

LETTER TO SHAREHOLDERS

Dear Fellow Shareholders:

This Semi-Annual Report covers the six-month period ended March 31, 1992. The following table shows the average annual total return for several different periods ended on that date for the Fund and comparative indices of securities prices. The data quoted represents past performance, and an investment in the Fund may fluctuate so that an investor's shares when redeemed may be worth more or less than their original cost. First Pacific Advisors, Inc. commenced serving as investment adviser to the Fund in July 1984; therefore, the ten-year period includes the performance results of the prior investment adviser.

Average Annual Total Return
Periods Ended March 31, 1992
1 Year 5 Years 10 Years

FPA New Income, Inc. (NAV)	14.02%*	10.70%*	13.47%*
FPA New Income, Inc. (Net of Sales Charge)	8.89%‡	9.69%‡	12.95%‡
Lipper Fixed Income Fund Average	13.33%	7.74%	12.52%
Lehman Brothers Government/ Corporate Bond Index	11.38%	8.94%	13.13%

Your Fund's net asset value (NAV) closed at \$10.47 on March 31, 1992. Income dividends of \$0.22 and \$0.17 per share were paid on October 15, 1991 and January 10, 1992, respectively.

For the calendar year ended December 31, 1991, your Fund achieved a 18.80%* total return. By comparison, total returns for the Lipper Fixed Income Fund Average and the Lehman Brothers Index were 18.17% and 16.13%, respectively.

Commentary

Your Fund's positive relative performance continues. Its 5.80%* total return for this reporting period and its 18.80%* calendar 1991

total return exceeded those of the Lipper Average and the Lehman Brothers Index. A combination of timely shifts in the portfolio's average maturity and an exposure to high-yield/discount convertible bonds were responsible.

Our September 1991 Shareholder Letter discussed some of the prior shifts in portfolio strategy as well as what was to be expected going forward. It was anticipated that the portfolio's configuration would become considerably more defensive in character. As the bond market rallied throughout the December quarter, portions of the portfolio's zero coupon bond and high-yield bond holdings were sold. Additional sales of high-yield securities were conducted during the March quarter. These sales, in addition to the Fund's rapid growth in total assets, increased the portfolio's short-term liquidity. Liquidity grew from 4.7%, at September 30, 1991, to a high of almost 22%. These defensive actions helped protect your Fund from the negative effects of rising interest rates. Between December 31, 1991 and March 31, 1992, the yield on the ten-year U.S. Treasury bond rose from 6.70% to 7.53%. The average high quality bond fund declined while your Fund provided a 1.16%* total return for this period.

New portfolio additions have reflected our defensive strategy. We have purchased high coupon callable high-yield debt securities which have a high probability of being redeemed in the near future. They provide extremely attractive short-term yields (9.5% - 10%) with a minimum of principal risk. Bonds with average maturities of five to seven years have also been added. We have emphasized AA/AAA mobile home asset-backed securities as well as selected mortgage-backed securities. Our mortgage

* Does not reflect deduction of the sales charge which, if reflected, would reduce the performance shown

‡ Reflects deduction of the maximum sales charge of 4.50% of the offering price

securities selection process has targeted specific types which have demonstrated a reduced level of pre-payment risk. These holdings have been added with cash flow yields between 8.15% and 8.45%. These changes have reduced the short-term investments position to 5.1% as of March 31, 1992. Including the high coupon callable high-yield debt positions, short-term liquidity rises to 10.7%. The Fund's average maturity is currently about six years. Quality continues to be maintained at high levels. Government/Agency securities represent 54.9% of the portfolio while another 17.2% is invested in securities rated AAA and AA, the majority of which are backed by the U.S. Government. Convertible and high-yield bonds account for 21.8%.

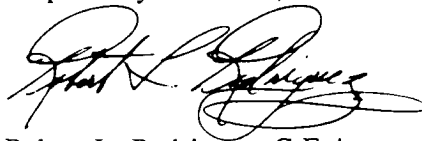
Our long-term investment strategy reflects a sense of caution because of the growing Federal budgetary problem. In the September Shareholder Letter, we briefly discussed the problems of uncontrolled spending. It was difficult to admit that budget deficits in excess of \$200-250 billion per year were rapidly becoming the norm. This fear has been confirmed recently since learning of the new long-term budget expectations presented by both the Congressional Budget Office and the President's Administration. Budget deficits of at least \$180 billion per year are forecast through 1996. For the first time, neither has forecast the possibility of a balanced budget. This is a dangerous path to follow. Unless we face the difficult budgetary choices, present fiscal policy trends are not sustainable. Uncontrolled spending will eventually lead to a budgetary crisis. The fallout from this possibility is still not forecastable. Investors appear to be starting to factor this potential risk into long-term yields. The yield curve is at its steepest slope ever—430 basis points. This means that long-term U.S. Treasury bonds yield 4.3% more than three-month Treasury bills. Purchasers of longer-term securities are requiring a large yield premium as compensation for accepting the risk of extending

maturities. Even with this large yield advantage, we do not believe yields of 7.5% and 8% on ten- and thirty-year U.S. Treasury bonds provide sufficient compensation for these potential risks.

In light of the above, we expect to maintain a somewhat defensive portfolio strategy with an emphasis on the five- to seven-year maturity range. This strategy reflects several compromises since a truly defensive posture would focus investments in the three-year maturity range or lower. At the present time, we are being challenged by the shape of the yield curve. The yield give-up from investing in shorter term securities is quite severe, especially if our fears prove to be unfounded. Our current strategy attempts to earn an attractive yield without undue principal risk. It provides approximately 90-95% of the yield of longer-term securities but with approximately 65% of the volatility risk. Should the budgetary problem heighten investor anxiety within the next two to four years, these investments will have remaining average maturities of three to five years. The portfolio should be somewhat insulated from the negative effects of a rise in interest rates.

We would like to close this letter by thanking our seasoned shareholders for their continued support and welcome our many new shareholders. Your Fund continues to grow rapidly, in recognition of its positive long-term performance. We will strive to retain your confidence through our disciplined investment approach.

Respectfully submitted,



Robert L. Rodriguez, C.F.A.
President and Chief Investment Officer

May 10, 1992