Annual Report 1998

Premium Income Corporation

Mulvihill Capital Management Inc.

CONTENTS

MESSAGE TO UNITHOLDERS

Premium Income Corporation was launched in October, 1996 with the objective of providing investors with a superior yield alternative to conventional income products.

A summary of the company's investments as well as its financial statements are included within this annual report.

The year ended October 31, 1998 represented a time of extremes within the Financial Services industry. The year began with record quarterly earnings announcements, merger proposals from four of the six major banks and a general feeling of continued optimism with respect to corporate earnings prospects. The year ended with the lingering effects of the Asian flu, growing concern over the probability of the mergers being approved, and a decline in the quarterly earnings growth of the Banks.

In this context, realized earnings of the corporations were strong as several special distributions were made to unitholders in addition to the regular quarterly distributions.

We would like to take this opportunity to once again thank investors for their continuing support during 1998 and we look forward to a mutually beneficial relationship in 1999.

John P. Mulvihill
President & CEO

Donald Biggs
Vice President

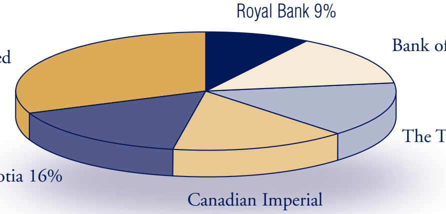
INVESTMENT OBJECTIVES

The Company's investment objectives are (i) to provide holders of Preferred Shares with cumulative preferential quarterly cash dividends in the amount of $0.215625 per share to yield 5.75% per annum; (ii) to provide holders of Class A Shares with quarterly cash dividends equal to the amount, if any, by which the net realized capital gains, dividends and option premiums earned on the Portfolio in any year, net of expenses and loss-carry-forwards, exceed the amount of the dividends paid on the Preferred Shares; and (iii) to return the original issue price to holders of both Preferred Shares and Class A Shares at the time of redemption of such shares on November 1, 2003.

INVESTMENT STRATEGY

The Company intends to achieve its investment objectives by investing the net assets in a portfolio consisting of common shares of: Bank of Montreal, The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Royal Bank of Canada, and The Toronto-Dominion Bank (the "Banks"). To generate additional returns above the dividend income generated by the Portfolio, the Company will write covered call options in respect of all or part of the common shares in the Portfolio.

Asset Mix



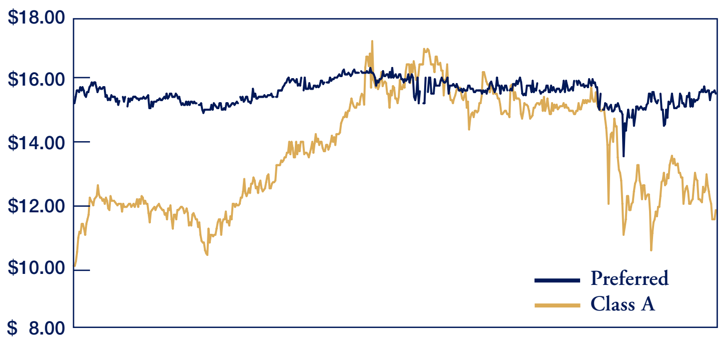
Distribution History

	Class A Regular	*Class A Special*	*Class A Total*	*Regular Preferred*
1997				
January	$0.20		$0.200000	$0.220400
April	$0.20	$0.100000	$0.300000	$0.215625
July	$0.20	$0.100000	$0.300000	$0.215625
October	$0.20	$1.701447	$1.901447	$0.226194
Total 1997			***$2.701447***	***$0.877844***
1998				
January	$0.20	$0.10	$0.30	$0.215625
April	$0.20	$0.10	$0.30	$0.223941
July	$0.20	$0.10	$0.30	$0.221305
October	$0.20	$0.20	$0.40	$0.223526
Total 1998			***$1.30***	***$0.884397***

Holdings:

BANK OF MONTREAL
THE BANK OF NOVA SCOTIA
CANADIAN IMPERIAL BANK OF COMMERCE
ROYAL BANK OF CANADA
THE TORONTO-DOMINION BANK

Trading History



October 1996 to October 1998

COMMENTARY

The Financial Services sector demonstrated significant volatility with respect to stock prices during 1998. The sector moved strongly upwards throughout the first and second fiscal quarters as a result of record quarterly earnings, Bank merger proposals and widespread investor enthusiasm.

From an intra-year high reached in mid April, the sector quickly reversed these earlier gains propelled downwards by the threat of a global economic crisis and a growing perception that the necessary regulatory approvals for the Bank mergers would be withheld.

In this context, we were pleased to be able to pay several special distributions to Class A shareholders and to also reposition the portfolio for continuing operations in fiscal 1999.

Distributions to the Preferred Shares amounted to $0.884397 representing a 5.90% annual yield on the initial price of $15.00. Distributions to Class A shareholders amounted to $0.80 in regular distributions and $0.50 in special distributions, for a total distribution amount of $1.30 per Class A share.

AUDITORS' REPORT

To the Shareholders of
Premium Income Corporation

We have audited the statements of financial position of Premium Income Corporation as at October 31, 1998 and 1997, the statement of investments at market value as at October 31, 1998 and the statement of operations and retained earnings, changes in net assets and changes in investments for the years ended October 31, 1998 and 1997. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at October 31, 1998 and 1997, its investments at market value at October 31, 1998 and the results of its operations and the changes in its net assets and investments for the years ended October 31, 1998 and 1997 in accordance with generally accepted accounting principles.

Deloitte & Touche (signed)

Chartered Accountants

Toronto, Ontario
November 30, 1998

STATEMENTS OF FINANCIAL POSITION

October 31, 1998 and 1997

	1998	*1997 (Note 3)*
Assets		
Investments at market value (average cost – $96,504,967; 1997–$88,178,556)	$ 95,070,548	*$ 98,708,750*
Cash and short-term investments	17,305	*13,018,077*
Interest, dividends and other receivables	1,286,959	*146,250*
Total assets	$ 96,374,812	*$ 111,873,077*
Liabilities		
Accounts payable and accrued liabilities	$ 116,919	*$ 115,604*
Due to brokers – investments purchased	–	*4,377,350*
Redeemable preferred shares *(Note 3)*	60,000,000	*60,000,000*
	60,116,919	*64,492,954*
Equity		
Class A and Class B shares *(Note 3)*	35,671,000	*35,671,000*
Retained Earnings	2,021,182	*1,178,929*
Unrealized appreciation (depreciation) in the market value of investments	(1,434,289)	*10,530,194*
	36,257,893	*47,380,123*
Total liabilities and equity	$ 96,374,812	*$ 111,873,077*
Net asset value per Class A share (Note 4)	$ 9.06	*$ 11.84*

On behalf of the Board,

John P. Mulvihill (signed)

John P. Mulvihill,
Director

Robert W. Korthals (signed)

Robert W. Korthals,
Director

STATEMENTS OF OPERATIONS AND RETAINED EARNINGS

Years ended October 31, 1998 and 1997

	1998	*1997 (Note 3)*
Revenue		
Interest	$ 1,961,186	*$ 1,024,220*
Dividends	2,026,280	*3,030,640*
	3,987,466	*4,054,860*
Net realized gains on investments and options	6,852,006	*12,612,969*
	10,839,472	*16,667,829*
Expenses *(Note 5)*		
Management fees	967,786	*938,011*
Administrative and other expenses	209,439	*83,650*
Government taxes	82,406	*67,673*
	1,259,631	*1,089,334*
Net Income Before Distributions	9,579,841	*15,578,495*
Preferred Share Distributions *(Note 7)*	3,537,588	*3,511,376*
Net Income	$ 6,042,253	*$ 12,067,119*
Net Income per Class A Share *(Note 4)*	$ 1.51	*$ 3.02*
Retained Earnings (Deficit)		
Balance, beginning of year	$ 1,178,929	*$ (82,402)*
Net income	6,042,253	*12,067,119*
Distributions on Class A shares *(Note 7)*	(5,200,000)	*(10,805,788)*
Balance, end of year	$ 2,021,182	*$ 1,178,929*

STATEMENTS OF CHANGES IN NET ASSETS

Years ended October 31, 1998 and 1997

	1998	*1997 (Note 3)*
Net Income Before Distributions	$ 9,579,841	*$ 15,578,495*
Less Distributions *(Note 7)*		
Preferred shares	(3,537,588)	*(3,511,376)*
Class A shares	(5,200,000)	*(10,805,788)*
Change in Net Unrealized Appreciation (Depreciation) in Market Value of Investments During the Year	(11,964,483)	*10,530,194*
Changes in Equity During the Year	(11,122,230)	*11,791,525*
Equity, Beginning of Year	47,380,123	*35,588,598*
Equity, End of Year	$ 36,257,893	*$ 47,380,123*
Distribution per Preferred Share *(Note 7)*	$ 0.884397	*$ 0.877844*
Distribution per Class A Share *(Note 7)*	1.300000	*2.701447*

STATEMENTS OF CHANGES IN INVESTMENTS

Years ended October 31, 1998 and 1997

	1998	*1997*
Investments at Market Value, Beginning of year	$98,708,750	*$ -*
Unrealized Appreciation in the Market Value of Investments, Beginning of year	10,530,194	*-*
Investments at Cost, Beginning of year	88,178,556	*-*
Cost of Investments Purchased, During the Year	279,370,619	*413,797,067*
Cost of Investments Sold, During the Year		
Proceeds from sales	277,896,344	*338,231,480*
Net realized gains on sales	6,852,006	*12,612,969*
	271,044,338	*325,618,511*
Investments at Cost, End of Year	96,504,837	*88,178,556*
Unrealized Appreciation (Depreciation) of Investments, End of Year	(1,434,289)	*10,530,194*
Investments at Market Value, End of Year	$ 95,070,548	*$ 98,708,750*

STATEMENT OF INVESTMENTS AT MARKET VALUE

October 31, 1998

	Number of Shares/ Par Value	*Average Cost*	*Market Value*	*% of Portfolio*
Common Stocks				
Bank of Montreal	205,000	$14,607,172	$12,935,500	13.6%
The Bank of Nova Scotia	475,000	15,426,067	15,295,000	16.1%
Canadian Imperial Bank of Commerce	469,000	13,792,092	14,374,850	15.1%
Royal Bank of Canada	123,000	8,601,307	8,745,300	9.2%
The Toronto-Dominion Bank	306,000	16,154,390	14,045,400	14.8%
		68,581,028	65,396,050	68.8%
Government Insured Bonds				
CMHC 6% *December 9, 1998*	29,995,000	30,016,964	30,009,998	31.6%

	Number of Contracts	*Proceeds*	*Market Value*	*% of Portfolio*
Written Call Options *(100 Shares per contract)*				
Bank of Montreal				
November 1998 at $75	(775)	(764,150)	(775)	0.0%
The Bank of Nova Scotia				
April 1999 at $35	(1,000)	(250,300)	(202,000)	(0.2)%
Canadian Imperial Bank of Commerce				
April 1999 at $35	(475)	(74,575)	(71,725)	(0.1)%
Royal Bank of Canada				
January 1999 at $75	(200)	(43,600)	(61,000)	(0.1)%
The Toronto-Dominion Bank				
November 1998 at $62	(1,225)	(960,400)	-	0.0%
		(2,093,025)	(335,500)	(0.4)%
Total Investments		$96,504,967	$95,070,548	100.0%

1. Corporate Information

The Company is a mutual fund corporation incorporated under the laws of the Province of Ontario on August 27, 1996. The Company was inactive prior to the initial public offering of Preferred Shares and Class A Shares on October 30, 1996. All shares outstanding on November 1, 2003 will be redeemed by the Company on that date.

The Company invests in a portfolio consisting principally of common shares of Bank of Montreal, The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Royal Bank of Canada and The Toronto-Dominion Bank.

To generate additional returns above the dividend income earned on the portfolio, the Company will from time to time write covered call options in respect of all or part of the common shares in the portfolio. Additionally, the Company may use put options to preserve the value of the portfolio where appropriate. From time to time, the portfolio may include debt securities having a remaining term to maturity of less than one year issued or guaranteed by the government of Canada or a province or short-term commercial paper issued by one or more of the Banks.

2. Summary of Significant Accounting Policies

Investment valuation policies

Investments are recorded in the financial statements at their market value at the end of the period, determined as follows:

Shares or other securities for which market quotations are readily available are valued at the closing sale price or, if there is no sale price, the average of the closing bid and ask prices.

Listed options are valued at market values as reported on recognized exchanges. Over the counter options are valued using an appropriate valuation model.

Short-term investments are valued at quoted market values.

Policies for the recognition of investment appreciation, depreciation and income

Realized gains and losses on investment sales, which are included in income, and unrealized appreciation or depreciation in investment values, which are included in a separate component of shareholders' equity, are calculated on the average cost basis.

Option fees paid or received are deferred and included in investments on the statement of financial position. Income is recognized when options are exercised, expire or are closed out.

Deferred gains and losses on options are recognized in investments and as a component of net unrealized appreciation (depreciation) in the value of investments in shareholders' equity.

Dividend income is recognized on the ex-dividend date. Interest income is recognized when earned.

3. Share Capital

The Company is authorized to issue an unlimited number of Preferred and Class A Shares and 1,000 Class B Shares.

Issued and outstanding:

		1998	*1997*
Preferred Shares	4,000,000	$ 60,000,000	*$ 60,000,000*
Class A Shares	4,000,000	$ 35,670,000	*$ 35,670,000*
Class B Shares	1,000	1,000	*1,000*
		$ 35,671,000	*$ 35,671,000*

Preferred Shares are entitled to a cumulative preferential quarterly dividend of $0.215625 per share payable on the last day of January, April, July and October in each year. To the extent that a quarterly dividend is a capital gains dividend funded by net realized capital gains or option premiums, holders of Preferred Shares will receive an additional capital gains dividend of $0.068 for each $1.00 of Preferred Share dividend so funded.

All Preferred Shares and Class A Shares outstanding on November 1, 2003 will be redeemed by the Company on that date.

Preferred Shares and Class A Shares may be surrendered at any time for retraction at specified retraction amounts. Holders of Preferred Shares and Class A Shares may concurrently retract one Preferred Share and one Class A Share on an October 31 valuation date at their net asset values. Shares retracted at any other valuation date or not retracted concurrently at an October 31 valuation date will be retracted at a discount to net asset value. Under the terms of a Recirculation Agreement, the Company may, but is not obligated to, require the Recirculation Agent to use its best efforts to find purchasers for any Preferred Shares and Class A Shares tendered for retraction. The Preferred Shares rank in priority to the Class A Shares and the Class A Shares rank in priority to the Class B Shares with respect to the payment of dividends and repayment of capital on the dissolution, liquidation or winding up of the Company.

The holders of Class B Shares are not entitled to receive dividends. The Class B Shares are retractable at a price of $1.00 per share.

Class B Shares are entitled to one vote per share. Preferred Shares and Class A Shares are entitled to vote on certain shareholder matters.

The Company's Preferred Shares have been reclassified, on a retroactive basis, from equity to liabilities in accordance with the new accounting guidelines of The Canadian Institute of Chartered Accountants. Accordingly, net income for the year is stated after Preferred Shares distributions and the net income for 1997 has been restate for comparative purposes. Apart from these reclassifications, there is no other impact on the financial statements.

4. *Net Asset/Net Income per Class A Share*

The net asset and income per Class A Share is based on the weighted average number of shares outstanding during the period.

5. *Expenses*

The Company is responsible for all ongoing trustee, manager, legal, accounting and audit fees as well as all other expenses incurred by the trustee and manager in the ordinary course of business relating to the Company's operations.

Fees are paid to Mulvihill Capital Management Inc. ("MCM") under the terms of an investment management agreement and to Mulvihill Fund Services Inc. ("Mulvihill") under the terms of a management agreement. The fees are comprised of monthly fees calculated at 1/12 of 0.80% and 1/12 of 0.10%, respectively, of the net asset value.

The expense ratio for the Company is as follows:

	1998	*1997*
Total expenses	$ 1,259,631	*$ 1,089,334*
Expenses as a percent of average net assets	1.17%	*1.04%*

Average net assets are calculated to be the average of the net assets of the Company at each month end.

6. *Income Taxes*

The Company is a "mutual fund corporation" as defined in the Income Tax Act (Canada) (the "Act") and is subject to tax in respect of its net realized capital gains. This tax is refundable in certain circumstances. Also, the Company is generally subject to a tax of 331/3% under Part IV of the Act on taxable dividends received in the year. This tax is fully refundable upon payment of sufficient dividends.

The Company is also a "financial intermediary corporation" as defined in the Act and, as such, is not subject to tax under Part IV.1 of the Act on dividends received nor is it generally liable to tax under Part VI.1 on dividends paid on taxable preferred shares.

Under the dividend policy of the Company, premiums received in respect of written call options that are still outstanding at year end are not to be distributed in the year to the shareholders. The premium income retained by the Company is subject to a refundable tax at 44.6%. This tax, amounting to $600,000 in 1998, will be refundable to the Company in a subsequent year when premium income is distributed to the shareholders.

7. Distributions

Distributions per share paid to shareholders during the year were allocated as follows:

	1998		*1997*	
	Preferred	*Class A*	*Preferred*	*Class A*
Capital gains dividends	$ 0.343910	$ 1.300000	*$ 0.143922*	*$ 2.701447*
Taxable dividends	0.540487	-	*0.733922*	-
	$ 0.884397	$ 1.300000	*$ 0.877844*	*$ 2.701447*

The difference between net income per Class A Share and the amount distributed per Class A Share represents primarily share issue expenses which are being deducted for tax purposes over five years.

8. Financial Instruments and Risk Management

The value of Company's assets and liabilities is affected by changes in interest rates and equity markets. The Company manages these risks through the use of various risk limits and trading strategies. The Company's assets and liabilities are included in the statements of financial position at market value.

9. Year 2000

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and , if not addressed, the impact on operations and the financial reporting may range from minor errors to significant systems failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the entity, including those related to the efforts of customers, suppliers, or third parties, will be fully resolved.

10. Statement of Portfolio Transactions

The Company will provide, without charge, a Statement of Portfolio Transactions (unaudited) upon written request by any shareholder to the Company at 121 King Street West, Suite 2600, Toronto, Ontario, M5H 3T9.

Mulvihill Capital Management Inc. is a leading Canadian investment counsellor responsible for the care of institutional and personal assets. The company manages corporate, pension, insurance, endowment, trust and mutual funds under a wide variety of investment mandates. Founded in 1985 as CT Investment Counsel Inc., the investment arm of Canada Trust, the company emerged in 1995 as an independent company operated by a cohesive team of senior managers and owners who have been together for more than a decade. The company's scale and independent structure allow it to provide clients with a uniquely customized approach to asset management.

Premium Income Corporation is managed by Mulvihill Capital's structured finance group. This area of the company concentrates exclusively on creating and managing products tailored to meet very specific investment objectives. Assets are generally managed to meet specific absolute return levels rather than taking on the additional risk of targeting relative returns. This methodology allows the company to make investment decisions that meet the client's needs rather than to make investments to rival the competition.

Mulvihill's personal asset management division, Mulvihill Wealth Management, offers a comprehensive specialized approach tailored to client's personal strategies. This not only relieves the client's burden of day-to-day investment decisions but also provides financial peace of mind for today and tomorrow. The company's personalized service and customized reporting assure that its powerful team of professionals is always working toward your current objectives and that you are fully aware of the progress you are making.

Mulvihill's reputation has been built on its ability to provide customized portfolios that meet the stated needs of its clients. The Premium Income investments are prime examples of that customized approach to asset management.

Other Premium Income products within the Mulvihill Group include First Premium Income Trust, First Premium U.S. Income Trust, First Premium Oil & Gas Income Trust, MCM Split Share Corp. and Global Telecom Split Share Corp.

These Funds are either Unit Trusts or Mutual Fund Corporations and are traded on the Toronto Stock Exchange and the Montreal Exchange over the past year as follows:

	Symbol	*High*	*Low*
First Premium Income Trust	FPI.UN	$ 30.25	$ 23.15
First Premium U.S. Income Trust	FPU.UN	$ 25.50	$ 20.65
First Premium Oil & Gas Income Trust	FPG.UN	$ 11.00	$ 6.05
MCM Split Share Corp.	MUH.A	$ 15.70	$ 9.75
	MUH.PR.A	$ 15.30	$ 12.75
Global Telecom Split Share Corp.	GT.A	$ 14.90	$ 8.00
	GT.PR.A	$ 14.90	$ 12.80

YEAR 2000

In conducting its business, the Company utilizes the computer information systems of third party service providers, including MCM, Mulvihill, the Custodian and the Transfer Agent. The Company is currently reviewing the potential Year 2000 readiness issues of its third party service providers and will determine what action, if any, is required. MCM and Mulvihill have advised the Company that they have put in place a Year 2000 plan in an effort to ensure that their information systems are Year 2000 compliant by the end of first quarter of 1999. None of the expenditures for the Year 2000 readiness plan will be borne by the Company. They have also made enquiries of the Custodian and Transfer Agent in order to assess the status of their information systems with respect to Year 2000 readiness issues. There can be no assurance, however, that the Company's third party service providers have, or will have, information systems that are Year 2000 compliant. In addition, there is no assurance that the corporations that are included in the Company's portfolio of investments will be Year 2000 compliant. If any such corporations are not Year 2000 compliant, the net asset value of the Company could be adversely affected.

BOARD OF DIRECTORS

John P. Mulvihill*
Chairman & President,
Mulvihill Capital Management Inc.

Robert W. Korthals*
Corporate Director

David N. Middleton
Vice President, Finance,
Mulvihill Capital Management Inc.

C. Edward Medland*
President, Beauwood Investments Inc.

** Audit Committee*

OFFICERS

John P. Mulvihill
President & Secretary

David N. Middleton
Chief Financial Officer

CORPORATE INFORMATION

Auditors:
Deloitte & Touche
BCE Place
181 Bay Street, Suite 1400
Toronto, Ontario M5J 2V1

Transfer Agent:
Montreal Trust
151 Front Street, 8th Floor
Toronto, Ontario M5J 2N1

Corporate Head Office:
Premium Income Corporation
121 King Street West, Suite 2600
Toronto, Ontario M5H 3T9

Shares Listed:
Toronto Stock Exchange and
Montreal Exchange
trading under PIC.PR.A & PIC.A

Trustee:
Royal Trust
Royal Trust Tower
77 King Street West, 11th Floor
Toronto, Ontario M5W 1P9

(416) 681-3966
(800) 725-7172
fax: (416) 681-3901
premium@mulvihill.com

Visit our website at www.mulvihill.com for additional information on all Premium Income Funds.

OTHER FUNDS MANAGED BY
MULVIHILL CAPITAL MANAGEMENT INC.

First Premium Income Trust

First Premium U.S. Income Trust

First Premium Oil & Gas Income Trust

MCM Split Share Corp.

Global Telecom Split Share Corp.

MULVIHILL

Premium Income Corporation

Managed by:

Mulvihill Capital Management Inc.
121 King Street West, Suite 2600
Toronto, Ontario M5H 3T9
Tel: 416-681-3966 800-725-7172
Fax: 416-681-3901
E-mail: premium@mulvihill.com
www.mulvihill.com