

N O R T H W A T E R

**Northwater Five-Year Market-Neutral Trust
March 31, 2006
Quarterly Portfolio Disclosure and Update**





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MESSAGE TO UNITHOLDERS FROM THE INVESTMENT ADVISOR

The Northwater Five-Year Market-Neutral Trust (the “Trust”) is a closed-end investment trust that delivers the return of both a diversified portfolio of market-neutral hedge funds and a fixed-for-floating interest rate swap. These returns are delivered to the Trust by way of a forward agreement. Units of the Trust are traded on the Toronto Stock Exchange under the symbol NYF.UN. For the first quarter of 2006, the return of the Trust was 2.73%. During the same time period, the Scotia Capital Universe Bond Index decreased by 0.43%, the TSX Composite Index rose by 7.98% and the S&P 500 rose by 4.21%. The Trust made distributions of \$0.4375 per unit during the quarter.

The Trust’s exposure to the fixed-for-floating interest rate swap had a negative impact on the quarterly return of approximately 0.72% as Canadian mid-term interest rates rose. American monetary policy tightened as the U.S. Federal Open Market Committee raised the federal funds rate twice in the first quarter quarter, to 4.75%. Longer term rates in Canada and the U.S. rose as well. The benchmark 10-year U.S. treasury bond rose from 4.40% to 4.85% and the Canadian 10-year bond rose by 0.28% to close at 4.26%.

Broader global equity markets registered strong gains during the first quarter, as investors shrugged off higher energy prices in light of strong economic news and corporate profits. Economic indicators, including GDP and employment were all very strong during the quarter. Real estate prices continued their extraordinary rise, but the rate of price appreciation began to moderate in response to rising interest rates.

Credit markets during the first quarter were largely positive and stable. A flurry of high yield issuance resulting from leveraged buy-out activity was met with equal or greater demand from CDO (Collateralized Debt Obligation) buyers. Corporate balance sheets have been very strong, with high operating cash flows and low capital expenditures driving their conservative stance.

Overall, the Trust’s exposure to a portfolio of market-neutral hedge funds experienced robust returns in the first quarter. The vast majority of the hedge funds recorded gains for the quarter and these profits were generated in almost every hedge fund strategy.

Convertible bond arbitrage enjoyed a strong quarter because of renewed investor interest and positive cash flows into the sector. Managers engaged in market-neutral equity and statistical arbitrage strategies posted strong results due to favorable equity conditions for their strategies. Distressed securities managers also experienced strong gains, as positions in both energy-related distressed holdings and in aircraft holdings were higher during the quarter.

Asset-backed securities were relatively strong for the quarter but conditions are becoming more difficult in asset-backed markets due to tight spreads and a limited number of distressed asset-backed securities in the market. The performance of the underlying collateral has been very good due to appreciating home prices and low unemployment leading to strong consumer credit performance.

During the first quarter, Northwater continued to actively manage the Trust's portfolio by adding, amongst others, two statistical arbitrage funds and two distressed securities funds to the portfolio. Northwater continues to focus on improving the portfolio by refining its stable of managers and focusing on market-neutral strategies that are able to deliver strong risk-adjusted returns consistent with the investment objectives.



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Northwater Capital Management Inc.



PETER B. SCHENDEL, CFA
Vice-President,
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May 16, 2006

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Statement of Net Assets
(in Canadian dollars)

	As at March 31, 2006 (unaudited)
Assets	
Cash and short-term investments	\$ 3,797,547
Common shares – at fair value (cost: 2005 – \$62,249,831)	74,356,069
	<u>78,153,616</u>
Liabilities	
Audit, legal and custody fees payable	106,294
Service fee payable	57,017
Management fee payable	28,295
Distribution payable	1,342,031
Bank loan	1,500,000
Unrealized loss on forward contract	5,644,364
	<u>8,678,001</u>
Net assets and unitholders' equity	<u>\$69,475,615</u>
Number of units outstanding	<u>3,067,500</u>
Net asset value per unit	<u>\$ 22.65</u>

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Statement of Operations
(in Canadian dollars)

	For the three-month period ended March 31, 2006 (unaudited)
Investment income	
Interest	\$ 2,578
	<u>2,578</u>
Expenses	
Service fees	55,769
Forward financing fees	195,721
Management fees	28,241
Audit fees	11,101
Directors' fees	5,350
Custodian fees	1,883
Legal fees	9,458
Security holder reporting costs	(36,789)
Loan interest and standby fees	9,738
Other fees	5,199
	<u>285,671</u>
Net investment loss	<u>(283,093)</u>
Realized and unrealized gain (loss) on investments	
Net realized gain on:	
Common shares	370,751
Change in unrealized appreciation (depreciation) on:	
Common shares	10,832,729
Forward contract	<u>(9,130,073)</u>
Realized and unrealized gain on investments for the period	<u>2,073,407</u>
Net income from operations for the period	<u>\$ 1,790,314</u>
Net income from operations per unit for the period*	<u>\$ 0.58</u>

* Based on the average number of units outstanding for the period.

NORTHWATER FIVE-YEAR MARKET-NEUTRAL TRUST

Summary of Investment Portfolio⁽¹⁾

As at March 31, 2006

(in Canadian dollars)

(unaudited)

The following table presents information regarding the hedge funds to which the Trust has exposure through a forward purchase and sale agreement including the asset allocation by investment strategy, the number of hedge funds by investment strategy and the largest individual hedge fund holding for each investment strategy as a percentage of the total net asset value of the Trust as at March 31, 2006. The multi-strategy funds may invest in multiple investment strategies.

<u>Strategy</u>	<u>Asset allocation by hedge fund strategy As at March 31, 2006</u>			<u>Largest individual hedge fund holding for each individual strategy As at March 31, 2006</u>
	<u>No. of Hedge Funds</u>	<u>Fair Value (in U.S. dollars)</u>	<u>Percentage</u>	<u>Percentage of Net Assets of the Trust</u>
Activist	1	\$ 2,157,961	3%	3.62%
Asset-backed securities				
arbitrage	5	10,856,105	13%	6.77%
Capital structure arbitrage ..	2	3,462,050	4%	3.89%
Convertible bond arbitrage ..	2	1,529,256	2%	2.25%
Distressed securities	6	8,966,266	11%	4.74%
Energy relative value	2	1,658,970	2%	1.69%
Fixed-income arbitrage	2	4,575,089	5%	4.43%
Merger arbitrage	1	1,961,444	2%	3.29%
Mortgage-backed security				
arbitrage	4	11,944,420	14%	8.74%
Multi-strategy	10	22,561,361	27%	9.08%
Re-insurance	2	2,825,285	3%	3.40%
Statistical arbitrage	2	2,146,468	2%	1.80%
Structured finance	8	9,742,792	12%	3.09%
	<u>47</u>	<u>\$84,387,467</u>	<u>100%</u>	<u>56.79%</u>

The following table lists the largest 25 hedge funds by fair value to which the Trust has exposure through a forward purchase and sale agreement as at March 31, 2006. The Trust will disclose the names of those hedge funds to which it has exposure that represent more than 5% of the net assets of the Trust at quarter-end. 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 will be used consistently in reporting going forward.

<u>Top 25 Investments</u>	<u>Type of Investment</u>	<u>Percentage of Net Assets</u>
D.E. Shaw Composite International Fund*	Trust units	9.08%
New Ellington Overseas, Ltd.*	Participating shares	8.74%
New Ellington Credit Fund Ltd.*	Participating shares	6.78%
DPFMG Multi Limited*	Participating shares	5.13%
Fund 101*	Participating shares	4.75%
Fund 146*	Participating shares	4.67%
Fund 169*	Participating shares	4.63%
Fund 140*	Participating shares	4.44%
Fund 103*	Participating shares	4.42%
Fund 130*	Participating shares	4.09%
Fund 109*	Participating shares	3.97%
Fund 170*	Participating shares	3.89%
Fund 183*	Participating shares	3.84%
Fund 121*	Participating shares	3.79%
Fund 184*	Participating shares	3.76%
Fund 200*	Participating shares	3.75%
Fund 209*	Participating shares	3.63%
Fund 190*	Participating shares	3.57%
Fund 158*	Participating shares	3.41%
Fund 189*	Participating shares	3.34%
Fund 181*	Participating shares	3.30%
Fund 191*	Participating shares	3.25%
Fund 108*	Participating shares	3.09%
Fund 116*	Participating shares	2.89%
Fund 205*	Participating shares	2.63%

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

The Trust also has holdings in the following common shares as at March 31, 2006. 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.

<u>Share Investments</u>	<u>Type of Investment</u>	<u>Percentage of Net Assets</u>
Western Oil Sands Inc. CI/A	Common shares	11.91%
Kinross Gold Corp.	Common shares	11.27%
Glamis Gold Ltd.	Common shares	9.98%
Martinrea International Inc.	Common shares	9.90%
Forzani Group Ltd.	Common shares	9.87%
Bombardier Inc. B	Common shares	8.70%
Lionore Mining Intl Ltd.	Common shares	7.31%
Cognos Inc.	Common shares	6.73%
ATI Technologies Inc.	Common shares	6.47%
Research In Motion Ltd.	Common shares	5.68%
Angiotech Pharmaceuticals Inc.	Common shares	5.26%
RONA Inc.	Common shares	5.05%
Canfor Corporation	Common shares	4.69%
Nortel Networks Corp.	Common shares	4.20%

(1) The Summary of Investment Portfolio may change due to ongoing portfolio transactions of the investment fund. 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.

ADDITIONAL PORTFOLIO INFORMATION

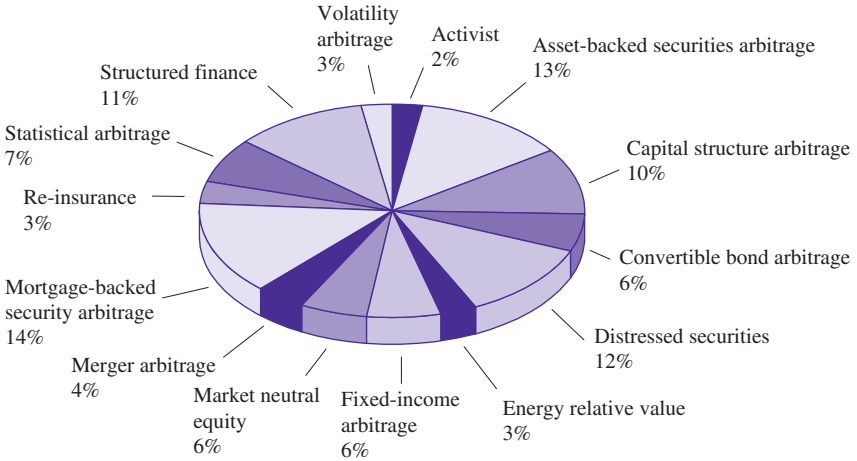
Investment Portfolio and Activity

The Trust has obtained exposure to a portfolio of market-neutral hedge funds (the “Hedge Fund Portfolio”) held by Northwater Five-Year Market-Neutral Fund Limited (the “Fund”), a Cayman Islands exempt company, through a forward purchase and sale agreement (the “Forward”) with a U.S. bank. The Hedge Fund Portfolio emphasizes sectors of the capital markets that Northwater Capital Management Inc. (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 14 broad investment strategies. The hedge funds that the Trust has exposure to have been established in offshore jurisdictions and prepare annual audited financial statements, in accordance with US or International generally accepted accounting principles (GAAP).

During the three-month period ended March 31, 2006, investments were placed with seven new hedge funds (consisting of one structured finance funds, two statistical arbitrage funds, two distressed securities funds, one energy relative value fund and one asset-backed securities arbitrage fund) and redemptions were made from five hedge funds (consisting of three capital structure arbitrage funds, one distressed securities fund and one merger arbitrage fund).

The following chart illustrates the hedge fund holdings by strategy as at March 31, 2006. The multi-strategy hedge funds have been allocated to various hedge fund strategies to reflect their exposure to their constituent strategies. Strategy weights are dynamic and change from period to period.



Investment Portfolio Risk Characteristics

The following tables present information for the period from inception and for the three-month periods ended March 31, 2006 regarding elements of the risk profile of both the Trust and the Trust's exposure to the Hedge Fund Portfolio held by the Fund.

Trust Statistics

# of positive monthly returns	16
# of negative monthly returns	5
% of negative months	23.8%
Average size of negative months	-0.86%
Worst monthly return	-1.56%

For the period from inception to March 31, 2006

Single Hedge Fund Statistics of the Fund

# of hedge funds with positive returns ⁽¹⁾	41
# of hedge funds with negative returns ⁽¹⁾	6
Average annual hedge fund standard deviation ⁽²⁾	3.49%
Average correlation between hedge funds ⁽³⁾	0.127

Three-month period ended March 31, 2006

Notes:

- (1) Measured for hedge funds in the Hedge Fund Portfolio of the Fund as at March 31, 2006.
- (2) As measured over the past 24 months for hedge funds in the Hedge Fund Portfolio of the Fund as at March 31, 2006, excludes hedge funds with less than 24 months of historical returns.
- (3) As measured over the past 24 months for hedge funds in the Hedge Fund Portfolio of the Fund as at March 31, 2006, excludes hedge funds with less than 24 months of historical returns.

Hedge Fund Performance

The following table presents the return by investment strategy of the Hedge Fund Portfolio held by the Fund for the three month period ended March 31, 2006.

<u>Strategy</u>	<u>Three-month period ended March 31, 2006</u>
Activist	4.06%
Asset-backed securities arbitrage	2.85%
Capital structure arbitrage	2.44%
Convertible bond arbitrage	4.18%
Distressed securities	2.91%
Energy relative value	-0.36%
Fixed-income arbitrage	3.70%
Merger arbitrage	8.01%
Mortgage-backed security arbitrage	2.23%
Multi-strategy	8.64%
Re-insurance	0.03%
Statistical arbitrage	7.32%
Structured finance	3.20%

Distributions

The following table presents the distribution history for the Trust since inception.

Distribution History

<u>Record date</u>	<u>Date distribution paid</u>	<u>Character of distribution for tax purposes</u>	<u>Amount per unit</u>
September 30, 2004	October 15, 2004	Return of capital	\$0.4375
December 31, 2004	January 14, 2005	Return of capital	\$0.4375
March 31, 2005	April 15, 2005	Return of capital	\$0.4375
June 30, 2005	July 15, 2005	Return of capital	\$0.4375
September 30, 2005	October 14, 2005	Return of capital	\$0.4375
December 31, 2005	January 13, 2006	Return of capital	\$0.4375
March 31, 2006	April 13, 2006	To be determined	\$0.4375

NORTHWATER CAPITAL MANAGEMENT INC.

Northwater, a leader in financial innovation since January 1989, offers customized portfolio solutions to the global investment community by providing stable, diversified alpha and precise, low-cost market exposure.

Utilizing its expertise in constructing market-neutral portfolios that seek to generate consistent returns in both normal and extreme markets, Northwater seeks to deliver a reliable source of alpha that can be tailored to meet an investor's active risk budget. In addition, the firm's established indexing capability allows access to the global equity and fixed income markets to complement an investor's unique asset/liability profile. Northwater's proven structuring technology then 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 over a ten year track record in fund of hedge funds, Northwater has steadily grown assets under management to approximately CDN \$10.9 billion total, including CDN \$4.5 billion invested in hedge funds as at December 31, 2005. 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, the United Kingdom and the rest of Europe. The firm has offices in Toronto and New York.

Northwater launched Northwater Market-Neutral Trust, which was the first publicly-listed investment vehicle of its kind in Canada, to invest in a diversified portfolio of market-neutral hedge funds, in 1997. Northwater also advises Northwater Five-Year Market-Neutral Trust and Northwater Top 75 Income Trusts^{Plus}, two additional publicly-listed vehicles.

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TSE Symbol: NYF.UN

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