

# Annual Management Report of Fund Performance

## Income Portfolio

# Meritage Moderate Income Portfolio

As at December 31, 2007

This annual management report of fund performance contains financial highlights, but does not contain the complete annual financial statements of the Portfolio. You can get a copy of the annual financial statements at your request, and at no cost, by calling 1-866-603-3601, by emailing us at [infomeritage@nbc.ca](mailto:infomeritage@nbc.ca) or by visiting our website at [www.meritageportfolios.com](http://www.meritageportfolios.com) or SEDAR at [www.sedar.com](http://www.sedar.com).

Security holders may also contact us using one of these methods to request a copy of the Portfolio's proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure.

## Management Discussion of Fund Performance

### Investment Objectives and Strategies

The Portfolio seeks to gain long-term capital growth while generating current income, by investing in a diversified mix of fixed income and equity mutual funds. The target weight for this portfolio is 60% - 70% of net assets in Canadian and global income with 30% - 40% of net assets in Canadian and global equity. While the Portfolio may invest up to 100% of the Fund's assets in the underlying investment funds managed by third parties, changes such as the removal, addition or percentage held in the underlying investment fund may occur, including the position held in cash, money market securities or money market funds as a defensive measure during certain market conditions. The Portfolio may also invest in foreign equity mutual funds and directly invest in securities held in foreign equities.

### Risks

The risks of investing in the Portfolio remain as discussed in the prospectus. The overall risk level of the portfolio has not changed significantly. However, the following external factors are worth noting.

Some investments within the Portfolio are denominated in foreign currencies. Although some of the underlying funds do partly or fully hedge the currency, an exposure remains for most of the other funds. All equity underlying funds have the possibility to hedge. The relative strength or weakness in the Canadian dollar against these other currencies will have an impact on the performance of the portfolio. Investors who elect to invest in a currency other than their domestic currency face currency risks.

This Portfolio's underlying funds could invest a portion of their assets in companies domiciled in emerging markets, which tend to have higher political risks than developed markets.

The fixed-income allocation of the Portfolio is subject to interest-rate risks. This is particularly important when interest rates are rising as the principal value of the holdings will therefore decline.

Other risks to the Portfolio are asset mix risks, security selection risks and equity risks. The investment alternatives are many, so the decision to allocate investment capital to a particular type of security, geographic region or company may have a significant impact on the Portfolio's results, especially relatively to its blended benchmark. Finally, the underlying funds managers mitigate equity risk through sector diversification by ensuring a high quality among the companies that are selected for the fund.



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## Results of Operations

The Meritage Moderate Income Portfolio returned 0.80% during the 12-month period ended December 31, 2007 compared to 4.97% for its blended benchmark during the same period. The blended benchmark is comprised of the DEX Universe Bond Index (65%), the S&P/TSX Composite Index (30%) and the MSCI World Index (\$C) (5%). Unlike the benchmark, the Portfolio's return is calculated after the deduction of fees and expenses. Please see the "Past Performance" section for performance returns of the other series.

The DEX Universe Bond Index returned 3.68% for the period. With equities reeling and investors seeking refuge from the carnage, bonds benefited. However, not all bonds gained, as corporate and high yield bonds suffered their worst year since the beginning of the decade as spreads widened on fears of a financial contagion. Government issues proved the big winners.

The S&P/TSX Composite Index returned 9.83% during the period. The Canadian equity markets managed to eek out solid gains on the year. However, these gains were sliced by half from the peak reached in July. While markets did show plus signs at the end of the period, these pluses, upon further analysis, were somewhat deceiving.

The Canadian dollar continued its ascent compared to most major currencies, especially its U.S. counterpart, breaching US\$1.10 in November, prior to ending the year near parity. The strength of the Loonie has a significant impact on Canadian manufacturers, particularly those companies with U.S. dollar revenues and Canadian dollar costs.

The MSCI World Index (\$C) returned -7.53%. Global equity markets exhibited significant volatility in 2007. The weak U.S. housing market, and the resulting tightening in the credit market, weighed on equities, particularly in the fourth quarter, as massive write downs by global banks, investment banks and other financial institutions tied to U.S. subprime mortgages rattled investor confidence.

Seven of the ten Portfolio holdings added to performance. The largest contribution came from the Dynamic Focus + Diversified Income Fund with a return of 7.39%. The other contributors were, the GGOF Monthly High Income II Fund with a return of 5.99%, the Beutel Goodman Income Fund with 3.61%, the RBC Canadian Dividend Fund with 2.96%, the TD Short Term Bond Fund with 2.53%, the TD Canadian Bond Fund with 1.78% and the TD Real Return Bond Fund with 0.84%. These positive results were partly offset by the negative performance of the following funds: the Trimark Fund at -10.39%, the CI Signature Dividend Fund at -5.09% and the Mackenzie Sentinel Corporate Bond Fund at -0.28%.

With the exception of the GGOF Monthly High Income II Fund and the Dynamic Focus + Diversified Income Fund, all the other underlying funds underperformed the blended benchmark. In most cases, differences in performance with respect to the benchmark can be explained by the specific investment styles, which materialized in substantial sector allocation differences from the benchmark.

The Portfolio's target mix was unchanged during the period, and the Portfolio was continuously invested in line with its initial targets. The Portfolio's net assets totalled \$16.0 million at the end of the period. The increase is attributable to the overall portfolio performance.

## Recent Events

During the period, no changes were made to the Portfolio's asset allocation or underlying funds. The Portfolio continues to invest its assets with some of the most respected money management firms in Canada and around the world. The Portfolio expects to remain fully diversified across the underlying funds, and money managers. A purely quantitative selection and monitoring process, the Select Rating System, as well as objective and regular review by Aon Consulting will ensure that your investment remains on target, while auto-rebalancing of the Portfolio will maintain the risk profile of your investment. No biases or economic forecasts are made with regards to specific assets, sectors or regions.

## **Related Party Transactions**

### **Management Fee**

For its services as manager of the Portfolio, the Portfolio pays to Altamira Investment Services Inc. (“Altamira Services”) a management fee (“Management Fee”) based on the average daily net asset value of the Portfolio. Altamira Services is an indirect wholly-owned subsidiary of the National Bank of Canada (the “Bank”).

The Management Fee is calculated daily and paid monthly. The Management Fee covers Altamira Services’ costs of managing the Portfolio’s investments. As the Portfolio invests in underlying funds, the fees and expenses payable in connection with the management of the underlying funds are in addition to those payable by the Portfolio. However, Altamira Services makes sure that the Portfolio does not pay any management fees that, to a reasonable person, would duplicate a fee payable by an underlying fund in the Portfolio for the same service.

Altamira Services has appointed Natcan Trust Company (“NTC”), an indirect wholly-owned subsidiary of the Bank, as the portfolio advisor for the Portfolio, the custodian, the registrar and the transfer agent. NTC is also the trustee of the Portfolio and has responsibility for valuation of the Portfolio and the Portfolio’s accounting and records. NTC is paid for these functions by Altamira Services.

### **Operating Expenses**

The Portfolio reimbursed Altamira Services for operating expenses, at cost, incurred in administering the Portfolio, including trustee, record-keeping, custodial, legal, audit, investor servicing, and security holder reporting fees.

### **Brokerage Commissions**

NTC, as portfolio advisor to the Portfolio, is responsible for the execution of all portfolio transactions, including, as applicable, the selection of market and dealer and the negotiation of commissions and other terms. In effecting portfolio transactions, NTC seeks to obtain prompt execution of orders on favourable terms.

NTC may place portfolio transactions with National Bank Direct Brokerage Inc. (“NBDB”) and National Bank Financial Inc. (“NBF”), each of which are, indirect and direct respectively, wholly-owned subsidiaries of the Bank or with another affiliated dealer. Pricing, services and other terms must be comparable to those offered by third party dealers for such transactions to be executed. Altamira Services pays commissions to affiliated dealers such as NBDB and NBF for purchases, sales and holdings of Portfolio units. Altamira Services earns commissions from NBDB for trades executed by NBDB and for Portfolio assets held at NBDB.

# Financial Highlights

## Advisor Series

The following tables show selected key financial information about the Portfolio and are intended to help you understand the Portfolio's financial performance for the past two years. This information is derived from the Portfolio's audited annual financial statements.

## Net Asset Value (NAV) per Unit

	2007	2006 95 days
Net asset value, beginning of year	\$ 9.99	\$ 10.00
<b>Increase (decrease) from operations:</b>		
Total revenue	\$ 0.49	\$ 0.11
Total expenses	\$ (0.20)	\$ (0.05)
Realized gains (losses)	\$ 0.14	\$ 0.20
Unrealized gains (losses)	\$ (0.40)	\$ (0.14)
<b>Total increase (decrease) from operations<sup>(1)</sup></b>	<b>\$ 0.03</b>	<b>\$ 0.12</b>
<b>Distributions:</b>		
From income (excluding dividends)	\$ (0.19)	\$ (0.02)
From dividends	\$ (0.09)	\$ (0.01)
From capital gains	\$ (0.12)	\$ (0.09)
Return of capital	\$ (0.27)	\$ (0.06)
<b>Total annual distributions<sup>(2)</sup></b>	<b>\$ (0.67)</b>	<b>\$ (0.18)</b>
<b>Net asset value as at December 31 of year shown</b>	<b>\$ 9.40</b>	<b>\$ 9.99</b>

<sup>(1)</sup> Net asset value and distributions are based on the actual number of units outstanding at the relevant time. The increase or decrease from operations is based on the weighted average number of units outstanding over the financial period.

<sup>(2)</sup> Distributions were paid in cash or reinvested in additional units of the Portfolio, or both.

## Ratios and Supplemental Data

	2007	2006 95 days
Net assets (000's) <sup>(1)</sup>	\$ 15,864	\$ 6,227
Number of units outstanding <sup>(1)</sup>	1,688,359	623,403
Management expense ratio <sup>(2)</sup>	2.03 %	2.04 %
Management expense ratio before waivers or absorptions	2.47 %	2.87 %
Portfolio turnover rate <sup>(3)</sup>	18.89 %	0.25 %
Trading expense ratio <sup>(4)</sup>	0.00 %	0.00 %

<sup>(1)</sup> This information is provided as at December 31 of the year shown.

<sup>(2)</sup> Management expense ratio is based on total expenses for the stated period and is expressed as an annualized percentage of daily average net assets during the period.

<sup>(3)</sup> The portfolio turnover rate indicates how actively the portfolio advisor manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Portfolio buying and selling all of the securities in its portfolio once in the course of the year. The higher the portfolio turnover rate in a year, the greater the trading costs payable by the Portfolio in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a Portfolio.

<sup>(4)</sup> The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net assets during the period.

# Financial Highlights

## F Series

The following tables show selected key financial information about the Portfolio and are intended to help you understand the Portfolio's financial performance for the past two years. This information is derived from the Portfolio's audited annual financial statements.

### Net Asset Value (NAV) per Unit

	2007	2006 95 days
Net asset value, beginning of year	\$ 9.94	\$ 10.00
<b>Increase (decrease) from operations:</b>		
Total revenue	\$ 0.46	\$ 0.13
Total expenses	\$ (0.12)	\$ (0.03)
Realized gains (losses)	\$ 0.15	\$ 0.21
Unrealized gains (losses)	\$ (0.42)	\$ (0.12)
<b>Total increase (decrease) from operations<sup>(1)</sup></b>	<b>\$ 0.07</b>	<b>\$ 0.19</b>
<b>Distributions:</b>		
From income (excluding dividends)	\$ (0.23)	\$ (0.07)
From dividends	\$ (0.08)	\$ (0.04)
From capital gains	\$ (0.12)	\$ (0.10)
Return of capital	\$ (0.24)	\$ (0.03)
<b>Total annual distributions<sup>(2)</sup></b>	<b>\$ (0.67)</b>	<b>\$ (0.24)</b>
<b>Net asset value as at December 31 of year shown</b>	<b>\$ 9.43</b>	<b>\$ 9.94</b>

<sup>(1)</sup> Net asset value and distributions are based on the actual number of units outstanding at the relevant time. The increase or decrease from operations is based on the weighted average number of units outstanding over the financial period.

<sup>(2)</sup> Distributions were paid in cash or reinvested in additional units of the Portfolio, or both.

### Ratios and Supplemental Data

	2007	2006 95 days
Net assets (000's) <sup>(1)</sup>	\$ 143	\$ 102
Number of units outstanding <sup>(1)</sup>	15,141	10,222
Management expense ratio <sup>(2)</sup>	1.24 %	1.20 %
Management expense ratio before waivers or absorptions	1.68 %	1.82 %
Portfolio turnover rate <sup>(3)</sup>	18.89 %	0.25 %
Trading expense ratio <sup>(4)</sup>	0.00 %	0.00 %

<sup>(1)</sup> This information is provided as at December 31 of the year shown.

<sup>(2)</sup> Management expense ratio is based on total expenses for the stated period and is expressed as an annualized percentage of daily average net assets during the period.

<sup>(3)</sup> The portfolio turnover rate indicates how actively the portfolio advisor manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Portfolio buying and selling all of the securities in its portfolio once in the course of the year. The higher the portfolio turnover rate in a year, the greater the trading costs payable by the Portfolio in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a Portfolio.

<sup>(4)</sup> The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net assets during the period.

# Management Fees

The Portfolio pays annual management fees to Altamira Services (the “Manager”) in consideration for management and administrative services and facilities required by the Portfolio in its day to day operations. The management fees charged to the Portfolio amounted to \$229,767 for the year ended December 31, 2007. The fees are calculated as a fixed percentage of the Portfolio’s average daily net asset value and accrued on a daily basis. The Portfolio Advisor fees are paid by the Manager and are calculated monthly based on the average assets of the Portfolio and can fluctuate depending on the size of the assets. Dealers are paid by the Manager – called a trailer commission – for all assets that their sales representatives place in the Portfolio. The trailer commission is calculated as a percentage of the assets each dealer has placed in a Portfolio. Trailer commissions are paid as a percentage of assets to dealers based on the range shown below. The fee depends on the fund and the sales charge option.

Category of Portfolio	Management fees (%)	Initial Sales Charge		Deferred Sales Charge <sup>(2)</sup>		Low Load Charge <sup>(3)</sup>		
		Commission %	Trailer Commission %	Commission %	Trailer Commission %	Commission %	Trailer Commission %	
							(1-3 yrs)	(+3 yrs)
<b>Meritage Moderate Income Portfolio</b>								
Advisor Series	1.75	0 - 5.0	0.75	5.0	0.25	2.50	0.25	0.75
F Series <sup>(1)</sup>	1.00							

<sup>(1)</sup> For F Series, no trailer commissions are paid. The dealer or broker is paid an annual fee based on the asset value of your account instead of paying a commission for each purchase, switch or redemption.

<sup>(2)</sup> Under the DSC option, you will have to pay a redemption fee to redeem your units. The fee depends on the initial cost of your securities and the length of time you hold them. After 6 years, the fee is 0%.

<sup>(3)</sup> Under the low load 2 sales option, you have to pay a redemption fee to redeem your units. The fee depends on the initial cost of your securities and the length of time you hold them. After 3 years, the fee is 0%.

## Summary of Investment Portfolio

The summary of investment portfolio may change due to ongoing portfolio transactions of the investment fund. A quarterly update is available. For more information please contact us at [infomeritage@nbc.ca](mailto:infomeritage@nbc.ca) or 1-866-603-3601 or your financial advisor.

The prospectus and other information about the underlying investment funds are available on the internet at [www.sedar.com](http://www.sedar.com).

Total net assets as at December 31, 2007 .....\$16 Million

### Top 25 Holdings

	% NAV
Beutel Goodman Income Fund.....	17.81
TD Canadian Bond Fund.....	17.58
TD Short Term Bond Fund.....	10.12
TD Real Return Bond Fund.....	9.95
Mackenzie Sentinel Corporate Bond Fund.....	9.85
Dynamic Focus + Diversified Income Trust Fund.....	7.88
GGOF Monthly High Income II Fund.....	7.80
RBC Canadian Dividend Fund.....	7.67
CI Signature Dividend Fund.....	7.13
Trimark Fund.....	4.40
Cash & Other Assets.....	-0.19
Top 25 Holdings as % of Total Portfolio.....	100.00

### Asset Allocation

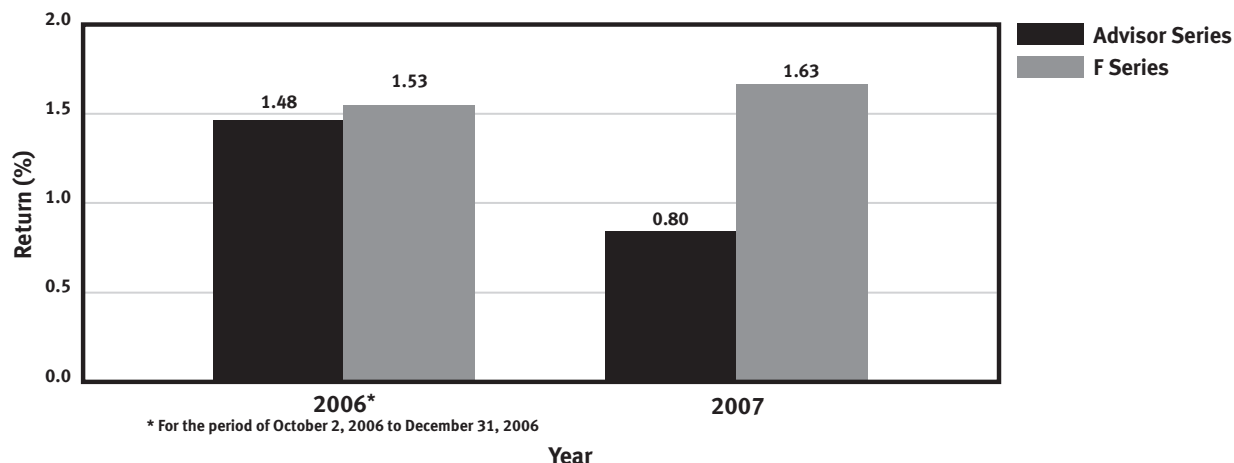
	% of Portfolio
Fixed Income.....	65.31
Canadian Equity.....	30.48
Global Equity.....	4.40
Cash & Other Assets.....	-0.19
Total Asset Allocation.....	100.00

# Past Performance

The returns of each Portfolio or series of a Portfolio are calculated as of December 31 in each year, assume the reinvestment of all distributions and do not take into account sales, redemption charges, distributions, or optional charges that would have reduced returns. Past performance of a Portfolio or series of a Portfolio does not necessarily indicate how it will perform in the future.

## Annual Returns

The following bar chart shows the Portfolio's annual performance for each of the years shown and illustrates how the Portfolio's performance has changed from year to year. It shows in percentage terms how an investment made on January 1 would have increased or decreased by December 31 for each year.



## Annual Compound Returns

The following table shows the Portfolio's annual compound total return for the one year period ended on December 31, 2007, and the period from inception of the Portfolio to December 31, 2007. The annual compound total return is also compared to a blended index consisting of the DEX Universe Bond Index (65%), the S&P/TSX Composite Index (30%) and the MSCI World Index (\$C) (5%) calculated on the same compound basis for the same period (a comparison has also been provided for each index). A discussion of the Portfolio's relative performance in comparison to the index (or indices) can be found in the Results of Operations section of this report.

Meritage Moderate Income Portfolio	Since inception	Past year
Advisor Series	1.83 %	0.80 %
F Series	2.54 %	1.63 %
DEX Universe Bond Index (65%), S&P/TSX Composite Index (30%) and MSCI World Index (\$C) (5%)	7.49 %	4.97 %
DEX Universe Bond Index	3.51 %	3.68 %
S&P/TSX Composite Index	16.69 %	9.83 %
MSCI World Index (\$C)	4.09 %	-7.53 %

The DEX Universe Bond Index (previously known as the SCM Universe Bond Index) is comprised of over 900 bonds with a term to maturity of more than one year and reflects the Canadian Bond market. The S&P/TSX Composite index is comprised of over 300 Canadian stocks and is designed to represent the Canadian equity market. The MSCI World Index is comprised of over 1500 stocks representing approximately 22 countries and measures the total return of equity securities available in developed markets globally.

### Note on forward-looking statements

This document may contain forward-looking statements concerning the Portfolio, its future performance, its strategies or prospects or about future events or circumstances. Such forward-looking statements include, among others, statements with respect to beliefs, plans, expectations, estimates and intentions.

By their very nature, forward-looking statements imply the use of assumptions and necessarily involve inherent risks and uncertainties, both general and specific. There is a significant risk that the explicit or implicit forecasts contained in these forward-looking statements might not materialize or that they may not prove to be accurate. A number of factors could cause future results, conditions or events to differ materially from those expressed in the forward-looking statements. Such differences might be caused by several factors including changes in Canadian and worldwide economic and financial conditions, market trends, new regulatory provisions, competition, changes in technology and the potential impact of conflicts and other international events, and other risks described in detail in the Portfolio's current simplified prospectus.

The foregoing list of factors is not exhaustive. Before making any investment decision, investors and others relying on our forward-looking statements should carefully consider the foregoing factors and the uncertainties and risks they contain. We caution readers not to place undue reliance on these forward-looking statements.

Forward-looking statements are issued in good faith and may be modified without notice. We assume no obligation to update forward-looking statements in the light of new information, future events or other circumstances unless required by applicable legislation.

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