

PIMCO INCOME STRATEGY FUND  
Form N-CSRS  
March 29, 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: January 31, 2012

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Item 1: Report to Shareholders

January 31, 2012



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Dear Shareholder:

The U.S. economy gained momentum during the six-month fiscal period ended January 31, 2012. Expansion was reflected by growth in key sectors such as manufacturing and construction, and by companies that increased capital expenditures and hiring. This in turn boosted consumer confidence and helped push unemployment to its lowest level in three years. Growth was held back by political dysfunction in Washington and a spate of geopolitical worries, which at times sparked extraordinary market volatility.

### Six-Month Period in Review through January 31, 2012

For the six-month period ended January 31, 2012:

- PIMCO Income Strategy Fund returned -3.04 % on net asset value ( NAV ) and -4.70 % on market price.
- PIMCO Income Strategy Fund II returned -2.19% on NAV and 0.92 % on market price.

The Barclays Capital U.S. Credit Index, a measure of high quality corporate bond performance, advanced 4.45% and the Barclays Capital U.S. High Yield Bond Index, a measure of below investment-grade corporate bond performance, rose 1.86% during the reporting period. Government bonds, as represented by the Barclays Capital Long Term Treasury Index, returned 21.68%. The Barclays Capital U.S. Aggregate Bond Index, a broad credit market measure of government and corporate securities, rose 4.25%, and mortgage-backed securities, reflected by the Barclays Capital Mortgage Index, advanced 2.77%. As for stocks, the Standard & Poor's 500 Index increased 2.71% during the six-month 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 2.8% annual rate (preliminary estimate) between October and December 2011. This was a marked improvement from the preceding two quarters, in which annualized growth was 0.4% and 1.3%, respectively. The latest Beige Book report from the Federal Reserve ( the Fed ), released in January 2012, indicated economic expansion in all but one of twelve banking districts across the country. The central bank described auto manufacturing as vibrant, and signified consumer spending was growing more robust. The labor market also

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improved, as the U.S. unemployment rate dropped from 9.1% to 8.3% during the six-month reporting period. The government indicated that private sector job creation during 2011 was the best since 2005.

As the economy expanded, U.S. companies continued to post strong results. The Commerce Department reported that profits were approximately \$1.97 trillion (seasonally adjusted at annualized rates) between July and September 2011. Corporate strength was reflected in Fed data signifying non-financial companies holding in excess of \$2 trillion in cash and other liquid assets at the end of June 2011. Relative to total corporate assets, this was the highest level since 1963.

### **The Road Ahead**

Despite the improving U.S. economy, actions taken by the Fed during the six-month period indicate caution. The Fed extended its policy of maintaining low interest rates at least through late 2014 and began another effort to stimulate the economy by swapping \$400 billion in short-term Treasury securities in exchange for a similar amount of longer-term bonds. The lower long-term yields, the Fed intimated, could help breathe life into the housing market. Concerned with Europe's deepening sovereign debt crisis, the Fed warned of significant downside risks to the economic outlook, including strains in global financial markets.

**Receive this report electronically and eliminate paper mailings. To enroll, go to [www.allianzinvestors.com/edelivery](http://www.allianzinvestors.com/edelivery).**

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](http://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

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

January 31, 2012 (unaudited)

For the six months ended January 31, 2012, PIMCO Income Strategy Fund returned -3.04% on net asset value ( NAV ) and -4.70% on market price.

For the six months ended January 31, 2012, PIMCO Income Strategy Fund II returned -2.19% on NAV and 0.92% on market price.

The unmanaged Barclays Capital U.S. Aggregate Bond Index and Barclays Capital U.S. Credit Index returned 4.25% and 4.45%, respectively, during the six month reporting period ended January 31, 2012.

The overall U.S. fixed income market, as measured by the Barclays Capital U.S. Aggregate Bond Index, generated a 4.25% return during the reporting period. However, there were periods of heightened volatility due to shifting expectations for the economy and periodic flights to quality. During the first two months of the period, most spread sectors (non-U.S. Treasuries) underperformed equal-duration Treasuries. Investor risk aversion was elevated during that time given Standard & Poor's downgrade of U.S. government securities, concerns of moderating global economic growth and an escalation of the European sovereign debt crisis. However, during the last four months of the reporting period, investor risk aversion was generally replaced with risk appetite. Triggering this shift in investor sentiment were signs that the U.S. economy was gaining some momentum and hopes for progress in the European sovereign debt crisis. During the six months ended January 31, 2012, both short- and long-term Treasury yields declined and the yield curve flattened. In this environment, spread sectors produced mixed results versus equal-duration Treasuries.

Despite a setback when investor risk aversion was elevated in August and September 2011, the U.S. corporate bond market posted a positive return during the reporting period. Supporting corporate bond prices were generally strong corporate profits, strengthening corporate balance sheets and improving demand from investors seeking to generate incremental yield in the low interest rate environment.

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**Sector exposures largely detracted from the Funds' performance**

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

An underweighting to retailers detracted from performance, as consumer spending increased toward the end of 2011. An overweighting to the banking sector adversely impacted performance as increased European sovereign debt concerns and uncertainties surrounding new financial regulations hindered results. Security selection within insurance companies also detracted from returns, as select life insurance companies underperformed the broader insurance sector. The Funds' underweighting to technology hindered results as this sector outperformed the overall credit market due to growth in mobile devices.

On the upside, an allocation to Build America Bonds was rewarded, as these subsidized taxable municipal securities generally outperformed the broader market. An underweighting to metals and mining also contributed to results, as slower emerging market growth caused this sector to perform poorly.



**PIMCO Income Strategy Fund  
Performance & Statistics**

January 31, 2012 (unaudited)

<b>Total Return(1):</b>	<b>Market Price</b>	<b>NAV</b>
Six Month	-4.70%	-3.04%
1 Year	-0.06%	1.75%
5 Year	0.42%	1.16%
Commencement of Operations (8/29/03) to 1/31/12	3.77%	3.63%

**Market Price/NAV Performance:**

Commencement of Operations (8/29/03) to 1/31/12

Market Price

NAV

**Market Price/NAV:**

Market Price

NAV

Premium to NAV

Market Price Yield(2)

\$11.13

\$10.40

7.02%

8.09%

**Moody's Ratings**

(as a % of total investments)

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

January 31, 2012 (unaudited)

<b>Total Return(1):</b>	<b>Market Price</b>	<b>NAV</b>
Six Month	0.92%	-2.19%
1 Year	3.43%	0.92%
5 Year	-1.36%	-1.57%
Commencement of Operations (10/29/04) to 1/31/12	1.27%	1.19%

**Market Price/NAV Performance:**

Commencement of Operations (10/29/04) to 1/31/12

Market Price  
NAV

**Market Price/NAV:**

Market Price	\$9.93
NAV	\$9.41
Premium to NAV	5.53%
Market Price Yield(2)	7.85%

**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 less than one year is not annualized. 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 the Funds' 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 per common share dividend (comprised of net investment income) payable to common shareholders by the market price per common share at January 31, 2012.

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**PIMCO Income Strategy Fund Schedule of Investments**

January 31, 2012 (unaudited)

Principal Amount (000s)		Value	
<b>CORPORATE BONDS &amp; NOTES</b>	<b>55.0%</b>		
<b>Airlines</b>	<b>0.2%</b>		
	\$3,774	American Airlines Pass Through Trust, 9.73%, 9/29/14 (e)	\$905,616
<b>Banking</b>	<b>8.2%</b>		
	2,600	AgFirst Farm Credit Bank, 7.30%, 3/1/12 (a) (b) (d) (g) (j) (acquisition cost-\$2,225,000; purchased 2/26/10-4/15/10)	2,659,116
	£7,800	Barclays Bank PLC, 14.00%, 6/15/19 (g)	14,749,495
	3,000	Cooperatieve Centrale Raiffeisen-Boerenleenbank BA, 6.875%, 3/19/20	3,714,034
	\$4,400	11.00%, 6/30/19 (a) (d) (g) (i)	5,470,987
	600	HBOS PLC, 6.75%, 5/21/18 (a) (d)	528,735
	800	Regions Financial Corp., 7.375%, 12/10/37	717,000
	1,500	7.75%, 9/15/24	1,342,500
	£2,000	Santander Issuances S.A. Unipersonal, 7.30%, 7/27/19, (converts to FRN on 9/27/14)	2,757,692
			31,939,559
<b>Chemicals</b>	<b>0.2%</b>		
	\$624	Lyondell Chemical Co., 8.00%, 11/1/17	698,880
<b>Consumer Products</b>	<b>0.2%</b>		
	800	Reynolds Group Issuer, Inc., 9.00%, 4/15/19 (a) (d)	800,000
<b>Energy</b>	<b>0.1%</b>		
	1,100	Dynergy Roseton/Danskammer Pass Through Trust, 7.67%, 11/8/16 Ser. B (e)	638,000
<b>Financial Services</b>	<b>27.1%</b>		
	304	Ally Financial, Inc., 5.90%, 1/15/19	277,871
	156	5.90%, 10/15/19	137,554
	55	6.00%, 2/15/19	48,908
	90	6.00%, 3/15/19	80,056
	8	6.00%, 4/15/19	7,103
	325	6.00%, 9/15/19	288,947
	95	6.05%, 8/15/19	84,699
	413	6.05%, 10/15/19	367,976
	31	6.125%, 10/15/19	27,752
	1,208	6.15%, 8/15/19	1,085,269
	1,371	6.25%, 2/15/16	1,281,664
	25	6.25%, 1/15/19	23,307
	120	6.30%, 8/15/19	108,813
	1,168	6.35%, 2/15/16	1,095,836
	285	6.35%, 4/15/16	266,748
	216	6.40%, 3/15/16	202,777
	360	6.40%, 11/15/19	323,790
	1,357	6.50%, 2/15/16	1,280,032
	20	6.50%, 9/15/16	18,728
	442	6.50%, 10/15/16	413,464
	170	6.50%, 12/15/18	160,901
	22	6.50%, 5/15/19	20,427
	358	6.55%, 12/15/19	324,797
	14	6.60%, 5/15/18	12,864

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**PIMCO Income Strategy Fund Schedule of Investments**

January 31, 2012 (unaudited) (continued)

Principal Amount (000s)		Value
<b>Financial Services</b> (continued)		
\$60	6.70%, 6/15/18	\$55,908
329	6.75%, 4/15/13	327,487
3	6.75%, 8/15/16	2,900
13	6.75%, 6/15/17	12,363
89	6.75%, 5/15/19	82,595
10	6.75%, 6/15/19	9,277
205	6.80%, 9/15/16	194,291
3	6.80%, 10/15/18	2,804
938	6.85%, 4/15/16	897,501
30	6.85%, 5/15/18	27,941
336	6.875%, 8/15/16	319,675
5	6.875%, 7/15/18	4,696
140	6.90%, 6/15/17	131,182
32	6.90%, 8/15/18	30,097
151	6.95%, 6/15/17	144,724
25	7.00%, 12/15/16	23,833
27	7.00%, 6/15/17	25,414
130	7.00%, 7/15/17	122,676
367	7.00%, 2/15/18	345,635
12	7.00%, 3/15/18	11,170
155	7.00%, 8/15/18	147,077
5	7.00%, 9/15/18	4,787
42	7.05%, 3/15/18	39,221
39	7.05%, 4/15/18	36,723
160	7.125%, 10/15/17	152,344
40	7.15%, 3/15/25	36,781
75	7.20%, 10/15/17	71,981
288	7.25%, 6/15/16	279,329
293	7.25%, 9/15/17	280,282
10	7.25%, 4/15/18	9,507
10	7.25%, 8/15/18	9,575
328	7.25%, 9/15/18	314,230
25	7.30%, 1/15/18	23,638
396	7.35%, 4/15/18	378,549
57	7.50%, 6/15/16	55,929
45	7.55%, 5/15/16	44,256
47	7.75%, 10/15/17	46,086
110	8.125%, 11/15/17	107,945
110	9.00%, 7/15/20	110,379
750	Bank of America Corp., 6.00%, 9/1/17	786,898
1,400	Capital One Capital VI, 8.875%, 5/15/40	1,480,014
	CIT Group, Inc.,	
1,251	7.00%, 5/1/16	1,252,758
2,210	7.00%, 5/1/17	2,215,952
2,500	Citigroup Capital XXI, 8.30%, 12/21/77, (converts to FRN on 12/21/37)	2,550,750
	Credit Agricole S.A. (g),	
2,500	6.637%, 5/31/17 (a) (d)	1,796,875
£1,000	8.125%, 10/26/19	1,189,730

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\$15,500	Ford Motor Credit Co. LLC, 8.00%, 12/15/16 (i)	18,391,664
4,600	8.125%, 1/15/20	5,647,351
7,000	ILFC E-Capital Trust I, 4.34%, 12/21/65, FRN (a) (d) (i)	4,457,390

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**PIMCO Income Strategy Fund Schedule of Investments**

January 31, 2012 (unaudited) (continued)

Principal Amount (000s)		Value
<b>Financial Services (continued)</b>		
	LBG Capital No.1 PLC,	
500	6.439%, 5/23/20	\$513,409
200	7.375%, 3/12/20	206,672
£300	7.588%, 5/12/20	387,647
£4,800	7.867%, 12/17/19	6,315,809
£700	7.869%, 8/25/20	915,540
\$2,500	7.875%, 11/1/20 (a) (d)	2,100,000
1,400	8.00%, 6/15/20 (a) (d) (g)	1,127,000
2,000	8.50%, 12/17/21 (a) (d) (g)	1,390,000
£900	11.04%, 3/19/20	1,379,220
	LBG Capital No.2 PLC,	
£534	9.125%, 7/15/20	723,671
£2,500	11.25%, 9/14/23	3,584,947
\$1,500	Lehman Brothers Holdings, Inc., 7.50%, 5/11/38 (e)	1,650
1,500	National City Preferred Capital Trust I, 12.00%, 12/10/12 (g) (i)	1,603,299
5,000	PNC Financial Services Group, Inc., 6.75%, 8/1/21 (g) (i)	5,193,175
1,000	PNC Preferred Funding Trust I, 6.517%, 3/15/12 (a) (d) (g)	745,000
3,700	Royal Bank of Scotland Group PLC, 7.648%, 9/30/31 (g)	2,886,000
	SLM Corp.,	
400	6.25%, 1/25/16	408,764
6,200	8.00%, 3/25/20 (i)	6,618,500
6,400	8.45%, 6/15/18 (i)	6,960,000
2,168	SMFG Preferred Capital USD 3 Ltd., 9.50%, 7/25/18 (a) (d) (g)	2,563,660
8,200	Springleaf Finance Corp., 6.50%, 9/15/17 (i)	5,986,000
900	State Street Capital Trust III, 5.536%, 3/1/12 (g)	902,871
500	USB Capital IX, 3.50%, 3/1/12 (g)	374,725
		105,565,440
<b>Insurance 12.8%</b>		
10,000	American General Capital II, 8.50%, 7/1/30 (i)	9,859,550
1,600	American General Institutional Capital A, 7.57%, 12/1/45 (a) (d)	1,432,000
	American General Institutional Capital B, 8.125%, 3/15/46	
2,000	(a) (d) (i)	1,885,000
	American International Group, Inc.,	
4,000	6.25%, 3/15/87, (converts to FRN on 3/15/37) (i)	3,180,000
£591	6.765%, 11/15/17 (a) (d)	929,727
	6.797%, 11/15/17 (a) (b) (d) (j) (acquisition cost-\$1,829,737;	
1,995	purchased 5/21/10)	2,596,021
MXN8,000	7.98%, 6/15/17	579,388
1,900	8.00%, 5/22/68, (converts to FRN on 5/22/18) (a) (d)	2,124,927
\$8,200	8.175%, 5/15/68, (converts to FRN on 5/15/38) (i)	7,995,000
4,400	8.25%, 8/15/18 (i)	5,081,767
£650	8.625%, 5/22/68, (converts to FRN on 5/22/18)	898,285
\$2,200	Dai-ichi Life Insurance Co., Ltd., 7.25%, 7/25/21 (a) (d) (g) (i)	2,302,357
	Hartford Financial Services Group, Inc., 8.125%, 6/15/68,	
2,300	(converts to FRN on 6/15/18)	2,420,750
	MetLife Capital Trust IV, 7.875%, 12/15/67, (converts to FRN on	
2,000	12/15/37) (a) (d) (i)	2,145,000
	MetLife Capital Trust X, 9.25%, 4/8/68, (converts to FRN on	
3,300	4/8/38) (a) (d) (i)	3,918,750



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2,440	Progressive Corp., 6.70%, 6/15/67, (converts to FRN on 6/15/17) (i)	2,503,799 49,852,321
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**PIMCO Income Strategy Fund Schedule of Investments**

January 31, 2012 (unaudited) (continued)

Principal Amount (000s)		Value
<b>Oil &amp; Gas 2.4%</b>		
	NGPL PipeCo LLC (a) (d), 7.119%, 12/15/17	\$4,467,980
\$5,000	7.768%, 12/15/37 (i)	4,243,715
5,000	SandRidge Energy, Inc., 8.00%, 6/1/18 (a) (d)	624,000
600		9,335,695
<b>Telecommunications 3.1%</b>		
	CenturyLink, Inc., 6.00%, 4/1/17	842,322
800	7.60%, 9/15/39 (i)	11,212,839
11,000		12,055,161
<b>Utilities 0.7%</b>		
	AES Andres Dominicana Ltd., 9.50%, 11/12/20 (a) (d)	1,947,500
1,900	Dominion Resources, Inc., 2.879%, 9/30/66, FRN	340,351
390	PPL Capital Funding, Inc., 6.70%, 3/30/67, (converts to FRN on 3/30/17)	395,424
400		2,683,275
		214,473,947
Total Corporate Bonds & Notes (cost-\$214,560,448)		
<b>MUNICIPAL BONDS 23.2%</b>		
<b>California 10.0%</b>		
	Alameda Cnty. Joint Powers Auth. Rev., 7.046%, 12/1/44, Ser. A	11,088,852
9,200	Fresno Cnty. Rev., zero coupon, 8/15/24, Ser. A (FGIC-NPFGC)	1,357,170
3,000	Golden State Tobacco Securitization Corp. Rev., 5.125%, 6/1/47, Ser. A-1	3,408,250
5,000	Long Beach Redev. Agcy., Tax Allocation, 8.36%, 8/1/40	984,609
900	Los Angeles Cnty. Public Works Financing Auth. Rev., 7.618%, 8/1/40	9,925,904
7,600	Oakland Unified School Dist., Alameda Cnty., GO, 9.50%, 8/1/34	1,239,150
1,100	Riverside Cnty. Dev. Agcy., Tax Allocation, 7.50%, 10/1/30, Ser. A-T	618,372
600	Riverside Electric Rev., 7.605%, 10/1/40	1,354,590
1,000	San Luis Obispo Cnty. Rev., zero coupon, 9/1/27, Ser. C (NPFGC)	371,980
1,000	San Marcos Unified School Dist., GO, zero coupon, 8/1/32	137,468
400	State Public Works Board Rev., 7.804%, 3/1/35, Ser. B-2	4,531,320
4,000	Stockton Public Financing Auth. Rev., 7.942%, 10/1/38, Ser. B	3,947,544
3,600		38,965,209
<b>Colorado 1.3%</b>		
	Denver Public Schools, CP, 7.017%, 12/15/37, Ser. B	5,130,360
4,000		
<b>District of Columbia 2.2%</b>		
	Metropolitan Airports Auth. Rev., 7.462%, 10/1/46	8,405,400
7,500		
<b>Nevada 2.9%</b>		
	Las Vegas Valley Water Dist., GO, 7.263%, 6/1/34	11,419,400
10,000		
<b>New Jersey 0.6%</b>		
	Middlesex Cnty. Improvement Auth. Rev. (AGM-GTD), zero coupon, 10/1/22	1,098,693
1,935	zero coupon, 10/1/23	1,306,944
2,455		2,405,637

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