NORTHWATER

Northwater Five-Year Market-Neutral Trust
December 31, 2008
Annual Report

BACKGROUND

Northwater Five-Year Market-Neutral Trust (the "Trust") is a closed-end investment trust established under the laws of the Province of Ontario. Financial statements of the Trust, denominated in Canadian dollars, for the year ended December 31, 2008 are included in this report.

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MESSAGE TO UNITHOLDERS FROM THE INVESTMENT ADVISOR

The Northwater Five-Year Market-Neutral Trust (the "Trust") is a closed-end fund traded on the Toronto Stock Exchange under the symbol NYF.UN that delivers the return of both a diversified portfolio of market-neutral hedge funds and a fixed-for-floating interest rate swap by way of a forward agreement. As at December 31, 2008, the net asset value of the Trust per unit was $12.06. For the year ended December 31, 2008, the return of the Trust was -36.80% including distributions. During the same time period, the DEX Universe Bond Index returned 6.41%, the S&P/TSX Composite Index declined by 33.00% and the S&P 500 in U.S. dollar terms, fell by 37.00% which translates to a loss of 21.20% in Canadian dollar terms. The Trust made distributions of $1.75 per unit during the year.

Overall, the return of the Trust in 2008 was disappointing from both an absolute return basis as well as from its lack of neutrality in respect of other asset class returns. Performance of all asset classes was impacted by the escalating uncertainty which surrounded the state of the global financial system. The Trust's hedge fund investments were not immune to these stresses in the capital markets. The Trust's levered exposure to the portfolio of hedge funds exacerbated the negative performance of the Trust.

The credit crisis which began to unfold in the US sub-prime housing market during the last quarter of 2007, continued to unravel across all markets during 2008. Credit markets contracted, banks restricted lending to each other and the deleveraging spiral negatively impacted all market participants including hedge funds. Strategies that rely on normalization of historical spreads were dramatically impacted by widening spreads while the price and availability of leverage altered the fundamental economics of some profitable trades. Regulatory uncertainty increased in mid 2008 when new short selling rules altered some fund's abilities to adequately hedge in the equity markets. The bankruptcy of Lehman Brothers and subsequent AIG bailout increased the overall market uncertainty leading into the final quarter of 2008. Spread widening in credit markets combined with technical pricing pressures and increased volatility in the hedging instruments made for extremely volatile and often negative returns in many of the hedge funds held by the Trust. While the hedge fund managers were reducing risk in their portfolios, the investor demand for the return of capital from these hedge fund managers increased leading into year end, putting further pressure on hedge fund's underlying investments.

Although the market outlook for many of the hedge fund strategies has improved, the Trust is proceeding with an orderly windup scheduled for

June 30, 2009 in accordance with the prospectus of the Trust. As such we are focused on creating liquidity and returning capital to unitholders.

Based on current market conditions, the Manager anticipates that due to liquidity constraints in the underlying hedge funds it is likely that the Trust will continue to exist and be winding down its operation beyond the originally scheduled June 30, 2009 termination date.

As of January 31, 2009, approximately 55% of the Fund (76% of the Trust) will continue to have exposure to underlying hedge funds market movements. Based on the most recent information that the Manager had available to it, the Manager anticipates that approximately 42% of the Fund (representing 18 hedge funds) (58% of the Trust) may be subject to restrictions on liquidity that could extend beyond the June 30, 2009 termination date of the Fund.

DANIEL C.R. MILLS, CFA
Managing Director and Deputy Chief Investment Officer
Northwater Capital Management Inc.

DAVID S. FINCH, CFA
Managing Director and Chief Investment Officer
Northwater Capital Management Inc.

March 23, 2009

MANAGEMENT REPORT OF FUND PERFORMANCE

This Management Report of Fund Performance contains financial highlights but does not contain the complete financial statements of Northwater Five-Year Market-Neutral Trust (the “Trust”). A copy of the financial statements of the Trust for the year ended December 31, 2008 is attached to this report for your reference.

Security holders may contact us using one of the following methods and may, at no cost, request a copy of the Trust’s proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure. You can contact us, at no cost, by calling toll-free 1-888-429-8774 or by writing to us at Northwater Fund Management Inc., Suite 4700, Brookfield Place, Bay Wellington Tower, 181 Bay Street, P.O. Box 794, Toronto, Ontario, M5J 2T3. You may also visit our website at *www.northwatercapital.com* or the SEDAR website at *www.sedar.com*.

Northwater Five-Year Market-Neutral Trust is managed by Northwater Fund Management Inc. (the “Manager”). The Manager is responsible for managing the business and administering the Trust pursuant to the provisions of the declaration of trust as well as for monitoring the Trust’s investment portfolio. The Manager has retained Northwater Capital Management Inc. (the “Investment Advisor”) to provide investment advice and manage the Trust’s investment portfolio in accordance with the Trust’s investment objectives. In fulfilling its responsibilities, the Manager must ensure that appropriate information systems, procedures and controls are in place in order to ascertain that information used internally and disclosed to unitholders is complete and reliable. The Manager takes this responsibility seriously and is satisfied that appropriate systems, procedures and controls are in place for the Trust.

All amounts noted throughout this report are in Canadian dollars unless otherwise specifically indicated.

Adoption of New Accounting Standards

In December 2006, the Accounting Standards Board issued Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 3862, “Financial Instruments – Disclosures” (“S. 3862”) and Section 3863, “Financial Instruments – Presentation” (“S. 3863”), which provide comprehensive disclosure and presentation requirements for financial instruments.

In addition, in December 2006, the Accounting Standards Board issued CICA Handbook Section 1535 “Capital Disclosures” (“S.1535”), which provides standards for disclosing information about an entity’s capital and how it is managed.

The requirements of S. 3862, S. 3863 and S.1535 are effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007 and have been reflected in the notes to the financial statements.

Investment Objective and Strategies

Investment Objectives

The investment objectives of Northwater Five-Year Market-Neutral Trust (the "Trust") comprise making tax-efficient cash distributions to unitholders, while achieving low correlation and low volatility, as well as on termination of the Trust providing for capital repayment to the unitholders of the original subscription price of the units.

Investment Strategies

The Trust has invested the net proceeds of its offering in a portfolio of common shares of Canadian public companies (the "Common Share Portfolio"). The Trust has entered into a forward purchase and sale agreement (the "Forward") with a U.S. bank (the "Counterparty") that has a long term credit rating of AA. The Forward provides the Trust with exposure to the performance of Northwater Five-Year Market-Neutral Fund Limited (the "Fund"), an exempt company formed under the laws of the Cayman Islands and advised by the Investment Advisor, in exchange for the return of the Common Share Portfolio. Pursuant to the Forward, the Common Share Portfolio has been pledged to the Counterparty. The Trust's valuation is not affected by the change in the market value of the Common Share Portfolio as gains or losses are offset by the Forward. The Trust's return is based on its exposure, through the Forward, to the Fund.

The Fund holds a diversified portfolio of market-neutral hedge funds (the "Hedge Fund Portfolio"). The target exposure to the Hedge Fund Portfolio is equivalent to 150% of the net asset value of the Trust. The actual exposure as at December 31, 2008 was 146% (December 31, 2007 was 145%). In establishing the Hedge Fund Portfolio "mix," the Investment Advisor seeks out strategies that have a low correlation with one another, thereby increasing the benefits of diversification and reducing expected volatility. There can be no assurance that the Trust's performance will exhibit strong risk-adjusted returns. The Investment Advisor believes, however, that the Trust's exposure to the Fund, which holds a well-diversified portfolio of market-neutral hedge funds, should result in the returns of the Trust having a low correlation with major equity and fixed income markets and a low volatility. The additional exposure provided by the leverage in the Forward will increase the risk to unitholders and will not enhance returns in the event that the Hedge Fund Portfolio declines in value.

Through the Forward, the Trust also has exposure to interest rate swaps (the "Swaps") entered into by the Fund. The Trust is expected to earn a blended fixed rate of 4.45% over its life plus the returns in excess of money market rates earned by exposure to the diversified portfolio of market-neutral hedge funds. The Trust has exposure to changes in mid-term interest rates. For example, if mid-term interest rates were to decrease (increase) by 1%, the value of the Trust would increase (decrease) by approximately 0.49%.

Investment Management Process

The Trust's investment objectives and strategy are supported by the implementation of an investment management process. The Trust is dependent on the knowledge and expertise of the Investment Advisor to implement the investment management process. The Investment Advisor's ability to deliver results is dependent upon a team of investment professionals that research, analyze and monitor the investments of the Trust and the Hedge Fund Portfolio. The Investment Advisor conducts all of its investment research in-house.

This investment management process comprises selection and ongoing monitoring of the hedge fund investments, including but not limited to: comprehensive quantitative and qualitative assessment of hedge fund managers, including hedge fund manager reviews involving on-site interviews, monthly portfolio reviews and various industry references; comprehensive investment and operational due diligence process; the construction of a diversified model portfolio using various portfolio construction techniques, including mathematical optimization, statistical process control and factor analysis and use of an established operational infrastructure necessary for managing complex fund of market-neutral hedge fund and derivatives strategies.

The Investment Advisor manages and advises client accounts in addition to the Trust and the Fund. Client accounts with similar investment objectives are generally managed in a similar manner. Investment allocation decisions are subject to client guidelines and restrictions. Limited investment opportunities will be allocated to client accounts in a manner that the Investment Advisor determines is equitable to clients in the circumstances.

The Trust is entitled to borrow up to 10% of the net asset value for purposes of funding redemptions of units, purchases of units in the market and payment of expenses.

As at December 31, 2008, financial leverage employed by the Trust was nil (December 31, 2007 was nil).

Risks

The following table presents information for the period from inception ending December 31, 2008 and 2007 regarding the risk profile of the Trust and the Fund.

Trust Statistics	For the period from inception to December 31, 2008	For the period from inception to December 31, 2007
# of positive monthly returns	33	31
# of negative monthly returns	21	11
% of negative months	38.9%	26.2%
Average size of negative months	(2.77)%	(1.08)%
Worst monthly return	(15.80)%	(4.29)%

The following table presents information for the years ended December 31, 2008 and 2007, regarding the risk profile of the Fund's hedge fund holdings.

	Year ended December 31,	
Single Hedge Fund Statistics	2008	2007
# of hedge funds with positive returns(1, 2)	6	24
# of hedge funds with negative returns(1, 2)	22	9
Average annual hedge fund standard deviation(2, 3)	15.21%	6.92%
Average correlation between hedge funds(2, 4)	0.42	0.25

(1) Measured for hedge funds in the Hedge Fund Portfolio of the Fund as at December 31, 2008 and December 31, 2007, respectively.

(2) As measured over the past 24 months for hedge funds in the Hedge Fund Portfolio of the Fund as December 31, 2008 and December 31, 2007 respectively, excludes hedge funds with less than 24 months of historical returns.

(3) Standard deviation is defined as a measure of dispersion of returns around a mean (average return). A low standard deviation implies low risk of experiencing returns that vary highly in magnitude from the mean.

(4) Correlation is a measure of the degree to which variables (such as performance of two hedge funds) move together.

No material changes affecting the overall risk of investing in the Trust were made by the Manager in the year ended December 31, 2008. However, the hedge fund industry, like other market participants, has been subject to unprecedented turmoil in the markets due to the ongoing credit crisis.

The change in the risk characteristics of the Trust reflects the magnitude of the stress felt across the entire financial system in 2008. Trust returns in 2008 were uncharacteristically skewed to the negative on a monthly basis and the Trust experienced its worst monthly return since inception.

As illustrated in the Single Hedge Fund Strategies chart above, diversification across managers was not sufficient to avoid the overwhelming negative impact from the industry wide deleveraging. The volatility in the underlying managers (as expressed by standard deviation) rose to 15.21% versus the 2007 level of 6.92%.

The similarity of manager returns (average correlation between hedge funds), which had historically been very low and stable, spiked in 2008, which is reflective of the magnitude of the problems across all financial markets.

Many of the trading strategies employed by hedge funds depend on functional financial markets, including the ability of managers to enter into short positions. Hedge funds have not only suffered losses as a result of the stress felt in the markets, including the difficulty encountered in maintaining short positions, but also because of the liquidity freeze experienced in many markets. Certain of the managers have been unable to sell assets to prevent additional losses or fund investor redemptions. Continuing illiquidity has caused numerous underlying hedge funds held by the Trust to invoke various restrictions on redemptions including, without limitation, restricting redemptions to a limited percentage of the aggregate net asset value of such underlying hedge funds, the temporary suspension of redemptions altogether, or the commencement of a controlled liquidation and wind-up of the underlying hedge funds' business.

Based on current market conditions, the Manager anticipates that due to liquidity constraints in the underlying hedge funds it is likely that the Fund and the Trust will continue to exist and be winding down its operations beyond the originally scheduled June 30, 2009 termination date.

As of January 31, 2009, approximately 55% (76% of the Trust) of the Fund will continue to have exposure to underlying hedge funds market movements. Based on the most recent information that the Manager had available to it, the Manager anticipates that approximately 42% of the Fund (representing 18 hedge funds) (58% of the Trust) may be subject to restrictions on liquidity that could extend beyond the June 30, 2009 termination date of the Fund.

As at December 31, 2008, the Investment Advisor submitted redemption requests to all the underlying hedge funds in anticipation of the Fund's scheduled termination date.

The following table shows the expected payout timeline of redemption proceeds from the underlying hedge funds held by the Fund:

Payments of redemptions expected in 2009, classified by status of the hedge funds being redeemed from:

	Amount (USD$)	% of hedge fund portfolio as at December 31, 2008
Normal Course	9,325,495	34%
Restricted redemptions [1, 2]	3,377,623	12%
Liquidating	1,094,197	4%
	13,797,315	50%

Payments of redemptions expected beyond 2009, classified by status of the hedge funds being redeemed from:

	Amount (USD$)	% of hedge fund portfolio as at December 31, 2008
Restricted redemptions [1]	10,118,350	36%
Liquidating	3,838,496	14%
	13,956,846	50%

(1) Restricted redemptions category includes situations where the hedge fund manager has placed some form of restriction on the redemption request, including suspending redemptions, enforcing gates on redemption or restructuring the fund, to for example, create a liquidating share class.

(2) Although these redemptions are currently restricted, the Investment Advisor anticipates that the redemption proceeds will still be received during 2009.

The detailed risks of investing in the Trust are listed in the Trust's prospectus. A copy of the prospectus of the Trust is available by visiting the SEDAR website at www.sedar.com.

Results of Operations

For the year ended December 31, 2008, the Trust posted a return of -36.80% year ended December 31, 2007: -0.26%), taking into account the distributions made during the year. Distributions during the year totaled $4,221,481 or $1.75 interest rate per Unit.

The Trust's exposure through the forward to the interest rate swaps held by the Fund had a positive impact on the performance of the Trust in the year ended December 31, 2008 (year ended December 31, 2007: negative contribution). The mark-to-market valuation of the interest rate swaps held by the Fund increased by USD $531,291 during the year ended December 31, 2008 (year ended December 31, 2007; decrease of USD $100,116). As the economic environment deteriorated over 2008, interest rates declined across the yield curve and contributed to the positive performance in the interest rate swap held by the Fund.

The Trust purchased 247,300 units under its repurchase and cancellation programs of the units of the Trust for the year ended December 31, 2008 (year ended December 31, 2007; 274,500 units were repurchased). Over the year ended December 31, 2008, this program contributed 0.98% to the overall return of the Trust (year ended December 31, 2007: 0.64% contribution).

The most significant factor affecting the performance of the Trust in 2008 was the return of the hedge funds underlying the forward.

The following table presents returns by investment strategy for the year ended December 31, 2008 and 2007:

Strategy	Year ended December 31, 2008	2007
Activist Investments	(35.34)%	6.08%
Asset-backed securities arbitrage	0.80%	10.48%
Capital structure arbitrage	—	5.62%
Distressed securities arbitrage	(23.00)%	11.18%
Fixed-income arbitrage	(54.37)%	5.25%
Merger arbitrage	—	(22.69)%
Mortgage-backed security arbitrage	(34.49)%	(3.23)%
Multi-strategy	(34.36)%	10.41%
Re-insurance arbitrage	(1.82)%	14.47%
Statistical arbitrage	(7.16)%	(5.87)%
Structured finance	(52.95)%	1.64%

As the credit crisis continued to unravel across all the markets, the hedge fund performance across almost all strategies was negatively impacted. Strategies which rely on normalization of historical spreads were dramatically impacted by the continued spread widening while the price and availability of leverage altered the fundamental economics of some profitable trades. Regulatory uncertainty increased in mid 2008 when new short selling rules altered some fund's abilities to adequately hedge in the equity markets. While the hedge fund managers were reducing risk in their portfolios, the investor demand for the return of capital from these hedge fund managers increased leading into year end, putting further pressure on hedge fund's underlying investments.

Specific manager returns within the asset-backed securities arbitrage strategy were enough to generate a slightly positive return for the year, however, the returns generated from the mortgage-backed securities arbitrage managers were more reflective of the heightened volatility and illiquidity in the mortgage markets.

Fixed income arbitrage and structured finance strategies were the largest negative contributors to performance and were driven by the negative consequences of a dislocated credit market. The structured finance strategy was also negatively impacted by the full write down of a trade finance hedge fund which was the victim of the Petter's fraud uncovered through an FBI investigation in the U.S. that became public in September 2008. Losses related to this write down at the Fund level were U.S.$1,082,617.

The activist strategy was ineffective as the hedging actions of the underlying hedge fund manager were not sufficient to offset the impact of the negative equity markets.

Multistrategy managers that historically were able to reap the benefits of strategy diversification, were caught up in the technical market behaviours and ultimately in the investor liquidation pressures which combined to deliver the negative result.

Summary of Investment Portfolio (1)

The Trust has obtained exposure to a portfolio of market-neutral hedge funds through the Forward. The Hedge Fund Portfolio emphasizes sectors of the capital markets that the Investment Advisor believes are relatively inefficient or present opportunities to generate uncorrelated returns. The Investment Advisor believes that such sectors offer arbitrage, relative value or absolute return opportunities and should reward insightful investment analysis.

The Hedge Fund Portfolio is invested in hedge funds that pursue non-traditional investment strategies and is, therefore, subject to the special risks of investing in these strategies. For this reason, the Investment Advisor seeks to diversify the Hedge Fund Portfolio across up to 14 broad investment strategies, which may include strategies to which the Fund is exposed through its investment in multi-strategy hedge funds. The hedge funds to which the Trust has exposure have been established in offshore jurisdictions and prepare annual audited financial statements, in accordance with U.S. or International generally accepted accounting principles (GAAP).

During the year ended December 31, 2008, the Fund redeemed from ten hedge funds (consisting of three structured finance, two statistical arbitrage and one fund in each of merger arbitrage, distressed securities, Mortgage-backed securities, Multi-strategy and asset-backed securities) (year ended December 31, 2007: the Fund placed investments with five new hedge funds and redeemed from seven hedge funds).

Asset Allocation by Investment Strategy

The following table shows the hedge fund holdings by strategy at the Fund level as at December 31, 2008 and 2007. The multi-strategy funds have not been allocated to any of the underlying hedge fund strategies set out in this table.

	As at December 31, 2008			As at December 31, 2007		
Strategy	No. of Hedge Funds	Fair Value (in U.S. Dollars)		No. of Hedge Funds	Fair Value (in U.S. Dollars)	
Activist investments	1	$ 1,774,637	6%	1	$ 2,744,536	3%
Asset-backed security arbitrage	3	4,625,196	17%	4	7,914,440	10%
Distressed securities arbitrage	3	3,363,483	12%	5	12,791,205	16%
Fixed-income arbitrage	3	2,222,721	8%	3	5,387,185	7%
Merger arbitrage	—	—	—	1	995,490	1%
Mortgage-backed security arbitrage	3	3,296,758	12%	4	9,305,743	12%
Multi-strategy	6	5,501,011	20%	6	17,072,702	21%
Re-insurance arbitrage	2	1,236,228	4%	2	4,407,933	6%
Statistical arbitrage	4	3,779,595	14%	6	10,854,126	14%
Structured finance	3	1,954,532	7%	6	8,039,314	10%
	28	$27,754,161	100%	38	$79,512,674	100%

The following table presents the largest individual hedge fund holding for each investment strategy of the Trust as a percentage of the total reported net asset value of the Trust as at December 31, 2008 and 2007.

Strategy	As at December 31, 2008	As at December 31, 2007
Activist investments	7.88%	4.95%
Asset-backed securities arbitrage	12.34%	6.17%
Distressed securities arbitrage	9.58%	6.71%
Fixed-income arbitrage	5.43%	4.47%
Merger arbitrage	—	1.80%
Mortgage-backed security arbitrage	7.87%	4.99%
Multi-strategy	4.96%	6.85%
Re-insurance arbitrage	4.60%	6.09%
Statistical arbitrage	8.98%	8.02%
Structured finance	5.20%	3.24%

The following table lists the top 25 hedge funds by fair value as at December 31, 2008. The Trust discloses the names of those hedge funds held by the Fund that represent more than 5% of the net assets of the Trust at the end of the year. For hedge funds that represent less than 5% of the Trust's net assets, the Trust has adopted unique fund numbers as identifiers. These numbers are used consistently in reporting by the Trust.

Top 25 Investments	Type of Investment	Cost (In U.S. Dollars)	Fair Value (In U.S. Dollars)	Fair Value as a % of Net Assets
Mariner-Tricadia Credit Strategies, Ltd.*	Participating shares	$1,377,626	$2,776,882	12.34%
Cerberus International Ltd.*	Participating shares	1,589,887	2,157,218	9.58%
Two Sigma Spectrum Cayman Fund, Ltd.*	Participating shares	2,000,000	2,020,081	8.98%
Icahn Fund Ltd.*	Participating shares	2,000,000	1,774,637	7.88%
Sorin Offshore Fund, Ltd.*	Participating shares	1,800,000	1,771,300	7.87%
CRC Global Structured Credit Fund, Ltd.*	Participating shares	1,200,000	1,575,359	7.00%
Platinum Grove Contingent Capital Offshore Fund, Ltd.*	Participating shares	2,400,000	1,221,050	5.43%
BDC Offshore Fund Ltd*	Participating shares	1,400,000	1,170,339	5.20%
Tykhe portfolios Ltd.*	Participating shares	2,000,000	1,134,458	5.04%
Fund 183*	Participating shares	1,068,750	1,115,945	4.96%
Fund 146*	Participating shares	1,637,299	1,112,006	4.94%
Fund 121*	Participating shares	1,095,452	1,077,600	4.79%
Fund 195*	Participating shares	800,000	1,036,368	4.60%
Fund 101*	Participating shares	1,526,762	937,705	4.17%
Fund 103*	Participating shares	1,681,804	907,823	4.03%
Fund 130*	Participating shares	931,520	796,969	3.54%
Fund 140*	Participating shares	1,108,003	785,808	3.49%
Fund 205*	Voting shares and capital Balance	1,285,145	784,188	3.48%
Fund 208*	Participating shares	949,903	780,389	3.47%
Fund 190*	Participating shares	700,000	617,616	2.74%
Fund 225*	Participating shares	500,000	583,069	2.59%
Fund 118*	Participating shares	—	460,785	2.05%
Fund 212*	Participating shares	—	425,876	1.89%
Fund 171*	Participating shares	302,250	272,955	1.21%
Fund 191*	Participating shares	830,198	215,863	0.96%

* Held by other investment funds managed or advised by Northwater Fund Management Inc.

The Trust also has holdings in the following common shares as at December 31, 2008. The Trust does not have economic exposure to these holdings as these common shares have been sold forward by the Trust for a price based on the return of a portfolio of hedge funds.

Share Investments	Type of Investment	Fair Value as a % of Net Assets
Aastra Technologies Ltd.	Common shares	4.26%
Atrium Innovations Inc.	Common shares	9.46%
Celestica Inc.	Common shares	5.57%
CGI Group Inc.	Common shares	12.50%
Fairborne Energy Ltd	Common shares	4.51%
Galleon Energy	Common shares	3.49%
Gildan Activewear Inc.	Common shares	5.56%
Great Canadian Gaming Corp.	Common shares	3.27%
Macdonald Dettwiler & Assoc.	Common shares	6.28%
Quandra Mining Ltd.	Common shares	1.65%
Research in Motion Ltd.	Common shares	5.09%
RONA Inc.	Common shares	6.79%
Sino-Forest Corp .	Common shares	6.35%
Stantec Inc.	Common shares	10.09%
Tristar Oil and Gas Ltd	Common shares	7.88%
Westjet	Common shares	8.87%

(1) The Summary of Investment Portfolio may change due to ongoing portfolio transactions of the Trust. There are no non-arm's length relationships between the Trust or Northwater Fund Management Inc. and any of the hedge funds for which the Trust has exposure. On a quarterly basis, an updated listing of holdings will be available.

Financial Highlights

The following tables show selected key financial information about the Trust and are intended to assist in understanding the Trust's financial performance for the years ended December 31, 2008, 2007, 2006 and 2005, and for the period from June 30, 2004 to December 31, 2004. The information included in the below tables is derived from the Trust's audited annual financial statements. The net assets per unit presented in the financial statements differ from the net asset value calculated for pricing purposes. An explanation of these differences can be found in the notes to the financial statements.

The Trust's Net Assets per Unit

	For the year ended December 31,				For the period from June 30 to December 31,
	2008	2007	2006	2005	2004
Net Assets, beginning of period	$21.24	$23.07	$22.47	$23.89	$23.75
Increase (decrease) from operations:					
Total revenue	0.02	0.02	0.01	—	0.05
Total expenses	(0.42)	(0.41)	(0.41)	(0.46)	(0.22)
Realized gains (losses) for the period	(0.69)	3.12	1.25	0.52	—
Unrealized gains (losses) for the period	(7.79)	(2.82)	1.29	0.24	1.52
Total increase (decrease) from operations(1)	(7.50)	(0.09)	2.14	0.30	1.36
Distributions:					
From income (excluding dividends)	—	—	—	—	—
From capital gains	—	—	—	—	—
Return of capital	1.75	1.75	1.75	1.75	0.875
Total Annual Distributions(2)	1.75	1.75	1.75	1.75	0.875
Net Assets at end of period(3)	$11.97	$21.24	$23.07	$22.47	$23.89

(1) Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase (decrease) from operations are based on the weighted average number of units outstanding over the financial period.

(2) Distributions were paid in cash for the year ended December 31, 2008.

(3) It is not intended that the Trust's Net Assets per Unit table act as a reconciliation of opening and closing net assets per unit.

Ratios and Supplemental Data

	2008	2007	2006	2005	2004
Net asset value (000's)[1]	$ 27,864	$ 54,571	$ 65,587	$ 70,702	$ 77,173
Number of units outstanding[1]	2,321,500	2,568,800	2,843,300	3,146,200	3,230,000
Management expense ratio[2]	10.96%	8.72%	7.27%	11.75%	18.02%
Management expense ratio before waivers or absorptions	10.96%	8.72%	7.27%	11.75%	18.02%
Portfolio turnover rate[3]	81.63%	9.49%	10.61%	62.33%	0.00%
Trading expense ratio[4]	0.04%	0.02%	0.00%	0.00%	0.02%
Closing market price, end of period	$ 9.40	$ 19.50	$ 20.56	$ 20.50	$ 26.40

(1) This information is provided as at December 31 of the years shown.

(2) Management expense ratio is based on total expenses for the stated period and is expressed as an annualized percentage of month-end average net asset value during the period. Please note that the management expense ratio includes not only the expenses of the Trust and Fund itself but also reflects an estimate of expenses to which the underlying hedge funds were subject. The management expense ratio of the underlying hedge funds held by the Fund plus the expenses of the Fund included in the above ratios for the year ended December 31, 2008 added 9.79% and for the year ended December 31, 2007 added 5.54% and the year-ended December 31, 2006 added 5.47 % (2005 added 9.80% and 2004 added 9.66%) to the expense ratio of the Trust. This annualized expense ratio has been calculated using the total expenses of the underlying hedge funds, invested in by the Fund, per their annual audited financial statements for the periods ended December 31, 2007, 2006, 2005 and 2004 respectively. These statements represent the most recent audited information available. The expenses together with estimates for hedge funds with year-ends other than December 31 have been prorated based on the relative percentage of the hedge fund held by the Fund at the end of the respective period. Performance fees incurred by the underlying hedge funds can vary significantly from period to period based on such factors as the market conditions, fund strategy, manager performance and the timing of redemptions. As a result, the expense ratio of the underlying funds for the prior year may be significantly different than the actual expenses incurred by these underlying hedge funds for the current period.

(3) The Trust's portfolio turnover rate indicates how actively the Trust's portfolio adviser manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Trust buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rate in a year, the greater the trading costs payable by the fund 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 fund.

(4) The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of monthly average net asset value during the period.

Past Performance

General

With respect to the following information in the "Past Performance" section of this report, please note the following:

(a) the performance information shown assumes that all distributions made by the Trust in the years shown were reinvested in additional securities of the Trust;

(b) the performance information does not take into account sales and distribution charges that would have reduced returns or performance; and

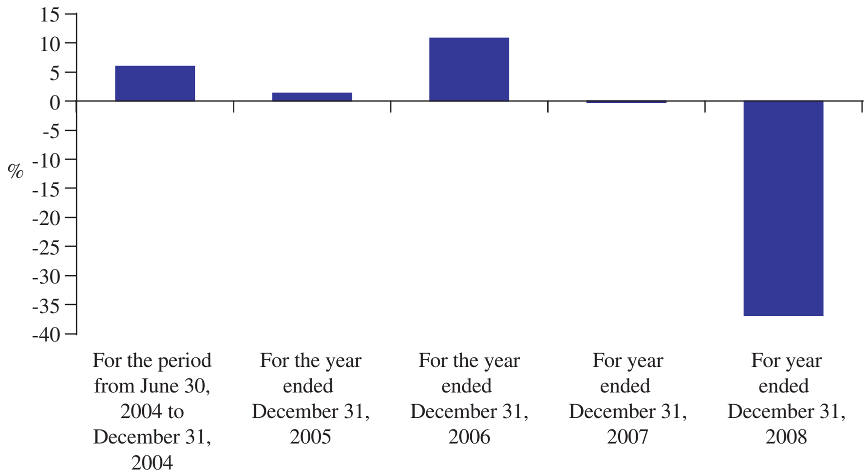
(c) how the Trust has performed in the past does not necessarily indicate how it will perform in the future.

Year-by-Year Returns

With respect to the following chart, please note the following:

(a) the bar chart shows the Trust's performance for each of the periods shown, and illustrates how the Trust's performance has changed from year to year; and

(b) the bar chart shows, in percentage terms, how much an investment made on the first day of each financial period would have grown or decreased by the last day of each financial period.



Annual Compound Returns

This chart compares the historical annual compound returns of the Fund over the periods indicated relative to various market Indices

	Since Inception*	Past 3 years	Past year
Northwater Five-Year Market-Neutral Trust	(6.19)%	(11.27)%	(36.80)%
S&P/TSX Composite Index	3.54%	(4.80)%	(33.00)%
Scotia Capital 91 day T-Bill Index	3.43%	3.91%	3.33%
DEX Universe Bond Index	5.93%	4.71%	6.41%

* inception date of the Fund is June 30, 2004.

The S&P/TSX Composite Index is a broad index of Canadian common shares.

The Scotia Capital 91-day T-Bill Index shows how a portfolio of three month T-Bills would have performed over the relevant period.

The DEX Universe Bond Index is a broad index of Canadian federal government, provincial government and corporate fixed income securities.

The Trust returns do not currently compare favourably to relevant benchmarks as outlined in the above chart. These results are the combination of the leverage employed by the Trust and the unusually poor results delivered by the hedge funds in 2008 due to market dislocation caused by the credit crisis.

Management Fees and Related Party Transactions

The Manager is responsible for the day-to-day administration, portfolio management and unitholder services to the Trust. In exchange for these services, the Manager is entitled to an annual management fee calculated as 0.15% per annum of the net asset value of the Trust, as of the close of business on each month-end valuation date. The fee is paid monthly in arrears.

The Trust also pays to the Manager a service fee of 0.30% per annum of the net asset value of the Trust, accrued monthly, and calculated based on the net asset value of the Trust on the last Valuation Date of each quarter. The service fee is applied by the Manager to pay a service fee to registered dealers for services they provide to unitholders, including investment advice and account statements, based on the number of units held by clients of such dealers at the end of the relevant quarter. The fee is accrued monthly and calculated and paid quarterly in arrears. Substantially all of the management fees are applied to provisions of portfolio management and investment advisory services of the Manager.

During the year ended December 31, 2008, the management fee and service fee expense were $69,376 and $134,021 respectively, and the management fee and service fee payable by the Trust as at December 31, 2008 were $12,227 and $21,334 respectively. (year ended December 31, 2007, the management fee and service fee expense were $96,567 and $189,946 respectively.)

Other Fees

The Trust pays forward fees of approximately 0.55% per annum of the U.S. notional amount and 0.90% per annum of the Canadian notional amount to the Counterparty of the Forward that may vary based on the value of the Common Share Portfolio, calculated and paid quarterly in arrears.

Net Asset Value and Price Per Unit

The value of the Hedge Fund Portfolio is affected by factors beyond the control of the Investment Advisor, the Manager or the Trust. The process of valuing investments for which no published market price exists is based upon the definitive or provisional net asset value of the hedge funds supplied by the administrators or managers of such underlying hedge funds. These values are net of the management fees and expenses to which the underlying hedge funds are subject.

The Trust's net asset value per unit is calculated and reported monthly. During the year ended December 31, 2008, the net asset value of the Trust fluctuated between $12.06 per unit and $21.15 per unit after taking into account distributions (year ended December 31, 2007: between $21.30 per unit and $23.65 per unit).

The market price for units of the Trust is determined by the actions of buyers and sellers in the market. The daily closing price of the units fluctuated between $7.75 and $19.89 during the year ended December 31, 2008 (year ended December 31, 2007: between $17.51 per unit and $22.79 per unit).

Distributions

During the year ended December 31, 2008, distributions totaling $1.75 per unit and $4,221,481 in aggregate were declared (year ended December 31, 2007: $1.75 per unit and $4,671,932 in aggregate). This represents a 7% return on the initial subscription price of $25.00 per unit consistent with the targeted annual yield for the Trust of 7%.

The Trust is required to distribute all of its net income and net realized capital gains so that the Trust will not be liable to pay income tax under Part I of the Income Tax Act.

The character of the quarterly distributions for tax purposes has been determined at the end of the year in accordance with the declaration of trust and the tax laws then in effect. There can be no assurance that income tax laws will not be changed in a manner that adversely affects the Trust or distributions paid by the Trust and the Manager will continue to monitor any changes in the tax laws as they occur.

The following table presents the distribution history for the year ended December 31, 2008

Distribution History

Record Date	Date distribution paid	Character of distribution for tax purposes	Amount per unit
March 31, 2008	April 15, 2008	Return of Capital	0.4375
June 30, 2008	July 15, 2008	Return of Capital	0.4375
September 30, 2008	October 15, 2008	Return of Capital	0.4375
December 31, 2008	January 15, 2009	Return of Capital	0.4375

Purchases for Cancellation

Under its declaration of trust, the Trust is required to make purchases of units of up to 2.5% of the outstanding units per quarter if the price at which the units are offered for sale is less than 95.0% of the current net asset value per unit as at the close of business on the preceding valuation date.

On August 24, 2007, the Trust filed a notice of intention to make normal-course purchases of units with the Toronto Stock Exchange. In its filing with the Exchange, the Trust indicated an intention to purchase up to 262,405 of the units of the Trust, representing 10% of the public float of the Trust then outstanding during the period from August 30, 2007 to August 29, 2008. In August of 2008, the Trust filed a notice of intention to make normal-course purchases of units with the Toronto Stock Exchange, the Trust indicated an intention to purchase up to 237,847 of the units of the Trust, representing 10% of the public float of the Trust then outstanding during the period from September 11, 2008 to September 10, 2009. In accordance with exchange rules and by-laws, the Trust may not pay more than the most recent market price for the units purchased. Units purchased under the bid are cancelled.

During the year ended December 31, 2008, the Trust purchased 247,300 units for a total cost of $4,378,822 for cancellation under this program (year ended December 31, 2007: 274,500 units were repurchased for $5,854,569)

Potential Tax Implication of Wind-Up

The Manager currently anticipates commencing cash distributions ("Termination Distributions") to investors effective as of June 30, 2009. Upon the commencement of the payment of Termination Distributions from the Trust, the percentage of a particular illiquid holding in relation to the Trust's assets is likely to exceed the 10% concentration limits required in order for the Trust to continue to qualify as a unit trust for Canadian income tax purposes.

If and when the Trust fails to qualify as a unit trust it will no longer qualify as a mutual fund trust for Canadian income tax purposes and the Trust will no longer be a "qualified investment" for registered accounts, including without limitation, RRIF's, RRSP's and RESP's. The Manager anticipates that the Trust will lose its "qualified investment" status for Canadian income tax purposes on or about June 30, 2009. Investors are advised to speak with their advisors as soon as possible to obtain tax advice regarding the anticipated failure of the Trust to maintain its "qualified investment" status.

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST
– and –
NORTHWATER FIVE-YEAR MARKET-NEUTRAL FUND LIMITED
INDEPENDENT REVIEW COMMITTEE REPORT

Dear Investor:

Effective November 1, 2007, the advisory board (the "Advisory Board") of each of Northwater Five-Year Market-Neutral Trust (the "Trust") and Northwater Five-Year Market-Neutral Fund Limited (the "Fund") was designated as the independent review committee of the Trust and the Fund (the "IRC") pursuant to the provisions of *National Instrument 81-107, Independent Review Committee for Investment Funds*.

This report is the IRC's second annual report under the requirements of National Instrument 81-107. However, the Advisory Board has reported annually to unitholders since it August 25, 2004.

Our role as required by securities regulators is to review investment fund conflict of interest matters identified and referred to us by Northwater Fund Management Inc., in its capacity as manager of the Trust and Northwater Capital Management Inc. as investment advisor to the Fund (together, the "Manager") and to give our approval or recommendation with respect to such matters. The focus of our review of such conflict of interest matters is whether or not the Manager's proposed action achieves a fair and reasonable result for the Trust and the underlying Fund.

At least once per year, we will also review the Manager's policies and procedures relating to conflict of interest matters and will assess the adequacy and effectiveness of such policies and procedures in respect of the Trust and the Fund.

In addition to the regulatory requirements for independent fund governance, we are also retaining our role as an advisory board and, as such, assisting the Manager on other issues relating to the management and operation of the Trust and the Fund.

As previously disclosed by the Trust, both the Trust and the Fund are scheduled to terminate effective as of June 30, 2009. We will be working with the Manager throughout the scheduled termination of the Trust and the Fund in accordance with the terms of our mandate.

In addition, we wanted to take this opportunity to advise unitholders that effective as of March 31, 2009, Jeff Francoz has had to resign his position as chair of the independent review committee. Mr. Francoz' employment relationship has recently changed and his new employer has an internal policy against sitting on boards such as the independent review committee. The remaining members of the independent review committee wish to thank Mr. Francoz for his contribution and will continue to fulfill their mandate under NI 81-107 as they work with the Manager to seek a replacement.

We look forward to continuing our open and effective relationship with the Manager for the benefit of the Trust and the Fund.

Regards,

Jeffrey D. Francoz
Chair of the Independent Review Committee

Members of the Independent Review Committee		Length of Service on Advisory Board / IRC
Name	**Residence**	**First Appointed**[1]
Jeffrey D. Francoz . . . . Chair of the IRC	Toronto, Ontario	August 25, 2004[2]
Ann Marshall	Toronto, Ontario	August 25, 2004[2]
Peter Vesely	Toronto, Ontario	November 1, 2007

* There were no changes in the composition of the IRC during the period.

* Ann Marshall also serves as an independent review committee member for iShares funds managed by Barclays Global Investors Canada Limited. Jeffrey Francoz and Peter Vesely do not currently serve as independent review committee members for other investment funds other than those managed by the Manager.

Holdings of Securities

(a) The Trust and the Fund

As at December 31, 2008, the percentage of units of the Trust beneficially owned, directly or indirectly, in aggregate, by all members of the IRC did not exceed 10%. The shares of the underlying Fund are held exclusively by the swap counterparty and no shares of the Fund have been offered to the public.

(b) The Manager

As at December 31, 2008, no member of the IRC beneficially owned, directly or indirectly, any class or series of voting or equity securities of the Manager.

(c) Service Providers

As at December 31, 2008, no member of the IRC beneficially owned, directly or indirectly, any class or series of voting or equity securities of a company that provides services to the Trust or the Manager that could reasonably result in an actual or perceived loss of independence of the member.

The IRC is pleased to report on its activities for the period ended December 31, 2008.

All of the members of the IRC are non-related and independent of management.

(1) Each member of the IRC listed has been a member of the independent review committee since its inception on November 1, 2007.

(2) Since the inception of the original Advisory Board of the Trust.

General

During the period ended December 31, 2008, the members of the IRC held four meetings. Mr. Francoz, and Mr. Vesely attended all of the meetings held by the IRC during the period, while Ms. Marshall attended all but one of the meetings.

During the period ended December 31, 2008, the IRC reviewed: (i) the Charter of the IRC, (ii) the reporting to unitholders as required by National Instrument 81-106, (iii) periodic reports on the performance and the composition of the investment portfolio of the Trust and the Fund, (iv) compliance with Investment Guidelines, (v) the compensation of the IRC members to determine whether such compensation continues to be reasonable, (vi) the presentation of certain information in the quarterly and annual reports, and (vii) the standing instructions issued to the Manager in respect of conflict of interest matters under National Instrument 81-107. In addition, the IRC reviewed the various policies and procedures of the Manager related to conflict on interest matters to determine their adequacy and effectiveness.

The IRC reports that management of the Manager has been open and cooperative, permitting the members to review such documents and speak to such members of management of the Manager as deemed necessary by the IRC in order to properly execute their responsibilities.

Compensation and Indemnities

The aggregate compensation paid by the Trust and the Fund to the IRC for the twelve-month period through December 31, 2008 was $21,620.44.

No indemnities were paid to the IRC during the period.

The initial compensation of the IRC was set by the Manager. At least annually, the IRC will review member compensation giving consideration to the following:

1. the best interests of the Trust and the Fund;
2. that compensation paid to the IRC by the Trust and the underlying Fund should fairly and reasonably reflect the general and specific benefits accruing to the Trust and the Fund;
3. the recommendation of the Manager;
4. the nature and complexity of the business of the Trust and the Fund; and
5. the nature and extent of the workload of each member of the IRC.

Conflict of Interest Matters

No Conflict of Interest Matters were referred to the IRC during the period. The IRC is not aware of any instance in which the Manager acted in a conflict of interest matter referred to the IRC for which the IRC did not give a positive recommendation.

Furthermore, the IRC is not aware of any instance in which the Manager acted in a conflict of interest matter but did not meet a condition imposed by the IRC in its recommendation or approval.

The Manager relied on the following standing instructions of the IRC in the period. In each case, the standing instructions required the Manager to comply with its related policy and procedures and to report periodically to the IRC.

Standing Instructions

1. allowing transfers between the Trust or the Fund and other entities advised by the Manager, provided that all such transfers will exclusively involve hedge fund investments transferred at an independently determined net asset value and must be consistent with the investment guidelines of the transferee; and
2. allowing the Manager and its affiliates to act in various capacities with respect to other entities, including without limitation in such capacities as manager, investment advisor, administrator or trustee, provided that the Manager and its affiliates shall in all cases act in accordance with its Procedures for Minimizing Potential Conflicts of Interest and its Code of Ethics.

The Manager also received positive recommendations and standing instructions with respect to the conflict of interest matters addressed by the following policies. In each case, the standing instructions required the Manager to comply with its related policies and procedures and to periodically report to the IRC.

Policies that address conflict of interest matters

1. Statement of Policies Respecting Related and Connected Issuers and Procedures for Minimizing Potential Conflicts of Interest
2. Code of Ethics
3. Allocation of Trades Procedures
4. Selection of Brokers, Best Execution and Soft Dollar Procedures
5. Consistency of Client Portfolio with Client Investment Objectives
6. Personal Securities Transactions Policy
7. Insider Trading Policy
8. Cross Trading Procedures

We look forward to continuing to discharge our duties in 2009 for the benefit of the Trust and the Fund.

Jeffrey D. Francoz
Chair of the IRC

Ann Marshall

Peter Vesely

MANAGEMENT'S RESPONSIBILITY

The accompanying financial statements have been prepared by Northwater Fund Management Inc., the Manager of the Trust (the "Manager"), and approved by the Board of Directors of the Manager. The Manager is responsible for the information and representations contained in these financial statements and other sections of the annual report.

The Manager maintains appropriate processes to ensure that relevant and reliable financial information is produced. The financial statements have been prepared in accordance with accounting principles generally accepted in Canada and include certain amounts that are based on estimates and judgments. The significant accounting policies that management believes are appropriate for the Trust are described in note 2 to the financial statements.

Paul Robson, CFA
President and
Chief Operating Officer

Eve N. Jedrzejewska, CA, CFA
Vice-President and
Chief Compliance Officer

March 23, 2009

AUDITORS' REPORT TO THE UNITHOLDERS OF NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

We have audited the statement of investment portfolio of **Northwater Five-Year Market-Neutral Trust** (the Trust) as at December 31, 2008, the statements of net assets as at December 31, 2008 and 2007 and the statements of operations, changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian 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 Trust as at December 31, 2008 and 2007 and the results of its operations, the changes in its net assets and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants,
Licensed Public Accountants
March 23, 2009

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Statements of Net Assets

	As at December 31, 2008	As at December 31, 2007
Assets		
Cash and short-term investments (cost: 2008 – $2,100,000; 2007 – $1,572,156)	$ 2,215,032	$ 1,571,991
Common shares – at fair value (cost: 2008 – $44,791,796; 2007 – $53,455,776)	28,233,749	73,304,362
	30,448,781	74,876,353
Liabilities		
Unrealized loss on forward contract (note 6)	1,539,916	19,072,251
Audit, legal and custody fees payable	62,409	29,869
Service fees payable (note 7)	21,334	44,408
Management and advisory fees payable (note 7)	12,227	22,202
Independent review committee fees payable	12,897	12,897
Distribution payable (note 9)	1,015,656	1,123,850
	2,664,439	20,305,477
Net assets	$ 27,784,342	$54,570,876
Net assets and unitholders' equity (note 5)		
Unit capital	$ 54,712,580	$60,540,890
Contributed surplus	3,065,689	1,616,201
Deficit	(29,993,927)	(7,586,215)
Total	$ 27,784,342	$54,570,876
Number of units outstanding (note 5)	2,321,500	2,568,800
Net assets per unit	$ 11.97	$ 21.24

Signed on behalf of the Trustee,

Northwater Fund Management Inc.

Per: Paul Robson

Per: [illegible]

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Statements of Operations

	For the years ended December 31,	
	2008	**2007**
Investment income		
Interest	$ 47,082	$ 54,231
	47,082	54,231
Expenses		
Service fees (note 7)	$ 134,021	$ 189,946
Forward financing fees (note 7)	510,146	614,594
Management fees (note 7)	69,376	96,567
Audit fees	92,059	62,332
Independent review committee fees	21,620	9,052
Custodian fees	14,039	21,291
Legal fees	50,532	14,197
Security holder reporting costs	88,059	77,624
Loan interest and standby fees (note 8)	29,260	5,520
Transaction costs	16,156	12,238
	1,025,268	1,103,361
Net investment loss	(978,186)	(1,049,130)
Realized and unrealized gain (loss) on investments		
Net realized gain (loss) on:		
Common shares and short-term investments	1,666,252	8,378,102
Change in unrealized appreciation (depreciation) on:		
Common shares	(36,406,633)	(488,552)
Forward contract (note 6)	17,532,335	(7,070,862)
Realized and unrealized gain (loss) on investments for the year	(17,208,046)	818,688
Increase (decrease) in net assets from operations for the year	$(18,186,232)	$ (230,442)
Increase (decrease) in net assets from operations per unit for the year*	$ (7.50)	$ (0.09)

* Based on the average number of units outstanding of 2,424,315 (2007 – 2,686,823) for the year.

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Statements of Changes in Net Assets

	For the years ended December 31	
	2008	**2007**
Net assets – beginning of the year	$ 54,570,876	$65,586,531
Increase (decrease) in net assets from operations for the year	(18,186,232)	(489,154)
Unit transactions (note 5)		
Units purchased for cancellation	(4,378,822)	(5,854,569)
	32,005,822	59,242,808
Distribution to unitholders (note 9)		
Return of capital	(4,221,480)	(4,671,932)
Net assets – end of the year	$ 27,784,342	$54,570,876

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Statements of Cash Flows

	For the years ended December 31, 2008	2007
Cash flows from operating activities		
Increase (decrease) in net assets from operations	$(18,186,232)	$ (230,442)
Items not affecting cash:		
Change in unrealized (appreciation) depreciation on common shares and short-term investments	36,406,633	488,552
Change in unrealized (appreciation) depreciation on forward	(17,532,335)	7,070,862
Realized (gain) loss on common share and short-term investments	(1,666,252)	(8,378,102)
Changes in non-cash working capital:		
Change in payables	(509)	(30,767)
Purchase of common shares	(42,188,491)	(25,806,592)
Proceeds on sale of common shares	52,518,724	37,893,439
	9,351,538	11,006,950
Cash flows from financing activities		
Repurchase of trust units	(4,378,822)	(5,854,569)
Distribution paid to trust unitholders	(4,329,675)	(4,792,026)
	(8,708,497)	(10,646,595)
Net increase (decrease) in cash and short term investments	643,041	360,355
Cash and short-term investments at the beginning of the year	1,571,991	1,211,636
Cash and short-term investments at the end of the year	$ 2,215,032	$ 1,571,991
Supplementary information:		
Interest paid	$ 29,260	$ 5,520

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Statement of Investment Portfolio
As at December 31, 2008

	Credit Rating*	Maturity date	No. of shares/ Face value	Cost	Fair value	Fair value as a % of Net Assets
Common share portfolio						
Aastra Technologies Ltd.			100,000	$ 1,180,000	$ 1,184,000	4.26%
Atrium Innovations Inc.			203,943	3,140,722	2,628,825	9.46%
Celestica Inc			280,445	2,810,059	1,548,056	5.57%
CGI Group			365,511	3,614,904	3,472,355	12.50%
Fairborne Energy Ltd.			214,334	1,210,987	1,253,854	4.51%
Galleon Energy Inc			191,479	3,117,278	970,799	3.49%
Gildan Activewear Inc.			108,872	3,750,640	1,544,894	5.56%
Great Canadian Gaming Corp.			253,026	3,117,268	908,363	3.27%
Macdonald Dettwiler & Assoc.			80,791	3,550,747	1,742,662	6.28%
Quadra Mining Ltd.			169,602	3,117,285	459,621	1.65%
Research In Motion Ltd			28,586	1,995,329	1,413,864	5.09%
RONA Inc			157,366	2,340,464	1,886,818	6.79%
Sino-Forest Corp.			182,653	1,210,989	1,760,775	6.35%
Stantec Inc.			93,862	2,970,732	2,804,597	10.09%
Tristar Oil and Gas			193,674	4,113,636	2,188,516	7.88%
Westjet			188,369	3,550,756	2,465,750	8.87%
Common share portfolio				44,791,796	28,233,749	101.62%
Cash					115,033	0.41%
Banker's Acceptances *						
Royal Bank of Canada	R-1 (High)	January 2, 2009	1,300,100	1,300,000	1,299,999	4.68%
Canadian Imperial Bank of Commerce	R-1 (High)	January 2, 2009	800,000	800,000	800,000	2.88%
Total cash and short-term investments				2,100,000	2,215,032	7.97%
Total investment portfolio					$30,448,781	109.59%
Other net assets (liabilities)					(2,664,439)	(9.59)%
Net assets and unitholders' equity					$27,784,342	100%

* Credit ratings as at December 31, 2008 as per DBRS rating agency.

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Notes to Financial Statements
For the years ended December 31, 2008 and 2007

1. Establishment and Operations of the Trust

The Northwater Five-Year Market-Neutral Trust (the "Trust") is a closed-end investment trust established under the laws of the Province of Ontario pursuant to a declaration of trust made as of June 18, 2004. Northwater Fund Management Inc. acts as Trustee. Northwater Fund Management Inc. (the "Manager") acts as Trustee of the Trust and RBC Dexia Investor Services Trust ("RBC Dexia") acts as Custodian for the Trust. The Trust began operations on June 30, 2004 when it completed its initial public offering. The Northwater Five-Year Market-Neutral Fund Limited (the "Fund") began operations on June 30, 2004. The Trust issued additional units on December 31, 2004 through a secondary offering. The Trust's units are listed on the Toronto Stock Exchange under the symbol NYF.UN. The Trust will terminate on or about June 30, 2009 (the "Termination Date"), and the net assets will be distributed pro rata to the unitholders unless an alternative later termination date is approved by a two-thirds majority vote of the unitholders at a meeting called for this purpose.

The assets of the Trust, invested in cash, short-term investments and common shares (the "Common Share Portfolio") are combined with a forward contract (the "Forward") to achieve a return based on a diversified portfolio of market-neutral hedge funds.

2. Summary of Significant Accounting Policies

These financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

Adoption of New Accounting Standards

In December 2006, the Accounting Standards Board issued CICA Handbook Section 3862, "Financial Instruments – Disclosures" ("S. 3862") and Section 3863, "Financial Instruments – Presentation" ("S. 3863"), which provide comprehensive disclosure and presentation requirements for financial instruments.

In addition, in December 2006, the Accounting Standards Board issued CICA Handbook Section 1535 "Capital Disclosures" ("S.1535"), which provides standards for disclosing information about an entity's capital and how it is managed.

The requirements of S. 3862, S. 3863 and S.1535 are effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007 and have been reflected in the notes to the financial statements.

The following paragraphs outline the accounting policies of the Trust :

(a) Cash and Short-Term Investments

Cash consists of cash in interest bearing accounts. Short-term investments are valued at the bid price for such instruments on each Valuation Date. Interest income is accrued on a monthly basis.

(b) Investments

Investment transactions are accounted for on a trade date basis. Investments are valued on the last day of each month ("Valuation Date") at closing bid prices.

The common shares listed on a public securities exchange are valued at their bid price on each Valuation Date. Common shares not traded on that date are valued at the average of the closing bid and ask or the latest available sale price. Realized gains and losses are calculated using the average cost. Distribution income is recorded on ex-dividend date or ex-distribution date on a gross basis.

The fair value of the forward contract is the gain or loss, if any, that would be realized if, on the Valuation Date, the forward contract was "closed out". The difference between fair value and cost is shown as an unrealized gain or loss on forward. The value of the forward contract is based on the change in valuation of the Fund, which invests primarily in a diversified portfolio of market-neutral hedge funds, and on the change in value of the Common Share Portfolio less the costs of leverage. The investments in market-neutral hedge funds held by the Fund are valued at fair value on the basis of the definitive net asset values reported by the administrators or the portfolio managers of the funds on the Valuation Date or, if not available, the most recent provisional net asset values based on preliminary returns reported by the administrators or the portfolio managers of such funds. The Manager or Investment Advisor may in its sole discretion, use a different valuation methodology to price the underlying hedge funds, that in the opinion of the Manager or Investment Advisor, is more reflective of fair value.

(c) Foreign Currency Translation

Assets and liabilities in foreign currencies are translated into Canadian dollars at the rate of exchange prevailing at the end of the period. Revenues and expenses denominated in foreign currencies are translated using the average exchange rate for the year.

(d) Use of Estimates

The preparation of financial statements in accordance with GAAP requires the Trust to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

(e) Transaction Costs

Transaction costs are expensed and are included in the Statement of Operations. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of an investment.

3. Financial Instrument Risk

The Trust's investment activities may expose it to a variety of financial risks including market price risk, currency risk, interest rate risk, and credit risk. The following provides an overview of these risks and describes actions taken by the Trust in an effort to mitigate the potential adverse impact of these risks on the performance of the Trust.

No material changes affecting the overall risk of investing in the Trust were made by the Manager in the year ended December 31, 2008. However, the hedge fund industry, like other market participants, has been subject to unprecedented turmoil in the markets due to the ongoing credit crisis. This has had both an impact on the returns and the volatility the Trust has experienced in 2008. In addition, as the Trust goes through the wind up process its exposure to hedge funds will continuously change and the diversification of the Fund's hedge fund holdings will decrease, causing concentration risk to increase. Hence, the overall risk profile of the Trust has been impacted as discussed below.

Market price risk

Market price risk is the risk that the future value of a financial instrument will fluctuate as a result of changes in its market price, whether caused by factors specific to the individual investment, its issuer, or any other market factor that may affect its price.

The Trust primarily invests in a portfolio of Canadian publicly traded common shares and through a forward agreement with a counterparty agrees to sell the common shares at a price based on the return of an underlying portfolio of hedge funds. As such the Trust has no exposure to the market price risk for the common shares held.

The Trust is exposed through a forward agreement to a portfolio of hedge funds. The process of fair valuing hedge fund investments for which no published market exists, is based upon the fair value of the underlying holdings of the hedge fund. These values may differ from values available had a ready market existed for such investments and may differ from the prices at which such investments may be sold.

The Investment Advisor of the Fund attempts to mitigate market price risk by investing in a diversified portfolio of hedge funds whose returns exhibit low correlation to the markets and each other. In addition, the Investment Advisor monitors the investments on a regular basis in order to ensure the decision to invest in a particular hedge fund strategy continues to be suitable for the Fund's portfolio, including performing ongoing qualitative and quantitative assessments and comprehensive investment and operational due diligence. Special attention is paid to organizational changes made by the hedge fund managers and to changes in policy relative to their investment objectives, valuation, hedging strategy, degree of diversification, leverage and costs.

The impact on net assets of the Fund based on a change in the Strategy's returns as approximated by that Strategy's standard deviation as at December 31, 2008, is included in the following table.

Strategy	Potential change in strategy return (%)*	Impact on net assets of the Fund (USD$)
Activist Investment	16.73%	296,815
Asset-backed securities arbitrage	5.08%	235,152
Distressed securities arbitrage	9.51%	319,862
Fixed-income arbitrage	28.40%	631,223
Mortgage-backed security arbitrage	13.22%	435,732
Multi-strategy	15.86%	872,239
Re-insurance arbitrage	4.67%	57,787
Statistical arbitrage	12.86%	485,880
Structured finance	24.54%	479,728

* Potential change in strategy return is based on standard deviation for each strategy measured over the past 24 months for hedge funds in the hedge fund portfolio as at December 31, 2008.

Currency risk

Currency risk arises from the Trust holding financial instruments denominated in a currency other than Canadian dollars, which is the Trust's functional currency.

As the Trust is exposed to hedge fund investments through the forward, that are primarily denominated in U.S. dollars through a forward agreement, the value of such investments may fluctuate with the exchange rate. To manage its currency risk, the Trust attempts to hedge such currency fluctuations through the use of currency forwards entered into by the Fund.

As at December 31, 2008, the impact on net assets per 1% change in the Canadian dollar would have been $14,052.

Liquidity risk

Liquidity risk is the risk that the Trust will encounter difficulty in meeting its obligations associated with its financial liabilities. The financial liabilities of the Trust may consist of loans, distributions, and obligations due to market support requirements.

The Trust primarily invests in a Common Share Portfolio of publicly traded Canadian securities. As such the investments are considered highly liquid. In addition, the Trust is exposed to hedge fund investments through a forward agreement for which there is no active secondary market. As such the investments of the Fund are considered illiquid. The Fund is subject to redemption restrictions for each of the hedge funds forming part of its portfolio that are generally monthly, quarterly, semi-annually or annually. Notice periods for redemptions range from 30 days notice to 180 days notice. Redemptions may, in some cases, be subject to lock-up periods, gates, redemption suspensions and side pocket restrictions.

To assist the Trust in its ability to meet its financial obligations, a credit facility is available to provide liquidity within certain restrictions. In addition, the hedge fund portfolio is diversified and managed considering the Trust's termination date.

To mitigate liquidity risk, the hedge fund portfolio has been diversified across different managers and strategies. However, due to the ongoing credit crisis, many of the trading strategies employed by hedge funds, which depend on functional financial markets, including the ability of managers to enter into short positions, have suffered losses not only due to market movements, but also due to liquidity constraints. Certain of the hedge fund managers have been unable to sell assets to prevent additional losses or fund investor redemptions. Continuing illiquidity has caused numerous underlying hedge funds held by the Fund to invoke various restrictions on redemptions including, without limitation, restricting redemptions to a limited percentage of the aggregate net asset value of such underlying hedge funds (invoking gates), the temporary suspension of redemptions altogether, or the commencement of a controlled liquidation and wind-up of the underlying hedge funds' business.

The Investment Advisor has been managing the Fund's portfolio taking into account the Fund's Termination Date. As such, as of December 31, 2008, the Investment Advisor submitted redemption requests to all of the underlying hedge funds.

The value of total redemption requests made prior to December 31, 2008, for hedge funds held as equity as at December 31, 2008 broken out by effective date of redemption, are included in the table below:

Effective date of redemption	Amount ($) as at December 31, 2008	% of total hedge fund portfolio	Amounts (USD$) received subsequent to year end
January 1, 2008	784,188	3%	71,617
April 1, 2008	314,942	1%	117,390
July 1, 2008	3,101,369	11%	448,905
August 1, 2008	199,860	1%	147,607
October 1, 2008	1,672,474	6%	112,715
December 1, 2008	1,221,068	4%	—
January 1, 2009	17,714,562	64%	10,096,950[1]
June 1, 2009	1,575,359	6%	—
July 1, 2009	1,170,339	4%	—
	27,754,161	100%	10,995,184

(1) for one of the hedge funds, the Fund received the redemption proceeds prior to the effective date of the redemption. This amount is included here and is disclosed in the Statement of Net Assets of the Fund as hedge fund investment sales in advance. This amount is U.S.$1,502,797.

The following table shows the expected payout timeline of redemption proceeds from the underlying hedge funds held by the Fund:

Payments of redemptions expected in 2009, classified by status of the hedge funds being redeemed from.

	Amount (U.S.$)	% of hedge fund portfolio as at December 31, 2008
Normal Course	9,325,495	34%
Restricted redemptions (1, 2)	3,377,623	12%
Liquidating	1,094,197	4%
	13,797,315	50%

Payments of redemptions expected beyond 2009, classified by status of the hedge funds being redeemed from:

	Amount (U.S.$)	% of hedge fund portfolio as at December 31, 2008
Restricted redemptions (1)	10,118,350	36%
Liquidating	3,838,496	14%
	13,956,846	50%

(1) Restricted redemptions category includes situations where the hedge fund manager has placed some form of restriction on the redemption request, including suspending redemptions, enforcing gates on redemption or restructuring the fund, to for example, create a liquidating share class.

(2) Although these redemptions are currently restricted, the Investment Advisor anticipates that the redemption proceeds will still be received during 2009.

The receipt of redemption proceeds by the Fund could extend beyond the scheduled Termination Date and hence impact the ultimate distribution of the assets to unitholders.

The Fund has hedge fund redemption receivables outstanding of U.S.$727,481 as at December 31, 2008. The Fund is exposed to liquidity risk as these amounts may not be realized (collected) for an extended period of time. As at December 31, 2008 the hedge fund redemptions receivable aging was as follows:

	< 60 days	61-90 days	91-120 days	> 120 days	Total
Hedge Fund Redemptions Receivable	U.S.$49,915		U.S.$339,803	U.S.$337,763	U.S.$727,481

The Investment Advisor is in regular contact with hedge fund administrators to determine timing of receipt of remaining redemptions. Most of the receivables outstanding as at year end fall into two categories: audit holdbacks, which represent a small percentage of redemptions being withheld by the hedge fund managers on full redemptions pending completion of the hedge fund's audit; and liquidations, which primarily represent underlying hedge fund positions in assets that are being liquidated.

The below table shows hedge fund redemptions receivable as at December 31, 2008 broken down by type.

Type	Amount (U.S.$)
Audit Holdbacks	292,378
Liquidations	435,103
	727,481

Credit risk

The Trust invests in debt obligations of both government and corporate issuers and is exposed to hedge fund investments through a forward agreement. These financial instruments involve the risk that the counterparty cannot or will not fulfill its obligations in respect of such financial instruments.

The Trust also assumes credit risk to its financial counterparties in connection with derivatives, loans and cash. In evaluating credit risk, the Manager will often be dependent upon information provided by the counterparty or a rating agency which may be materially inaccurate. As at December 31, 2008 the credit rating of the counterparty was as follows:

Counterparty to:	Credit Rating *
Cash	AA-
Credit facilities	AA-
Forward contract	AA-

* credit ratings as per Standard and Poor's rating agency.

For all debt securities purchased the debt issuer must have a credit rating of R-1 Mid or higher. For a listing of all current ratings by debt issuer see the Statement of Investment Portfolio.

Certain of the hedge funds invest in various debt securities and as such are exposed to movements in credit markets in many cases hedge fund managers mitigate their risk to overall credit market changes through various hedging techniques.

In addition, credit risk on hedge fund investments is mitigated through an extensive due diligence process which focuses on monitoring each hedge fund investment in order to ensure the decision to invest in a particular hedge fund strategy continues to be suitable for the Trust's portfolio.

Interest rate risk

Interest rate risk is the risk that a change in interest rates will adversely affect the fair value of fixed income securities or cause fluctuations in future cash flows of a financial instrument. The financial instruments which potentially expose the Trust to interest rate risk are short-term fixed income securities, bank loan and exposure to an interest rate swap at the Fund level. Effective duration, a commonly used measure of interest rate risk, incorporates a security's yield, coupon, final maturity, call features and other embedded options into one number expressed in years that indicates how price-sensitive a security is to changes in interest rates. The effective duration of a security indicates the approximate change in fair value expected for a 1% change in interest rates. The longer the duration, the more sensitive the security is to changes in interest rates. The Trust has minimal sensitivity to change in rates from fixed-income securities since they are usually held to maturity and short-term in nature. The Trust's exposure to interest rate risk arises from the interest rate swap held by the Fund.

As at December 31, 2008, assuming the yield curve shifting in a parallel move, if the interest rates are increased/decreased by 1%, the impact on the Trust's net assets would be $199,222.

4. Interest Rate Swap held by Northwater Five-Year Market-Neutral Fund Limited

The Fund has swapped an exposure to a floating money market rate with a U.S. Bank (the "Counterparty") in return for receiving a fixed rate of 4.45%. As a result, if mid-term rates were to decrease (increase) by 1%, the value of the Fund would increase (decrease) by approximately 0.49%. The Trust has exposure to the swap through the Forward.

The Counterparty to the swap has a credit rating of AA-. The credit worthiness of the Counterparty was reviewed prior to entering into the swap and is monitored on a regular basis.

The notional amount of the interest rate swaps as at December 31, 2008 was $40,000,000 CAD with a maturity date of June 30, 2009 (December 31, 2007: total $ 60,516,000 CAD with a maturity date of June 30, 2009).

5. Unitholders' Equity

The authorized capital of the Trust consists of an unlimited number of non-redeemable units and was derived from the public offering. The capital is managed in accordance with the Trust's investment objectives and is not subject to any external capital requirements. The Trust is a closed end vehicle and as such redemptions are not permitted. Unitholders may trade their units on the exchange. Units are transferable and represent an equal, undivided interest in the net assets of the Trust. All units are of the same class with equal rights and privileges. Each unit is entitled to one vote at any meeting of unitholders and to equal participation in any distributions made by the Trust. Fractional units will not be issued.

Under the declaration of trust, the Trust is required to make purchases of units of up to 2.5% of the outstanding units per quarter if the price at which the units offered in the market is less than 95.0% of the net asset value per unit as at the close of business on the preceding Valuation Date. In addition, the Trust may purchase units whenever they are offered for sale at less than their net asset value. In August of 2008, the trust filed a notice of intention to make normal-course purchases of units with the Toronto Stock Exchange. In its filing with the Exchange, the Trust indicated an intention to purchase up to 237,847 of the units of the Trust, representing 10% of the public float of the Trust then outstanding during the period from September 11, 2008 to September 10, 2009. Under a normal course issuer bid and the Trust's quarterly market support obligation, the Trust purchased 247,300 units for a cost of $4,378,822 during December 31, 2008 (year ended December 31, 2007: 274,500 units were repurchased).

Unitholders' equity is comprised of unit capital and deficit. The following table shows the transactions for unit capital and deficit during year ended December 31, 2008 and 2007:

Year ended December 31, 2008	Units Outstanding	Unit Capital	Contributed Surplus	Deficit	Unitholders' Equity
Balance – December 31, 2007	2,568,800	$60,540,890	$1,616,201	$ (7,586,215)	$ 54,570,876
Increase (decrease) in net assets from operations for the year				(18,186,232)	(18,186,232)
Units cancelled during the year	(247,300)	(5,828,310)	1,449,488	—	(4,378,822)
Distributions				(4,221,481)	(4,221,480)
Balance – December 31, 2008	2,321,500	54,712,580	3,065,689	(29,993,928)	27,784,342

Year ended December 31, 2007	Units Outstanding	Unit Capital	Contributed Surplus	Deficit	Unitholders' Equity
Balance – December 31, 2006	2,843,300	$67,010,243	$1,001,417	$(2,683,840)	$65,327,820
Increase (decrease) in net assets from operations for the year	—	—	—	(230,442)	(230,442)
Units cancelled during the year	(274,500)	(6,469,353)	614,784	—	(5,854,569)
Distributions	—	—	—	(4,671,932)	(4,671,932)
Balance – December 31, 2007	2,568,800	$60,540,890	$1,616,201	$ 7,586,215	$54,570,876

6. Forward Agreement

The Trust has entered into a forward agreement (the "Forward") with a U.S. Bank (the "Counterparty") to obtain exposure to a diversified portfolio of market-neutral hedge funds and an interest rate swap. The target exposure to the Fund is equal to 150% of the net asset value of the Trust. The actual exposure as at December 31, 2008 was 146% (December 31, 2007 actual exposure was 145%) calculated as net assets of the Trust divided by the net assets of the Fund. This exposure is achieved through leverage employed through the Forward. The Trust has purchased and pledged to the Counterparty the Common Share Portfolio listed on the Statement of Investment Portfolio. The Trust has agreed to deliver the Common Share Portfolio to the Counterparty, on or about the Termination Date, in exchange for the redemption proceeds of the Fund less the leverage provided by the Counterparty in order to provide the exposure to the Fund less the related costs of leverage. As a result, the value of the Forward is determined based on the change in the valuation of the Fund and the Common Share Portfolio. The Forward matures on June 30, 2009.

The notional amounts of the Forward as at December 31, 2008 are U.S. $5,841,765 and Canadian $35,545,959 (December 31, 2007: U.S. $34,551,740 and CAD$46,352,081). During the year ended December 31, 2008, the Counterparty redeemed 2,922 participating shares of the Fund for $33,176,430 USD and paid CAD$10,330,232 to the Trust as a result of a reduction in the notional amounts of the Forward and in return for partial settlement of the Common Share Portfolio.

The creditworthiness of the Counterparty was reviewed prior to the transaction and is monitored on a regular basis pursuant to credit standards established by the Manager. As at December 31, 2008 the credit rating of the counterparty was AA-. The Trust is exposed to monies to be received from the Counterparty at the maturity of the Forward. The Forward provides for the Trust's ability to terminate the Forward if the credit rating of the Counterparty goes below a certain threshold.

The Trust, through its exposure to the interest rate swap in the Fund, has exposure to changes in mid-term interest rates. For example, if mid-term interest rates were to decrease (increase) by 1%, the value of the Trust would increase (decrease) by approximately 0.49%. The interest rate swap has a maturity date of June 30, 2009.

The following table presents information regarding the Hedge Fund Portfolio held by the Fund to which the Trust has exposure through the Forward. The multi-strategy funds have not been allocated to any of the underlying hedge fund strategies set out in this table.

	As at December 31, 2008			As at December 31, 2007		
Strategy	No. of Hedge Funds	Fair Value (in U.S. Dollars)		No. of Hedge Funds	Fair Value (in U.S. Dollars)	
Activist Investments	1	$ 1,774,637	6%	1	$ 2,744,536	3%
Asset-backed security arbitrage	3	4,625,196	17%	4	7,914,440	10%
Distressed securities arbitrage	3	3,363,483	12%	5	12,791,205	16%
Fixed-income arbitrage	3	2,222,721	8%	3	5,387,185	7%
Merger arbitrage	—	—	—	1	995,490	1%
Mortgage-backed security arbitrage	3	3,296,758	12%	4	9,305,743	12%
Multi-strategy	6	5,501,011	20%	6	17,072,702	21%
Re-insurance arbitrage	2	1,236,228	4%	2	4,407,933	6%
Statistical arbitrage	4	3,779,595	14	6	10,854,126	14%
Structured finance	3	1,954,532	7%	6	8,039,314	10%
	28	$27,754,161	100%	38	$79,512,674	100%

The following table shows the number of hedge funds held by the Fund as at December 31, 2008 and 2007 categorized by the size of each hedge fund.

Total Assets of each hedge fund in U.S.$ Millions	2008	2007
< 100	4	1
100-250	4	4
250-500	2	7
500-750	3	2
750-1000	0	5
> 1000	15	19
	28	38

The following table shows the number of hedge funds held by the Fund as at December 31, 2008 and 2007 categorized by the years since inception of each hedge fund.

Years	2008	2007
< 3	1	3
3-6	8	18
6-9	10	10
9-12	4	3
12-15	3	3
> 15	2	1
	28	38

The following chart illustrates the number of hedge fund holdings of the Fund by jurisdiction of organization as at December 31, 2008 and 2007.

Location	2008	2007
Cayman Islands	24	33
British Virgin Islands	2	2
Bermuda	2	2
Bahamas	0	1
	28	38

7. Management, Advisory and Other Fees

The Trust retained the Manager under a management agreement dated June 18, 2004. Northwater Capital Management Inc. (the "Investment Advisor"), a Company formed under the laws of Ontario, Canada, acts as the advisor for the Trust. The Investment Advisor is registered in Canada as an advisor in the categories investment counsel and portfolio manager and as a dealer in the category limited market dealer under the *Securities Act (Ontario)*, as amended, and as an advisor in the category commodity trading manager under the *Commodity Futures Act (Ontario)*, as amended. The Investment Advisor is registered as a securities advisor under the *Securities Act (Quebec)*, as amended. The Investment Advisor also has equivalent registrations in the Canadian provinces of New Brunswick, Prince Edward Island, Nova Scotia, Saskatchewan, Alberta and British Columbia under the securities legislation in these provinces. The Investment Advisor is also registered in the United States as an investment advisor under the *U.S. Investment Advisers Act of 1940*, as amended, and as a commodity trading advisor and commodity pool operator under the *U.S. Commodity Exchange Act*, as amended. The Investment Advisor is a member of the U.S. National Futures Association.

The Manager is responsible for the day-to-day administration, portfolio management and unitholder services of the Trust. In exchange for these services, the Manager is entitled to an annual fee of 0.15% of the net asset value of the Trust, calculated on the last Valuation Date of each month. The fee is paid monthly in arrears.

A service fee of 0.30% per annum of the net asset value of the Trust, is payable to the Manager calculated on the last Valuation Date of each quarter. The service fee will be applied by the Manager to pay a service fee to registered dealers for services they provide to unitholders. The fee is accrued monthly and calculated and paid quarterly in arrears.

Forward fees of approximately 0.55% per annum of the U.S. notional amount and 0.90% per annum of the Canadian notional amount are payable to the Counterparty of the Forward, may vary based on the value of the Common Share Portfolio, calculated and paid quarterly in arrears. The leverage costs have been included in the Statement of Operations as part of the value of the forward contract (see note 6).

8. Bank Loan Facility

The Trust has a revolving loan facility with a U.S. financial institution (the "Bank"). The facility entitles the Trust to borrow funds in Canadian dollars up to an amount not exceeding the lesser of $6,000,000 or 10% of the net asset value of the Trust for the purposes of funding redemptions of units, purchases of units in the market and payment of expenses. Interest and stand-by fees are payable on a monthly basis. Interest rates are based on bank prime and/or Bankers' Acceptances for Canadian funds. A general security interest in the assets of the Trust has been provided in favour of the Bank.

During the year ended December 31, 2008, the bank loan balance varied between nil and $1,000,000 (year ended December 31, 2007: between nil and $2,800,000).

The average rate of interest paid on the loan for the year was 3.94%.

Since there is no loan balance outstanding as at December 31, 2008 a change in interest rates would have no impact on the Trust from interest payments.

9. Distributions

The Trust pays quarterly distributions to unitholders of $0.4375 per unit.

During the year ended December 31, 2008, distributions of $1.75 per unit and $4,221,481 in aggregate were declared by the Trust (year ended December 31, 2007: $1.75 per unit and $4,671,932 in aggregate).

10. Income Taxes

As at December 31, 2008, the Trust qualifies as a "mutual fund trust" within the meaning of the *Income Tax Act* (Canada) (the "Tax Act"). In determining its income for tax purposes, the Trust intends to treat gains or losses on the disposition of securities in the Common Share Portfolio under the Forward as capital gains and losses. As all of the net taxable income of the Trust, including net realized gains from its investment, will be paid or payable to unitholders in each calendar year, no income tax will be payable by the Trust under the present provisions of the Tax Act. Such income is taxable in the hands of the unitholder. Occasionally, more income may be distributed than is earned by the Trust for tax purposes. This excess distribution is called a "return of capital" and is not taxable to the unitholder but reduces the adjusted cost base of the unit for tax purposes. Net taxable income may differ from net income for accounting purposes.

As at December 31, 2008, the Trust had $2,187,511 available in non-capital loss carryforwards (December 31, 2007: $961,132) with expiry dates commencing in 2025 and no capital loss carryforwards (December 31, 2007: nil).

11. Reconciliation of Net Assets

The below table reconciles the reported net asset value as at December 31, 2008 with the net assets as calculated in accordance with GAAP.

	Total	Per Unit
Reported net asset value	$27,864,584	$12.06
Section 3855 adjustment	(80,242)	(0.09)
Net assets per the Statement of Net Assets	$27,784,342	$11.97

12. Indemnities

The Trust enters into various agreements that contain indemnity provisions, whereupon payment by the Trust may become due upon the occurrence of certain events. Historically, no payments have been required to be made under these indemnities and the Trust estimates the current liability at zero.

NORTHWATER CAPITAL MANAGEMENT INC.

Northwater Capital Management Inc., a leader in financial innovation since January 1989, offers customized portfolio solutions to the global investment community through the firm's Portfolio Platform™, a proprietary platform that incorporates the flexibility and scalability necessary to meet a variety of investor needs.

The firm's established indexing capability allows investors to access global equity and fixed income markets on a cost-effective basis. In addition, utilizing its expertise in constructing market-neutral fund of hedge fund portfolios that seek to generate consistent returns in both normal and extreme markets, Northwater seeks to deliver a reliable source of alpha, or excess return. Northwater's structuring technology combines these two components in a portable alpha framework that seeks to achieve an investor's return/risk objectives in an efficient, cost-effective manner.

With fourteen years of experience in fund of hedge funds, Northwater has steadily grown exposure under management to approximately CAD $7.9 billion in total, including $2.8 billion USD invested in hedge funds as at December 31, 2008. Northwater has focused on developing, delivering and continuously improving its market-neutral fund of hedge fund portfolios since launching its first such portfolio in 1994.

Northwater advises institutional clients in Canada, the United States, Australia, the United Kingdom and the rest of Europe. The firm has offices in Toronto, New York and Chicago.

Northwater also acts as an advisor to the following two closed-ended funds listed on the TSX:

- Northwater Market-Neutral Trust, the first publicly-listed investment vehicle of its kind in Canada to invest in a diversified portfolio of market-neutral hedge funds, which was launched in 1997; and
- Northwater Top 75 Income Trusts Plus, launched in 2005.

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