

# **Diversified Investment Grade Income Trust, Series 1**

Financial Statements  
**June 30, 2007**  
(unaudited)

# Diversified Investment Grade Income Trust, Series 1

Statements of Net Assets

As at June 30, 2007 and December 31, 2006

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	June 30, 2007 (unaudited) \$	December 31, 2006 (audited) \$
<b>Assets</b>		
Cash	86,125	73,241
Short-term investments (note 3)	2,811,947	3,730,274
Credit default swap receivable (note 5)	8,841,867	7,928,125
Other accounts receivable	634	3,526
	<hr/> 11,740,573	<hr/> 11,735,166
<b>Liabilities</b>		
Accounts payable and accrued liabilities	128,198	53,021
Distributions payable (note 7)	408,000	408,000
Credit default swap related liability (note 4)	325,903	386,838
	<hr/> 862,101	<hr/> 847,859
<b>Net Assets, representing Unitholders' Equity</b>	<hr/> 10,878,472	<hr/> 10,887,307
Unitholders' capital (note 7)	3,137,608	3,953,608
Retained earnings	7,740,864	6,933,699
	<hr/> 10,878,472	<hr/> 10,887,307
<b>Number of units outstanding</b>	<hr/> 1,200,000	<hr/> 1,200,000
<b>Net assets per unit</b>	<hr/> 9.07	<hr/> 9.07

The accompanying notes form an integral part of these financial statements.

Approved by the Trustee, Metcalfe & Mansfield Alternative Investments Corp.

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*Claude Dalphond*  
Claude Dalphond

Director

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*Benoit Deschamps*  
Benoît Deschamps

Director

# Diversified Investment Grade Income Trust, Series 1

Statements of Operations and Retained Earnings

For the six month period ending June 30, 2007 and 2006

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	<b>June 30, 2007</b> (unaudited) \$	<b>June 30, 2006</b> (unaudited) \$
<b>Revenue</b>		
Interest on cash	1,156	719
Interest on short-term investments	64,279	89,999
Interest on credit default swap	(64,807)	(90,187)
Income from credit default swap	903,608	903,018
	<hr/>	<hr/>
	904,236	903,549
<b>Expenses</b>		
Audit fees	40,000	16,817
Legal fees	60,000	21,403
Administrative fees	19,006	19,712
Directors' fees	30,000	12,472
Regulatory and reporting fees	9,000	8,348
	<hr/>	<hr/>
	158,006	78,752
<b>Net investment income for the period</b>	746,230	824,797
<b>Change in unrealized appreciation (depreciation) in value of credit default swap related asset or related liability</b>	<hr/>	<hr/>
	60,935	(738,555)
<b>Increase in net assets from operations for the period</b>	807,165	86,242
<b>Retained earnings – Beginning of period</b>	<hr/>	<hr/>
	6,933,699	6,204,661
<b>Retained earnings – End of period</b>	<hr/>	<hr/>
	7,740,864	6,290,903
<b>Increase in net assets from operations per unit</b>	<hr/>	<hr/>
	0.67	0.07

The accompanying notes form an integral part of these financial statements.

# Diversified Investment Grade Income Trust, Series 1

Statements of Changes in Net Assets

For the six month period ending June 30, 2007 and 2006

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	<b>June 30, 2007</b> (unaudited) \$	<b>June 30, 2006</b> (unaudited) \$
<b>Increase in net assets from operations for the period</b>	807,165	86,242
<b>Distributions to unitholders</b>		
Return of capital (note 7)	(816,000)	(816,000)
<b>Decrease in net assets for the period</b>	(8,835)	(729,758)
<b>Net assets – Beginning of period</b>	10,887,307	11,790,269
<b>Net assets – End of period</b>	10,878,472	11,060,511

The accompanying notes form an integral part of these financial statements.

# Diversified Investment Grade Income Trust, Series 1

## Statements of Cash Flows

For the six month period ending June 30, 2007 and 2006

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	June 30, 2007 (unaudited) \$	June 30, 2006 (unaudited) \$
<b>Cash flows from</b>		
<b>Operating activities</b>		
Increase in net assets from operations for the period	807,165	86,242
Adjustments for		
Change in unrealized appreciation (depreciation) in value of credit default swap related asset or related liability	(60,935)	738,555
Decrease (increase) in other accounts receivable	2,892	(4,451)
Increase (decrease) in accounts payable and accrued liabilities	75,177	(61,867)
	<u>17,134</u>	<u>672,237</u>
	824,299	758,479
<b>Investing activities</b>		
Increase in credit default swap receivable	(913,742)	(898,865)
<b>Financing activities</b>		
Distributions paid to unitholders	(816,000)	(816,000)
<b>Decrease in cash and cash equivalents</b>	(905,443)	(956,386)
<b>Cash and cash equivalents – Beginning of period</b>	<u>3,803,515</u>	<u>5,633,478</u>
<b>Cash and cash equivalents – End of period</b>	<u>2,898,072</u>	<u>4,677,092</u>
Cash and cash equivalents comprise:		
Cash	86,125	27,922
Short-term investments	2,811,947	4,649,170
	<u>2,898,072</u>	<u>4,677,092</u>

The accompanying notes form an integral part of these financial statements.

# Diversified Investment Grade Income Trust, Series 1

Notes to Financial Statements

June 30, 2007 and 2006

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## 1 Creation of Trust and nature of operations

The Diversified Investment Grade Income Trust, Series I (the “Trust”) is a closed-end income trust which was established under the laws of the Province of Ontario on September 16, 2002 by a trust agreement.

National Bank of Canada has been acting as administrative agent since October 16, 2006 (previously and in 2005 – National Bank Trust Inc.) and National Bank Financial Inc., the promoter of the Trust, holds no voting securities of the Trustee, Metcalfe & Mansfield Alternative Investments Corp.

In order to provide the Trust with the means to meet its investment objectives, the Trust entered on September 24, 2002 into a credit default swap agreement with a financial institution (the “Bank”) having a S&P rating of AA-

The Trust provides levered exposure to a portfolio containing 99 corporate credits (2006 – 99) (“reference entities”), the objective of which is to provide unitholders with a stream of quarterly distributions and redeem all outstanding units on October 9, 2007.

Through to the maturity date, the redemption price and the net asset value of the Trust will vary depending on a number of factors such as the quarterly distributions to be made on the units, interest rates, the creditworthiness of the reference entities and cumulative net loss amounts incurred upon the occurrence of credit events in the portfolio. Credit events include bankruptcy, failure to pay and restructuring of a reference entity. However, the Trust will not be exposed to a cumulative net loss greater than \$11,200,000.

## 2 Significant accounting policies

### Generally accepted accounting principles

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles (the “Canadian GAAP”). The significant accounting policies are the following.

### Accounting estimates

The preparation of financial statements in accordance with GAAP requires the Trustee to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. The Trustee believes that the estimates used in preparing the financial statements are reasonable and prudent. Actual results could differ from those estimates.

### Short-term investments

Short-term investments are carried at the lower of cost and net realizable value, increased by related accrued interest.

# Diversified Investment Grade Income Trust, Series 1

Notes to Financial Statements

June 30, 2007 and 2006

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## 2 Significant accounting policies (continued)

### Income recognition

Interest income, interest expense and income from the credit default swap are recorded on an accrual basis.

### Valuation of the credit default swap

The credit default swap is presented in the statement of net assets at its estimated replacement cost with changes in the unrealized appreciation or depreciation for the year reported in the statement of operations. The replacement cost is estimated by using several assumptions, including the discounting of the expected contractual cash flows using a rate that reflects the credit quality of the reference entities of the swap. The replacement cost is strongly influenced by other assumptions such as the amount and timing of future estimated cash flows, discount rates, time value of money and yield curves. The estimated replacement cost reflects market conditions on a given date and for this reason cannot be representative of future fair values. Also, the replacement cost does not necessarily reflect the value at which the credit default swap could be liquidated.

## 3 Short-term investments

Under the credit default swap agreement, short-term investments are pledged to the Bank. They are issued or fully and unconditionally guaranteed as to principal and interest by the Government of Canada or a Canadian financial institution having a short-term or long-term rating from Standard & Poor's Rating Service of at least A1 or AA- and a short-term or long-term rating from Moody's of at least P-1 or Aa3 respectively. The amount outstanding as at June 30, 2007 has a maturity date of July 7, 2007 (2006 - July 7, 2006) and bears interest at 4.32% (2006 - 4.02%).

## 4 Financial derivative instrument

The Trust has entered into a credit default swap agreement with the Bank pursuant to which the Trust will pay the Bank if a credit event occurs in the reference entities. The maximum loss that could be assumed by the Trust for a credit event with respect to a reference entity amounts to \$1,120,000, up to a cumulative net loss of \$11,200,000.

# Diversified Investment Grade Income Trust, Series 1

## Notes to Financial Statements

June 30, 2007 and 2006

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The notional amount of the credit default swap as at June 30, 2007 is \$10,782,206 (2006 - \$10,782,206) for a portfolio that consists of a pool of \$110,880,000 (2006 - \$110,880,000 in reference bonds of 99 (2006 - 99) equally weighted entities that had average Moody's ratings of Ba1 on June 30, 2007 (December 31, 2006 - Baa3). The credit default swap will mature on September 24, 2007. The net quarterly payments under the swap are based on:

- a) a quarterly payment by the Trust to the Bank based on a banker's acceptance three-month rate on the collateral amount outstanding on the immediately preceding quarterly payment date, pro-rated based on the number of days of the period; and
- b) a quarterly release by the Bank to the Trust of the outstanding collateral amount calculated at an annual rate of 16.9% of the average outstanding amount over the period.

### Credit risk

As a result of entering into the credit default swap agreement, the Trust is exposed to levered credit exposure. Any credit event (bankruptcy, failure to pay or restructuring of a reference entity) relating to a reference entity would result in a net loss for the Trust. The first \$11,200,000 of net losses within the portfolio of reference entities is the maximum loss that can be assumed by the Trust.

In addition, the Trust is exposed to counterparty credit risk arising from any unrealized gain on the credit default swap plus any amount receivable from the Bank. As the maturity date of the Trust approaches, the amount of exposure to the counterparty risk will gradually grow to approximately \$9,500,000 plus any unrealized gain or minus any unrealized loss on the credit default swap. Management believes that the probability of default is low. The counterparty credit risk exposure on June 30, 2007 was \$8,515,964 (2006 - 6,801,870).

During the six month period ended June 30, 2007, no credit event occurred in the portfolio of reference obligations.

### Interest rate risk

There is an interest rate risk associated with the derivative instrument, which has several components, one of which is to compensate for a risk assumed with time. Market rates can vary and cause fluctuations in the fair value of the derivative instrument having a fixed rate at the signing of the contract.

## 5 Credit default swap receivable

The credit default swap receivable consists of the unpaid amount to the Trust with regard to the income on the credit default swap, which is calculated at the annual rate of 16.9% and is reduced by the amount of interest paid on the credit default swap to the Bank at the Canadian banker's acceptance three-month rate.

The amount receivable, net of any excess net loss amounts incurred upon the occurrence of credit events over the short-term investments given as a collateral amount, will be received on October 9, 2007, the maturity date of the Trust.

# Diversified Investment Grade Income Trust, Series 1

Notes to Financial Statements

June 30, 2007 and 2006

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## 6 Income taxes

The Trust qualifies as a unit trust within the meaning of the Income Tax Act (Canada). The Trust is subject to income taxes under this Act on the amount of taxable income for the year and can deduct in computing its income tax for all amounts paid or payable to the Trust's unitholders in determining its income for tax purposes.

Any amount payable under the credit default swap is considered to be an amount of income payable under the swap agreement and taxable as such. According to the terms of the swap agreement, the amount will be determinable only on the maturity date, and therefore the swap payment to the Trust should only be taxable as income at the maturity date.

## 7 Unitholders' capital

### Authorized units

The Trust is authorized to issue in series an unlimited number of transferable and redeemable units, each of which represents an equal undivided interest in the net assets of the Trust.

All units have equal rights and privileges. Each whole unit is entitled to one vote and to participate equally with respect to any and all distributions made by the Trust.

Units may be surrendered for redemption at any time but will be redeemed only on a quarterly basis on the last business day of each of the months of March, June, September and December (the "redemption date") for an amount equal to the redemption price of the units determined as of such redemption date.

The redemption price will be equal to the lesser of:

- a) 90% of the daily weighted average trading price per unit on the principal exchange on which the units are listed for the five trading days preceding the redemption date; and
- b) an amount equal to:
  - i) the closing price of the units on the principal exchange on which the units are listed; or
  - ii) the average of the highest and lowest prices of the units if the exchange or other market on which the units are listed provides only the highest and lowest trading prices; or
  - iii) the average of the latest bid and ask prices on the principal exchange on which the units are listed if there was no trading on such redemption date.

# Diversified Investment Grade Income Trust, Series 1

Notes to Financial Statements

June 30, 2007 and 2006

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## 7 Unitholders' capital (continued)

### Quarterly distributions

Distributions to unitholders constitute partial capital reimbursement at the issue price of the units and may fluctuate from quarter to quarter depending on the occurrence of credit events in the portfolio.

	2007	2006
	\$	\$
Unitholders' capital – Beginning of period	3,953,608	5,585,608
Distributions to unitholders	(816,000)	(816,000)
	<hr/>	<hr/>
Unitholders' capital – End of period	3,137,608	4,769,608

# Diversified Investment Grade Income Trust, Series 1

## Schedule

As at June 30, 2007

Name	Moody's Industries	Moody's Rating		S&P Rating	
		Initial September 23, 2002	June 30, 2007	Initial September 23, 2002	June 30, 2007
Abitibi-Consolidated Inc.	Printing and Publishing	Baa3	B3	BBB-	B
ACE Limited	Insurance	A2	(P)A3	A-	A-
Aetna Inc.	Insurance	Baa3	A3	BBB	A-
Agrium Inc.	Farming and Agriculture	Baa2	Baa2	BBB	BBB
Ambac Assurance Corp.	Insurance	Aaa	Aaa	AAA	AAA
Amerada Hess Corp.	Oil and Gas	Baa2	Baa3	BBB	BBB-
American Electric Power Company Inc.	Utilities	Baa1	Baa2	BBB+	BBB
American International Group Inc.	Insurance	Aaa	Aa2	AAA	AA
Amgen Inc.	Chemicals, Plastics and Rubber	A2	A2	A+	A+
Anadarko Petroleum Corp.	Oil and Gas	Baa1	Baa3	BBB+	BBB-
AOL Time Warner Inc.	Leisure, Amusement, Motion Pictures, Entertainment	Baa1	Baa2	BBB+	BBB+
Aramark Corp.	Personal, Food and Misc. Services	Baa3	(P)B3	BBB-	B+
ArvinMeritor Inc.	Automobile	Baa3	Ba3	BBB-	BB-
AT&T Corp.	Telecommunications	Baa2	A2	BBB+	A
Goodrich Corp.	Aerospace and Defense	Baa1	Baa2	BBB+	BBB
Bank of America Corp.	Banking	Aa2	Aa1	A+	AA
BCE Inc.	Telecommunications	Baa1	Baa2	A	A-
BellSouth Corp.	Telecommunications	Aa3	A2	A+	A
Boeing Capital Inc.	Finance	A3	A2	A+	A+
Bowater Inc.	Printing and Publishing	Baa3	B3	BBB	B
Burlington Northern Santa Fe Corp.	Cargo Transport	Baa2	Baa1	BBB+	BBB
Carnival Corp.	Cargo Transport	A2	A3	A	A-
Caterpillar Inc.	Machinery (Non-agriculture, Non-construction, Non-electronic)	A2	A2	A+	A
Cendant Corp.	Diversified/Conglomerate Services	Baa1	Ba2	BBB	BB+
Cinergy Corp.	Utilities	Baa2	Baa2	BBB+	A-
Cingular Wireless LLC (unlisted)	Telecommunications	A3	A3	A+	A
Citigroup Inc.	Banking	Aa1	Aa1	AA-	AA
CNA Financial Corp.	Insurance	Baa2	Baa3	BBB-	BBB-
CNF Inc.	Cargo Transport	Baa3	Baa3	BBB-	BBB
Comcast Corp.	Broadcasting	Baa3	Baa2	BBB	BBB+
Conagra Inc.	Beverage, Food and Tobacco	Baa1	Baa2	BBB+	BBB+
Constellation Energy Group Inc.	Utilities	Baa1	Baa1	BBB+	BBB+
Cooper Industries Inc.	Machinery (Non-agriculture, Non-construction, Non-electronic)	A3	A3	A-	A
Countrywide Home Loans	Finance	A3	A3	A	A
Cox Enterprises Inc.	Broadcasting	Baa1	Baa3	BBB	BBB-
CSX Corp.	Cargo Transport	Baa2	Baa3	BBB	BBB-
Deere and Company	Farming and Agriculture	A3	A2	A-	A
Devon Energy Corp.	Oil and Gas	Baa2	Baa2	BBB	BBB
Domtar Inc.	Printing and Publishing	Baa3	B2	BBB-	BB-
Eastman Kodak Company	Healthcare, Education and Childcare	Baa1	B2	BBB+	B+
Electronic Data Systems Corp.	Electronics	A1	Ba1	A	BBB-

# Diversified Investment Grade Income Trust, Series 1

Schedule (continued)

As at June 30, 2007

Name	Moody's Industries	Moody's Rating		S&P Rating	
		Initial September 23, 2002	June 30, 2007	Initial September 23, 2002	June 30, 2007
ERAC USA Finance Co.	Personal Transportation	Baa1	Baa2	A	BBB
FedEx Corp.	Cargo Transport	Baa2	Baa2	BBB	BBB
Federated Department Stores Inc.	Retail Stores	Baa1	(P)Baa2	BBB+	BBB
FleetBoston Financial Corp.	Banking	A1	Aa1	A	AA
Ford Motor Credit Company	Finance	A3	B1	BBB+	B
General Electric Capital Corp.	Finance	Aaa	Aaa	AAA	AAA
General Motors Acceptance Corp.	Finance	A2	Ba1	BBB+	BB+
Harrah's Entertainment Inc.	Hotels, Motels, Inns and Gaming	Baa3	Baa3	BBB-	BB
Hewlett-Packard Company	Electronics	A3	A2	A-	A
Household International Inc. Inco Ltd.	Finance	A3	Aa3	A	AA-
Ingersoll-Rand Company	Mining, Steel, Iron and Non-precious Metals Machinery (Non-agriculture, Non-construction, Non-electronic)	Baa3	Baa3	BBB-	BBB
International Business Machines Corp.	Electronics	A3	A3	BBB+	BBB+
International Lease Finance Corp.	Electronics	A1	A1	A+	A+
International Paper Co.	Diversified/Conglomerate Services	A1	A1	AA-	AA-
Interpublic Group of Companies Inc.	Printing and Publishing Diversified/Conglomerate Services	Baa2	Baa3	BBB	BBB
Jones Apparel Group Inc.	Textiles and Leather	Baa1	Ba3	BBB+	B
Lockheed Martin Corp.	Aerospace and Defense	Baa2	Baa3	BBB	BBB-
Marriott International Inc.	Hotels, Motels, Inns and Gaming	Baa2	Baa1	BBB	A-
MBNA Corp.	Banking	Baa2	Baa2	BBB+	BBB+
McKesson HBOC Inc.	Healthcare, Education and Childcare	Baa2	Aa1	BBB	AA
Merrill Lynch and Company Inc.	Finance	Baa2	Baa3	BBB	BBB
Metlife Inc.	Insurance	Aa3	Aa3	AA-	AA-
Motorola Inc.	Electronics	A2	A2	A	A
Nabors Industries Inc.	Oil and Gas	Baa2	Baa1	BBB	A-
National Rural Utilities Coop. Finance Corp.	Utilities	A3	A3	A-	A-
Newmont Mining Corp.	Utilities	A2	A2	NR	A
News America Inc.	Mining, Steel, Iron and Non-precious Metals	Baa3	Baa1	BBB	BBB+
Nordstrom Inc.	Broadcasting	Baa3	Baa2	BBB-	BBB
Norfolk Southern Corp.	Retail Stores	Baa1	Baa1	A-	A
Telus Corp.	Cargo Transport	Baa1	Baa1	BBB	BBB+
Raytheon Co.	Telecommunications	Ba1	Baa1	BBB	BBB+
Reebok International Ltd.	Aerospace and Defense	Baa3	Baa1	BBB-	BBB+
RyderSystem Inc.	Textiles and Leather	Baa3	Baa2	BBB-	NR
Sabre Holdings Corp.	Personal Transportation	Baa1	Baa1	BBB	BBB+
Safeway Inc.	Electronics	Baa2	Caa1	BBB+	B+
SBC Communications Inc.	Grocery	Baa2	Baa2	BBB	BBB-
Sears Roebuck Acceptance Corp.	Telecommunications	Aa3	A2	AA-	A
Sempra Energy	Finance	Baa1	Ba2	A-	BB+
Shaw Communications Inc.	Utilities	A2	Baa1	A-	BBB+
Simon Property Group L.P.	Broadcasting	Baa3	Ba1	BBB	BB+
Southwest Airlines Company	Buildings and Real Estate	Baa1	A3	BBB+	A-
	Personal Transportation	Baa1	Baa1	A	A

# Diversified Investment Grade Income Trust, Series 1

Schedule (continued)

As at June 30, 2007

Name	Moody's Industries	Moody's Rating		S&P Rating	
		Initial September 23, 2002	June 30, 2007	Initial September 23, 2002	June 30, 2007
Supervalu Inc.	Grocery	Baa3	B1	BBB	BB-
Temple-Inland Inc.	Printing and Publishing	Baa3	Baa3	BBB	BBB
Textron Inc.	Diversified/Conglomerate Services	A3	A3	A	A-
The Dow Chemical Company	Chemicals, Plastics and Rubber	A3	A3	A	A-
The Hertz Corp.	Personal Transportation	Baa2	Ba1	BBB	BB-
The Sherwin-Williams Company	Chemicals, Plastics and Rubber	A2	A3	A	A-
Toys R Us Inc.	Retail Stores	Baa3	Caa1	BBB	B-
TransOcean Sedco Forex Inc.	Oil and Gas	Baa2	Baa1	A-	A-
TXU Corp.	Utilities	Baa3	Ba1	BBB+	BB
Tyson Foods Inc.	Beverage, Food and Tobacco	Baa3	Ba2	BBB	BBB-
Verizon Global Funding Corp.	Telecommunications	A1	A3	A+	A
Viacom Inc.	Broadcasting	A3	Baa3	A-	BBB
Visteon Corp.	Automobile	Baa2	Caa2	BBB	B
Walt Disney Company	Broadcasting	A3	A2	A-	A-
Weatherford International Inc.	Oil and Gas	Baa1	Baa1	BBB+	BBB+
Weyerhaeuser Company	Diversified Natural Resources, Precious Metals, and Minerals	Baa2	Baa2	BBB	BBB