COHEN & STEERS QUALITY INCOME REALTY FUND INC
Form N-CSR
March 09, 2017

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 811-10481

Cohen & Steers Quality Income Realty Fund, Inc.
(Exact name of registrant as specified in charter)

280 Park Avenue, New York, NY — 10017
(Address of principal executive offices) — (Zip code)

Tina M. Payne
Cohen & Steers Capital Management, Inc.
280 Park Avenue
New York, New York 10017
(Name and address of agent for service)

Registrant s telephone number, including area code: (212) 832-3232

Date of fiscal year end: December 31

Date of reporting period: December 31, 2016

Item 1. Reports to Stockholders.

COHEN & STEERS QUALITY INCOME REALTY FUND, INC.

To Our Shareholders:

We would like to share with you our report for the year ended December 31, 2016. The net asset value (NAV) at that date was $13.42 per common share. The Fund's common stock is traded on the New York Stock Exchange (NYSE) and its share price can differ from its NAV; at year end, the Fund's closing price on the NYSE was $12.21.

The total returns for the Fund and its comparative benchmarks were:

	Six Months Ended December 31, 2016	Year Ended December 31, 2016
Cohen & Steers Quality Income Realty Fund at NAV[a]	5.09%	7.41%
Cohen & Steers Quality Income Realty Fund at Market Value[a]	7.54%	7.64%
FTSE NAREIT Equity REIT Index[b]	4.29%	8.52%
Blended Benchmark 80% FTSE NAREIT Equity REIT Index/20% BofA Merrill Lynch REIT Preferred Securities Index[b]	4.72%	6.58%
S&P 500 Index[b]	7.82%	11.96%

The performance data quoted represent past performance. Past performance is no guarantee of future results. The investment return and the principal value of an investment will fluctuate and shares, if sold, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Performance results reflect the effects of leverage, resulting from borrowings under a credit agreement. Current total returns of the Fund can be obtained by visiting our website at cohenandsteers.com. The Fund's returns assume the reinvestment of all dividends and distributions at prices obtained under the Fund's dividend reinvestment plan. Index performance does not reflect the deduction of any fees, taxes or expenses. An investor cannot invest directly in an index. Performance figures for periods shorter than one year are not annualized.

Managed Distribution Policy

Cohen & Steers Quality Income Realty Fund, Inc. (the Fund), acting in accordance with an exemptive order received from the Securities and Exchange Commission and with approval of its Board of Directors (the Board), adopted a managed distribution policy under which the Fund intends to include

[a] As a closed-end investment company, the price of the Fund's NYSE-traded shares will be set by market forces and can deviate from the NAV per share of the Fund.

[b] The FTSE NAREIT Equity REIT Index contains all tax-qualified REITs except timber and infrastructure REITs with more than 50% of total assets in qualifying real estate assets other than mortgages secured by real property that also meet minimum size and liquidity criteria. The BofA Merrill Lynch REIT Preferred Securities Index tracks the performance of fixed-rate U.S. dollar-denominated preferred securities issued in the U.S. domestic market including all real estate investment trusts. The S&P 500 Index is an unmanaged

index of 500 large-capitalization stocks that is frequently used as a general measure of U.S. stock market performance.

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long-term capital gains, where applicable, as part of the regular cash distributions to its shareholders (the Plan). On September 15, 2016, the Board of Directors of the Fund approved a change in the frequency of the Fund's cash distributions to shareholders from quarterly to monthly, effective October 1, 2016. The Plan gives the Fund greater flexibility to realize long-term capital gains and to distribute those gains on a regular monthly basis. In accordance with the Plan, the Fund currently distributes $0.08 per share on a monthly basis.

The Fund may pay distributions in excess of the Fund's investment company taxable income and net realized gains. This excess would be a return of capital distributed from the Fund's assets. Distributions of capital decrease the Fund's total assets and, therefore, could have the effect of increasing the Fund's expense ratio. In addition, in order to make these distributions, the Fund may have to sell portfolio securities at a less than opportune time.

Shareholders should not draw any conclusions about the Fund's investment performance from the amount of these distributions or from the terms of the Fund's Plan. The Fund's total return based on net asset value is presented in the table above as well as in the Financial Highlights table.

The Plan provides that the Board may amend or terminate the Plan at any time without prior notice to Fund shareholders; however, at this time, there are no reasonably foreseeable circumstances that might cause the termination. The termination of the Plan could have the effect of creating a trading discount (if the Fund's stock is trading at or above net asset value) or widening an existing trading discount.

Market Review

The real estate securities market reached a major milestone in 2016 when, for the first time since the Global Industry Classification Standard (GICS) was created in 1999, a new sector classification was added to the major stock market indexes. The move elevated real estate to its own sector category, separate from the financials sector. The reclassification acknowledged that while property investment companies share certain similarities with other capital-intensive businesses, their cash-flow-oriented business models and ties to real estate market cycles have produced a distinctive risk-return profile. Investors had other reasons to cheer real estate as well, with the sector producing a favorable total return during the year.

The broad stock market got off to a difficult start early in the year as global growth slowed and interest rates declined to record lows on renewed deflation concerns. Real estate investment trusts (REITs) outperformed during this period as investors favored the stocks' predictable income generation and attractive yields. Global economic fears subsided as the year progressed, however, as data generally improved. The amended growth outlook resulted in a rebound in interest rates and an increase in investors' risk appetite. REITs continued to advance as real estate market fundamentals strengthened, before surrendering some of their gains as expectations of a Federal Reserve interest rate hike grew.

Donald Trump's surprise victory in the November U.S. presidential election further lifted growth and inflation expectations, due to the anticipated impact of changes in fiscal and tax policies. The sharp rise in yields weighed on the returns of many higher yielding equities. During this time, the more cyclical real estate sectors such as hotels and industrial REITs produced favorable returns, while those considered to be more defensive like health care and free standing landlords generally declined.

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REIT Preferred Securities Underperformed

REIT preferred securities delivered modestly negative total returns in 2016. They came under pressure early in the year from widening credit spreads and late in the year from rising bond yields. In response to a tightening U.S. labor market and signs of firming inflation, the Federal Reserve raised its target interest rate by 0.25% in December to a range of 0.50% to 0.75% the central bank's only rate hike in 2016. Overall, the preferred securities' strong income generation over the course of the year was not enough to make up for price pressures.

Fund Performance

The Fund had a positive total return for the year and outperformed its blended benchmark on both a market price and NAV basis. Our security selection and underweight allocation to REIT preferreds was a large contributor to relative performance, as we chose not to own a number of issues, particularly in the self storage sector, that underperformed during the year. In addition, the Fund's performance benefited from several out-of-benchmark positions, including preferreds from specialty REIT EPR Properties and Alexandria Real Estate Equities. The latter benefited from strong office demand in prime coastal markets.

Regarding common shares, the effect of the Fund's allocations to shopping centers contributed to relative performance. Most notably, performance benefited from an overweight in the first quarter as the sector outperformed the benchmark and we were underweight when it underperformed in the fourth quarter. The sector, with properties that are generally anchored by non-discretionary grocery stores and bargain-priced retailers, produced a positive total return but lagged the benchmark in the slow-growth environment that prevailed throughout the year.

The Fund's overweight in free standing REITs also contributed to relative performance, although this was partially offset by our stock selection in the sector. Additionally, the effect of our allocations to health care contributed to relative performance, although this was largely offset by our stock selection in the sector. Companies with the most stable cash flows, such as owners of medical office buildings, generally performed quite well during the year, while those with skilled nursing care tenants underperformed amid concerns that regulatory issues could threaten tenants' profit margins.

Our underweight in industrial landlords, the top-performing sector during the year, was a large detractor from relative performance. We were underweight the sector due to generally high valuations, but the shares displayed remarkable strength due to rising logistics demand related to burgeoning internet retailing and as supply absorption exceeded the market's expectations, which resulted in healthy pricing power for the property owners.

The Fund's stock selection and overweight in the underperforming apartment sector also detracted from relative performance. Despite generally healthy demand for apartments, investors were concerned that the sector's cash-flow growth is peaking amid rising supply.

Hotels rallied strongly, particularly in the second half of the year. Investors looked ahead to the end of the new supply cycle, anticipating that industry fundamentals would recover in 2017 along with the economy. Our security selection in the sector contributed to relative performance, but this was more than offset by our underweight allocation. Due to unattractive valuations we did not own several companies that produced impressive returns.

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Impact of Leverage on Fund Performance

The Fund employs leverage as part of a yield-enhancement strategy. Leverage, which can increase total return in rising markets (just as it can have the opposite effect in declining markets), significantly contributed to the Fund's performance for the 12-month period ended December 31, 2016.

Impact of Derivatives on Fund Performance

The Fund engaged in the buying and selling of single stock options with the intention of enhancing total returns and reducing overall volatility. These contracts did not have a material impact on the Fund's total return for the 12-month period ended December 31, 2016.

Sincerely,

WILLIAM F. SCAPELL	THOMAS N. BOHJALIAN
Portfolio Manager	*Portfolio Manager*

JASON YABLON

Portfolio Manager

The views and opinions in the preceding commentary are subject to change without notice and are as of the date of the report. There is no guarantee that any market forecast set forth in the commentary will be realized. This material represents an assessment of the market environment at a specific point in time, should not be relied upon as investment advice and is not intended to predict or depict performance of any investment.

Visit Cohen & Steers online at cohenandsteers.com

For more information about the Cohen & Steers family of mutual funds, visit cohenandsteers.com. Here you will find fund net asset values, fund fact sheets and portfolio highlights, as well as educational resources and timely market updates.

Our website also provides comprehensive information about Cohen & Steers, including our most recent press releases, profiles of our senior investment professionals and their investment approach to each asset class. The Cohen & Steers family of mutual funds invests in major real asset categories including real estate securities, listed infrastructure, commodities and natural resource equities, as well as preferred securities and other income solutions.

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Our Leverage Strategy
(Unaudited)

Our current leverage strategy utilizes borrowings up to the maximum permitted by the Investment Company Act of 1940 to provide additional capital for the Fund, with an objective of increasing the net income available for shareholders. As of December 31, 2016, leverage represented 24% of the Fund's managed assets.

Through a combination of variable and fixed rate financing, the Fund has locked in interest rates on a significant portion of this additional capital for periods expiring in 2017, 2018 and 2019[a] (where we effectively reduce our variable rate obligation and lock in our fixed rate obligation over various terms). Locking in a significant portion of our leveraging costs is designed to protect the dividend-paying ability of the Fund. The use of leverage increases the volatility of the Fund's net asset value in both up and down markets. However, we believe that locking in portions of the Fund's leveraging costs for the various terms partially protects the Fund's expenses from an increase in short-term interest rates.

Leverage Facts[b,c]

Leverage (as a % of managed assets)	24%
% Fixed Rate	85%
% Variable Rate	15%
Weighted Average Rate on Financing	1.9%[a]
Weighted Average Term on Financing	4.4 years[a]

The Fund seeks to enhance its dividend yield through leverage. The use of leverage is a speculative technique and there are special risks and costs associated with leverage. The net asset value of the Fund's shares may be reduced by the issuance and ongoing costs of leverage. So long as the Fund is able to invest in securities that produce an investment yield that is greater than the total cost of leverage, the leverage strategy will produce higher current net investment income for shareholders. On the other hand, to the extent that the total cost of leverage exceeds the incremental income gained from employing such leverage, shareholders would realize lower net investment income. In addition to the impact on net income, the use of leverage will have an effect of magnifying capital appreciation or depreciation for shareholders. Specifically, in an up market, leverage will typically generate greater capital appreciation than if the Fund were not employing leverage. Conversely, in down markets, the use of leverage will generally result in greater capital depreciation than if the Fund had been unlevered. To the extent that the Fund is required or elects to reduce its leverage, the Fund may need to liquidate investments, including under adverse economic conditions which may result in capital losses potentially reducing returns to shareholders. There can be no assurance that a leveraging strategy will be successful during any period in which it is employed.

[a] On February 24, 2015, the Fund amended its credit agreement to extend the fixed rate financing terms by three years expiring in 2020, 2021 and 2022. The weighted average rate on financing does not include the three year extension and will increase as the extended fixed-rate tranches become effective. The weighted average term on financing includes the three year extension.

[b] Data as of December 31, 2016. Information is subject to change.

[c] See Note 7 in Notes to Financial Statements.

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December 31, 2016
Top Ten Holdings[a]
(Unaudited)

Security	Value	% of Managed Assets
Simon Property Group	$125,129,783	6.5
Prologis	85,124,772	4.4
Vornado Realty Trust	67,046,453	3.5
Equinix	64,468,901	3.3
UDR	63,061,772	3.3
Essex Property Trust	47,252,603	2.5
Public Storage	45,317,084	2.4
Kilroy Realty Corp.	40,506,402	2.1
Brixmor Property Group	40,348,897	2.1
Equity Residential	39,856,925	2.1

[a] Top ten holdings are determined on the basis of the value of individual securities held. The Fund may also hold positions in other types of securities issued by the companies listed above. See the Schedule of Investments for additional details on such other positions.

Sector Breakdown

(Based on Managed Assets)
(Unaudited)

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SCHEDULE OF INVESTMENTS

December 31, 2016

		Number of Shares	Value
COMMON STOCK REAL ESTATE	101.2%		
DIVERSIFIED	7.9%		
American Assets Trust[a,b]		337,860	$ 14,555,009
BGP Holdings PLC (EUR) (Australia)[c,d]		3,927,678	216,646
Gramercy Property Trust		2,181,024	20,021,800
Vornado Realty Trust[a,b]		642,392	67,046,453
Washington REIT		445,188	14,553,196
			116,393,104
HEALTH CARE	9.8%		
HCP[a,b]		1,300,536	38,651,930
Healthcare Trust of America, Class A[a]		1,246,447	36,284,072
Physicians Realty Trust[a,b]		1,913,060	36,271,618
Quality Care Properties[d]		314,701	4,877,865
Ventas		430,300	26,902,356
			142,987,841
HOTEL	4.8%		
Host Hotels & Resorts[a,b]		1,997,973	37,641,811
Pebblebrook Hotel Trust		345,497	10,278,536
Sunstone Hotel Investors[a]		1,493,037	22,768,814
			70,689,161
INDUSTRIALS	5.8%		
Prologis[a,b]		1,612,517	85,124,772
NET LEASE	5.6%		
Four Corners Property Trust		400,705	8,222,467
Gaming and Leisure Properties[a]		615,634	18,850,713
Spirit Realty Capital		3,574,515	38,819,233
STORE Capital Corp.		677,452	16,739,839
			82,632,252
OFFICE	12.6%		
Alexandria Real Estate Equities[a]		308,406	34,273,159
Boston Properties[a,b]		192,744	24,243,340
Douglas Emmett[a,b]		828,297	30,282,539
Highwoods Properties		176,862	9,021,731
Hudson Pacific Properties[a,b]		512,400	17,821,272
Kilroy Realty Corp.[a,b]		553,215	40,506,402

See accompanying notes to financial statements.

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SCHEDULE OF INVESTMENTS (Continued)

December 31, 2016

		Number of Shares	Value
SL Green Realty Corp.		270,275	$ 29,068,076
			185,216,519
RESIDENTIAL	22.8%		
APARTMENT	20.3%		
American Campus Communities[a]		796,447	39,639,167
Apartment Investment & Management Co.[a]		858,711	39,028,415
Colony Starwood Homes[a,b]		1,128,348	32,507,706
Equity Residential[a,b]		619,281	39,856,925
Essex Property Trust[a,b]		203,237	47,252,603
Mid-America Apartment Communities		367,770	36,012,039
UDR[a,b]		1,728,667	63,061,772
			297,358,627
MANUFACTURED HOME	2.5%		