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FOR THE BENEFIT OF THE INUIT

OF NUNAVUT, PRESENT AND

FUTURE IKAYUGUTIKHAIT

INUIT NUNAVUMI, UBLUMI

OVALO HIVUNIKHAPTINI


Our
Land

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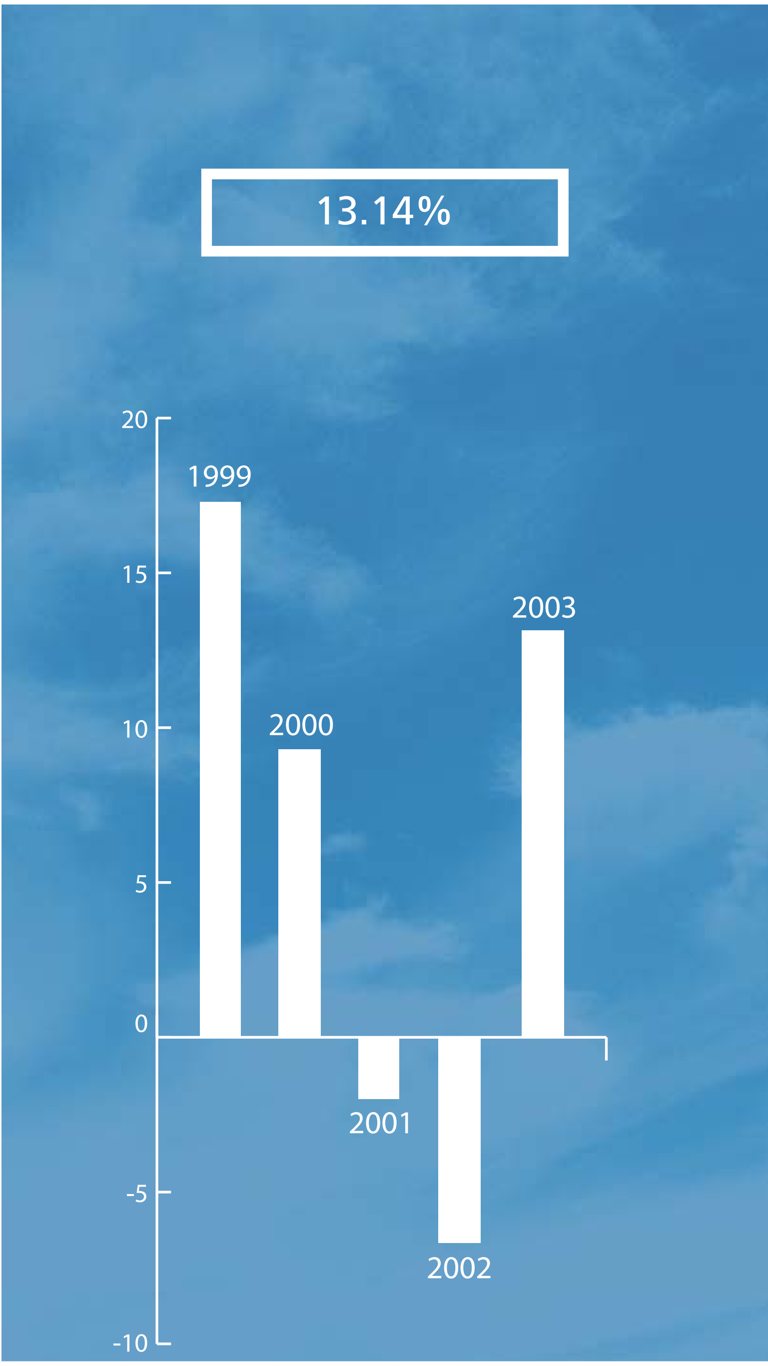
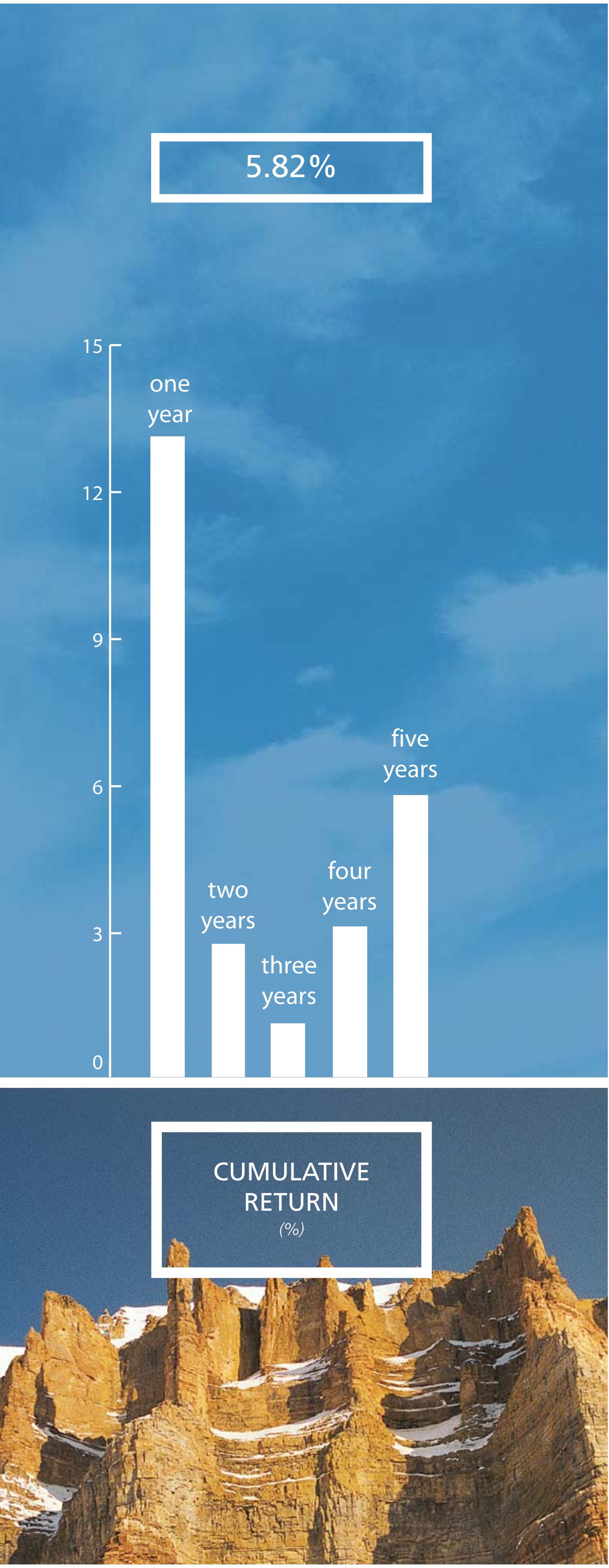

13.14%
20
15
10
5
0
-5
-10
1999
2000
2001
2002
2003

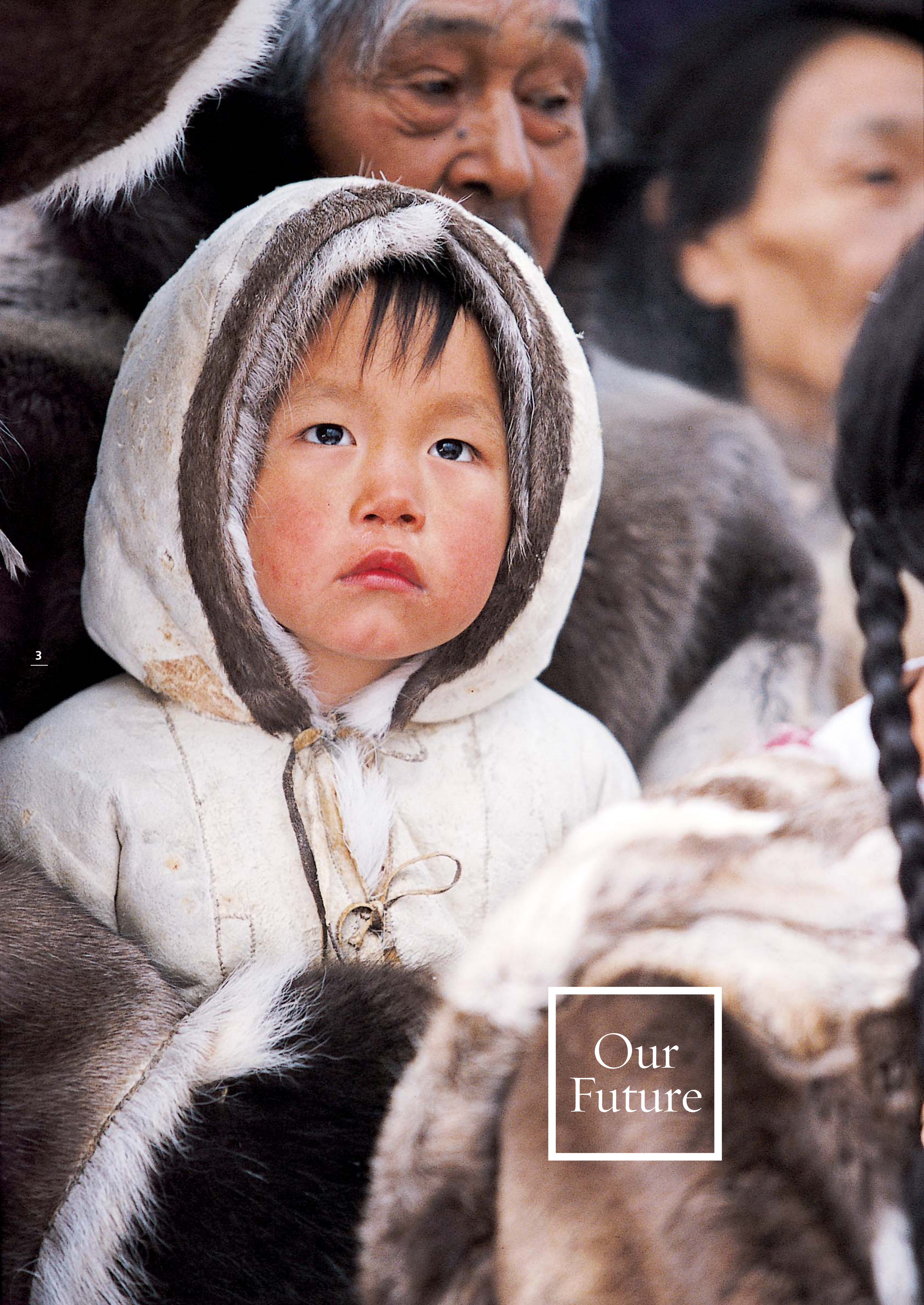

INVESTMENT
PERFORMANCE
(%)

FINANCIAL HIGHLIGHTS 2003


$19,673,237
100
80
60
40
20
0
1999
2000
2001
2002
2003
DISTRIBUTION
TO BENEFICIARIES
(in millions of dollars)
$115,686,100
120
100
80
60
40
20
0
1999
2000
2001
2002
2003
CAPITAL LOANS
TO BENEFICIARIES
(in millions of dollars)



5.82%
15
12
9
6
3
0
one year
two years
three years
four years
five years
CUMULATIVE RETURN
(%)



Our Future

MESSAGE FROM THE TRUSTEES

2003 was a year that had significant positive and negative swings during the twelve-month period. When it was all over, the one-year return was 13.1%, a return that was strong enough to place Nunavut Trust in the top quarter of all the institutional investors measured by Royal Trust in their endowment and foundations universe. During the same period, the median fund manager produced a return of 11.3%. While this is good news, market declines that affected all investors in 2001 and 2002 will continue to be reflected in our 5-year cumulative rate of return of 5.8%. We took on some additional risk that is currently providing a return premium over the median investment manager's return of 5.5% over the same period.

This year, Nunavut Trust distributed $19.7 million in income to beneficiary organizations. That brings the total income distributed since inception to $283.4 million. In addition, beneficiary organizations borrowed $28.9 million during 2003, bringing the outstanding loan balance due to the Trust up to $115.7 million. The loan must be repaid out of any excess income that will be earned in future years.

Forecasting the future is always a difficult task. Currently, it would seem that the U.S.A. economic outlook remains positive and will produce growth but the growth rate will be much weaker than it has been in the past few years. The slow growth will allow interest rates to remain relatively low although rates will rise gradually. For the next few years, many forecasters are expecting market returns of inflation plus 3%, a level below the long-term average. At an average 3 to 3.5% level of inflation, this would mean portfolio returns are expected to be 6 to 6.5% before expenses. If the Trust can continue to outperform the market as it has in the past, growing fund assets by 3% per annum will be difficult but hopefully achievable.

The pension fund, endowment and foundation industry, has always been faced with the reality that it needs to produce a steady and increasing annual cash flow to fund programs or to pay benefits to pensioners. On the other hand, the investment returns, which make these cash flows possible, are subject to cycles where returns can be very high for one or two periods followed by periods when returns may be very low or even negative.

We must balance today's spending needs against the spending needs of tomorrow

Over the last 5 years, the magnitude of these changes has been much larger making it more difficult to find the delicate balance between portfolio risk and return and between current and future levels of spending on programs. Given the extreme conditions experienced in the last 5 years, it has become clear to the industry that Trustees must ensure that their spending and investment policies are fully compatible.

At Nunavut Trust, we face exactly the same problem. The Nunavut Trust Deed requires that the Trustees:

- invest as a prudent person would,
- attempt to generate income that is to be paid out to beneficiary organi zations to be used to offer programs to beneficiaries, and
- grow the asset base year by year so that the income produced by our investments will grow and offset the effects of inflation.

In practice, the Trustees can estimate the long-term level of investment returns, net of the long-term inflation rate, that investment markets will provide to successful investors. Because there are many pension funds, endowments and foundations that have been successful for long periods of time, sufficient data exists to come up with a reasonable expectation regarding what can be achieved. For an organization that is required to maintain the real buying power of its capital, the annual spending rate must be held slightly below the average real (after inflation) rate of return on the portfolio.

In a recent study conducted by the Council on Foundations covering the period 1969-1983 it was discovered that an endowment that set an annual spending limit at 5% of the market value of the investments, averaged over either 60 months or 20 quarters, would have seen the real value of its capital decline by more than 36% and the real level of spending decline by 44% as a result of less capital upon which to earn income. More recently, a leading organization in the investment consulting industry conducted a study covering the period 1969-September 2002. Their analysis showed that a $10 million endowment paying out at the 5% level would have the value of its portfolio lowered to $9.3 million by the end of the period and the results would have been much worse were it not for the exceptional market performance in the late 1990's. They also carried out the analysis using a 6% payout rate, which created a 33% decline in the purchasing power of the assets, despite the strong bull markets of the 1980's and 1990's. Clearly there is a need to balance today's spending needs against those of future generations. Excess current spending has the potential to seriously impair the ability of the fund to meet the financial needs of the beneficiaries of the future.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Some critics would argue that a decline in long-term funding is a price worth paying to provide higher levels of funding today. This seems to have been the approach adopted by Nunavut Tunngavik Incorporated (our major beneficiary) when it developed the most recent strategic financial plan in 1999 that called for increased spending during the 2000-2004 period that would be followed by reductions starting in 2005. These 2000 to 2004 spending levels were forecasted to be significantly higher than the income distributed by Nunavut Trust.
As a result, a large debt, owed to the Trust, has accumulated. The problem with having an outstanding loan balance is that these funds are not earning any investment income, and cannot generate distributions to beneficiary organizations. Had there been no borrowing from the Trust over the past ten years, an additional $72.8 million could have been earned that would then have been distributed to beneficiary organizations.

The study of the hypothetical $10 million fund showed that a "spend now, save later" approach, reduced the total spending over the entire period. In their analysis covering the period 1969 – September 2002, they showed that a 5% spending policy would over the period produce almost $40 million in income that could be used to fund programs. A 7% spending policy would have produced only $38 million of income over the same period and eroded the capital base as well.

Given this new, detailed and independent research, many organizations have been re-thinking their approach to spending and have been recommending a reasonable level of spending at 3.5% to 4.0% of the market value of the portfolio assets. Called the "total return" approach, most perpetual funds have decided that they will commit a fixed level of funding of roughly 4% of the 20 quarter moving average of the market value of the fund regardless of actual returns. With this approach, they hope to provide beneficiary organizations with a steady and known level of funding each and every year regardless of the actual short-term market results.

We have been recommending that Nunavut Tunngavik Incorporated and our other beneficiary organizations limit their demands for funding from the Trust to 4% of the market value of the portfolio for several years. To meet our fiduciary obligations as Trustees of Nunavut Trust, we believe we must phase in a 20-quarter moving average "total return" approach by the time the funding from the Government of Canada ceases in 2007. Beneficiary organizations will have to find other funding sources if their operations require more than what we can prudently provide.

In closing, we want to assure the beneficiaries of the Nunavut Land Claim Agreement that we will not allow incompatible spending and investment policies to jeopardize the future of the Nunavut Trust portfolio.

Our Success

THE FUND

ASSET STATUS

At December 31, 2003, the market value of the Nunavut Trust portfolio was $857.0 million, an increase of $142 million above the market value at December 31, 2002. Although markets experienced wild swings throughout 2003, by the time the year was over the end result was surprisingly strong. Another surprise was the strength of the Canadian Dollar relative to the US Dollar that moderated the investment returns earned by Canadian investors. In Nunavut Trust's case, the change in currency valuation reduced our realized investment returns by $1.3 million. Other foreign currencies, tended to appreciate relative to the US dollar and this moderated the effect on our asset valuations.

The market value reserve graph shown below tries to reflect how much of a market reserve exists at any point in time to absorb the effects of short term investment return shortfalls or spending increases that if sustained could force the trust off track. By the end of 2003, the deficit declined from $73.3 million to $16.0 million reversing the trend.

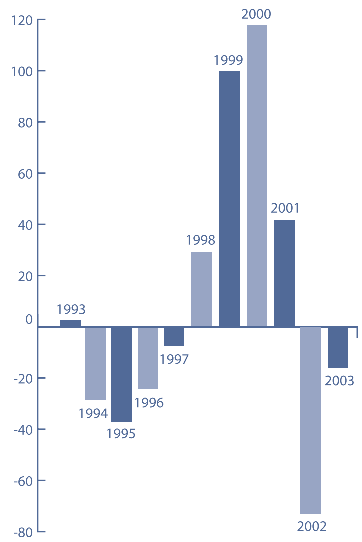
Capital loans to Beneficiaries reached a record high of $115.7 million at the end of 2003. This was the combined result of the weak investment markets and beneficiary spending levels well above sustainable spending amounts. There is a great deal of debate within the pension, endowment and foundation community over what is an appropriate, sustainable spending level, expressed as a percentage of the market value of assets. In some jurisdictions, regulators have set the minimum level at 5% of the average market value over the last 60 months. Several long-term studies have examined this limit and determined that 5% is too high and will ultimately cause serious erosion of the assets.

When outstanding beneficiary loans exist, it means the Trust will not have that money to invest. In a recent independent study carried out by a leading investment consulting firm, the conclusion reached was that policies designed to increase current spending and create savings later will ultimately generate less income than a prudent policy of spending only the income available. We have calculated the opportunity cost that the outstanding loan has had upon Nunavut Trust based upon actual portfolio market valuations and actual investment returns. The loss of income from 1993-2003, because of the existence of outstanding beneficiary loans, totaled almost $80 million – almost as much as the outstanding loan balance. This shows that if beneficiary organizations had delayed the implementation of some activities, they could have provided almost the same benefit package and had no outstanding debt. In addition an extra $4 million of ongoing cash flows would have been generated.

MARKET VALUE RESERVE

(in millions of dollars)

$-15,965,594

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INCOME DISTRIBUTION TO BENEFICIARY ORGANIZATIONS

For fiscal 2003, the Excess of Revenue over Expenditures was $4.2 million, a nice change from the previous year when investment markets yielded a loss of $10.7 million. The market value of the portfolio may fluctuate over time but gains and losses on sales of investments are not recognized as income until the investment managers sell their holdings and convert the excess of the sell price over the purchase cost into actual cash.

Under the Nunavut Trust Deed, 100% of the income for tax purposes each year must be distributed to the beneficiaries of the Nunavut Trust. The calculation of taxable income is very different from the calculation of income reported in the Trust's financial statements. For example, only one half of all gains on sales of investments are brought into the calculation of income for tax purposes. For 2003, the income distribution was $19.7 million. Between 1993 and 2003, Nunavut Trust has distributed a total of $283.4 million to beneficiary organizations.

INVESTMENTS

Investment Philosophy, Policy and Criteria

The Nunavut Trust investment portfolio has been designed to reduce the overall portfolio risk by using a carefully selected mix of external investment counsellors, each having a target percentage of the overall portfolio to invest in their individual areas of specialization. Our investment counsellors invest in fixed-income securities (bonds, short term investments and cash) as well as equity investments (Canadian stocks, foreign stocks, etc.). The fixed income investments provide a regular and predictable amount of income while the equity investments provide dividends and future growth of our assets that would not be available in the fixed income asset class.

Those responsible for managing money must initially decide how comfortable they are with the varying levels of risk associated with each type of security. The trustees developed Nunavut Trust's risk profile with help from specialists from the actuarial firm Mercer Investment Consulting and they revisit their assumptions on a regular basis. To try to support higher levels of beneficiary organizations' spending and to meet the requirements to grow trust assets, the consultants recommended that the trustees adopt a more aggressive risk profile by increasing the overall level of equity held within the portfolio. With the current asset mix, we should expect the portfolio to underperform when markets are declining and outperform when markets are rising. We recognize this will create more volatility in the short term but it offers the potential for better relative returns in a market that can be expected to produce substantially lower rates of return than those seen in the past 5 years. Our investment philosophy can be stated in the following manner:

- Our goal is to produce and distribute a positive amount of income for tax purposes each year. A negative result in any single year can be tolerated (if driven by market conditions) but we would not want to see two negative years in a row.
- Variability in investment return over the long term is not of concern unless it becomes significantly greater than the variability of the underlying investment markets themselves.
- There must be enough money available to allow for beneficiary organization spending at an annual level of no more than 4% of a twenty quarter moving average of the market value of trust assets.
- We expect the investment counsellors hired to invest Trust funds to add value relative to the performance of the markets within which they invest over the longer term.

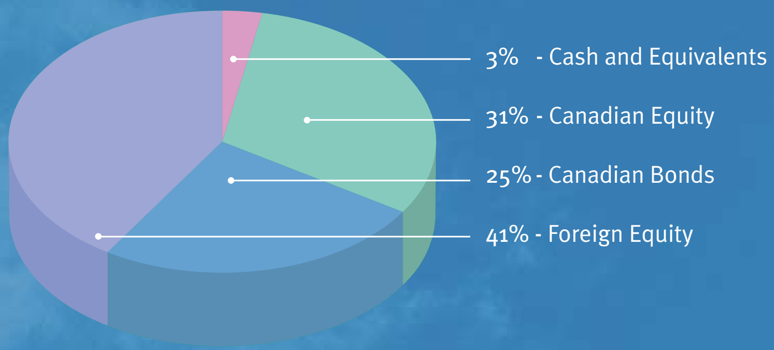
Trust assets are diversified to reduce risk in two ways. First, the portfolio is diversified by asset class and then assets are allocated to different investment managers who invest using different investment styles.

Incompatible spending and investment policies will jeopardize the future of Nunavut Trust

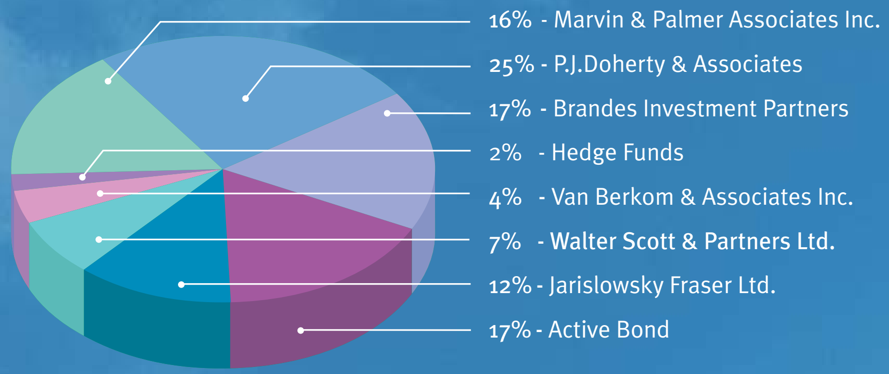
DIVERSIFICATION BY ASSET CLASS

The following charts show the diversification of Trust assets.

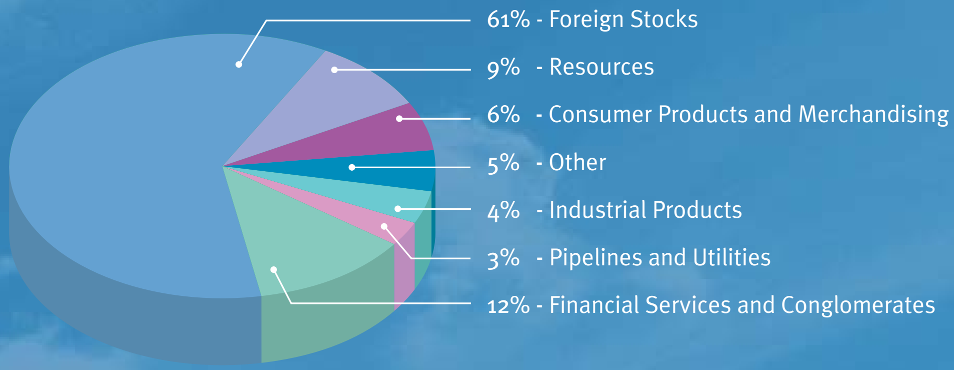
Asset Classes



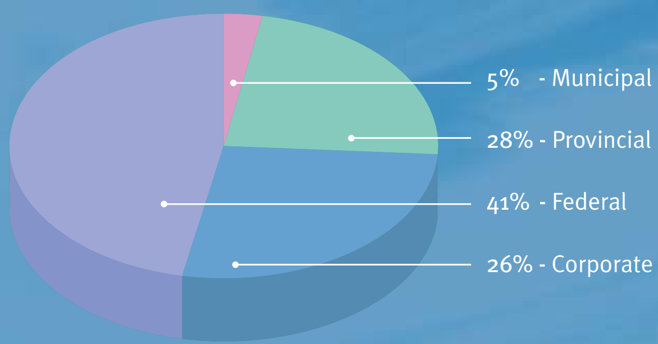
Investment Manager's



Stocks by Industry Group



Bonds by Issuer



DIVERSIFICATION BY INVESTMENT MANAGER AND STYLE

During 2003 an analysis was done on the three managers who were investing in foreign equities on behalf of Nunavut Trust. The aim of the analysis was to identify three different styles of global investing which when combined would provide a higher level of return for a smaller level of risk than the mix of global investment managers we had at the start of the year. As a result, one global investment manager was terminated and Walter Scott & Partners Limited joined Brandes Investment Partners and Marvin & Palmer Associates, Inc. as the "team" responsible for Nunavut Trust's foreign equities.

Similarly, the Canadian equity "team" was revisited and one manager was terminated but not replaced. This resulted in two managers having Canadian equity mandates with a third Canadian small cap manager completing the domestic asset "team".

Given the expectation that interest rates will gradually rise, one can expect to see the market value of bond portfolios to decline. On a net basis, we expect bond returns to be at best equal to the coupon rate less any market value losses. As a result, the Trustees have been looking for a new investment product called "income trusts". In recent times, companies have been converting their structures into the income trust model because the income trust structure allows for the return of capital before paying out income to taxable investors.
The structure is tax efficient for many taxable investors, and as such, the vehicle performs partly like a bond, and partly like a stock.
By transferring some of the bond holdings to income trusts, we should be able to moderate the negative impact of increasing interest rates and produce a positive contribution to our monthly cash flow that will be needed to fund beneficiary operations after the government capital payments cease.

At the end of 2003, the portfolio held 31% of its assets in bonds, 25% in Canadian equities, 39% in foreign investments and 2 % in hedge funds with the balance in cash and cash equivalents.

Return on Investment

The Trust Deed clearly defines the goals that are set for the Trustees to achieve. These are:

- To invest as a prudent person would
- To attempt to generate sufficient annual net income to allow the beneficiary corporations meet their responsibilities to the Inuit of Nunavut
- To attempt to ensure that the Net Capital of the Trust maintains it's buying power for future generations.

For the purpose of long term financial planning, the Trustees adopted, as a long-term rate of return, the objective of inflation plus 4.0% per annum net of operating expenses. The selection of a real (after inflation) rate of return is critical given the requirement that the Trustees preserve the real buying power of trust capital for future generations.

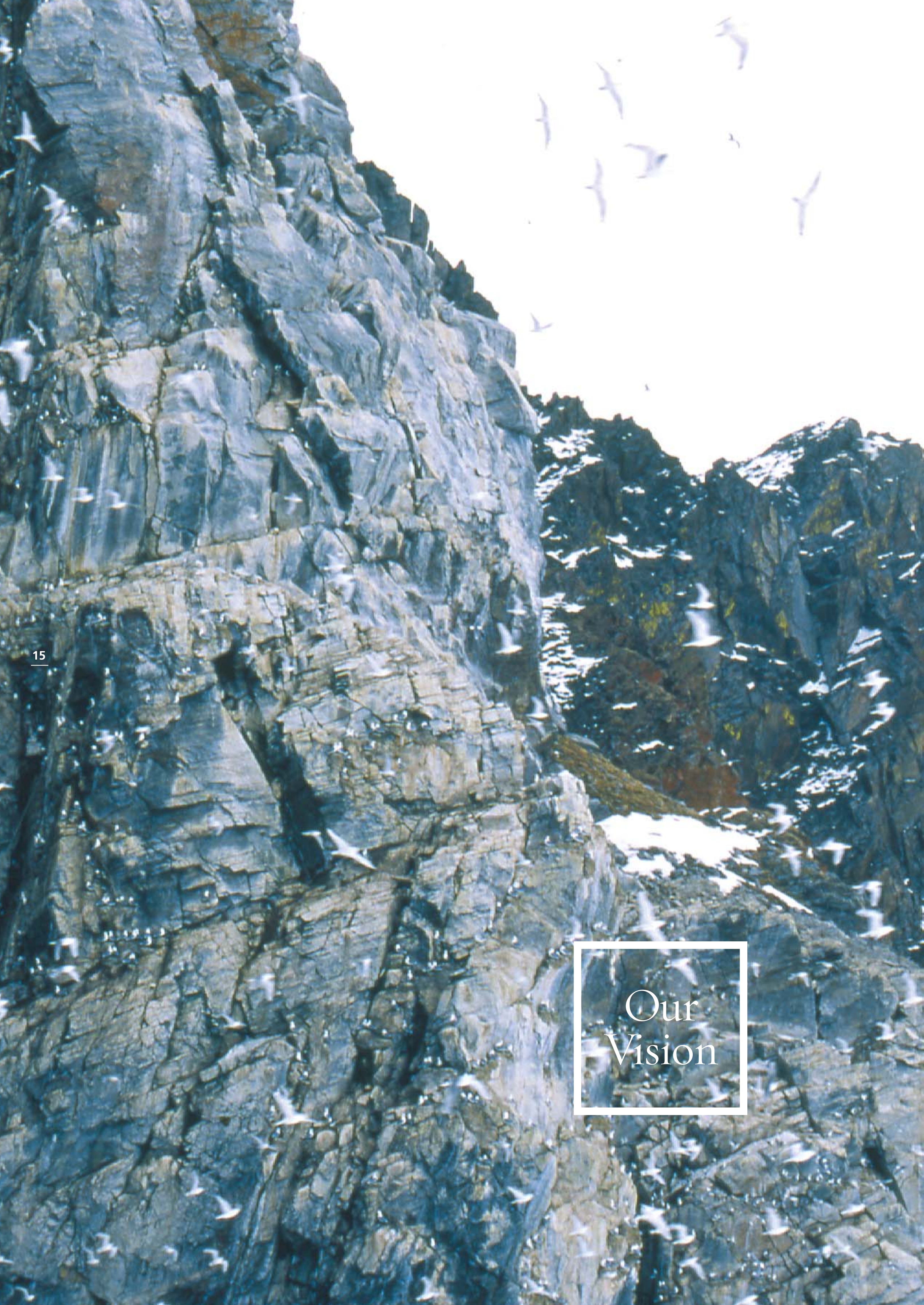
Investment returns are calculated every quarter by an independent performance measurement service, the Royal Trust Benchmark Service.
At the end of 2003, the returns reported by the Benchmark Service were as follows:

Annual Time Weighted Portfolio Rates of Return (TWRR)

	1999	2000	2001	2002	2003
Actual	17.25%	9.33%	-2.00%	-6.64%	13.14%
Benchmark	14.17%	3.04%	-5.13%	-9.55%	12.17%
Median	10.35%	12.44%	2.12%	-4.17%	13.89%

Annualized (TWRR)

	Last 5 Years	Last 4 Years	Last 3 Years	Last 2 Years	Last 1 Year
Actual	5.82%	3.14%	1.16%	2.78%	13.14%
Benchmark	2.52%	-0.21%	-1.26%	0.73%	12.17%
Median	5.46%	3.11%	0.99%	2.71%	13.89%



Our Vision

THE TRUSTEES, COMMITTEES AND ADMINISTRATION

Trustees
A small group of six beneficiaries of the Nunavut Land Claim Agreement are appointed by the Regional Inuit Associations, two from each region, and these are the people who have the extraordinary responsibility for ensuring that the $1.14 billion capital of Nunavut Trust is preserved for current and all future generations of beneficiaries. The Trustees' overall management and administrative responsibilities are defined in the Nunavut Trust Deed, including the determination of the overall portfolio asset mix and ranges of variability, investment policies and objectives, performance measurement standards used to measure progress against long term objectives as well as the selection of investment counsellors. Trustees serve three-year terms with two appointments coming up for re-consideration each year.

On December 31, 2003 the trustees were:

Jack Kupeuna, Acting Chairperson
& Kitikmeot Trustee

Darrell Ohokannoak,
Acting Vice-Chairperson & Kitikmeot Trustee

Archie Angnakak, Baffin Trustee

James Arreak, Baffin Trustee

Dorthy Gibbons, Keewatin Trustee

Peter Tatty, Keewatin Trustee

Investment Advisory Committee
To assist the Trustees, a committee consisting of experienced investment professionals, well known within the institutional investment community, was established to recommend investment policies, strategies and investment counsellors to the Trustees.

The external members of the Investment Advisory Committee include:

Roger Chiniara, Chairperson

Arthur Donner

Robert Rabinovitch

Bonita Then

A representative from the Board of Trustees of Nunavut Trust attends each of the Investment Advisory Committee meetings as does the Chief Executive Officer and the Chief Financial Officer. Once each year a joint meeting of the Trustees and the Investment Advisory Committee members is held.

Asset Custody

Although the investment counsellors are given the authority to determine the selection of individual companies in which Nunavut Trust invests and the weights that each will have within their mandates, they do not physically hold Trust assets within their accounts. Instead, to provide a segregation of duties, Nunavut Trust employs the services of one or more major trust companies specializing in the settlement of security transactions. Based on trading instructions provided by the investment counsellors, the Custodian effects the investment transactions and holds the securities of the Trust in segregated investment accounts.

Administration

A small office staff of four carries out the day-to-day management of the Fund on behalf of the Trustees. A Chief Executive Officer oversees strategic communications between the trustees and beneficiary company personnel and researches new trends emerging in the investment markets and in institutional investment fields and provides overall support to the office operations. The Chief Financial Officer also serves as the Treasurer and has a mandate covering the areas of actuarial valuations, strategic forecasting, portfolio compliance and control, income and commodity taxation, financial information systems, regulatory affairs, compensation, accounting and reporting. Our Corporate Secretary serves as our office manager, and an Administrative Assistant covers the tasks of office reception and assistant to the Chief Financial Officer. Staff members are supported by external professionals including a legal advisor (Arthur B. C Drache, Q.C.) and KPMG the external audit firm responsible for the annual external audit of Trust financial statements and the review of income tax returns.

We must not jeapardize the future of the Nunavut Trust Portfolio

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Nunakput


www.nunavuttrust.ca