

PIMCO Income Strategy Fund II
Form N-CSRS
April 02, 2013

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 811-21601

PIMCO Income Strategy Fund II
(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, 2013
end:

Date of reporting period: January 31, 2013

Item 1. Report to Shareholders

January 31, 2013

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Dear Shareholder:

The US economy continued to advance during the six-month fiscal reporting period ended January 31, 2013. The housing market nationwide displayed signs of strength, hiring increased at a steady pace and export orders were on the rise. As consumer confidence increased, investors shifted from US Treasuries to equities. Bond yields rose from all-time lows and stocks approached their highest levels in five years.

Six-Month Period in Review through January 31, 2013

Hans W. Kertess

Chairman

For the six-month period ended January 31, 2013:

- PIMCO Income Strategy Fund returned 16.05% on net asset value (NAV) and 13.38% on market price.
- PIMCO Income Strategy Fund II returned 14.03% on NAV and 14.88% on market price.

Brian S. Shlissel

The Barclays U.S. Credit Index, a measure of high quality corporate bond performance, advanced 0.96% and the Barclays U.S. High Yield Bond Index, a measure of below investment-grade corporate bond performance, rose 7.37% during the reporting period. Government bonds, represented by the Barclays Long-Term Treasury Index, declined 7.12%. The Barclays U.S. Aggregate Bond Index, a broad credit market measure of government and corporate securities, fell 0.29%, and mortgage-backed securities, reflected by the Barclays Fixed Rate MBS Index, declined 0.41%. As for stocks, the Standard & Poor's 500 Index increased 9.91% during the six-month fiscal period ended January 31, 2013.

President & CEO

US gross domestic product (GDP), the value of goods and services produced in the country, the broadest measure of US economic activity and the principal indicator of economic performance, expanded at an annual rate of 3.1% during the third quarter of 2012 before declining to a negative 0.1% annually during the fourth quarter of 2012. The government indicated that the drop in defense spending was the principal reason for the slowdown. US unemployment fell to 7.9% from 8.1% during the six-month reporting period. For the 2012 calendar year the economy created on average 181,000 nonfarm jobs each month according to the government. The S&P/Case-Shiller Home Price Index, a leading measure of the US residential housing market, signified that home prices rose 5.5% in its 20-City Composite during the 12-months ended November 30, 2012. According to a study by CoreLogic, a leading

provider of consumer, financial and property information analytics and services to businesses and governments, home prices advanced in 46 of 50 states during the 12-months ended December 31, 2012. Auto sales increased 13% during the same period.

Outlook

In addition to the drop in defense spending that contributed to a weaker-than-expected GDP figure in the fourth quarter of 2012, further spending cuts by the government began on March 1, 2013. These cuts known as the sequester, are split between defense and domestic spending. The sequester is designed to cut federal spending by \$1.2 trillion, spread out over the next ten years. Both the White House and Congress say the cuts are such that the economic recovery could be jeopardized. As of this writing, the cuts are underway, and the issue has not been resolved.

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Beyond this uncertainty, we see positive signs for the US economy in 2013. The economy is expected to grow between 2.50% to 2.75%, largely driven by the strengthening housing market. Home prices are anticipated to appreciate 10% on a national basis and the improving labor market is expected to drive wage gains beyond the drag created by the December 31, 2012 expiration of the 2% payroll tax holiday.

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.us.allianzgi.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, 2013

For the six-months ended January 31, 2013, PIMCO Income Strategy Fund returned 16.05% on net asset value (NAV) and 13.38% on market price.

For the six-months ended January 31, 2013, PIMCO Income Strategy Fund II returned 14.03% on NAV and 14.88% on market price.

The unmanaged Barclays U.S. Aggregate Bond Index and Barclays U.S. Credit Index returned -0.29% and 0.96% respectively, during the reporting period.

The overall US fixed income market was volatile at times during the reporting period. This was triggered by a number of macro issues that impacted investor sentiment, including the European sovereign debt crisis, moderating global growth and the US fiscal cliff. Against this backdrop, the spread sectors (non-US Treasuries) produced mixed results during the six-months ended January 31, 2013. Most spread sectors initially rallied as investor sentiment was buoyed given some signs of progress in Europe, coupled with additional quantitative easing by the Federal Reserve Board and the European Central Bank. However, a portion of those gains were given back in some spread sectors toward the end of the period. This occurred as the worst of the fiscal cliff was averted and interest rates rose sharply. One exception was high yield corporate bonds, as they continued to rally given strong demand from investors looking to generate incremental yield in the low interest rate environment. All told, during the six-months ended January 31, 2013 both short- and long-term Treasury yields moved higher and the yield curve steepened.

After producing solid results during the first half of the reporting period, the US corporate bond market posted weak results as the period progressed. Initially supporting the corporate bond market were corporate profits that often exceeded expectations, cash-rich corporate balance sheets, low defaults and overall solid demand. While the fundamentals in the corporate bond market remained solid, the market sold off toward the end of 2012 and in January 2013 as interest rates rose sharply.

PIMCO Income Strategy Fund

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

January 31, 2013 (continued)

Sector exposures largely contributed to the Funds' performance

During the reporting period, the Funds' outperformed the broad US fixed income market (as measured by the Barclays U.S. Aggregate Bond Index) as well as the US 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 generally outperformed the broader market, supported by positive supply/demand technicals. An overweight to the Financial sector was beneficial as it outperformed the broad credit market during the past six months. In addition, the Funds' overweight and security selection within the Insurance sector was additive to performance. Finally, the Funds' underweight to the long end of the yield curve helped performance as the yield curve steepened during the six months ended January 31, 2013.

On the downside, an underweighting to lower rated Telecommunications issues detracted from results as this sector outperformed the overall credit market.

**PIMCO Income Strategy Fund
Performance & Statistics**

January 31, 2013 (unaudited)

Total Return(1):	Market Price	NAV
Six Month	13.38%	16.05%
1 Year	33.28%	32.58%
5 Year	9.00%	8.80%
Commencement of Operations (8/29/03) to 1/31/13	6.56%	6.37%

Market Price/NAV Performance:

Commencement of Operations (8/29/03) to 1/31/13

Market Price

NAV

Market Price/NAV:

Market Price

NAV

Premium to NAV

Market Price Yield(2)

Leverage Ratio(3)

\$13.26

\$12.27

8.07%

7.18%

21.20%

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

January 31, 2013 (unaudited)

Total Return(1):	Market Price	NAV
Six Month	14.88%	14.03%
1 Year	32.41%	29.60%
5 Year	7.48%	5.78%
Commencement of Operations (10/29/04) to 1/31/13	4.61%	4.26%

Market Price/NAV Performance:

Commencement of Operations (10/29/04) to 1/31/13

Market Price
NAV

Market Price/NAV:

Market Price	\$11.52
NAV	\$10.65
Premium to NAV	8.17%
Market Price Yield(2)	7.46%
Leverage Ratio(3)	20.63%

(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 and capital gain 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 and includes the effect of any expense reductions. 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 each Fund, market conditions, supply and demand for each Fund's shares, or changes in each Fund's dividends.

An investment in each Fund 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

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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 January 31, 2013.

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

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PIMCO Income Strategy Fund Schedule of Investments

January 31, 2013 (unaudited)

Principal Amount (000s)		Value
CORPORATE BONDS & NOTES	51.7%	
Airlines	1.5%	
\$900	American Airlines, Inc., 10.50%, 10/15/12 (d)	\$1,046,250
3,614	American Airlines Pass-Through Trust (d), 9.73%, 9/29/14	2,891,441
1,861	10.18%, 1/2/13 (b) (e)	2,103,263
		6,040,954
Auto Manufacturers	2.3%	
7,800	Ford Motor Co., 7.70%, 5/15/97	9,126,000
Banking	24.2%	
2,600	AgFirst Farm Credit Bank, 7.30%, 3/4/13 (a) (b) (c) (f) (i) (acquisition cost-\$2,225,000; purchased 2/26/10-4/15/10)	2,600,000
475	Ally Financial, Inc., 5.90%, 1/15/19-10/15/19	467,307
535	6.00%, 2/15/19-9/15/19	524,147
538	6.05%, 8/15/19-10/15/19	529,968
20	6.10%, 9/15/19	19,749
31	6.125%, 10/15/19	30,578
1,345	6.15%, 8/15/19-10/15/19	1,323,737
22	6.20%, 4/15/19	21,674
1,406	6.25%, 2/15/16-7/15/19	1,397,863
120	6.30%, 8/15/19	118,794
1,468	6.35%, 2/15/16-4/15/19	1,458,165
629	6.40%, 3/15/16-11/15/19	623,164
2,021	6.50%, 2/15/16-5/15/19	1,988,478
383	6.55%, 12/15/19	378,414
24	6.60%, 5/15/18-6/15/19	23,654
71	6.65%, 6/15/18-10/15/18	70,550
197	6.70%, 6/15/18-6/15/19	195,087
464	6.75%, 4/15/13-6/15/19	465,214
208	6.80%, 9/15/16-10/15/18	205,954
968	6.85%, 4/15/16-5/15/18	968,462
341	6.875%, 8/15/16-7/15/18	339,677
182	6.90%, 6/15/17-8/15/18	181,738
151	6.95%, 6/15/17	149,556
721	7.00%, 12/15/16-9/15/18	714,850
81	7.05%, 3/15/18-4/15/18	80,304
160	7.125%, 10/15/17	158,404
40	7.15%, 3/15/25	39,465
75	7.20%, 10/15/17	74,563
929	7.25%, 6/15/16-9/15/18	924,854
25	7.30%, 1/15/18	24,756
396	7.35%, 4/15/18	394,005
57	7.50%, 6/15/16	57,263
45	7.55%, 5/15/16	44,519
47	7.75%, 10/15/17	46,469
110	8.125%, 11/15/17	109,127
110	9.00%, 7/15/20	109,996
£10,400	Barclays Bank PLC, 14.00%, 6/15/19 (f)	22,143,403
\$600	BNP Paribas S.A., 7.195%, 6/25/37 (a) (c) (f)	627,300

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650	BPCE S.A., 9.00%, 3/17/15 (f)	913,461
3,000	Cooperatieve Centrale Raiffeisen-Boerenleenbank BA, 6.875%, 3/19/20	4,568,321

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PIMCO Income Strategy Fund Schedule of Investments

January 31, 2013 (unaudited) (continued)

Principal Amount (000s)		Value
Banking (continued)		
\$9,400	11.00%, 6/30/19 (a) (b) (c) (f) (i) (acquisition cost-\$12,041,500; purchased 4/30/10-7/27/12) Credit Agricole S.A. (f),	\$12,673,080
2,000	7.875%, 10/26/19	2,873,107
\$2,200	8.375%, 10/13/19 (a) (c) LBG Capital No. 1 PLC,	2,411,750
500	6.439%, 5/23/20	674,657
200	7.375%, 3/12/20	279,451
£300	7.588%, 5/12/20	497,163
4,800	7.867%, 12/17/19	7,996,485
2,400	7.869%, 8/25/20	4,029,090
\$1,400	8.00%, 6/15/20 (a) (b) (c) (f) (i) (acquisition cost-\$1,174,250; purchased 2/2/10-3/23/10)	1,500,265
2,000	8.50%, 12/17/21 (a) (b) (c) (f) (i) (acquisition cost-\$1,820,000; purchased 5/3/10)	2,143,236
£900	11.04%, 3/19/20 LBG Capital No. 2 PLC,	1,665,920
534	9.125%, 7/15/20	921,331
2,500	11.25%, 9/14/23	4,641,033
\$3,300	Santander Finance Preferred S.A. Unipersonal, 10.50%, 9/29/14 (f)	3,515,163
£2,000	Santander Issuances S.A. Unipersonal, 7.30%, 7/27/19 (converts to FRN on 9/27/14)	3,227,510
		94,162,231
Diversified Financial Services 9.0%		
\$7,000	ILFC E-Capital Trust I, 4.54%, 12/21/65 (a) (c) (k) SLM Corp.,	5,600,000
6,200	8.00%, 3/25/20	7,207,500
12,200	8.45%, 6/15/18	14,596,202
8,200	Springleaf Finance Corp., 6.50%, 9/15/17	7,749,000
		35,152,702
Electric Utilities 0.7%		
1,900	AES Andres Dominicana Ltd., 9.50%, 11/12/20 (a) (c)	2,109,000
1,100	Dynegy Roseton LLC / Dynegy Danskammer LLC Pass-Through Trust, 7.67%, 11/8/16, Ser. B (b) (d)	27,500
400	PPL Capital Funding, Inc., 6.70%, 3/30/67 (converts to FRN on 3/30/17)	426,386
		2,562,886
Household Products/Wares 0.2%		
800	Reynolds Group Issuer, Inc., 9.00%, 4/15/19	848,000
Insurance 12.2%		
2,000	American General Institutional Capital B, 8.125%, 3/15/46 (a) (c) American International Group, Inc.,	2,615,000
4,000	6.25%, 3/15/87 (converts to FRN on 3/15/37) (h)	4,285,000
MXN8,000	7.98%, 6/15/17	614,096
1,000	8.00%, 5/22/68 (converts to FRN on 5/22/18)	1,585,626
4,700	8.00%, 5/22/68 (converts to FRN on 5/22/18) (a) (b) (c) (i) (acquisition cost-\$6,097,976; purchased 4/4/11-2/8/12)	7,452,444
\$16,571	8.175%, 5/15/68 (converts to FRN on 5/15/38)	21,625,155

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£1,350	8.625%, 5/22/68 (converts to FRN on 5/22/18)	2,644,263
3,500	8.625%, 5/22/68 (converts to FRN on 5/22/18) (a) (b) (c) (i) (acquisition cost-\$5,656,211; purchased 4/19/12-5/7/12)	6,855,497
		47,677,081

PIMCO Income Strategy Fund Schedule of Investments

January 31, 2013 (unaudited) (continued)

Principal Amount (000s)			Value
Oil & Gas 0.2%			
\$600		SandRidge Energy, Inc., 8.00%, 6/1/18 (a) (c)	\$633,000
Pipelines 1.4%			
5,000		NGPL PipeCo LLC, 7.768%, 12/15/37 (a) (c)	5,325,000
Total Corporate Bonds & Notes (cost-\$177,107,213)			201,527,854
MORTGAGE-BACKED SECURITIES 20.6%			
127		Banc of America Alternative Loan Trust, 6.00%, 1/25/36 CMO	101,144
		Banc of America Funding Trust, CMO,	