000
Net Assets Applicable to Common Shareholders	\$283,285,313	\$597,682,680
Composition of Net Assets Applicable to Common Shareholders:		
Common Shares:		
Par value (\$0.00001 per share)	\$250	\$584
Paid-in-capital in excess of par	412,546,536	936,643,827
Undistributed net investment income	8,515,743	29,196,693
Accumulated net realized loss	(171,517,945)	(440,231,690)
Net unrealized appreciation of investments, swaps and foreign currency transactions	33,740,729	72,073,266
Net Assets Applicable to Common Shareholders	\$283,285,313	\$597,682,680
Common Shares Issued and Outstanding	24,956,448	58,431,583
Net Asset Value Per Common Share	\$11.35	\$10.23

PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Statements of Operations

Year ended July 31, 2012

	Income Strategy	Income Strategy II
Investment Income:		
Interest	\$30,958,463	\$61,438,604
Dividends	2,402,379	6,796,701
Facility and other fee income	121,303	741
Total Investment Income	33,482,145	68,236,046
Expenses:		
Investment management fees	3,080,382	5,984,439
Legal fees	608,749	612,224
Interest expense	512,172	649,518
Custodian and accounting agent fees	161,498	241,187
Auction agent fees and commissions	137,600	273,398
Audit and tax services	133,274	112,400
Shareholder communications	86,690	127,180
Transfer agent fees	38,775	34,490
Trustees' fees and expenses	31,286	68,138
New York Stock Exchange listing fees	21,377	46,438
Insurance expense	9,888	19,257
Miscellaneous	22,740	23,365
Total Expenses	4,844,431	8,192,034
Net Investment Income	28,637,714	60,044,012
Realized and Change in Unrealized Gain (Loss):		
Net realized gain (loss) on:		
Investments	6,487,834	(1,138,830)
Futures contracts	998,969	1,837,275
Swaps	(9,737,771)	(13,714,812)
Foreign currency transactions	3,219,589	12,398,252
Net change in unrealized appreciation/depreciation of:		
Investments	(4,095,396)	(4,464,536)
Futures contracts	(577,182)	(890,772)
Swaps	2,025,124	3,674,345
Foreign currency transactions	912,651	3,805,199
Net realized and change in unrealized gain (loss) on investments, futures contracts, swaps and foreign currency transactions	(766,182)	1,506,121
Net Increase in Net Assets Resulting from Investment Operations	27,871,532	61,550,133
Dividends on Preferred Shares from Net Investment Income	(1,141,460)	(2,327,391)
Net Increase in Net Assets Applicable to Common Shareholders Resulting from Investment Operations	\$26,730,072	\$59,222,742

PIMCO Income Strategy Fund
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PIMCO Income Strategy Fund**Statements of Changes in Net Assets Applicable to Common Shareholders**

	2012	Year ended July 31,	2011
Investment Operations:			
Net investment income	\$28,637,714		\$30,689,912
Net realized gain on investments, futures contracts, swaps and foreign currency transactions	968,621		6,383,400
Net change in unrealized appreciation/depreciation of investments, futures contracts, swaps, unfunded loan commitments and foreign currency transactions	(1,734,803)		13,014,572
Net increase in net assets resulting from investment operations	27,871,532		50,087,884
Dividends on Preferred Shares from Net Investment Income	(1,141,460)		(1,166,363)
Net increase in net assets applicable to common shareholders resulting from investment operations	26,730,072		48,921,521
Dividends to Common Shareholders from Net Investment Income	(27,503,217)		(29,956,842)
Common Share Transactions:			
Reinvestment of dividends	1,367,723		1,666,381
Total increase in net assets applicable to common shareholders	594,578		20,631,060
Net Assets Applicable to Common Shareholders:			
Beginning of year	282,690,735		262,059,675
End of year (including undistributed net investment income of \$8,515,743 and \$4,998,713, respectively)	\$283,285,313		\$282,690,735
Common Shares Issued in Reinvestment of Dividends	126,940		146,096

PIMCO Income Strategy Fund

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PIMCO Income Strategy Fund II**Statements of Changes in Net Assets Applicable to Common Shareholders**

	Year ended July 31,	
	2012	2011
Investment Operations:		
Net investment income	\$60,044,012	\$59,883,484
Net realized gain (loss) on investments, futures contracts, swaps and foreign currency transactions	(618,115)	19,192,118
Net change in unrealized appreciation/depreciation of investments, futures contracts, swaps, unfunded loan commitments and foreign currency transactions	2,124,236	22,736,170
Net increase in net assets resulting from investment operations	61,550,133	101,811,772
Dividends on Preferred Shares from Net Investment Income	(2,327,391)	(2,379,363)
Net increase in net assets applicable to common shareholders resulting from investment operations	59,222,742	99,432,409
Dividends to Common Shareholders from Net Investment Income	(48,115,485)	(56,277,446)
Common Share Transactions:		
Reinvestment of dividends	2,224,177	3,854,345
Total increase in net assets applicable to common shareholders	13,331,434	47,009,308
Net Assets Applicable to Common Shareholders:		
Beginning of year	584,351,246	537,341,938
End of year (including undistributed net investment income of \$29,196,693 and \$6,957,156, respectively)	\$597,682,680	\$584,351,246
Common Shares Issued in Reinvestment of Dividends	232,354	385,713

PIMCO Income Strategy Fund

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PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Statements of Cash Flows

Year ended July 31, 2012

	Income Strategy	Income Strategy II
Decrease in Cash and Foreign Currency from:		
Cash Flows provided by Operating Activities:		
Net increase in net assets resulting from investment operations	\$27,871,532	\$61,550,133
Adjustments to Reconcile Net Increase in Net Assets Resulting from Investment Operations to Net Cash provided by Operating Activities:		
Purchases of long-term investments	(91,639,048)	(135,414,459)
Proceeds from sales of long-term investments	127,831,942	146,995,221
(Purchases) sales of short-term portfolio investments, net	(3,473,853)	4,911,051
Net change in unrealized appreciation/depreciation of investments, futures contracts, swaps and foreign currency transactions	1,734,803	(2,124,236)
Net realized (gain) loss on investments, futures contracts, swaps and foreign currency transactions	(968,621)	618,115
Net amortization premium on investments	(445,559)	(1,011,159)
Increase in unsettled reverse repurchase agreements	(12,452,000)	(9,162,000)
Decrease in interest and dividends receivable	1,963,852	827,222
Proceeds from futures contracts transactions	515,062	1,170,491
Decrease in deposits with brokers for futures contracts collateral	548,000	841,000
Decrease in prepaid expenses	9,089	18,539
Increase in payable for investments purchased	17,497,739	13,218,232
Increase in payable to brokers for cash collateral received	2,195,000	5,230,000
Net cash used for swap transactions	(11,304,100)	(16,726,329)
Net cash provided by foreign currency transactions	3,198,129	12,272,520
Decrease in investment management fees payable	(26,803)	(21,123)
Increase in interest payable for reverse repurchase agreements	30,877	107,122
Increase in accrued expenses and other liabilities	49,349	51,986
Net cash provided by operating activities*	63,135,390	83,352,326
Cash Flows used for Financing Activities:		
Decrease in payable for reverse repurchase agreements	(39,135,093)	(46,200,225)
Cash dividends paid (excluding reinvestment of dividends of \$1,367,723 and \$2,224,177, respectively)	(26,886,488)	(47,331,372)
Net cash used for financing activities	(66,021,581)	(93,531,597)
Net decrease in cash and foreign currency	(2,886,191)	(10,179,271)
Cash and foreign currency, at beginning of year	3,547,448	10,196,455
Cash and foreign currency, at end of year	\$661,257	\$17,184

* Included in operating expenses is cash paid by Income Strategy and Income Strategy II for interest primarily related to participation in reverse repurchase agreement transactions of \$481,181 and \$542,140, respectively.

PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II

Notes to Financial Statements

July 31, 2012

1. Organization and Significant Accounting Policies

PIMCO Income Strategy Fund (Income Strategy) and PIMCO Income Strategy Fund II (Income Strategy II), each a Fund and collectively the

Funds , were organized as Massachusetts business trusts on June 19, 2003 and June 30, 2004, respectively. Prior to commencing operations on August 29, 2003 and October 29, 2004, respectively, Income Strategy and Income Strategy II had no operations other than matters relating to their organization and registration as diversified, closed-end management investment companies registered under the Investment Company Act of 1940 and the rules and regulations thereunder, as amended. Allianz Global Investors Fund Management LLC (the Investment Manager) serves as the Funds investment manager and is an indirect, wholly-owned subsidiary of Allianz Asset Management of America L.P. (AAM). AAM is an indirect, wholly-owned subsidiary of Allianz SE, a publicly traded European insurance and financial services company. Each Fund has authorized an unlimited amount of common shares with \$0.00001 par value.

Each Fund s investment objective is to seek high current income, consistent with the preservation of capital. There can be no assurance that the Funds will meet their stated objectives.

The preparation of the Funds 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 each Fund s financial statements. Actual results could differ from those estimates.

In the normal course of business, the Funds enter into contracts that contain a variety of representations that provide general indemnifications. The Funds maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Funds that have not yet occurred.

In December 2011, the Financial Accounting Standards Board issued Accounting Standards Update No. 2011-11, Disclosures About Offsetting Assets and Liabilities , which requires enhanced disclosures that will enable users to evaluate the effect or potential effect of netting arrangements on an entity s financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments. The amendments are effective for fiscal years beginning on or after January 1, 2013. The Funds management is currently evaluating the effect that the guidance may have on its financial statements.

The following is a summary of significant accounting policies consistently followed by the Funds:

(a) Valuation of Investments

Portfolio securities and other financial instruments for which market quotations are readily available are stated at market value. Market value is generally determined on the basis of last reported sales prices, or if no sales are reported, on the basis of quotes obtained from a quotation reporting system, established market makers, or independent pricing services. The Funds investments are valued daily using prices supplied by an independent pricing service or dealer quotations, or by using the last sale price on the exchange that is the primary market for such securities, or the mean between the last quoted bid and ask price. Independent pricing services use information provided by market makers or estimates of market values obtained from yield data relating to investments or securities with similar characteristics.

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The Board of Trustees has adopted methods for valuing portfolio securities and other financial derivative instruments in circumstances where market quotes are not readily available, and has delegated the responsibility for applying the valuation methods to the Investment Manager and Pacific Investment Management Company LLC (the Sub-Adviser), an affiliate of the Investment Manager. The Valuation Committee has been established by the Board of Trustees to oversee the implementation of the Funds' valuation methods and to make fair value determinations on behalf of the Board of Trustees as instructed. The Sub-Adviser monitors the continual appropriateness of methods applied and determines if adjustments should be made in light of market changes, events affecting the issuer, or other factors. If the Sub-Adviser determines that a valuation method may no longer be appropriate, another valuation method may be selected, or the Valuation Committee will be convened to consider the matter and take any appropriate action in accordance with procedures set forth by the Board of Trustees. The Board of Trustees shall review the appropriateness of the valuation methods and these methods may be amended or supplemented from time to time by the Valuation Committee.

Benchmark pricing procedures are used as the basis for setting the base price of a fixed-income security and for subsequently adjusting the price proportionally to market value changes of a pre-determined security deemed to be comparable in duration, generally a U.S. Treasury or sovereign note based on country of issuance. The base price may be a broker-dealer quote, transaction price, or an internal value as derived by analysis of market data. The base price

PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II

Notes to Financial Statements

July 31, 2012

1. Organization and Significant Accounting Policies (continued)

of the security may be reset on a periodic basis based on the availability of market data and procedures approved by the Valuation Committee. The validity of the fair value is reviewed by the Sub-Adviser on a periodic basis and may be amended as the availability of market data indicates a material change.

If third party evaluated vendor pricing is neither available nor deemed to be reliable of fair value, the Sub-Adviser may elect to obtain market quotations (broker quotes) directly from a broker-dealer.

Short-term securities maturing in 60 days or less are valued at amortized cost, if their original term to maturity was 60 days or less, or by amortizing their value on the 61st day prior to maturity, if the original term to maturity exceeded 60 days.

Investments initially valued in currencies other than the U.S. dollar are converted to the U.S. dollar using exchange rates obtained from pricing services. As a result, the net asset value (NAV) of each Fund 's shares may be affected by changes in the value of currencies in relation to the U.S. dollar. The value of securities traded in markets outside the United States or denominated in currencies other than the U.S. dollar may be affected significantly on a day that the New York Stock Exchange (NYSE) is closed.

The prices used by the Funds to value securities may differ from the value that would be realized if the securities were sold, and these differences could be material to the Funds ' financial statements. Each Fund 's NAV is normally determined as of the close of regular trading (normally, 4:00 p.m. Eastern time) on the NYSE on each day the NYSE is open for business.

(b) Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (*i.e.* the exit price) in an orderly transaction between market participants. The three levels of the fair value hierarchy are described below:

- Level 1 quoted prices in active markets for identical investments that the Funds have the ability to access
- Level 2 valuations based on other significant observable inputs, which may include, but are not limited to, quoted prices for similar assets or liabilities, interest rates, yield curves, volatilities, prepayment speeds, loss severities, credit risks and default rates or other market corroborated inputs
- Level 3 valuations based on significant unobservable inputs (including the Sub-Adviser 's or Valuation Committee 's own assumptions and single broker quotes in determining the fair value of investments)

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The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. The following are certain inputs and techniques that the Funds generally use to evaluate how to classify each major category of assets and liabilities for Level 2 and Level 3, in accordance with Generally Accepted Accounting Principles (GAAP).

Equity Securities (Common and Preferred Stock) Equity securities traded in inactive markets are valued using inputs which include broker-dealer quotes, recently executed transactions adjusted for changes in the benchmark index, or evaluated price quotes received from independent pricing services that take into account the integrity of the market sector and issuer, the individual characteristics of the security, and information received from broker-dealers and other market sources pertaining to the issuer or security. To the extent that these inputs are observable, the values of equity securities are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

U.S. Treasury Obligations U.S. Treasury obligations are valued by independent pricing services based on pricing models that evaluate the mean between the most recently quoted bid and ask price. The models also take into consideration data received from active market makers and broker-dealers, yield curves, and the spread over comparable U.S. Treasury issues. The spreads change daily in response to market conditions and are generally obtained from the new issue market and broker-dealer sources. To the extent that these inputs are observable, the values of U.S. Treasury obligations are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

Government Sponsored Enterprise and Mortgage-Backed Securities Government sponsored enterprise and mortgage-backed securities are valued by independent pricing services using pricing models based on inputs that include issuer type, coupon, cash flows, mortgage prepayment projection tables and Adjustable Rate Mortgage evaluations that incorporate index data, periodic and life caps, the next coupon reset date, and the convertibility of the bond. To the

PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II

Notes to Financial Statements

July 31, 2012

1. Organization and Significant Accounting Policies (continued)

extent that these inputs are observable, the values of government sponsored enterprise and mortgage-backed securities are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

Municipal Bonds Municipal bonds are valued by independent pricing services based on pricing models that take into account, among other factors, information received from market makers and broker-dealers, current trades, bid-want lists, offerings, market movements, the callability of the bond, state of issuance, benchmark yield curves, and bond insurance. To the extent that these inputs are observable, the values of municipal bonds are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

Corporate Bonds & Notes Corporate bonds and notes are generally comprised of two main categories: investment grade bonds and high yield bonds. Investment grade bonds are valued by independent pricing services using various inputs and techniques, which include broker-dealer quotations, live trading levels, recently executed transactions in securities of the issuer or comparable issuers, and option adjusted spread models that include base curve and spread curve inputs. Adjustments to individual bonds can be applied to recognize trading differences compared to other bonds issued by the same issuer. High yield bonds are valued by independent pricing services based primarily on broker-dealer quotations from relevant market makers and recently executed transactions in securities of the issuer or comparable issuers. The broker-dealer quotations received are supported by credit analysis of the issuer that takes into consideration credit quality assessments, daily trading activity, and the activity of the underlying equities, listed bonds and sector-specific trends. To the extent that these inputs are observable, the values of corporate bonds and notes are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

Asset-Backed Securities and Collateralized Mortgage Obligations Asset-backed securities and collateralized mortgage obligations are valued by independent pricing services using pricing models based on a security's average life volatility. The models also take into account tranche characteristics such as coupon, average life, collateral types, ratings, the issuer and tranche type, underlying collateral and performance of the collateral, and discount margin for certain floating rate issues. To the extent that these inputs are observable, the values of asset-backed securities and collateralized mortgage obligations are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

Forward Foreign Currency Contracts Forward foreign currency contracts are valued by independent pricing services using various inputs and techniques, which include broker-dealer quotations, actual trading information and foreign currency exchange rates gathered from leading market makers and foreign currency exchange trading centers throughout the world. To the extent that these inputs are observable, the values of forward foreign currency contracts are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

Interest Rate Swaps OTC interest rate swaps are valued by independent pricing services using pricing models that are based on real-time intraday snapshots of relevant interest rate curves that are built using the most actively traded securities for a given maturity. The pricing models also incorporate cash and money market rates. In addition, market data pertaining to interest rate swaps is monitored regularly to ensure that interest rates are properly depicting the current market rate. Centrally cleared interest rate swaps are valued at the price determined by the relevant exchange. To the extent that these inputs are observable, the values of interest rate swaps are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

Credit Default Swaps OTC credit default swaps are valued by independent pricing services using pricing models that take into account, among other factors, information received from market makers and broker-dealers, default probabilities from index specific credit spread curves, recovery rates, and cash flows. Centrally cleared credit default swaps are valued at the price determined by the relevant exchange. To the extent that these inputs are observable, the values of credit default swaps are categorized as Level 2. To the extent that these inputs are unobservable, the values are categorized as Level 3.

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1. Organization and Significant Accounting Policies (continued)

The valuation techniques used by the Funds to measure fair value during the year ended July 31, 2012 maximized the use of observable inputs and minimized the use of unobservable inputs.

The Funds' policy is to recognize transfers between levels at the end of the reporting period. An investment asset's or liability's level within the fair value hierarchy is based on the lowest level input, individually or in aggregate, that is significant to fair value measurement. The objective of fair value measurement remains the same even when there is a significant decrease in the volume and level of activity for an asset or liability and regardless of the valuation techniques used. Assets categorized as Level 1 or 2 as of period end may have been transferred between Levels 1 and 2 since the prior period due to changes in the valuation method utilized in valuing the investments.

A summary of the inputs used at July 31, 2012 in valuing Income Strategy's assets and liabilities is listed below (refer to the Schedules of Investments and Notes 5(a), 5(b) and 5(c) for more detailed information on Investments in Securities and Other Financial Instruments):

	Level 1 Quoted Prices	Level 2 Other Significant Observable Inputs	Level 3 Significant Unobservable Inputs	Value at 7/31/12
Investments in Securities Assets				
Corporate Bonds & Notes:				
Airlines		\$990,000	\$4,353,771	\$5,343,771
Energy			709,500	709,500
All Other		224,885,792		224,885,792
Municipal Bonds		94,830,511		94,830,511
Mortgage-Backed Securities		53,869,219	136,790	54,006,009
Preferred Stock:				
Banking			4,654,320	4,654,320
Financial Services	\$5,611,800			5,611,800
Real Estate Investment Trust		8,984,048		8,984,048
Convertible Preferred Stock	8,450,200			8,450,200
Asset-Backed Securities		3,526,057		3,526,057
Short-Term Investments		11,006,359		11,006,359
Total Investments in Securities Assets	\$14,062,000	\$398,091,986	\$9,854,381	\$422,008,367
Other Financial Instruments* Assets				
Credit Contracts		\$30,812		\$30,812
Foreign Exchange Contracts		244,879		244,879
Interest Rate Contracts		1,262,286		1,262,286
Total Other Financial Instruments* Assets		\$1,537,977		\$1,537,977
Other Financial Instruments* Liabilities				
Foreign Exchange Contracts		\$(333,170)		\$(333,170)
Total Investments	\$14,062,000	\$399,296,793	\$9,854,381	\$423,213,174

At July 31, 2012, there were no transfers between Levels 1 and 2.

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July 31, 2012

1. Organization and Significant Accounting Policies (continued)

A roll forward of fair value measurements using significant unobservable inputs (Level 3) for Income Strategy for the year ended July 31, 2012, was as follows:

	Beginning Balance 7/31/11	Purchases	Sales	Accrued Discounts (Premiums)	Net Realized Gain (Loss)	Net Change in Unrealized Appreciation/ Depreciation	Transfers into Level 3**	Transfers out of Level 3***	Ending Balance 7/31/12
Investments in Securities	Assets								
Corporate Bonds & Notes:									
Airlines	\$22,043,236		\$(15,972,453)	\$6,285	\$151,184	\$(1,874,481)			\$4,353,771
Energy	852,500			(16,981)		(126,019)			709,500
Mortgage-Backed Securities	226,603	\$1,709	(241,762)	73,659	205,485	4,416		\$(133,320)	136,790
Preferred Stock:									
Banking							\$4,654,320		4,654,320
Total Investments	\$23,122,339	\$1,709	\$(16,214,215)	\$62,963	\$356,669	\$(1,996,084)	\$4,654,320	\$(133,320)	\$9,854,381

A summary of the inputs used at July 31, 2012 in valuing Income Strategy II's assets and liabilities is listed below (refer to the Schedules of Investments and Notes 5(a), 5(b) and 5(c) for more detailed information on Investments in Securities and Other Financial Instruments):

	Level 1 Quoted Prices	Level 2 Other Significant Observable Inputs	Level 3 Significant Unobservable Inputs	Value at 7/31/12
Investments in Securities	Assets			
Corporate Bonds & Notes:				
Airlines			\$9,720,341	\$9,720,341
Energy		\$9,565,955	1,483,500	11,049,455
All Other		421,038,457		421,038,457
Municipal Bonds		172,476,575		172,476,575
Mortgage-Backed Securities		99,451,545	808,520	100,260,065
Preferred Stock:				
Banking			20,500,680	20,500,680
Financial Services	\$19,327,332	5,810,937		25,138,269
Real Estate Investment Trust		6,288,834		6,288,834
Convertible Preferred Stock	29,977,840			29,977,840
Asset-Backed Securities		10,314,465		10,314,465
Short-Term Investments		6,047,121		6,047,121
Total Investments in Securities	\$49,305,172	\$730,993,889	\$32,513,041	\$812,812,102
Other Financial Instruments*	Assets			

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Foreign Exchange Contracts		\$1,310,801		\$1,310,801
Interest Rate Contracts		2,653,139		2,653,139
Total Other Financial Instruments* Assets		\$3,963,940		\$3,963,940
Other Financial Instruments* Liabilities				
Foreign Exchange Contracts		\$(675,651)		\$(675,651)
Total Investments	\$49,305,172	\$734,282,178	\$32,513,041	\$816,100,391

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July 31, 2012

1. Organization and Significant Accounting Policies (continued)

At July 31, 2012, \$6,226,652 were transferred from Level 2 to Level 1 due to the availability of a quoted price in an active market.

A roll forward of fair value measurements using significant unobservable inputs (Level 3) for Income Strategy II for the year ended July 31, 2012, was as follows:

	Beginning Balance 7/31/11	Purchases	Sales	Accrued Discounts (Premiums)	Net Realized Gain (Loss)	Net Change in Unrealized Appreciation/ Depreciation	Transfers into Level 3**	Transfers out of Level 3***	Ending Balance 7/31/12
Investments in Securities	Assets								
Corporate Bonds & Notes:									
Airlines	\$12,367,885		\$(177,145)	\$64,317	\$(14,215)	\$(2,520,501)			\$9,720,341
Energy	1,782,500			9,499		(308,499)			1,483,500
Mortgage-Backed Securities	1,076,658	\$3,418	(483,524)	240,736	410,996	(121,638)		\$(318,126)	808,520
Preferred Stock:									
Automotive Products	10,137				(2,000,000)	1,989,863			
Banking							\$20,500,680		20,500,680
Common Stock	813				(1,317,433)	1,316,620			
Total Investments	\$15,237,993	\$3,418	\$(660,669)	\$314,552	\$(2,920,652)	\$355,845	\$20,500,680	\$(318,126)	\$32,513,041

* Other financial instruments are derivatives not reflected in the Schedules of Investments, such as swap agreements and forward foreign currency contracts, which are valued at the unrealized appreciation (depreciation) of the instrument.

** Transferred out of Level 2 into Level 3 because single broker quote provided by a third-party pricing vendor was unobservable.

*** Transferred out of Level 3 into Level 2 because evaluated price from a third-party pricing vendor was available.

Security deemed worthless, removed from the Schedule of Investments.

The net change in unrealized appreciation/depreciation of Level 3 investments which Income Strategy and Income Strategy II held at July 31, 2012, was \$(1,356,592) and \$(2,844,922), respectively.

Net realized gain (loss) and net change in unrealized appreciation/depreciation are reflected on the Statements of Operations.

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The following tables present additional information about valuation techniques and inputs used for investments that are measured at fair value and categorized within Level 3 at July 31, 2012:

Income Strategy:

Investment in Securities Assets	Ending Balance at 7/31/12	Valuation Techniques Used	Unobservable Inputs	Input Values
Corporate Bonds & Notes	\$5,063,271	Third-Party pricing vendor	Single broker quote	\$64.50 \$92.00
Mortgage-Backed Securities	136,790	Third-Party pricing vendor	Single broker quote	\$18.00
Preferred Stock	4,654,320	Third-Party pricing vendor	Single broker quote	\$51.60
Total Investments	\$9,854,381			

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1. Organization and Significant Accounting Policies (continued)

Income Strategy II:

	Ending Balance at 7/31/12	Valuation Techniques Used	Unobservable Inputs	Input Values
Investment in Securities Assets				
Corporate Bonds & Notes	\$11,203,841	Third-Party pricing vendor	Single broker quote	\$64.50 \$92.00
Mortgage-Backed Securities	808,520	Third-Party pricing vendor	Single broker quote	\$18.00
Preferred Stock	20,500,680	Third-Party pricing vendor	Single broker quote	\$51.60
Total Investments	\$32,513,041			

(c) Investment Transactions and Investment Income

Investment transactions are accounted for on the trade date. Realized gains and losses on investments are determined on an identified cost basis. Interest income adjusted for the accretion of discount and amortization of premiums is recorded on an accrual basis. Discounts or premiums on debt securities purchased are accreted or amortized, respectively, to interest income over the lives of the respective securities. Dividend income is recorded on the ex-dividend date. Facility fees and other fees received after settlement date relating to senior loans, consent fees relating to corporate actions and commitment fees received relating to unfunded purchase commitments are recorded as other fee income upon receipt. Paydown gains and losses are netted and recorded as interest income on the Statements of Operations.

(d) Federal Income Taxes

The Funds intend to distribute all of their taxable income and to comply with the other requirements of Subchapter M of the U.S. Internal Revenue Code of 1986, as amended, applicable to regulated investment companies. Accordingly, no provision for U.S. federal income taxes is required.

Accounting for uncertainty in income taxes establishes for all entities, including pass-through entities such as the Funds, a minimum threshold for financial statement recognition of the benefit of positions taken in filing tax returns (including whether an entity is taxable in a particular jurisdiction), and requires certain expanded tax disclosures. The Funds' management has determined that its evaluation has resulted in no material impact to the Funds' financial statements at July 31, 2012. The Funds' federal tax returns for the prior three years remain subject to examination by the Internal Revenue Service.

(e) Dividends and Distributions Common Shares

The Funds declare dividends from net investment income to common shareholders monthly. Distributions of net realized capital gains, if any, are paid at least annually. The Funds record dividends and distributions on the ex-dividend date. The amount of dividends from net investment

income and distributions from net realized capital gains is determined in accordance with federal income tax regulations, which may differ from GAAP. These book-tax differences are considered either temporary or permanent in nature. To the extent these differences are permanent in nature, such amounts are reclassified within the capital accounts based on their federal income tax treatment; temporary differences do not require reclassification. To the extent dividends and/or distributions exceed current and accumulated earnings and profits for federal income tax purposes, they are reported as dividends and/or distributions to shareholders from return of capital.

(f) Foreign Currency Translation

The Funds' accounting records are maintained in U.S. dollars as follows: (1) the foreign currency market value of investments and other assets and liabilities denominated in foreign currencies are translated at the prevailing exchange rate at the end of the period; and (2) purchases and sales, income and expenses are translated at the prevailing exchange rate on the respective dates of such transactions. The resulting net foreign currency gain (loss) is included in the Funds' Statements of Operations.

The Funds do not generally isolate that portion of the results of operations arising as a result of changes in the foreign currency exchange rates from the fluctuations arising from changes in the market prices of securities. Accordingly, such foreign currency gain (loss) is included in net realized and unrealized gain (loss) on investments. However, the Funds do isolate the effect of fluctuations in foreign currency exchange rates when determining the gain (loss) upon the sale or maturity of foreign currency denominated debt obligations pursuant to U.S. federal income tax regulations; such amount is categorized as foreign currency gain (loss) for both financial reporting and income tax reporting purposes.

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1. Organization and Significant Accounting Policies (continued)

(g) Repurchase Agreements

The Funds enter into transactions with their custodian bank or securities brokerage firms whereby they purchase securities under agreements to resell such securities at an agreed upon price and date (repurchase agreements). The Funds, through their custodian, take possession of securities collateralizing the repurchase agreement. Such agreements are carried at the contract amount in the financial statements, which is considered to represent fair-value. Collateral pledged (the securities received), which consists primarily of U.S. government obligations and asset-backed securities, is held by the custodian bank for the benefit of the Funds until maturity of the repurchase agreement. Provisions of the repurchase agreements and the procedures adopted by the Funds require that the market value of the collateral, including accrued interest thereon, be sufficient in the event of default by the counterparty. If the counterparty defaults and the value of the collateral declines or if the counterparty enters an insolvency proceeding, realization of the collateral by the Funds may be delayed or limited.

(h) Reverse Repurchase Agreements

In a reverse repurchase agreement, the Funds sell securities to a bank or broker-dealer and agree to repurchase the securities at a mutually agreed upon date and price. Generally, the effect of such a transaction is that the Funds can recover and reinvest all or most of the cash invested in portfolio securities involved during the term of the reverse repurchase agreement and still be entitled to the returns associated with those portfolio securities. Such transactions are advantageous if the interest cost to the Funds of the reverse repurchase transaction is less than the returns it obtains on investments purchased with the cash. To the extent a Fund does not cover its positions in reverse repurchase agreements (by transferring liquid assets at least equal in amount to the forward purchase commitment), the Funds' uncovered obligations under the agreements will be subject to the Funds' limitations on borrowings. Reverse repurchase agreements involve leverage risk and also the risk that the market value of the securities that the Funds are obligated to repurchase under the agreement may decline below the repurchase price. In the event the buyer of securities under a reverse repurchase agreement files for bankruptcy or becomes insolvent, the Funds' use of the proceeds of the agreement may be restricted pending determination by the other party, or their trustee or receiver, whether to enforce the Funds' obligation to repurchase the securities.

(i) Mortgage-Related and Other Asset-Backed Securities

Investments in mortgage-related or other asset-backed securities include mortgage pass-through securities, collateralized mortgage obligations (CMOs), commercial mortgage-backed securities, mortgage dollar rolls, CMO residuals, stripped mortgage-backed securities (SMBSs) and other securities that directly or indirectly represent a participation in, or are secured by and payable from, mortgage loans on real property. The value of some mortgage-related or asset-backed securities may be particularly sensitive to changes in prevailing interest rates. Early repayment of principal on some mortgage-related securities may expose the Funds to a lower rate of return upon reinvestment of principal. The value of these securities may fluctuate in response to the market's perception of the creditworthiness of the issuers. The decline in liquidity and prices of these types of securities may make it more difficult to determine fair market value. Additionally, although mortgages and mortgage-related securities are generally supported by some form of government or private guarantee and/or insurance, there is no assurance that private guarantors or insurers will meet their obligations.

(j) Restricted Securities

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The Funds are permitted to invest in securities that are subject to legal or contractual restrictions on resale. These securities generally may be resold in transactions exempt from registration or to the public if the securities are registered. Disposal of these securities may involve time-consuming negotiations and expenses, and prompt sale at an acceptable price may be difficult.

(k) Interest Expense

Interest expense primarily relates to the Funds' participation in reverse repurchase agreement transactions. Interest expense is recorded as it is incurred.

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1. Organization and Significant Accounting Policies (continued)

(l) Custody Credits on Cash Balances

The Funds benefit from an expense offset arrangement with their custodian bank, whereby uninvested cash balances may earn credits that reduce monthly custodian and accounting agent expenses. Had these cash balances been invested in income-producing securities, they would have generated income for the Funds. Cash overdraft charges, if any, are included in custodian and accounting agent fees.

2. Principal Risks

In the normal course of business, the Funds trade financial instruments and enter into financial transactions where risk of potential loss exists due to, among other things, changes in the market (market risk) or failure of the other party to a transaction to perform (counterparty risk). The Funds are also exposed to other risks such as, but not limited to, interest rate, foreign currency, credit and leverage risks.

Interest rate risk is the risk that fixed income securities will decline in value because of changes in interest rates. As nominal interest rates rise, the values of certain fixed income securities held by the Funds are likely to decrease. A nominal interest rate can be described as the sum of a real interest rate and an expected inflation rate. Fixed income securities with longer durations tend to be more sensitive to changes in interest rates, usually making them more volatile than securities with shorter durations. Duration is used primarily as a measure of the sensitivity of a fixed income security's market price to interest rate (*i.e.* yield) movements.

Variable and floating rate securities generally are less sensitive to interest rate changes but may decline in value if their interest rates do not rise as much, or as quickly, as interest rates in general. Conversely, floating rate securities will not generally increase in value if interest rates decline. Inverse floating rate securities may decrease in value if interest rates increase. Inverse floating rate securities may also exhibit greater price volatility than a fixed rate obligation with similar credit quality. When a Fund holds variable or floating rate securities, a decrease (or, in the case of inverse floating rate securities, an increase) in market interest rates will adversely affect the income received from such securities and the NAV of the Funds' shares.

Mortgage-related and other asset-backed securities often involve risks that are different from or more acute than risks associated with other types of debt instruments. Generally, rising interest rates tend to extend the duration of fixed rate mortgage-related securities, making them more sensitive to changes in interest rates. As a result, in a period of rising interest rates, if a Fund holds mortgage-related securities, it may exhibit additional volatility. This is known as extension risk. In addition, adjustable and fixed rate mortgage-related securities are subject to prepayment risk. When interest rates decline, borrowers may pay off their mortgages sooner than expected. This can reduce the returns of the Funds because the Funds may have to reinvest that money at the lower prevailing interest rates. The Funds' investments in other asset-backed securities are subject to risks similar to those associated with mortgage-related securities, as well as additional risks associated with the nature of the assets and the servicing of those assets.

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The Funds are exposed to credit risk, which is the risk of losing money if the issuer or guarantor of a fixed income security is unable or unwilling, or is perceived (whether by market participants, rating agencies, pricing services or otherwise) as unable or unwilling, to make timely principal and/or interest payments, or to otherwise honor its obligations. Securities are subject to varying degrees of credit risk, which are often reflected in credit ratings.

To the extent the Funds directly invest in foreign currencies or in securities that trade in, and receive revenues in, foreign currencies, or in derivatives that provide exposure to foreign currencies, they will be subject to the risk that those currencies will decline in value relative to the U.S. dollar, or, in the case of hedging positions, that the U.S. dollar will decline in value relative to the currency being hedged. Currency rates in foreign countries may fluctuate significantly over short periods of time for a number of reasons, including economic growth, inflation, changes in interest rates, intervention (or the failure to intervene) by U.S. or foreign governments, central banks or supranational entities such as the International Monetary Fund, or the imposition of currency controls or other political developments in the United States or abroad. As a result, the Funds' investments in foreign currency-denominated securities may reduce the returns of the Funds.

The Funds are subject to elements of risk not typically associated with investments in the U.S., due to concentrated investments in foreign issuers located in a specific country or region. Such concentrations will subject the Funds to additional risks resulting from future political or economic conditions in such country or region and the possible imposition of adverse governmental laws or currency exchange restrictions affecting such country or region, which

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2. Principal Risks (continued)

could cause the securities and their markets to be less liquid and prices more volatile than those of comparable U.S. companies.

The market values of securities may decline due to general market conditions (market risk) which are not specifically related to a particular company, such as real or perceived adverse economic conditions, changes in the general outlook for corporate earnings, changes in interest or currency rates or adverse investor sentiment. They may also decline due to factors that affect a particular industry or industries, such as labor shortages or increased production costs and competitive conditions within an industry. Equity securities and equity-related investments generally have greater market price volatility than fixed income securities.

The Funds are exposed to counterparty risk, or the risk that an institution or other entity with which the Funds have unsettled or open transactions will default. The potential loss to the Funds could exceed the value of the financial assets recorded in the Funds' financial statements. Financial assets, which potentially expose the Funds to counterparty risk, consist principally of cash due from counterparties and investments. The Funds' Sub-Adviser seeks to minimize the Funds' counterparty risk by performing reviews of each counterparty and by minimizing concentration of counterparty risk by undertaking transactions with multiple customers and counterparties on recognized and reputable exchanges. Delivery of securities sold is only made once the Funds have received payment. Payment is made on a purchase once the securities have been delivered by the counterparty. The trade will fail if either party fails to meet its obligation.

The Funds are exposed to risks associated with leverage. Leverage may cause the value of the Funds' shares to be more volatile than if the Funds did not use leverage. This is because leverage tends to exaggerate the effect of any increase or decrease in the value of the Funds' portfolio securities. The Funds engage in transactions or purchase instruments that give rise to forms of leverage. Obligations to settle reverse repurchase agreements may be detrimental to a Fund's performance. In addition, to the extent the Funds employ leverage, dividend and interest costs may not be recovered by any appreciation of the securities purchased with the leverage proceeds and could exceed the Funds' investment returns, resulting in greater losses.

The Funds are party to International Swaps and Derivatives Association, Inc. Master Agreements (ISDA Master Agreements) with select counterparties that govern transactions, over-the-counter derivatives and foreign exchange contracts entered into by the Funds and those counterparties. The ISDA Master Agreements contain provisions for general obligations, representations, agreements, collateral and events of default or termination. Events of termination include conditions that may entitle counterparties to elect to terminate early and cause settlement of all outstanding transactions under the applicable ISDA Master Agreement. Any election to terminate early could be material to the financial statements of the Funds.

The Funds are also a party to Master Repurchase Agreements (Master Repo Agreements) with select counterparties. The Master Repo Agreements maintain provisions for initiation, income payments, events of default, and maintenance of collateral.

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The counterparty risk associated with certain contracts may be reduced by master netting arrangements to the extent that if an event of default occurs, all amounts with the counterparty are terminated and settled on a net basis. The Funds' overall exposure to counterparty risk with respect to transactions subject to master netting arrangements can change substantially within a short period, as it is affected by each transaction subject to the arrangement.

The Funds had credit default swap agreements and securities outstanding with Lehman Brothers entities as issuer, referenced entity, counterparty or guarantor at the time the relevant Lehman Brothers entity filed for protection or was placed in administration. Income Strategy settled all outstanding amounts from transactions with the relevant Lehman Brother's entity. The balance shown under payable to broker on the Statement of Assets and Liabilities for Income Strategy II represents the amount due to Lehman Brothers International (Europe).

3. Financial Derivative Instruments

Disclosure about derivatives and hedging activities requires qualitative disclosure regarding objectives and strategies for using derivatives, quantitative disclosure about fair value amounts of gains and losses on derivatives, and disclosure about credit-risk-related contingent features in derivative agreements. The disclosure requirements distinguish between derivatives, which are accounted for as hedges, and those that do not qualify for such accounting. Although the Funds sometimes use derivatives for hedging purposes, the Funds reflect derivatives at fair value and recognize changes in

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July 31, 2012

3. Financial Derivative Instruments (continued)

fair value through the Funds' Statements of Operations, and such derivatives do not qualify for hedge accounting treatment.

(a) Futures Contracts

The Funds use futures contracts to manage their exposure to the securities markets or the movements in interest rates and currency values. A futures contract is an agreement between two parties to buy and sell a financial instrument at a set price on a future date. Upon entering into such a contract, the Funds are required to pledge to the broker an amount of cash or securities equal to the minimum initial margin requirements of the exchange. Pursuant to the contracts, the Funds agree to receive from or pay to the broker an amount of cash or securities equal to the daily fluctuation in the value of the contracts. Such receipts or payments are known as variation margin and are recorded by the Funds as unrealized appreciation or depreciation. When the contracts are closed, the Funds record a realized gain or loss equal to the difference between the value of the contracts at the time they were opened and the value at the time they were closed. Any unrealized appreciation or depreciation recorded is simultaneously reversed. The use of futures transactions involves various risks, including the risk of an imperfect correlation in the movements in the price of futures contracts, interest rates and underlying hedging assets, and possible inability or unwillingness of counterparties to meet the terms of their contracts.

(b) Swap Agreements

Swap agreements are bilaterally negotiated agreements between a Fund and a counterparty to exchange or swap investment cash flows, assets, foreign currencies or market or event linked returns at specified, future intervals. Swap agreements may be privately negotiated in the over-the-counter market (OTC swaps) or may be executed in a multilateral or other trade facility platform, such as a registered commodities exchange (centrally cleared swaps). The Funds may enter into credit default, cross-currency, interest rate, total return, variance and other forms of swap agreements in order to, among other things, manage their exposure to credit, currency and interest rate risk. In connection with these agreements, securities may be identified as collateral or margin in accordance with the terms of the respective swap agreements to provide assets of value and recourse in the event of default or bankruptcy/insolvency.

OTC swap payments received or made at the beginning of the measurement period are reflected as such on the Funds' Statements of Assets and Liabilities and represent payments made or received upon entering into the swap agreement to compensate for differences between the stated terms of the swap agreement and prevailing market conditions (credit spreads, currency exchange rates, interest rates, and other relevant factors). These upfront payments are recorded as realized gains or losses on the Funds' Statements of Operations upon termination or maturity of the swap. A liquidation payment received or made at the termination of the swap is recorded as realized gain or loss on the Funds' Statements of Operations. Net periodic payments received or paid by the Funds are included as part of realized gains or losses on the Funds' Statements of Operations. Changes in market value, if any, are reflected as a component of net changes in unrealized appreciation/depreciation on the Funds' Statements of Operations. Daily changes in valuation of centrally cleared swaps, if any, are recorded as a receivable or payable as applicable, for variation margin on centrally cleared swaps on the Funds' Statement of Assets and Liabilities.

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Entering into these agreements involves, to varying degrees, elements of credit, legal, market and documentation risk in excess of the amounts recognized on the Funds' Statements of Assets and Liabilities. Such risks include the possibility that there will be no liquid market for these agreements, that the counterparties to the agreements may default on their obligation to perform or disagree as to the meaning of contractual terms in the agreements and that there may be unfavorable changes in interest rates.

Credit Default Swap Agreements Credit default swap agreements involve one party (referred to as the buyer of protection) making a stream of payments to another party (the seller of protection) in exchange for the right to receive a specified return in the event of a default or other credit event for the referenced entity, obligation or index. As sellers of protection on credit default swap agreements, the Funds will generally receive from the buyer of protection a fixed rate of income throughout the term of the swap provided that there is no credit event. As the sellers, the Funds would effectively add leverage to their investment portfolios because, in addition to their total net assets, the Funds would be subject to investment exposure on the notional amount of the swap.

If the Funds are sellers of protection and a credit event occurs, as defined under the terms of that particular swap agreement, a Fund will either (i) pay to the buyer of protection an amount equal to the notional amount of the swap

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3. Financial Derivative Instruments (continued)

and take delivery of the referenced obligation, other deliverable obligations or underlying securities comprising the referenced index or (ii) pay a net settlement amount in the form of cash or securities equal to the notional amount of the swap less the recovery value of the referenced obligation or underlying securities comprising the referenced index. If the Funds are buyers of protection and a credit event occurs, as defined under the terms of that particular swap agreement, a Fund will either (i) receive from the seller of protection an amount equal to the notional amount of the swap and deliver the referenced obligation, other deliverable obligations or underlying securities comprising the referenced index or (ii) receive a net settlement amount in the form of cash or securities equal to the notional amount of the swap less the recovery value of the referenced obligation or underlying securities comprising the referenced index. Recovery values are assumed by market makers considering either industry standard recovery rates or entity specific factors and considerations until a credit event occurs. If a credit event has occurred, the recovery value is determined by a facilitated auction whereby a minimum number of allowable broker bids, together with a specified valuation method, are used to calculate the settlement value.

Credit default swap agreements on corporate or sovereign issues involve one party making a stream of payments to another party in exchange for the right to receive a specified return in the event of a default or other credit event. If a credit event occurs and cash settlement is not elected, a variety of other deliverable obligations may be delivered in lieu of the specific referenced obligation. The ability to deliver other obligations may result in a cheapest to deliver option (the buyer of protection's right to choose the deliverable obligation with the lowest value following a credit event). The Funds use credit default swaps on corporate or sovereign issues to provide a measure of protection against defaults of the issuers (*i.e.*, to reduce risk where the Funds own or have exposure to the referenced obligation) or to take an active long or short position with respect to the likelihood of a particular issuer's default.

Credit default swap agreements on asset-backed securities involve one party making a stream of payments to another party in exchange for the right to receive a specified return in the event of a default or other credit events. Unlike credit default swaps on corporate or sovereign issues, deliverable obligations in most instances would be limited to the specific referenced obligation as performance for asset-backed securities can vary across deals. Prepayments, principal paydowns, and other writedown or loss events on the underlying mortgage loans will reduce the outstanding principal balance of the referenced obligation. These reductions may be temporary or permanent as defined under the terms of the swap agreement and the notional amount for the swap agreement will be adjusted by corresponding amounts. The Funds use credit default swaps on asset-backed securities to provide a measure of protection against defaults of the referenced obligation or to take an active long or short position with respect to the likelihood of a particular referenced obligation's default.

Credit default swap agreements on credit indices involve one party making a stream of payments to another party in exchange for the right to receive a specified return in the event of a write-down, principal shortfall, interest shortfall or default of all or part of the referenced entities comprising the credit index. A credit index is a basket of credit instruments or exposures designed to be representative of some part of the credit market as a whole. These indices are made up of reference credits that are judged by a poll of dealers to be the most liquid entities in the credit default swap market based on the sector of the index. Components of the indices may include, but are not limited to, investment grade securities, high yield securities, asset backed securities, emerging markets, and/or various credit ratings within each sector. Credit indices are traded using credit default swaps with standardized terms including a fixed spread and standard maturity dates. An index credit default swap references all the names in the index, and if there is a default, the credit event is settled based on that name's weight in the index, or in the case of a tranching index credit default swap, the credit event is settled based on the name's weight in the index that falls within the tranche for which the Funds bear exposure. The composition of the indices changes periodically, usually every six months, and for most indices, each name has an equal weight in the index. The Funds use credit default swaps on credit indices to hedge a portfolio of credit default swaps or bonds with a credit default swap

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on indices, which is less expensive than it would be to buy many credit default swaps to achieve a similar effect. Credit-default swaps on indices are benchmarks for protecting investors owning bonds against default, and traders use them to speculate on changes in credit quality.

Implied credit spreads, represented in absolute terms, utilized in determining the market value of credit default swap agreements on corporate or sovereign issues as of period end are disclosed later in the Notes to Financial Statements (see 5(a)) and serve as an indicator of the current status of the payment/performance risk and represent the likelihood or risk of default for the credit derivative. The implied credit spread of a particular referenced entity reflects the cost of buying/selling protection and may include upfront payments required to be made to enter into the agreement. For

PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Notes to Financial Statements

July 31, 2012

3. Financial Derivative Instruments (continued)

credit default swap agreements on asset-backed securities and credit indices, the quoted market prices and resulting values serve as the indicator of the current status of the payment/performance risk. Wider credit spreads and increasing market values, in absolute terms when compared to the notional amount of the swap, represent a deterioration of the referenced entity's credit soundness and a greater likelihood or risk of default or other credit event occurring as defined under the terms of the agreement.

The maximum potential amount of future payments (undiscounted) that the Funds as sellers of protection could be required to make under a credit default swap agreement would be an amount equal to the notional amount of the agreement. Notional amounts of all credit default swap agreements outstanding as of July 31, 2012 for which the Funds are sellers of protection are disclosed later in the Notes to Financial Statements (see 5(a)). These potential amounts would be partially offset by any recovery values of the respective referenced obligations, upfront payments received upon entering into the agreement, or net amounts received from the settlement of buy protection credit default swap agreements entered into by the Funds for the same referenced entity or entities.

Interest Rate Swap Agreements Interest rate swap agreements involve the exchange by the Funds with a counterparty of their respective commitments to pay or receive interest, e.g., an exchange of floating rate payments for fixed rate payments, with respect to the notional amount of principal. Certain forms of interest rate swap agreements may include: (i) interest rate caps, under which, in return for a premium, one party agrees to make payments to the other to the extent that interest rates exceed a specified rate, or cap, (ii) interest rate floors, under which, in return for a premium, one party agrees to make payments to the other to the extent that interest rates fall below a specified rate, or floor, (iii) interest rate collars, under which a party sells a cap and purchases a floor or vice versa in an attempt to protect itself against interest rate movements exceeding given minimum or maximum levels, (iv) callable interest rate swaps, under which the counterparty may terminate the swap transaction in whole at zero cost by a predetermined date and time prior to the maturity date, (v) spreadlocks, which allow the interest rate swap users to lock in the forward differential (or spread) between the interest rate swap rate and a specified benchmark, or (vi) basis swaps, under which two parties can exchange variable interest rates based on different money markets.

(c) Forward Foreign Currency Contracts

A forward foreign currency contract is an agreement between two parties to buy and sell a currency at a set exchange rate on a future date. The Funds enter into forward foreign currency contracts for the purpose of hedging against foreign currency risk arising from the investment or anticipated investment in securities denominated in foreign currencies. The Funds also enter into these contracts for purposes of increasing exposure to a foreign currency or shifting exposure to foreign currency fluctuations from one country to another. The market value of a forward foreign currency contract fluctuates with changes in foreign currency exchange rates. All commitments are marked to market daily at the applicable exchange rates and any resulting unrealized appreciation or depreciation is recorded. Realized gains or losses are recorded at the time the forward contract matures or by delivery of the currency. Risks may arise upon entering these contracts from the potential inability of counterparties to meet the terms of their contracts and from unanticipated movements in the value of a foreign currency relative to the U.S. dollar. In addition, these contracts may involve market risk in excess of the unrealized appreciation (depreciation) reflected in the Funds Statements of Assets and Liabilities.

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The following is a summary of the fair valuation of the Funds' derivatives categorized by risk exposure.

The effect of derivatives on the Statements of Assets and Liabilities at July 31, 2012:

Income Strategy:

Location	Interest Rate Contracts	Credit Contracts	Foreign Exchange Contracts	Total
Asset derivatives:				
Unrealized appreciation of OTC swaps	\$1,262,286	\$30,812		\$1,293,098
Unrealized appreciation of forward foreign currency contracts			\$244,879	244,879
Total asset derivatives	\$1,262,286	\$30,812	\$244,879	\$1,537,977

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Notes to Financial Statements

July 31, 2012

3. Financial Derivative Instruments (continued)

Location	Interest Rate Contracts	Credit Contracts	Foreign Exchange Contracts	Total
Liability derivatives:				
Unrealized depreciation of forward foreign currency contracts			\$(333,170)	\$(333,170)
Total liability derivatives			\$(333,170)	\$(333,170)

Income Strategy II:

Location	Interest Rate Contracts	Credit Contracts	Foreign Exchange Contracts	Total
Asset derivatives:				
Unrealized appreciation of OTC swaps	\$2,653,139			\$2,653,139
Unrealized appreciation of forward foreign currency contracts			\$1,310,801	1,310,801
Total asset derivatives	\$2,653,139		\$1,310,801	\$3,963,940
Liability derivatives:				
Unrealized depreciation of forward foreign currency contracts			\$(675,651)	\$(675,651)
Total liability derivatives			\$(675,651)	\$(675,651)

The effect of derivatives on the Statements of Operations for the year ended July 31, 2012:

Income Strategy:

Location	Interest Rate Contracts	Credit Contracts	Foreign Exchange Contracts	Total
Net realized gain (loss) on:				
Futures contracts	\$998,969			\$998,969
Swaps	(9,783,521)	\$45,750		(9,737,771)
Foreign currency transactions (forward foreign currency contracts)			\$3,054,121	3,054,121
Total net realized gain (loss)	\$(8,784,552)	\$45,750	\$3,054,121	\$(5,684,681)
Net change in unrealized appreciation/depreciation of:				
Futures contracts	\$577,182			\$577,182

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Swaps	2,049,315	\$(24,191)		2,025,124
Foreign currency transactions (forward foreign currency contracts)			\$934,111	934,111
Total net change in unrealized appreciation/depreciation	\$1,472,133	\$(24,191)	\$934,111	\$2,382,053

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Notes to Financial Statements

July 31, 2012

3. Financial Derivative Instruments (continued)

Income Strategy II:

Location	Interest Rate Contracts	Credit Contracts	Foreign Exchange Contracts	Total
Net realized gain (loss) on:				
Futures contracts	\$1,837,275			\$1,837,275
Swaps	(13,714,812)			(13,714,812)
Foreign currency transactions (forward foreign currency contracts)			\$12,077,002	12,077,002
Total net realized gain (loss)	\$(11,877,537)		\$12,077,002	\$199,465
Net change in unrealized appreciation/depreciation of:				
Futures contracts	\$(890,772)			\$(890,772)
Swaps	3,674,345			3,674,345
Foreign currency transactions (forward foreign currency contracts)			\$3,930,931	3,930,931
Total net change in unrealized appreciation/depreciation	\$2,783,573		\$3,930,931	\$6,714,504

The average volume (measured at each fiscal quarter-end) of derivative activity during the year ended July 31, 2012:

	Futures Contracts (1)	Forward Foreign Currency Contracts (2)		Credit Default Swap Agreements (3)	Interest Rate Swap Agreements (3)
	Long	Purchased	Sold	Sell	
Income Strategy	147	\$15,419,647	\$72,860,455	\$1,500	\$73,860
Income Strategy II	303	25,210,237	200,560,558		144,380

(1) Number of contracts

(2) U.S. \$ value on origination date

(3) Notional amount (in thousands)

4. Investment Manager/Sub-Adviser

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Each Fund has an Investment Management Agreement (each an Agreement) with the Investment Manager. Subject to the supervision of each Fund's Board of Trustees, the Investment Manager is responsible for managing, either directly or through others selected by it, the Funds' investment activities, business affairs and administrative matters. Pursuant to each Agreement, the Investment Manager receives an annual fee, payable monthly, at an annual rate of 0.75% of each Fund's average weekly total managed assets. Total managed assets refer to the total assets of each Fund (including assets attributable to any Preferred Shares or other forms of leverage that may be outstanding) minus accrued liabilities (other than liabilities representing leverage).

The Investment Manager has retained the Sub-Adviser to manage the Funds' investments. Subject to the supervision of the Investment Manager, the Sub-Adviser is responsible for making all of the Funds' investment decisions. The Investment Manager, and not the Funds, pays a portion of the fees it receives as Investment Manager to the Sub-Adviser in return for its services.

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**PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Notes to Financial Statements**

July 31, 2012

5. Investments in Securities

For the year ended July 31, 2012, purchases and sales of investments, other than short-term securities were:

	Purchases	Sales
Income Strategy	\$91,639,048	\$131,700,316
Income Strategy II	135,414,459	155,916,647

(a) OTC credit default swap agreements outstanding at July 31, 2012:

Sell protection swap agreements:

Income Strategy:

Swap

Counterparty/ Referenced	Notional Amount	Credit Spread	Termination Date	Payments Received	Market Value (2)	Upfront Premiums Paid	Unrealized Appreciation
Debt Issuer Goldman Sachs: HCA	(000s) (1) \$1,500	1.47%	9/20/13	3.00%	\$30,812		\$30,812

(1) This represents the maximum potential amount the Funds could be required to make available as a seller of credit protection or receive as a buyer of credit protection if a credit event occurs as defined under the terms of that particular swap agreement.

(2) The quoted market prices and resulting values for credit default swap agreements serve as an indicator of the status at July 31, 2012 of the payment/performance risk and represent the likelihood of an expected liability (or profit) for the credit derivative should the notional amount of the swap agreement be closed/sold as of the period end. Increasing market values, in absolute terms when compared to the notional amount of the swap, represent a deterioration of the referenced entity's credit soundness and a greater likelihood or risk of default or other credit event occurring as defined under the terms of the agreement.

(b) OTC Interest rate swap agreements outstanding at July 31, 2012:

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Income Strategy:

	Notional		Rate Type			Upfront	
Swap	Amount	Termination	Payments	Payments	Market	Premiums	Unrealized
Counterparty	(000s)	Date	Made	Received	Value	Paid	Appreciation
Royal Bank of Scotland	\$216,000	5/29/18	3-Month USD-LIBOR	1.75%	\$2,303,127	\$1,040,841	\$1,262,286

Income Strategy

II:

	Notional		Rate Type			Upfront	
Swap	Amount	Termination	Payments	Payments	Market	Premiums	Unrealized
Counterparty	(000s)	Date	Made	Received	Value	Paid	Appreciation
Royal Bank of Scotland	\$454,000	5/29/18	3-Month USD-LIBOR	1.75%	\$4,840,833	\$2,187,694	\$2,653,139

LIBOR London Inter-Bank Offered Rate

PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Notes to Financial Statements

July 31, 2012

5. Investments in Securities (continued)

(c) Forward foreign currency contracts outstanding at July 31, 2012:

Income Strategy:

	Counterparty	U.S.\$ Value on Origination Date	U.S.\$ Value July 31, 2012	Unrealized Appreciation (Depreciation)
<u>Purchased:</u>				
10,076,000 British Pound settling 8/2/12	Barclays Bank	\$15,806,221	\$15,797,659	\$(8,562)
7,152,000 British Pound settling 8/2/12	JPMorgan Chase	11,198,602	11,213,266	14,664
10,076,000 British Pound settling 8/2/12	UBS	15,874,738	15,797,660	(77,078)
6,975,000 Chinese Yuan Renminbi settling 2/1/13	UBS	1,112,706	1,085,731	(26,975)
4,598,000 Euro settling 8/2/12	Deutsche Bank	5,636,688	5,657,378	20,690
7,492,955 Mexican Peso settling 8/15/12	HSBC Bank	558,926	562,760	3,834
303,427 Mexican Peso settling 8/15/12	UBS	22,076	22,789	713
<u>Sold:</u>				
10,076,000 British Pound settling 9/4/12	Barclays Bank	15,805,647	15,797,357	8,290
27,304,000 British Pound settling 8/2/12	JPMorgan Chase	42,635,196	42,808,584	(173,388)
7,152,000 British Pound settling 9/4/12	JPMorgan Chase	11,197,879	11,213,051	(15,172)
10,076,000 British Pound settling 9/4/12	UBS	15,873,831	15,797,357	76,474
6,975,000 Chinese Yuan Renminbi settling 2/1/13	JPMorgan Chase	1,112,263	1,085,732	26,531
4,598,000 Euro settling 8/2/12	BNP Paribas	5,739,821	5,657,378	82,443
4,598,000 Euro settling 10/15/12	Deutsche Bank	5,642,091	5,662,584	(20,493)
220,000 Euro settling 10/15/12	HSBC Bank	269,958	270,937	(979)
7,603,000 Euro settling 10/15/12	UBS	9,367,550	9,363,337	4,213
2,756,000 Mexican Peso settling 8/15/12	Barclays Bank	200,000	206,990	(6,990)
7,492,955 Mexican Peso settling 12/3/12	HSBC Bank	553,353	556,886	(3,533)
5,040,382 Mexican Peso settling 8/15/12	JPMorgan Chase	385,586	378,559	7,027
				\$(88,291)

PIMCO Income Strategy Fund

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PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Notes to Financial Statements

July 31, 2012

5. Investments in Securities (continued)

Income Strategy II:

	Counterparty	U.S.\$ Value on Origination Date	U.S.\$ Value July 31, 2012	Unrealized Appreciation (Depreciation)
<u>Purchased:</u>				
20,743,000 British Pound settling 8/2/12	Barclays Bank	\$32,539,544	\$32,521,918	\$(17,626)
90,000 British Pound settling 9/4/12	Barclays Bank	139,431	141,104	1,673
4,252,000 British Pound settling 8/2/12	BNP Paribas	6,591,293	6,666,499	75,206
14,724,000 British Pound settling 8/2/12	JPMorgan Chase	23,054,839	23,085,028	30,189
20,744,000 British Pound settling 8/2/12	UBS	32,682,172	32,523,486	(158,686)
14,273,000 Chinese Yuan Renminbi settling 2/1/13	UBS	2,276,940	2,221,741	(55,199)
83,000 Euro settling 9/14/12	Citigroup	101,979	102,174	195
14,974,902 Mexican Peso settling 8/15/12	HSBC Bank	1,117,030	1,124,694	7,664
562,719 Mexican Peso settling 8/15/12	UBS	40,941	42,263	1,322
<u>Sold:</u>				
20,743,000 British Pound settling 9/4/12	Barclays Bank	32,538,362	32,521,296	17,066
60,463,000 British Pound settling 8/2/12	JPMorgan Chase	94,412,975	94,796,932	(383,957)
14,724,000 British Pound settling 9/4/12	JPMorgan Chase	23,053,352	23,084,586	(31,234)
20,744,000 British Pound settling 9/4/12	UBS	32,680,305	32,522,864	157,441
14,273,000 Chinese Yuan Renminbi settling 2/1/13	JPMorgan Chase	2,276,033	2,221,742	54,291
57,246,000 Euro settling 9/14/12	Citigroup	71,422,399	70,470,626	951,773
1,808,000 Euro settling 9/14/12	HSBC Bank	2,217,548	2,225,673	(8,125)
1,378,000 Mexican Peso settling 8/15/12	Barclays Bank	100,000	103,495	(3,495)
1,376,530 Mexican Peso settling 8/15/12	HSBC Bank	100,000	103,385	(3,385)
14,974,902 Mexican Peso settling 12/3/12	HSBC Bank	1,105,894	1,112,953	(7,059)
10,028,491 Mexican Peso settling 8/15/12	JPMorgan Chase	767,173	753,192	13,981
2,754,600 Mexican Peso settling 8/15/12	Morgan Stanley	200,000	206,885	(6,885)
				\$635,150

PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Notes to Financial Statements

July 31, 2012

5. Investments in Securities (continued)

At July 31, 2012, Income Strategy and Income Strategy II held \$2,295,000 and \$5,230,000, respectively, in cash as collateral for derivatives. Cash collateral held may be invested in accordance with the Funds' investment strategies.

(d) Open reverse repurchase agreements at July 31, 2012:

Income Strategy:

Counterparty	Rate	Trade Date	Due Date	Principal & Interest	Principal
Barclays Bank	0.60%	5/23/12	8/23/12	\$1,888,200	\$1,886,000
	0.60	6/22/12	8/17/12	872,581	872,000
	0.60	7/2/12	8/17/12	2,033,016	2,032,000
	0.80	6/22/12	8/17/12	5,145,570	5,141,000
Deutsche Bank	0.65	5/31/12	8/28/12	2,319,594	2,317,000
	0.65	6/15/12	9/17/12	1,198,016	1,197,000
	0.65	7/11/12	10/11/12	2,991,134	2,990,000
	0.75	5/17/12	8/17/12	916,449	915,000
	0.75	6/1/12	8/28/12	2,687,411	2,684,000
	0.80	5/24/12	8/28/12	5,797,876	5,789,000
	0.80	7/5/12	10/5/12	5,652,389	5,649,000
	0.80	7/26/12	10/22/12	1,837,245	1,837,000
UBS	0.50	5/4/12	8/6/12	770,952	770,000
	0.52	6/15/12	9/18/12	601,408	601,000
	0.55	7/31/12	10/26/12	12,452,000	12,452,000
	0.57	6/15/12	9/18/12	1,953,453	1,952,000
	0.58	5/1/12	8/2/12	984,457	983,000
	0.58	5/7/12	8/7/12	2,682,712	2,679,000
	0.58	7/12/12	10/4/12	1,191,384	1,191,000
	1.00	2/27/12	8/29/12	3,303,252	3,289,000
					\$57,226,000

Income Strategy II:

Counterparty	Rate	Trade Date	Due Date	Principal & Interest	Principal
Barclays Bank	1.00%	2/24/12	8/24/12	\$23,763,494	\$23,659,000
Deutsche Bank	0.65	5/8/12	8/9/12	1,524,336	1,522,000

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UBS	0.50	5/11/12	8/7/12	3,375,840	3,372,000
	0.54	7/25/12	10/26/12	6,841,718	6,841,000
	0.55	5/7/12	8/7/12	2,911,821	2,908,000
	0.57	7/25/12	10/26/12	8,458,937	8,458,000
	0.58	7/6/12	8/7/12	1,670,700	1,670,000
	0.58	7/31/12	10/26/12	9,162,000	9,162,000
					\$57,592,000

The weighted average daily balance of reverse repurchase agreements outstanding during the year ended July 31, 2012 for Income Strategy and Income Strategy II was \$67,982,626 and \$82,689,279, respectively, at a weighted average interest rate of 0.74% and 0.77%, respectively. The total market value of underlying collateral (refer to the Schedules of Investments for positions transferred for the benefit of the counterparty as collateral) for open reverse repurchase agreements at July 31, 2012 was \$50,386,616 and \$53,654,274 for Income Strategy and Income Strategy II, respectively.

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PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Notes to Financial Statements

July 31, 2012

5. Investments in Securities (continued)

At July 31, 2012, Income Strategy held \$1,294,208 in principal value of U.S. Treasury Obligations, and \$210,000 in Corporate Bonds as collateral for open reverse repurchase agreements. Income Strategy II held \$2,091,687 in principal value of U.S. Treasury Obligations as collateral for open reverse repurchase agreements. Securities held as collateral will not be pledged and are not reflected in the Schedules of Investments.

6. Income Tax Information

The tax character of dividends paid was:

	Year Ended July 31, 2012	Year Ended July 31, 2011
	Ordinary Income Distributions	Ordinary Income Distributions
Income Strategy	\$28,644,677	\$31,123,205
Income Strategy II	50,442,876	58,656,809

At July 31, 2012, the components of distributable earnings was:

	Ordinary Income	Capital Loss Carryforwards (1)	Post-October Short-Term Capital Loss (2)	Long-Term Capital Loss (2)
Income Strategy	\$8,885,967	\$171,440,617		
Income Strategy II	30,784,537	433,747,763		\$6,483,927

(1) Capital loss carryforwards available as a reduction, to the extent provided in the regulations, of any future net realized gains. To the extent that these losses are used to offset future realized capital gains, such gains will not be disbursed.

(2) Capital losses realized during the period November 1, 2011 through July 31, 2012 which the Funds elected to defer to the following taxable year pursuant to income tax regulations.

Under the Regulated Investment Company Modernization Act of 2010, the Funds will be permitted to carry forward capital losses incurred in taxable years beginning after December 22, 2010, for an unlimited period. However, any losses incurred during those future taxable years will be required to be utilized prior to the losses incurred in pre-enactment taxable years. As a result of this, pre-enactment capital loss carryforwards

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may be more likely to expire unused. Additionally, post-enactment capital losses that are carried forward will retain their character as either short-term or long-term capital losses rather than being considered all short-term capital losses.

At July 31, 2012, capital loss carryforward amounts was:

		Year of Expiration		No Expiration (3)	
	2016	2017	2018	Short-Term	Long-Term
Income Strategy		\$61,958,740	\$106,314,659	\$3,167,218	
Income Strategy II	\$3,057,541	145,330,255	277,492,526	7,867,441	

(3) *Carryforward amounts are subject to the provisions of the Regulated Investment Company Modernization Act of 2010.*

PIMCO Income Strategy Fund/PIMCO Income Strategy Fund II
Notes to Financial Statements

July 31, 2012

6. Income Tax Information (continued)

For the year ended July 31, 2012, permanent book-tax adjustments were:

	Undistributed Net Investment Income	Accumulated Net Realized Loss	Paid-In-Capital In Excess of Par
Income Strategy (a)(b)(c)(d)	\$3,523,993	\$(3,523,965)	\$(28)
Income Strategy II (a)(b)(c)	12,638,401	(12,638,401)	

These permanent book-tax differences were primarily attributable to:

- (a) Differing treatment of swap payments.
- (b) Reclassification of gains and losses on foreign currency transactions.
- (c) Reclassification of paydown losses.
- (d) Consent fees.