



First quarter 2008 results

National Bank releases its first quarter 2008 results:

- Net income up 6% to a record \$255 million
- Diluted earnings per share up 10% to \$1.58
- Return on equity of 22.9%

Financial highlights excluding specified items for the quarter⁽¹⁾:

- Net income of \$237 million
- Diluted earnings per share of \$1.46
- Return on equity of 21.3%

(1) The financial reporting method is explained in detail on page 3.

MONTREAL, February 28, 2008 – National Bank today announced record net income of \$255 million for the first quarter of 2008, up 6% from the corresponding quarter of 2007. Excluding specified items, namely, the gain related to the sale of the Bank's operations in Nassau, Bahamas, as well as the financing costs and professional fees related to asset-backed commercial paper (ABCP), net income was \$237 million, compared to \$240 million for the year-earlier period. Diluted earnings per share were \$1.58, up 10% compared to \$1.43 in the first quarter of 2007. Excluding specified items, diluted earnings per share were \$1.46, an increase of \$0.03.

“These are very good results considering the strong volatility currently being experienced on various global financial markets. We are continuing to lay the groundwork of the Bank's renewed development strategy with a view to accelerating our rate of growth in order to achieve our financial objectives,” said Louis Vachon, President and Chief Executive Officer.

Highlights

- Growth of 9% in consumer loans, attributable to the ever growing volume of personal mortgage lines of credit in branches and loans under partnership agreements.
- Excellent quality of the loan portfolio maintained, reflected mainly in the minimal increase in the provision for credit losses at Personal and Commercial, which totalled \$44 million this quarter, barely \$1 million more than in the first quarter of 2007.
- Net gain of \$32 million following the sale of the Bank's subsidiary in Nassau, Bahamas.
- Issuance of \$400 million of innovative Tier 1 capital.

Personal and Commercial

- Net income of \$130 million in the first quarter of 2008, for an increase of 6%, owing to higher revenues coupled with lower operating expenses.
- Robust growth of 9% in consumer loans. Business growth was mitigated by a narrowing of the net interest margin from 2.88% in the first quarter of 2007 to 2.66% in the first quarter of 2008.
- Increase of \$1.3 billion in personal deposits since October 31, 2007 to \$31.5 billion.
- Increase of 15% in the volume of deposits from medium-sized businesses since the first quarter of 2007, with the largest proportion of this growth coming from outside Quebec.

Wealth Management

- Total revenues of \$216 million in the quarter, as against \$223 million in the first quarter of 2007, a variation attributable to weaker financial markets that primarily affected the securities brokerage subsidiaries.
- In February 2008, acquisition of the securities brokerage firm Groupe Financier Everest and the investment management firm Aquilon Capital Corp., whose assets under management totalled \$1.1 billion.

Financial Markets

- Total revenues of \$284 million, including non-controlling interest, a level almost equal to one year earlier.
- Net income of \$73 million in the quarter, versus \$83 million in the year-earlier period.

2008 FINANCIAL OBJECTIVES

First quarter 2008	Objectives	Results	Results excluding specified items
Growth in diluted earnings per share	3% – 8%	10%	2%
Return on common shareholders' equity	16% – 21%	22.9%	21.3%
Tier 1 capital ratio	More than 8.0%	9.3%	9.3%
Dividend payout ratio	40% – 50%		41.3%

Financial Reporting Method

The Bank uses certain measurements that do not comply with generally accepted accounting principles (GAAP) to assess results. Securities regulators require companies to caution readers that net earnings and any other measurements adjusted using non-GAAP criteria are not standard under GAAP and cannot be easily compared with similar measurements used by other companies.

FINANCIAL INFORMATION**Quarter ended January 31***(unaudited)**(millions of dollars)*

	2008	2007	%
Personal and Commercial	130	123	6
Wealth Management	41	44	(7)
Financial Markets	73	83	(12)
Other	11	(10)	–
Net income	255	240	6
Less: Gain on the sale of the Bank's subsidiary in Nassau	(32)	–	
Plus: ABCP financing cost ⁽¹⁾ and professional fees	14	–	
Net income excluding specified items	237	240	(1)
Earnings per share – diluted	\$1.58	\$1.43	10
Less: Gain on the sale of the Bank's subsidiary in Nassau	(0.20)	–	
Plus: ABCP financing cost ⁽¹⁾ and professional fees	0.08	–	
Diluted earnings per share excluding specified items	\$1.46	\$1.43	2
Return on common shareholders' equity			
Including specified items	22.9%	20.7%	
Excluding specified items	21.3%	20.7%	

(1) No accrued interest receivable was recorded on the ABCP.

Caution Regarding Forward-Looking Statements

From time to time, National Bank of Canada (the “Bank”) makes written and oral forward-looking statements such as those contained in the “Major Economic Trends and Challenges” section and under “2008 Objectives” in the “Overview” section of the Annual Report and in the “2008 Financial Objectives” section of this Report to Shareholders for the purpose of describing the economic environment in which the Bank will operate during fiscal 2008 and the objectives it has set for itself for that period. Such statements are made pursuant to Canadian securities regulations and the provisions of the United States Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among others, statements with respect to the economy (in particular, the Canadian and U.S. economies), market changes, the achievement of strategic priorities and objectives, future strategies and actions, the price of Bank shares, certain risks as well as statements with respect to our beliefs, plans, expectations, estimates and intentions. These forward-looking statements are typically identified by the words “may,” “could,” “should,” “would,” “suspect,” “outlook,” “believe,” “anticipate,” “estimate,” “expect,” “intend,” “plan,” and words and expressions of similar import.

By their very nature, such forward-looking statements require us to make assumptions and involve inherent risks and uncertainties, both general and specific. Assumptions about the performance of the Canadian and U.S. economies in 2008 and how that will affect the Bank’s business are material factors considered in setting the Bank’s strategic priorities and objectives, and in determining its financial targets, including provisions for credit losses. Key assumptions include that economic growth in Canada and the United States will be modest in 2008 and that inflation will remain low in North America. The Bank has also assumed that interest rates in Canada and the United States will decline slightly in 2008 and that the Canadian dollar will likely trade at parity with the U.S. dollar at the end of the year. In determining its expectation for economic growth, both broadly and in the financial services sector, the Bank primarily considers historical economic data provided by the Canadian and U.S. governments and their agencies. Tax laws in the countries in which the Bank operates, primarily Canada and the United States, are material factors it considers when establishing its sustainable effective tax rate. There is significant risk that express or implied projections contained in such statements will not materialize or will not be accurate. A number of factors could cause actual future results, conditions, actions or events to differ materially from the targets, expectations, estimates or intentions expressed in the forward-looking statements. Such differences may be caused by factors, many of which are beyond the Bank’s control, which include, but are not limited to, the management of credit, market and liquidity risks; the strength of the Canadian and United States economies and the economies of other countries in which the Bank conducts business; the impact of the movement of the Canadian dollar relative to other currencies, particularly the U.S. dollar; the effects of changes in monetary policy, including changes in interest rate policies of the Bank of Canada; the effects of competition in the markets in which the Bank operates; the impact of changes in the laws and regulations regulating financial services and enforcement thereof (including banking, insurance and securities); judicial judgments and legal proceedings; developments with respect to the restructuring proposal relating to asset-backed commercial paper (ABCP) and liquidity in the ABCP market; the Bank’s ability to obtain accurate and complete information from or on behalf of its clients or counterparties; the Bank’s ability to successfully realign its organization, resources and processes; its ability to complete strategic acquisitions and integrate them successfully; changes in the accounting policies and methods the Bank uses to report its financial condition, including uncertainties associated with critical accounting assumptions and estimates; operational and infrastructure risks; other factors that may affect future results, including changes in trade policies, timely development of new products and services, changes in estimates relating to reserves, changes in tax laws, technological changes, unexpected changes in consumer spending and saving habits; natural disasters; the possible impact on the business from public health emergencies, conflicts, other international events and other developments, including those relating to the war on terrorism; and the Bank’s success in anticipating and managing the foregoing risks.

Additional information about these factors can be found under “Risk Management” and “Factors That Could Affect Future Results” in the 2007 Annual Report.

The Bank cautions that the foregoing list of important factors is not exhaustive. Investors and others who base themselves on the Bank’s forward-looking statements should carefully consider the above factors as well as the uncertainties they represent and the risk they entail. The Bank also cautions readers not to place undue reliance on these forward-looking statements. Moreover, these forward-looking statements may not be suitable for establishing strategic priorities and objectives, future strategies or actions, financial objectives and projections other than those mentioned above.

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HIGHLIGHTS*(unaudited)**(millions of dollars)*

Quarter ended	January 31, 2008	January 31, 2007	% Change
Operating results			
Total revenues	\$ 929	\$ 989	(6)
Total revenues adjusted for non-controlling interest ⁽²⁾	991	988	–
Net income	255	240	6
Return on common shareholders' equity	22.9%	20.7%	
Per common share (dollars)			
Earnings – basic	\$ 1.58	\$ 1.45	9
Earnings – diluted	1.58	1.43	10
EXCLUDING SPECIFIED ITEMS⁽¹⁾			
Operating results			
Total revenues	\$ 916	\$ 989	(7)
Total revenues adjusted for non-controlling interest ⁽²⁾	978	988	(1)
Net income	237	240	(1)
Return on common shareholders' equity	21.3%	20.7%	
Per common share (dollars)			
Earnings – basic	\$ 1.47	\$ 1.45	1
Earnings – diluted	1.46	1.43	2
Per common share (dollars)			
Dividends declared	\$ 0.62	\$ 0.54	15
Book value	28.13	28.34	(1)
Stock trading range			
High	54.25	66.59	
Low	45.15	61.36	
Close	50.53	64.29	

	January 31, 2008	October 31, 2007	% Change
Financial position			
Total assets	\$ 120,124	\$ 113,085	6
Loans and acceptances	52,095	52,045	–
Deposits	73,122	70,798	3
Subordinated debentures and shareholders' equity	6,505	6,242	4
Capital ratios – BIS under Basel II			
Tier 1	9.3%		
Total	12.9%		
Capital ratios – BIS under Basel I			
Tier 1	9.8%	9.0%	
Total	13.5%	12.4%	
Impaired loans, net of specific and general allowances	(168)	(179)	
as a % of loans and acceptances	(0.3)%	(0.3)%	
Assets under administration/management	233,835	239,028	
Total personal savings	104,024	106,288	
Interest coverage	7.83	7.88	
Asset coverage	4.36	3.89	
Other information			
Number of employees	16,856	16,863	–
Number of branches in Canada	446	447	–
Number of banking machines	846	835	1

(1) See "Financial Reporting Method" on page 3.

(2) Adjusted for gains or losses attributable to third parties using the Innocap platform.

MD&A | Management's Discussion and Analysis of Financial Condition and Operating Results

February 27, 2008 – The following text presents Management's discussion and analysis of the Bank's financial condition and operating results. This analysis was prepared in accordance with the requirements set out in National Instrument 51-102 respecting Continuous Disclosure Obligations of the Canadian Securities Administrators and is based on the unaudited interim consolidated financial statements for the first quarter of 2008. Additional information about National Bank of Canada, including the Annual Information Form, can be obtained from the SEDAR website at www.sedar.com and the Bank's website at www.nbc.ca.

Analysis of Results

Consolidated Results

National Bank reported record net income of \$255 million in the first quarter of fiscal 2008, as against net income of \$240 million in the corresponding quarter of 2007. Excluding specified items, namely, the gain related to the sale of the Bank's Nassau operations, as well as the financing cost and professional fees related to the ABCP held, net income in the first quarter of 2008 was \$237 million, down \$3 million from the first quarter of 2007. Diluted earnings per share rose 10% to \$1.58 from \$1.43 in the same period a year earlier. Excluding specified items, diluted earnings per share were \$1.46, up \$0.03 from the first quarter of 2007.

Return on common shareholders' equity in the first quarter of 2008 was 22.9%, compared to 20.7% for the corresponding period of 2007. Excluding the specified items of 2008, ROE was 21.3%, up 60 basis points versus the year-earlier period.

Total Revenues

The Bank's total revenues amounted to \$929 million in the first quarter of 2008, compared to \$989 million in the corresponding period of 2007. Taking into account non-controlling interest, total revenues reached \$991 million in the first quarter of 2008, for a year-over-year increase of \$3 million.

Net interest income for the quarter was \$428 million versus \$276 million in the first quarter of 2007. Net interest income at Personal and Commercial declined \$2 million to \$342 million for the quarter. This decrease was attributable to the net interest margin, which narrowed from 2.88% in the first quarter of 2007 to 2.66% in the first quarter of 2008. This narrowing stemmed from the reduction in the net interest margin on credit products due to higher financing costs, primarily because of tighter credit conditions around the world. Moreover, trading revenues recorded to net interest income increased \$155 million and the cost of financing the ABCP held by the Bank reduced net interest income for the quarter by \$19 million.

Other income for the first quarter totalled \$501 million, as against \$713 million for the same period of 2007. Trading losses recorded to other income reached \$68 million in the first quarter of 2008, compared to trading revenues of \$131 million a year earlier. These losses were more than offset by net interest income and non-controlling interest related to trading activities. Securities brokerage commissions declined \$10 million to \$59 million. Revenues from mutual funds and trust services fell \$6 million from the first quarter of 2007 to \$79 million this quarter. These decreases were essentially due to the weakness of financial markets. Underwriting commissions and advisory service fees totalled \$95 million in the first quarter of 2008, as against \$98 million a year earlier, and securitization revenues amounted to

\$46 million, compared to \$48 million in the same period of 2007. Insurance revenues were up \$4 million to \$34 million. Other income was up \$4 million to \$89 million owing to the \$32 million gain on sale of the Bank's subsidiary in Nassau, offset by lower merchant banking activities.

Operating Expenses

In the first quarter of 2008, operating expenses declined \$24 million from the first quarter of 2007 to \$632 million this quarter. The reduced cost of variable compensation at the Bank's full-service brokerage accounted for the decrease. In addition, technology expenses remained stable, while other expenses were down \$8 million.

Provision for credit losses

For the first quarter of 2008, the Bank recorded specific provisions for credit losses of \$32 million, or \$3 million more than in the corresponding period of 2007. As at January 31, 2008, gross impaired loans stood at \$249 million, or \$10 million more than at the same date a year earlier. This increase, attributable to credit to medium-sized businesses and consumer loans, was mitigated by the decrease in gross impaired loans to corporations. As at January 31, 2008, the provision for credit losses exceeded gross impaired loans by \$168 million, as against \$196 million as at January 31, 2007.

Income Taxes

Income taxes for the first quarter of 2008 were \$67 million, representing an effective tax rate of 25%. This is comparable to income taxes of \$56 million for the same quarter a year earlier and an effective tax rate of 18%. Excluding the gain on the sale of operations in Nassau and the non-controlling interest in revenues, the tax rate was 23% for the first quarter of 2008.

Results by Segment

Personal and Commercial

Personal and Commercial net income totalled \$130 million in the first quarter of 2008, up \$7 million from the \$123 million in net income earned in the corresponding quarter of 2007. Total revenues for the segment rose \$6 million to \$546 million. Loan and deposit volumes at Personal and Commercial experienced robust growth of 8% and 5%, respectively, in the first quarter of 2008 versus the year-earlier period. This growth was tempered by the narrowing of the net interest margin by 22 basis points in the first quarter of 2008 compared to the first quarter of 2007, reflecting tighter credit conditions on markets, which increased the cost of funds.

MD&A | Management's Discussion and Analysis of Financial Condition and Operating Results (cont.)

Total revenues at Personal Banking advanced \$6 million in the first quarter of 2008 as against the year-earlier period. This increase, which stemmed from the \$3.2 billion or 9% growth in the volume of average assets, was mitigated by the narrower net interest margin on credit products, while the margin on deposit products remained essentially unchanged.

Total revenues at Commercial Banking remained stable in the first quarter of 2008. Growth in business loan and deposit volumes was offset by the narrowing net interest margin on credit products. The margin on deposits, however, widened slightly.

Operating expenses at Personal and Commercial were \$309 million in the first quarter of 2008, a decrease of \$3 million from the corresponding quarter of 2007. This decrease was attributable to ongoing efforts to improve productivity, which focused on reducing operations – support expenses. At 57%, the efficiency ratio for the first quarter of 2008 improved 1% from the 58% posted for the year-earlier period. The segment's provision for credit losses was slightly up by \$1 million or 2% to reach \$44 million, due to higher credit losses for Commercial Banking.

Wealth Management

Wealth Management net income amounted to \$41 million in the first quarter of 2008, compared to \$44 million in the same quarter of 2007, for a decrease of \$3 million. Total revenues for the segment were \$216 million for the quarter, as against \$223 million for the year-earlier period. Robust private investment management, mutual fund and portfolio management operations were offset by a decline in securities brokerage activities attributable to more difficult market conditions during the quarter. The efficiency ratio for the first quarter of 2008 was 71%, compared to 70% for the same quarter of 2007. This change was mainly due to lower variable compensation.

Financial Markets

The Financial Markets segment recorded net income of \$73 million in the first quarter of 2008, down \$10 million versus the same period in 2007. Total revenues for the segment amounted to \$222 million, as against \$293 million for the first quarter of 2007. Including non-controlling interest, total revenues for the quarter were \$284 million, only 3% less than the year-earlier period. Trading revenues for the quarter totalled \$124 million, up \$16 million from the corresponding quarter of 2007. Financial market fees rose \$6 million to \$72 million, while the change in gains on available for sale securities and the change in banking service revenues offset each other. The decrease in other revenues was attributable to lower merchant banking activities.

Operating expenses for the first quarter of 2008 were \$173 million, up \$5 million from the same period in 2007. This rise stemmed from higher technology expenses, professional fees and other expenses, while the increase in variable compensation was due to the revenue mix for this quarter. The efficiency ratio was 61%, as against 58% in the first quarter of 2007. The provision for credit losses was nil for this segment for both the first quarter of 2007 and the first quarter of 2008.

FINANCIAL MARKET REVENUES

(taxable equivalent basis⁽¹⁾)

(millions of dollars)

	Q1 2008	Q1 2007
Trading revenues ⁽²⁾		
Equity	(13)	87
Fixed income	95	5
Commodity and foreign exchange	42	16
	124	108
Financial market fees	72	66
Gains on available for sale securities	23	29
Banking services	49	44
Other	16	45
Total	284	292

(1) See Note 17 to the Consolidated Financial Statements on page 40.

(2) Adjusted for non-controlling interest

Other

The *Other* heading of segment results posted net income of \$11 million in the first quarter of 2008, compared to a net loss of \$10 million in the corresponding quarter of 2007. The segment recognized a gain of \$32 million on the sale of the Bank's subsidiary in Nassau, Bahamas. A net loss of \$14 million, after income tax recovery, was recorded for the cost of financing ABCP held. Securitization revenues declined \$2 million to \$46 million in the quarter.

Comprehensive Income

In the first quarter of 2008, comprehensive income was \$303 million, which was \$48 million higher than net income. The difference comes primarily from unrealized gains on derivative financial instruments designated as cash flow hedges.

Cash Flows

Due to the nature of the Bank's business, most of its revenues and expenses are cash items. Moreover, certain activities, such as trading activities, generate significant cash flow movement, which can have an impact on several assets and liabilities such as held for trading securities, securities sold short or securities sold under repurchase agreements.

During the first quarter of 2008, cash and cash equivalents increased by \$1.2 billion, while they remained unchanged in the first quarter of 2007. As at January 31, 2008, cash and cash equivalents totalled \$4.2 billion versus \$10.8 billion one year earlier.

MD&A | Management's Discussion and Analysis of Financial Condition and Operating Results (cont.)

Operating activities required \$4.6 billion in cash flows, owing chiefly to the \$5.6 billion increase in held for trading securities. For the first quarter of 2007, operating activities required cash flows of \$2.0 billion, due to the \$2.3 billion increase in held for trading securities.

Financing activities generated cash flows of \$6.3 billion, due to the increase of \$2.1 billion in securities sold short, \$1.1 billion in securities sold under repurchase agreements and \$2.3 billion in deposits. For the corresponding period of 2007, financing activities generated \$4.3 billion in cash flows, mainly as a result of the \$2.2 billion increase in securities sold short and the \$2.3 billion increase in securities sold under repurchase agreements.

Lastly, investing activities required \$0.5 billion in cash flows in the first quarter of 2008, owing to the \$2.9 billion increase in securities purchased under reverse repurchase agreements, offset by the \$1.9 billion decrease in available for sale securities. For the corresponding period of 2007, investing activities required cash flows of \$2.4 billion, mainly due to the increase in securities purchased under reverse repurchase agreements.

Balance Sheet

As at January 31, 2008, the Bank had assets of \$120.1 billion, compared to \$113.1 billion as at October 31, 2007. Loans and acceptances were stable, as the decrease in retail mortgage volumes was offset by growth in other consumer credit, including credit card receivables. Cash, deposits with financial institutions, securities and securities purchased under reverse repurchase agreements rose \$7.7 billion. The table below presents the main portfolios.

AVERAGE MONTHLY VOLUMES (millions of dollars)

	January 2008	October 2007	January 2007
Loans and acceptances*			
Residential mortgages	22,977	22,858	21,689
Consumer loans	11,314	11,050	9,738
Credit card receivables	1,835	1,793	1,775
SME loans	14,195	14,048	13,599
Corporate loans	6,285	5,919	5,378
	56,606	55,668	52,179
Deposits			
Personal (balance)	31,522	30,215	29,628
Off-balance sheet personal savings (balance)	72,502	76,073	71,570
Business	12,134	11,870	11,029

* including securitized assets

Residential mortgage loans rose 6% as at January 31, 2008, reaching \$23.0 billion compared to \$21.7 billion as at January 31, 2007. Consumer loans climbed 16.2% to \$11.3 billion, primarily driven by higher volumes of secured lines of credit. SME loans increased \$0.6 billion to \$14.2 billion and corporate loans continued to grow, rising 16.9% to \$6.3 billion.

Personal deposits stood at \$31.5 billion as at January 31, 2008, up \$1.9 billion from the same period a year earlier, with most of that growth derived from term deposits. Off-balance sheet personal savings administered by the Bank as at January 31, 2008 totalled \$72.5 billion up \$0.9 billion in a year. The increase was primarily attributable to savings administered by private investment management. Business deposits advanced \$1.1 billion year over year to \$12.1 billion as at January 31, 2008.

Asset-Backed Commercial Paper

On December 23, 2007, the Pan-Canadian Investors Committee for Third-Party Structured Asset Backed Commercial Paper approved an agreement in principle to restructure 43 series of asset-backed commercial paper (ABCP) issued by 20 trusts. The restructuring plan will extend the maturity of the ABCP to provide for a maturity similar to that of the underlying assets. Trusts with ABCP supported in whole or in part by synthetic assets will pool their assets. Floating rate notes will be issued in exchange for their existing ABCP, with maturities based upon the maturities of the underlying pooled assets which are expected to be an average of seven years. Trusts with ABCP supported solely by traditional securitized assets will be restructured on a series-by-series basis, with each trust or series maintaining its separate assets. Noteholders will receive floating rate notes with maturities based upon the maturity of the underlying assets which will amortize and be repaid as assets mature or are sold. Trusts with ABCP supported by "ineligible" assets for which the credit quality is uncertain, principally as a result of exposure to sub-prime or home equity loan mortgages in the United States, will be restructured on a series-by-series basis, with each series maintaining its separate exposure to its own assets. Noteholders will receive floating rate notes with maturities based upon the maturity of the underlying assets which will amortize and be repaid as assets mature or are sold.

Taking into account this additional information and the higher probability of a successful restructuring of the ABCP, the Bank adjusted its valuation approach in order to assess the fair value of the ABCP it was holding as at January 31, 2008. For most of the ABCP held, the Bank considered the very high quality of the underlying assets and determined the fair value using a discounted cash flow analysis. The main assumptions pertain to the expected coupons, the expected maturity of the floating rate notes received in exchange of the ABCP, the expected rating and an appropriate discount rate taking into account risks of future losses. The expected discount rate is determined based on observable market inputs for comparable securities.

MD&A | Management's Discussion and Analysis of Financial Condition and Operating Results (cont.)

For ABCP that is not restructured or not under the Pan-Canadian Investors Committee process, as well as for ABCP supported by ineligible assets, observable market inputs for comparable securities from independent pricing sources were used to assess the fair value of each class of assets in the trusts.

To determine the value of the ABCP it holds, the Bank established a range of estimated fair value. Since the carrying value of the ABCP held by the Bank as of October 31, 2007 is within the range of the estimated fair value established as of January 31, 2008, no change was made to the carrying value as of January 31, 2008. The carrying value of the ABCP held by the Bank, as of January 31, 2008, was \$1,707 million of which \$1,580 million was classified in *Available for sale securities* and \$127 million was classified in *Held for trading securities*.

The Bank's valuation was based on its assessment of the conditions prevailing as at January 31, 2008, which may change in subsequent periods. Determining the fair value of ABCP is complex and involves an extensive process that includes the use of quantitative modeling and relevant assumptions. Possible changes that could have a material effect on the future value of the ABCP include (1) changes in the value of the underlying assets, (2) developments related to the liquidity of the ABCP market, (3) the outcome of the restructuring of the conduits and (4) a slowdown in economic conditions in North America.

Risk Management

The Bank views risk as an integral part of its development and the diversification of its activities. Information on risk management is included in Tables 1 to 6 presented in the Additional Financial Information section at the end of this Management's Discussion and Analysis and in Note 3 to the unaudited interim consolidated financial statements regarding management of the risks associated with financial instruments.

Accounting Policies and Estimates

The unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP). The reader is referred to Note 1 to the 2007 audited annual consolidated financial statements for more information on the significant accounting policies used to prepare the consolidated financial statements. Certain of these accounting policies are considered critical because they are important to the presentation of the Bank's financial condition and operating results and require difficult, subjective and complex judgments and estimates because they relate to matters that are inherently uncertain. The key assumptions and bases for estimates made by Management in accordance with GAAP are described in the 2007 Annual Report.

There have not been any changes to the Bank's significant accounting policies affecting fiscal 2008, other than the one described in Note 2a) to the unaudited interim consolidated financial statements on accounting changes.

Furthermore, the Bank adopted the new standards set out in the CICA Handbook relating to disclosure for financial instruments and capital as well as the standards relating to the presentation of financial instruments. The reader is referred to Note 2a) to the unaudited interim consolidated financial statements.

Details of a future change in accounting standards are presented in Note 2b) to the unaudited interim consolidated financial statements.

Disclosure on Internal Controls over Financial Reporting

During the first quarter of 2008, no changes were made to the Bank's internal control over financial reporting policies, procedures and other processes that have materially affected, or are reasonably likely to materially affect, the Bank's internal control over financial reporting.

Capital

Tier 1 and total capital ratios, according to the new rules of the Bank for International Settlements (BIS) – Basel II – stood at 9.3% and 12.9%, respectively, as at January 31, 2008. If these ratios had been calculated using the old BIS rules – Basel I – they would have been 9.8% and 13.5%, respectively, as at January 31, 2008, compared to 9.0% and 12.4% as at October 31, 2007.

The increase in the capital ratios was essentially attributable to the issue of \$400 million in NBC CapS II – Series 1 securities. Furthermore, as at January 31, 2008, risk-weighted assets under Basel I would have been \$49.3 billion, compared to \$51.6 billion under the new rules, an increase of 4.7% from October 31, 2007. This increase mitigated the rise in the ratios and was primarily due to the impact of including operational risk in the calculation of risk-weighted assets.

Other information on capital is provided in Table 7 presented in the Additional Financial Information section at the end of this Management's Discussion and Analysis as well as in Note 4 to the unaudited interim consolidated financial statements on capital disclosure.

Subsequent Events

In February 2008, a Bank's subsidiary acquired Groupe Financial Everest, a securities brokerage firm and Aquilon Capital Corp., an investment management firm. The combined assets under management totalled \$1.1 billion.

Dividends

The Board of Directors declared regular dividends on the various classes and series of preferred shares and a dividend of \$0.62 per common share, payable on May 1, 2008 to shareholders of record on March 27, 2008.

MD&A | Additional financial information

Quarterly information

(unaudited)

(millions of dollars except per share amounts)

	2008	2007				2006			2007	2006
	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Total	Total
Total revenues	\$ 929	\$ 402	\$ 1,010	\$ 1,022	\$ 989	\$ 970	\$ 921	\$ 941	\$ 3,423	\$ 3,803
Net income (loss)	255	(175)	243	233	240	220	220	214	541	871
Earnings (loss) per common share										
Basic	1.58	(1.14)	1.49	1.42	1.45	1.33	1.32	1.29	3.25	5.22
Diluted	1.58	(1.14)	1.48	1.40	1.43	1.31	1.30	1.26	3.22	5.13
Dividends per common share	0.62	0.60	0.60	0.54	0.54	0.50	0.50	0.48	2.28	1.96
Return on common shareholders' equity	22.9%	(16.0)%	20.6%	20.3%	20.7%	19.7%	20.2%	20.4%	11.5%	20.1%
Total assets	\$ 120,124	\$ 113,085	\$ 123,353	\$ 135,172	\$ 121,402	\$ 116,801	\$ 108,552	\$ 111,083		
Impaired loans, net	140	129	110	110	112	116	98	111		
Per common share										
Book value	28.13	26.85	28.70	28.92	28.34	27.17	26.57	25.77		
Stock trading range										
High	54.25	60.28	66.14	65.87	66.59	62.86	62.69	65.60		
Low	45.15	50.50	60.61	61.96	61.36	58.26	56.14	61.35		

Table 1 – Distribution of loans by borrower category

As at January 31, 2008

(unaudited)

(millions of dollars)

	Gross loans	Impaired loans	Specific allowances	Provision for credit losses	Write-offs
Personal ⁽¹⁾	13,784	35	12	16	30
Residential mortgage	15,044	26	2	–	–
Non-residential mortgage	1,379				
Agricultural	1,980				
Financial institutions	3,844				
Manufacturing	2,064				
Construction and real estate	1,161				
Transportation and communications	494				
Mines, quarries and energy	1,233				
Forestry	151				
Government	1,278				
Wholesale	546				
Retail	1,209				
Services	951				
Other	2,861				
Total – Business and government	19,151	188	95	16	29
Total	47,979	249	109	32	59

(1) Including consumer loans, credit cards and other personal loans

MD&A | Additional financial information (cont.)

Table 2 – Geographic distribution of loans

As at January 31, 2008
(unaudited)
(millions of dollars)

	Gross loans	Impaired loans	Specific allowances
Canada			
Residential mortgage	14,989	26	1
Personal and credit card	13,547	35	12
Business and government	16,444	171	94
	44,980	232	107
United States			
Residential mortgage	55	–	1
Personal and credit card	2	–	–
Business and government	2,693	17	1
	2,750	17	2
Others			
Residential mortgage	–	–	–
Personal and credit card	235	–	–
Business and government	14	–	–
	249	–	–
	47,979	249	109

Table 3 – Credit risk mitigation

As at January 31, 2008
(unaudited)
(millions of dollars)

	Eligible financial collateral	Total exposure covered by	
		Guarantees	Credit derivatives
Balance sheet exposures			
Securities purchased under reverse repurchase agreements and securities sold under repurchase agreements	10,772	–	–
Loans			
Residential mortgage	–	8,804	–
Personal and credit card	–	907	–
Business and government	1,197	1,377	66
Derivative financial instruments	416	–	–

MD&A | Additional financial information (cont.)

Table 4 – Breakdown of credit risk by derivative financial instrument portfolio

As at January 31, 2008
(unaudited)
(millions of dollars)

	Replacement cost	Credit equivalent	Risk-weighted amount
Interest rate contracts	1,106	1,790	425
Foreign exchange contracts	1,126	2,201	778
Equity contracts	1,170	3,399	1,855
Commodity contracts	248	253	192
Credit derivative contracts	329	1,449	290
	3,979	9,092	3,540
Impact of master netting agreements	(1,979)	(4,168)	(1,262)
	2,000	4,924	2,278
Impact of collateral held	(421)	(381)	(119)
	1,579	4,543	2,159

Excluding, in accordance with the guidelines of the Superintendent of Financial Institutions Canada, exchange-traded instruments and forward contracts with an original maturity of 14 days. The total positive fair value of these contracts amounted to \$254 millions as at January 31, 2008.

Table 5 – Credit derivative position (notional amounts)

As at January 31, 2008
(unaudited)
(millions of dollars)

	Loan portfolio		Trading	
	Protection purchased	Protection sold	Protection purchased	Protection sold
Credit default swaps	66	–	7,164	6,028

MD&A | Additional financial information (cont.)

Table 6 – Daily trading revenues

Quarter ended January 31, 2008
(unaudited)
(millions of dollars)

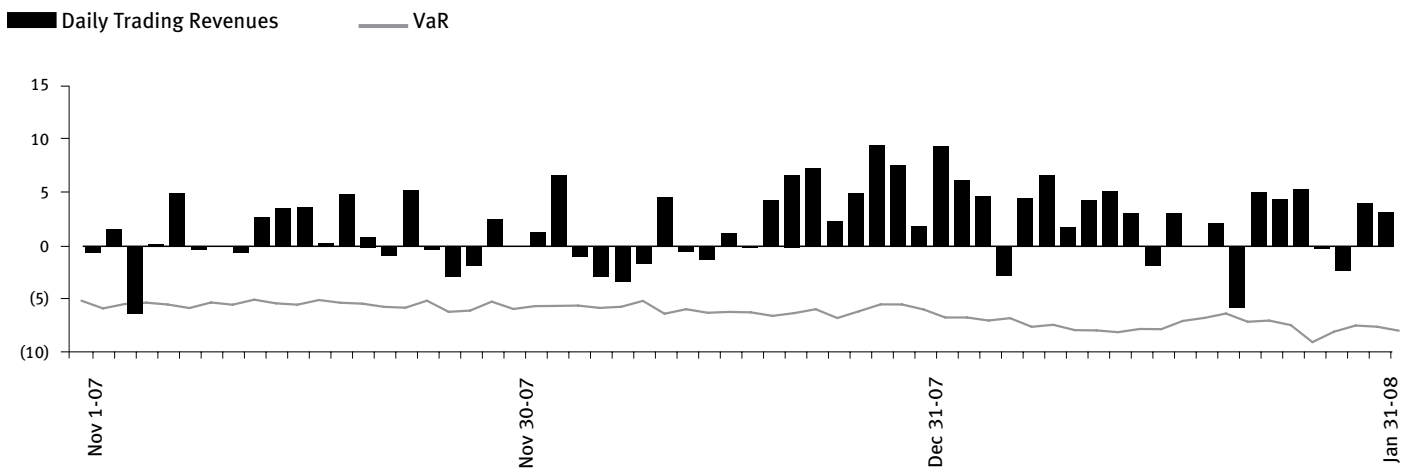


Table 7 – Capital adequacy

As at January 31, 2008
(unaudited)
(millions of dollars)

	Basel II Risk-weighted exposures	Basel I Risk-weighted exposures
Capital requirements for credit risk		
Retail residential mortgages	3,450	4,727
Other retail	6,668	8,891
Corporate	24,771	26,218
Sovereign	6	6
Bank	1,807	1,639
Trading book	1,903	1,218
Total capital requirements for credit risk	38,605	42,699
Capital requirements for securities available for sale – Equities	1,355	1,355
Capital requirements for market risk		
Standardized approach	3,351	2,845
Advanced measurement approach	876	876
Total capital requirements for market risk	4,227	3,721
Capital requirements for operational risk	5,913	–
Capital requirements for other assets	1,499	1,499
Total capital requirements	51,599	49,274
Tier 1 capital ratio	9.3%	9.8%
Total capital ratio	12.9%	13.5%

CONSOLIDATED FINANCIAL STATEMENTS | Consolidated Balance Sheet*(unaudited) (millions of dollars)*

	January 31, 2008	October 31, 2007	January 31, 2007
ASSETS			
Cash	262	283	262
Deposits with financial institutions	4,115	3,045	10,554
Securities			
Available for sale (Note 7)	6,634	8,442	9,378
Held for trading	36,396	30,828	34,186
	43,030	39,270	43,564
Securities purchased under reverse repurchase agreements	8,855	5,966	9,812
Loans (Notes 3 and 8)			
Residential mortgage	15,044	15,895	14,947
Personal and credit card	13,784	13,116	11,583
Business and government	19,151	19,377	18,406
	47,979	48,388	44,936
Allowance for credit losses	(417)	(428)	(435)
	47,562	47,960	44,501
Other			
Customers' liability under acceptances	4,533	4,085	4,162
Fair value of derivative financial instruments	4,233	4,883	2,746
Premises and equipment	433	426	383
Goodwill	702	703	684
Intangible assets	168	169	176
Other assets	6,231	6,295	4,558
	16,300	16,561	12,709
	120,124	113,085	121,402
LIABILITIES AND SHAREHOLDERS' EQUITY			
Deposits			
Personal	31,522	30,215	29,628
Business and government	35,285	33,797	30,613
Deposit-taking institutions	6,090	6,561	10,699
Deposit from NBC Capital Trust	225	225	225
	73,122	70,798	71,165
Other			
Acceptances	4,533	4,085	4,162
Obligations related to securities sold short	18,355	16,223	17,803
Securities sold under repurchase agreements	3,193	2,070	11,844
Fair value of derivative financial instruments	3,314	3,620	2,024
Other liabilities	9,438	9,087	6,775
	38,833	35,085	42,608
Subordinated debentures	1,656	1,605	1,942
Non-controlling interest (Note 11)	1,664	960	714
Shareholders' equity (Notes 12 and 14)			
Preferred shares	400	400	400
Common shares	1,590	1,575	1,583
Contributed surplus	33	32	24
Retained earnings	2,941	2,793	3,003
Accumulated other comprehensive income (loss)	(115)	(163)	(37)
	4,849	4,637	4,973
	120,124	113,085	121,402

CONSOLIDATED FINANCIAL STATEMENTS | Consolidated Statement of Income*(unaudited) (millions of dollars)*

Quarter ended	January 31, 2008	October 31, 2007	January 31, 2007
Interest income			
Loans	762	768	729
Securities available for sale	58	72	68
Securities held for trading	234	214	267
Deposits with financial institutions	93	102	130
	1,147	1,156	1,194
Interest expense			
Deposits	537	676	659
Subordinated debentures	20	25	25
Other	162	158	234
	719	859	918
Net interest income	428	297	276
Other income			
Underwriting and advisory fees	95	76	98
Securities brokerage commissions	59	60	69
Deposit and payment service charges	52	54	53
Trading revenues (losses) (Note 6)	(68)	99	131
Gains (losses) on available for sale securities, net	31	(502)	29
Card service revenues	10	3	10
Lending fees	27	33	29
Insurance revenues	34	30	30
Acceptances, letters of credit and guarantee	18	17	17
Securitization revenues	46	44	48
Foreign exchange revenues	29	28	29
Trust services and mutual funds	79	88	85
Other	89	75	85
	501	105	713
Total revenues	929	402	989
Provision for credit losses	32	29	29
	897	373	960
Operating expenses			
Salaries and staff benefits	374	336	390
Occupancy	41	42	40
Technology	98	107	98
Communications	19	19	17
Professional fees	44	57	40
Other	56	79	71
	632	640	656
Income (loss) before income taxes (recovery) and non-controlling interest			
	265	(267)	304
Income taxes (recovery)	67	(123)	56
	198	(144)	248
Non-controlling interest	(57)	31	8
Net income (loss)	255	(175)	240
Dividends on preferred shares	5	5	5
Net income (loss) available to common shareholders	250	(180)	235
Number of common shares outstanding (thousands)			
Average – basic	158,001	157,790	161,681
Average – diluted	158,731	157,790	164,398
End of period	158,141	157,806	161,367
Earnings (loss) per common share (dollars)			
Basic	1.58	(1.14)	1.45
Diluted	1.58	(1.14)	1.43
Dividends per common share (dollars)	0.62	0.60	0.54

CONSOLIDATED FINANCIAL STATEMENTS | Consolidated Statement of Comprehensive Income*(unaudited) (millions of dollars)*

Quarter ended	January 31, 2008	October 31, 2007	January 31, 2007
Net income (loss)	255	(175)	240
Other comprehensive income (loss), net of income taxes			
Net unrealized gains (losses) on translating financial statements of self-sustaining foreign operations	101	(195)	79
Impact of hedging net foreign currency translation gains or losses	(79)	159	(47)
Net change in unrealized foreign currency translation gains and losses, net of hedging activities	22	(36)	32
Net unrealized gains (losses) on available for sale financial assets	(17)	(18)	22
Reclassification to net income of (gains) losses on available for sale financial assets	(15)	10	(1)
Net change in unrealized gains and losses on available for sale financial assets	(32)	(8)	21
Net gains (losses) on derivative financial instruments designated as cash flow hedges	54	15	(21)
Reclassification to net income of (gains) losses on derivative financial instruments designated as cash flow hedges	4	5	2
Net change in gains and losses on derivative financial instruments designated as cash flow hedges	58	20	(19)
Total other comprehensive income (loss), net of income taxes	48	(24)	34
Comprehensive income (loss)	303	(199)	274

Income Taxes – Other Comprehensive Income

The income tax charge or recovery for each component of other comprehensive income is presented in the following table:

Quarter ended	January 31, 2008	October 31, 2007	January 31, 2007
Net unrealized gains (losses) on translating financial statements of self-sustaining foreign operations	3	(22)	–
Impact of hedging net foreign currency translation gains or losses	(33)	65	(22)
Net unrealized gains (losses) on available for sale financial assets	(8)	1	8
Reclassification to net income of (gains) losses on available for sale financial assets	(6)	4	(1)
Net gains (losses) on derivatives designated as cash flow hedges	25	8	(10)
Reclassification to net income of (gains) losses on derivative financial instruments designated as cash flow hedges	2	2	1
Total income taxes (recovery)	(17)	58	(24)

CONSOLIDATED FINANCIAL STATEMENTS | Consolidated Statement of Changes in Shareholders' Equity
(unaudited) (millions of dollars)

Quarter ended January 31	2008	2007
Preferred shares	400	400
Common shares at beginning	1,575	1,566
Issuance of common shares		
Dividend Reinvestment and Share Purchase plan	4	4
Stock Option Plan	11	19
Repurchase of common shares for cancellation (Note 12)	-	(7)
Impact of shares acquired or sold for trading purposes	-	1
Common shares at end	1,590	1,583
Contributed surplus at beginning	32	21
Stock option expense (Note 14)	2	5
Stock options exercised	(1)	(3)
Other	-	1
Contributed surplus at end	33	24
Retained earnings at beginning	2,793	2,893
Net income	255	240
Impact of initial adoption of financial instruments standards	-	2
Dividends		
Preferred shares	(5)	(5)
Common shares	(98)	(88)
Premium paid on common shares repurchased for cancellation (Note 12)	-	(39)
Share issuance and other expenses, net of income taxes	(4)	-
Retained earnings at end	2,941	3,003
Accumulated other comprehensive income (loss) at beginning, net of income taxes	(163)	(92)
Impact of initial adoption of financial instruments standards	-	21
Net change in unrealized foreign currency translation gains (losses), net of hedging activities	22	32
Net change in unrealized gains (losses) on available for sale financial assets	(32)	21
Net change in gains (losses) on derivative financial instruments designated as cash flow hedges	58	(19)
Accumulated other comprehensive income (loss) at end, net of income taxes	(115)	(37)
Shareholders' equity	4,849	4,973

Retained Earnings and Accumulated Other Comprehensive Income (Loss), Net of Income Taxes

As at January 31	2008	2007
Retained earnings	2,941	3,003
Accumulated other comprehensive income (loss), net of income taxes		
Unrealized foreign currency translation gains and losses, net of hedging activities	(158)	(60)
Unrealized gains and losses on available for sale financial assets	36	48
Gains and losses on derivative financial instruments designated as cash flow hedges	7	(25)
	(115)	(37)
Total	2,826	2,966

CONSOLIDATED FINANCIAL STATEMENTS | Consolidated Statement of Cash Flows*(unaudited) (millions of dollars)*

Quarter ended January 31	2008	2007
Cash flows from operating activities		
Net income	255	240
Adjustments for:		
Provision for credit losses	32	29
Amortization of premises and equipment	20	18
Future income taxes	(1)	3
Translation adjustment on foreign currency subordinated debentures	3	–
Gains on sale of available for sale securities, net	(31)	(29)
Gains on asset securitizations and other transfers of receivables, net	(31)	(31)
Stock option expense	2	5
Change in interest payable	(149)	60
Change in interest and dividends receivable	126	119
Change in income taxes payable	(3)	(22)
Change in fair value of derivative financial instruments, net	259	(99)
Change in held for trading securities	(5,568)	(2,322)
Change in other items	521	65
	(4,565)	(1,964)
Cash flows from financing activities		
Change in deposits	2,324	(752)
Issuance of NBC CapS II – Series 1	400	–
Issuance of subordinated debentures	–	500
Issuance of common shares	15	23
Repurchase of common shares for cancellation	–	(46)
Dividends paid on common shares	(95)	(165)
Dividends paid on preferred shares	(5)	(5)
Change in obligations related to securities sold short	2,132	2,182
Change in securities sold under repurchase agreements	1,123	2,327
Change in other items	385	193
	6,279	4,257
Cash flows from investing activities		
Change in deposits with financial institutions pledged as collateral	122	(22)
Change in loans (excluding securitization)	(438)	1,397
Proceeds from securitization of new assets and other transfers of receivables	1,204	1,018
Maturity of securitized assets	(400)	–
Purchases of available for sale securities	(4,369)	(6,086)
Sales of available for sale securities	6,254	3,551
Change in securities purchased under reverse repurchase agreements	(2,889)	(2,220)
Change in premises and equipment	(27)	(16)
	(543)	(2,378)
Increase (decrease) in cash and cash equivalents	1,171	(85)
Cash and cash equivalents at beginning	2,996	10,869
Cash and cash equivalents at end	4,167	10,784
Cash and cash equivalents		
Cash	262	262
Deposits with financial institutions	4,115	10,554
Less: Amount pledged as collateral	(210)	(32)
	4,167	10,784
Supplementary information		
Interest paid	868	858
Income taxes paid	54	52

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements

(unaudited) (millions of dollars)

These unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements for the year ended October 31, 2007. Certain comparative figures have been reclassified to conform with the presentation adopted in fiscal 2008.

1 – Significant Accounting Policies

These unaudited interim consolidated financial statements of the Bank have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”) and the accounting policies described in the Bank’s most recent Annual Report for the year ended October 31, 2007, except for the recent accounting standards adopted described in Note 2a). Under Canadian GAAP, additional disclosures are required in annual financial statements and these unaudited interim consolidated financial statements should therefore be read in conjunction with the audited consolidated financial statements for the fiscal year ended October 31, 2007 and the accompanying notes included on pages 84 to 137 of the 2007 Annual Report.

2 – Changes in Accounting Policies

2a) Recent Accounting Standards Adopted

CAPITAL DISCLOSURES AND FINANCIAL INSTRUMENTS – DISCLOSURES AND PRESENTATION

On November 1, 2007, the Bank adopted three new sections of the Canadian Institute of Chartered Accountants (CICA) Handbook, namely Section 1535, *Capital Disclosures*, Section 3862, *Financial Instruments – Disclosures*, and Section 3863, *Financial Instruments – Presentation*.

Sections 3862 and 3863 consist of a comprehensive series of disclosure and presentation requirements applicable to financial instruments. They revise and enhance the disclosure requirements set out in Section 3861, *Financial Instruments – Disclosure and Presentation*, and carry forward unchanged its presentation requirements.

ACCOUNTING CHANGES

On November 1, 2007, the Bank adopted the requirements of the new version of Section 1506, *Accounting Changes*.

The standard specifies that an entity must change an accounting policy only if the change is required by GAAP or in order for the financial statements to provide more relevant information. An entity must account for a change in accounting policy resulting from the application of GAAP in accordance with the specific transitional provisions of the standard, if any. If the standard does not include specific transitional provisions applicable to that change, or if the entity decides to change an accounting policy voluntarily, the change must be applied retrospectively and prior periods adjusted, unless it is impossible to determine the period-specific effects or the cumulative effect of the change.

The standard requires the disclosure of information about changes in accounting estimates during the current period and, unless it is impossible to estimate, for future periods. According to this standard, the entity must disclose that an error has occurred and the period in which it occurred. In this case, the financial statements are restated.

Furthermore, the standard requires that, when a new standard has been issued but is not yet effective, this fact be disclosed along with the expected impact of initial application on the financial statements.

The application of this standard did not have an impact on the Bank’s consolidated financial statements.

2b) Recent Accounting Standard Pending Adoption

GOODWILL AND INTANGIBLE ASSETS

In January 2008, CICA Handbook Section 3064, *Goodwill and Intangible Assets*, was published. This new accounting standard reinforces the approach under which assets are recorded only if they meet the definition of an asset and the recognition criteria for an asset. It also clarifies the application of the concept of matching costs with revenues, so as to eliminate the current practice of recognizing as assets items that do not meet the definition of an asset and the recognition criteria for an asset. On November 1, 2008, the Bank will apply this standard retrospectively with restatement of prior periods. The Bank is currently assessing the impact of the initial application of this standard on its consolidated financial statements.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***3 – Management of the Risks Associated with Financial Instruments**

The Bank views risk as an integral part of its development and the diversification of its activities. The purpose of sound risk management is to provide reasonable assurance that incurred risks do not exceed acceptable thresholds and that risk-taking contributes to the creation of shareholder value. For the Bank, it means striking a balance between the results obtained and the risks assumed.

The Bank is primarily exposed to the following risks:

Credit risk	Risk of a financial loss if a counterparty to a transaction does not fully honour its contractual commitments to the Bank. Counterparties to transactions may be borrowers, issuers, obligors or guarantors.
Market risk	Risk of a financial loss resulting from unfavourable changes in underlying market factors, namely, interest rates, foreign exchange rates, equity prices, commodity prices, credit risk and market volatility.
Liquidity risk	Risk that the Bank will be unable to honour daily cash commitments without resorting to costly and untimely measures.
Operational risk	Risk of loss resulting from an inadequacy or a failure ascribable to people, processes, technology or external events.
Reputational risk	Risk that the Bank's operations or practices will be judged by the public to be negative, whether that judgment is with or without basis, and will adversely affect the perception, image or trademarks of the Bank, potentially resulting in costly litigation or loss of income.

RISK MANAGEMENT FRAMEWORK

To achieve its risk management objectives, the Bank has created a risk management framework that comprises the following elements.

Risk management culture

The Bank and its management routinely promote a risk management culture through internal communications that advance a balanced model where business development initiatives are accompanied by a constant concern for sound risk management.

Governance structure

The governance structure at National Bank sets out the roles and responsibilities of all levels of the organization.

The Audit and Risk Management Committee (ARMC) of the Board of Directors

The ARMC approves risk management policies and sets risk tolerance limits. In addition to ensuring that the appropriate resources, policies and procedures are in place, it examines and approves all significant aspects of risk assessment systems.

The Bank's Management

The Bank's Management promotes the risk management culture Bank-wide and manages the primary risks to which the Bank is exposed.

The Risk Management Group

This group proposes risk management policies and implements tools and models for identifying, measuring and monitoring risks. In addition to instituting and applying various independent risk review and approval procedures, this group is responsible for setting risk limits that reflect the risk tolerance thresholds established by the Board of Directors and informs Management and the Board of Directors of significant risks.

The Business Units

The business units manage risks related to their operations within established limits and in accordance with risk management policies by identifying, analyzing and understanding the risks to which they are exposed and implement risk mitigation mechanisms.

Risk Management Policies

The risk management policies and related guidelines and procedures describe how business units must manage risk and the approval process for decisions and set the risk limits to be adhered to. These policies are reviewed on a regular basis to ensure that they are still relevant given changes in the markets and the business plans of the Bank's units.

The risk management policies are complemented by additional policies, standards and procedures that cover more specific aspects of management, such as the continuity of certain Bank activities.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***3 – Management of the Risks Associated with Financial Instruments (cont.)****Independent oversight by the Corporate Compliance Department**

The Bank's Corporate Compliance Department reports directly to the ARMC and helps provide assurance that the Bank's structures, management systems, programs, policies and procedures necessary to ensure compliance with legislation, regulations, guidelines and codes of professional conduct applicable to the Bank are in place and operational.

Independent assessment by the Internal Audit Department

The Internal Audit Department also reports directly to the ARMC and provides an independent, objective assessment of the effectiveness of the processes, policies, procedures and control measures implemented by managers. It also recommends solutions to improve the effectiveness of risk management, internal controls and operations at the Bank and its subsidiaries.

CREDIT RISK MANAGEMENT

Credit risk is the most significant risk facing the Bank. The Bank is exposed to credit risk not only through its direct lending activities and transactions but also through credit commitments such as letters of guarantee or credit, over-the-counter derivatives trading, available for sale debt securities, securities acquired under reverse repurchase agreements, deposits with financial institutions, and transactions carrying a settlement risk for the Bank.

Policy

A policy framework centralizes the governance of activities that generate credit risk for the Bank as a whole. It is supplemented by a series of subordinate internal or sector policies and guidelines used to provide more thorough coverage of the given business lines or deal with specific management issues, such as credit limits or collateral requirements.

Measuring credit risk – loans

The Bank uses a bi-dimensional risk rating system to establish a default risk rating for each counterparty and another risk rating for the credit facility on the basis of the collateral and guarantees that may be provided by the borrower or counterparty. The default risk rating for the counterparty is determined using an internal system by the Bank and is based on a graduated scale from 1 to 10 comprising 19 grades. As each grade corresponds to a borrower's or counterparty's probability of default, the credit risk for the Bank can be determined. The credit risk assessment method varies according to portfolio type.

Consumer and SME credit portfolios

The default risk rating is determined with models that use proven statistical methods that measure an applicant's characteristics and history based on internal and external information to estimate future credit behaviour and assign a risk rating. Consumer credit risk assessments are based on a group of borrowers with similar credit histories and behaviour profiles.

Commercial and government credit portfolios

This category comprises the portfolios of commercial businesses other than SMEs, large corporations, governments, real estate, the energy group, financial institutions, the agricultural group and the cinema and television group.

The default risk rating is assessed individually for each borrower and specifically in relation to the borrower's sector and in relation to its peers. To arrive at an appropriate rating, a detailed individual analysis of the financial and qualitative aspects of the borrower is performed that covers its financial health, sector of economic activity, competitive ability, access to capital and management quality. Moreover, the assessment models developed for each of the above portfolio categories are based on an internal bank of historical data or information from external sources. Loan portfolio managers then complete the information with a subjective evaluation of the qualitative elements.

Credit granting process

Each credit granting decision is made by authorities within the risk management teams and management who are independent of the business units and are at a reporting level commensurate with the size of the proposed credit transaction and the associated risk. Accordingly, a person in a senior position in the organization must approve credit facilities that are substantial or carry a higher risk for the Bank. The Credit Committee, chaired by the Senior Vice-President – Risk Management, manages risks, and approves and monitors all large risks. In exceptional cases, the decision may be submitted to the Board of Directors for approval.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***3 – Management of the Risks Associated with Financial Instruments (cont.)****Risk mitigation**

The Bank also controls credit risk using risk mitigation techniques. The most common way to mitigate credit risk is to obtain quality collateral. The need to take collateral depends on the level of risk the borrower represents to the Bank and on the type of credit granted. The Bank considers collateral to be of good quality if it can determine its legal validity and correctly measure its value on a regular basis. The Bank has established specific requirements in its internal policies with respect to the appropriate legal documentation and assessment for the kinds of collateral that business units may require in guarantee of the credit they grant. The categories of eligible collateral and the lending value of these assets have also been defined by the Bank. For the most part, they include the following asset categories: accounts receivable; inventory; machinery and equipment; rolling stock; real estate mortgages on residential, commercial and office buildings and industrial facilities; and cash and marketable securities.

Commitments related to the trading of contracts on derivative financial instruments are subject to credit risk mitigation measures. The first, and most widely used, of these measures is the signing of International Swaps and Derivatives Association, Inc. (ISDA) Master Agreements with the appropriate counterparties. These agreements make it possible to apply full netting of the gross amounts of the market price assessments when one of the contracting parties defaults on the agreement, for each of the transactions covered by the agreement and in force at the time of default. The Bank's policies require signing an ISDA agreement with each counterparty trading derivative financial instruments with its traders. Another mechanism for reducing credit risk completes the ISDA Master Agreement in many cases and provides the Bank or its counterparty (or both parties, if need be) with the right to request collateral from the counterparty when the net balance of gains and losses on each transaction exceeds a threshold defined in the agreement. These agreements are known as Credit Support Annexes (CSAs).

Portfolio diversification and management

The Bank is exposed to credit risk not only under its commitments to a particular borrower but also through the sector distribution (activity sector) of its commitments and the exposure of its various credit portfolios to geographical, concentration and settlement risks.

The Bank's approach to controlling these diverse risks begins with optimizing the diversification of its commitments. The management criteria set out in its internal policies and procedures include measures to maintain a healthy degree of diversification of credit risk in its portfolios. These policies define the following limits on the scope of its commitments: credit approval limits by level and credit concentration limits by counterparty, industry, country, region and type of financial instrument. Compliance with these limits is monitored through periodic reports submitted by Risk Management officers to the Board of Directors. The criteria established for portfolio diversification and the specific limits set for economic, industrial or geographical sectors are based on the findings of sector-based studies and analyses conducted by economists and the Bank's Risk Management Group, and are approved by the Credit Committee. Continuous analyses are performed in order to anticipate problems with a sector or borrower before they materialize as defaulted payments.

Other risk mitigation methods

To control credit risk, the Bank also uses synthetic protection mechanisms such as credit derivative financial instruments and securitization, loan syndication and loan assignments and, if required, an orderly reduction in the amount of credit granted.

- *Credit derivative financial instruments*

Credit default swaps are transactions in which one of the counterparties agrees to pay interest expenses to the other counterparty so that the latter counterparty can make a payment if a credit event occurs. Since, like borrowers, credit protection providers must be assigned a default risk rating, the Bank's internal policies set out the criteria for deeming a counterparty eligible to provide the Bank with credit protection.

- *Loan syndication*

The Bank states clearly guidelines regarding objectives, responsibilities and documentation requirements.

- *Securitization*

Securitization is a means for transferring to a third party a portion of the credit risk incurred on loans originally granted by the Bank. A more detailed analysis of this activity is provided in Note 8 to the consolidated financial statements.

Account follow-up and recovery

Credit granted and borrowers are monitored on an ongoing basis and in a manner commensurate with the related risk. Special care is taken by loan portfolio managers with problem loans, which are managed using an array of methods, including a monthly watchlist of problem commitments produced for the loan portfolio managers concerned, who must then submit a report to Credit Risk Management.

When, despite close monitoring, credit commitments continue to deteriorate and risk increases to the point where monitoring has to be increased, a group specialized in managing problem accounts steps in to maximize collection of the committed amounts and tailor strategies to these accounts. This unit's role is critical because, when a borrower defaults, the Bank's primary goal is to recover the maximum amount owing to it.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***3 – Management of the Risks Associated with Financial Instruments (cont.)****Identification of impaired loans and provisioning for credit losses**

A loan, other than a credit card receivable, is considered impaired when, in the opinion of Management, there is reasonable doubt as to the ultimate collectibility of a portion of principal or interest or where payment of interest is contractually 90 days past due, unless there is no doubt as to the collectibility of the principal or interest. The loan may revert to performing status only when principal and interest payments have become fully current. Credit card receivables are written off when payments are more than 180 days in arrears.

The allowance for credit losses reflects Management's best estimate as at the balance sheet date and relates primarily to loans, but may also cover the credit risk associated with deposits with financial institutions, derivative financial instruments, loan substitute securities and other credit instruments such as acceptances, letters of guarantee and letters of credit. The allowance for credit losses consists of specific allowances for impaired loans and the general allowance for credit risk.

The specific allowances for impaired loans are established for all such loans that can be identified and for which impairment can be estimated individually, reducing them to their estimated realizable amounts.

The general allowance allocated for credit risk represents Management's best estimate of probable losses within the portion of the portfolio that has not yet been specifically identified as impaired. This amount is determined by applying expected loss factors to outstanding and undrawn facilities. The allocated general allowance for corporate and government loans is based on the application of expected default and loss factors, determined by statistical loss migration analysis, delineated by loan type. For more homogeneous portfolios, such as residential mortgage loans, small and medium-sized enterprise loans, personal loans and credit card receivables, the allocated general allowance is determined on a product portfolio basis. Losses are determined by the application of loss ratios established through statistical analysis of loss migration over an economic cycle. The general allowance not allocated for credit risk is based on Management's assessment of probable losses in the portfolio that have not been captured in the determination of the specific allowances for impaired loans and the allocated general allowance. This assessment takes into account general economic and business conditions, recent loan loss experience, and trends in credit quality and concentrations. This allowance also reflects model and estimation risks. The unallocated general allowance does not represent future losses or serve as a substitute for the allocated general allowance.

Maximum credit risk exposure

The amounts shown in the table below represent the Bank's maximum exposure to credit risk as at the balance sheet date without taking into account any collateral held or any other credit enhancements. For financial assets recorded in the balance sheet, the maximum credit risk exposure represents the carrying amount. Letters of guarantee are the Bank's commitment to make payments for a client that does not meet its financial obligations to third parties. Loan commitments are the undrawn portions of credit authorizations provided in the form of loans, acceptances, letters of guarantee and documentary credit.

As at January 31, 2008

	Maximum exposure
Recorded on the Consolidated Balance Sheet	
Deposits with financial institutions	4,115
Securities – Available for sale	
Debt securities	5,363
Securities purchased under reverse repurchase agreements	8,855
Loans	
Residential mortgage	15,042
Personal and credit card	13,772
Business and government	18,748
Customers' liability under acceptances	4,533
Derivative financial instruments	4,233
Other assets	4,943
Total recorded on the Consolidated Balance Sheet	79,604
Off-balance sheet	
Letters of guarantee	1,692
Loan commitments	24,562
Total off-balance sheet	26,254

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)

(unaudited) (millions of dollars)

3 – Management of the Risks Associated with Financial Instruments (cont.)**GROSS LOANS BY TYPE OF BORROWER**

As at January 31, 2008

	Gross loans
Personal ⁽¹⁾	13,784
Residential mortgage	15,044
Non-residential mortgage	1,379
Agricultural	1,980
Financial institutions	3,844
Manufacturing	2,064
Construction and real estate	1,161
Transportation and communications	494
Mines, quarries and energy	1,233
Forestry	151
Government	1,278
Wholesale	546
Retail	1,209
Services	951
Other	2,861
	47,979
Securities purchased under reverse repurchase agreements (financial institutions)	8,855

*(1) Including consumer loans, credit cards and other personal loans***CREDIT QUALITY OF LOANS**

As at January 31, 2008

	Residential mortgages	Personal and credit card	Business and government ⁽²⁾	Total
Neither past due ⁽¹⁾ nor impaired	14,921	13,712	18,963	47,596
Past due but not impaired	97	37	–	134
Impaired	26	35	188	249
	15,044	13,784	19,151	47,979
Less: Specific allowances	2	12	95	109
Sub-total	15,042	13,772	19,056	47,870
Less: General allowance ⁽³⁾				308
Total				47,562

*(1) A loan is considered to be past due when the counterparty has not made a payment the day of the contractual expiry date.**(2) Business credit portfolios are closely monitored and a monthly watchlist of problem commitments is produced. The watchlist is analyzed by the loan portfolio managers involved, who must then submit a report to the management of Credit Risk Management.**(3) The general allowance for credit risk was created taking into account the Bank's credit in its entirety.***LOANS PAST DUE BUT NOT IMPAIRED**

As at January 31, 2008

	Residential mortgages	Personal and credit card
Past due but not impaired		
1 month late	24	14
2 months late	27	10
3 months late and more	46	13
Total	97	37

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)

(unaudited) (millions of dollars)

3 – Management of the Risks Associated with Financial Instruments (cont.)**IMPAIRED LOANS**

As at January 31, 2008

	Gross	Specific allowances	Net
Loans			
Residential mortgages	26	2	24
Personal and credit card	35	12	23
Business and government loans	188	95	93
Total	249	109	140

As at October 31, 2007

	Gross	Specific allowances	Net
Loans			
Residential mortgages	20	1	19
Personal and credit card	36	12	24
Business and government loans	193	107	86
Total	249	120	129

ALLOWANCE FOR CREDIT LOSSES

Quarter ended January 31, 2008

	Residential mortgages	Personal and credit card	Business and government	Total
Specific allowances at beginning	1	12	107	120
Provision for credit losses	–	16	16	32
Write-offs	–	(13)	(29)	(42)
Write-offs on credit cards	–	(17)	–	(17)
Recoveries	1	14	1	16
Specific allowances at end	2	12	95	109
General allowance ⁽¹⁾				308
Allowances at end	2	12	95	417

Quarter ended January 31, 2007

	Residential mortgages	Personal and credit card	Business and government	Total
Specific allowances at beginning	2	16	100	118
Provision for credit losses	–	17	12	29
Write-offs	(1)	(11)	(5)	(17)
Write-offs on credit cards	–	(17)	–	(17)
Recoveries	1	13	–	14
Specific allowances at end	2	18	107	127
General allowance ⁽¹⁾				308
Allowances at end	2	18	107	435

⁽¹⁾ The general allowance for credit risk was created taking into account the Bank's credit in its entirety.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***3 – Management of the Risks Associated with Financial Instruments (cont.)****MARKET RISK MANAGEMENT**

Market risk is intrinsically interlinked with participation in financial markets. Managing this risk is a core competency for the Bank in its trading, investing and asset/liability management activities.

Assessing market risk

One of the main tools used to manage market risk is the Value-at-Risk (VaR) simulation model. VaR is the maximum value of potential daily losses, in the portfolios held, measured at a 99% confidence level, which means that actual losses are likely to exceed the value only one day out of 100. VaR is calculated on an ongoing basis for both major classes of financial instruments, including derivative financial instruments, and all portfolios of the Financial Markets segment of the Bank. The VaR calculation model is based on two years of historical data.

The Bank monitors VaR daily in relation to established limits for each portfolio and business unit, as well as by type of activity: trading, investing and asset/liability management. Moreover, investment portfolio activities are governed by a special guideline. In this way, the Bank seeks to ensure that trading and investment decisions do not entail risks in excess of preset limits.

In addition, the Bank carries out backtesting in order to verify the capacity of the Bank's VaR model to estimate the maximum risk of market losses and thus validate, retroactively, the quality of the results obtained using the model.

The VaR model simulates losses in market situations similar to those revealed by historical data, namely, normal market conditions. The Bank also seeks to simulate the impact of abnormal situations, i.e., rare events, on the various portfolios of the Financial Markets segment. The Bank accordingly conducts daily stress tests and sensitivity analyses for all risk categories: interest rate risk, equity and commodity price risk, foreign exchange risk and market volatility risk. These many tests simulate the results that the portfolios of the Financial Markets segment would generate if the extreme scenarios in question were to occur. The Bank sets maximum potential loss limits for stress tests and sensitivity analyses. These limits are approved by the Board of Directors. The stress tests and sensitivity analyses are developed jointly by the Market Risk Management Group and the management of the business units, and are regularly reviewed to take into account changes in market conditions, new products and trading strategies.

Trading activities

VaR is a key market risk management tool for trading activities. The following table illustrates the VaR distribution of trading portfolios by risk category, as well as the risk diversification effect.

GLOBAL VaR BY RISK CATEGORY⁽¹⁾

Quarter ended	January 31, 2008			October 31, 2007	
	Low	High	Average	Period end	Period end
Interest rate	(3.3)	(5.7)	(4.5)	(4.9)	(3.4)
Foreign exchange	(1.4)	(3.4)	(2.4)	(2.3)	(1.7)
Equity	(3.7)	(7.7)	(5.1)	(5.0)	(7.0)
Commodity	(0.9)	(3.1)	(1.6)	(1.7)	(1.8)
Correlation effect ⁽²⁾	n.a.	n.a.	7.0	5.6	8.5
Global VaR	(5.3)	(9.4)	(6.6)	(8.3)	(5.4)

(1) Amounts are presented on a pre-tax basis and represent one-day VaR.

(2) The correlation effect is the result of the diversification of types of risks.

Structural interest rate risk

As part of its non-trading activities, such as granting mortgage loans and accepting term deposits, the Bank is exposed to structural interest rate risk. Interest rate movements cause changes in interest income and interest expense and, although these fluctuations do not move in the same direction, their relative magnitude will favourably or unfavourably impact annual net interest income and the economic value (present value of estimated cash flows) of shareholders' equity. The extent of that impact depends on several factors, including asset and liability matching and the interest rate curve. Assets and liabilities are managed to optimize the impact of interest rate movements in view of anticipated rate changes.

Regular simulations are performed to assess the impact of various scenarios on annual net interest income and the economic value of shareholders' equity and to guide the management of structural interest rate risk.

Interest rate risk is managed under a specific policy, the revision and application of which are overseen by various management committees, among others. The policy sets risk limits based on the impact of a 100-basis-point change in interest rates on the following parameters: annual net interest income, economic value and duration of shareholders' equity.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)

(unaudited) (millions of dollars)

3 – Management of the Risks Associated with Financial Instruments (cont.)

The following table provides the potential before tax impact of an immediate and sustained 100-basis-point and 200-basis-point increase in interest rates on net interest income and on the economic value of shareholders' equity of the Bank's non-trading portfolio, assuming that no further hedging is undertaken.

INTEREST RATE SENSITIVITY – NON-TRADING (BEFORE TAX)

As at January 31	2008	2007
100-basis-point increase in the interest rate		
Impact on net interest income (for the next 12 months)	(5)	(27)
Impact on shareholders' equity	(76)	(85)
200-basis-point increase in the interest rate		
Impact on net interest income (for the next 12 months)	(14)	(58)
Impact on shareholders' equity	(153)	(173)

Hedge of structural interest rate and foreign exchange riskHedge of a net investment in a self-sustaining foreign operation

The Bank's structural foreign exchange risk arises primarily from investments in self-sustaining foreign operations denominated in currencies other than the Canadian dollar. This risk is measured by assessing the impact of currency fluctuations. The Bank uses financial instruments denominated in foreign currencies to hedge structural foreign exchange risk. In a hedge of a net investment in a self-sustaining foreign operation, the financial instruments used will offset foreign exchange gains and losses on the investments.

For the quarter ended January 31, 2008, unrealized foreign exchange gains of \$104 million were recorded in *Other comprehensive income* related to the Bank's net investment in self-sustaining foreign operations and were offset by losses of \$112 million related to financial instruments designated as foreign exchange risk hedges. These financial instruments represent foreign currency denominated liabilities and totalled \$2.1 billion as at January 31, 2008.

Fair value hedge

Fair value hedge transactions mainly use interest rate swaps to hedge changes in the fair value of a financial asset or liability arising from changes in market interest rates. In a fair value hedge, the change in fair market value of the derivative financial instruments used as hedging items will offset the change in fair value of the hedged item. The Bank uses this strategy primarily for its securities, deposit and subordinated debenture portfolios.

For the quarter ended January 31, 2008, the amount representing the ineffective portion recognized as *Other income* in the Consolidated Statement of Income was negligible. All the components of the change in fair market value of the derivative financial instruments used were taken into account in assessing the effectiveness of the fair value hedge.

Cash flow hedge

Cash flow hedge transactions mainly use interest rate swaps to hedge exposure of the future cash flows related to a floating rate financial asset or liability. In a cash flow hedge, the derivative financial instruments used as hedging items will mitigate the variability in future cash flows related to the hedged item. The Bank uses this strategy primarily for its loan portfolio.

For the quarter ended January 31, 2008, an unrealized gain of \$79 million was recorded in *Other comprehensive income* for the effective portion of changes in fair value of derivative financial instruments designated as cash flow hedges. The amounts recognized are reclassified to *Net interest income* in the periods during which the variability in cash flows of the hedged items affects net interest income. Consequently, a net loss of \$6 million was reclassified to *Net income* in the quarter ended January 31, 2008. An estimated net gain of \$14 million deferred in *Accumulated other comprehensive income* as at January 31, 2008 is expected to be reclassified to *Net income* during the next 12 months. The maximum period over which the Bank hedges its exposure to the variability in future cash flows is five years.

For the quarter ended January 31, 2008, the amount representing the ineffective portion recognized as *Other income* in the Consolidated Statement of Income was negligible. All the components of the change in fair value of the derivative financial instruments used were taken into account in assessing the effectiveness of the cash flow hedge.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***3 – Management of the Risks Associated with Financial Instruments (cont.)****LIQUIDITY RISK MANAGEMENT**

Liquidity risk arises when sources of funds become insufficient to meet scheduled payments under the Bank's commitments. Liquidity risk stems from two sources: mismatched cash flows related to assets and liabilities and the characteristics of certain products, such as credit commitments and demand deposits.

The Bank strives to meet the following objectives at all times:

- honour all cash outflow commitments (both on- and off-balance sheet) on a continuous basis;
- avoid situations where funds have to be raised quickly, resulting in the Bank having to pay excessive funding costs or sell readily marketable assets under unfavourable conditions;
- adhere to risk limits; and
- closely follow the best practices used in the market and changes in liquidity regulations.

The Board is ultimately responsible for the liquidity management and funding policy. The Bank's liquidity management is governed by establishing a prudent policy that identifies oversight responsibilities, as well as setting limits and implementing effective techniques to monitor, measure and control exposure to liquidity risk.

Funding management and diversification

Core deposit liabilities are the Bank's primary funding source. In this context, diversification of funding by origination and term structure is an important element of a liquidity management strategy.

The Bank aims to achieve a diversified source of funding by geographical location, currency, instrument and depositor or counterparty in both the secured and unsecured borrowing markets. Furthermore, the Bank has been actively engaged in securitization programs that give it access to long-term funding and act as a capital management tool.

To ensure stability of market access, the Bank maintains and develops direct relationships with the major money lenders active on the Canadian money market, pursues and develops activities on inter-bank and corporate markets in the United States, Europe and Asia, and favours extending the terms of term deposits whenever this proves economically advantageous and strategically desirable.

Liquidity risk measurement

Liquidity risk is managed on a consolidated basis by assigning limits to a set of risk measures. Short-term day-to-day funding decisions are based on a daily cumulative net cash profile. Long-term funding and liquidity decisions are based on net cash capital, survival period and liquidity ratios, enabling the Bank to strike an optimal balance between long-term funding and purchased funds.

Furthermore, the Bank restricts its reliance on any one depositor and thereby avoids an unnecessary concentration of deposits from a single source. For this reason, purchased funds are limited to a percentage of total deposits and a maximum amount per depositor has been established.

Finally, a detailed liquidity contingency plan is outlined in the Policy.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***3 – Management of the Risks Associated with Financial Instruments (cont.)**

The following table shows financial liabilities and loan commitments by contractual maturity, except for the fair value of derivative financial instruments held for trading and commitments related to securities sold short.

As at January 31, 2008

	Payable on demand	Payable after notice	Payable on a fixed date				Total
			Less than 1 year	1 to 2 years	2 to 5 years	More than 5 years	
Personal	3,134	13,272	7,806	3,366	3,911	33	31,522
Other	7,083	6,347	22,783	1,442	2,392	1,553	41,600
Total deposits	10,217	19,619	30,589	4,808	6,303	1,586	73,122
			Less than 1 year	1 to 2 years	2 to 5 years	More than 5 years	Total
Designated derivative financial instruments							
Fair value hedges			5	6	7	10	28
Cash flow hedges			–	–	40	4	44
Total designated derivative financial instruments			5	6	47	14	72
Subordinated debentures			12	250	500	894	1,656
Loan commitments			24,562	–	–	–	24,562

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***4 – Capital Disclosure****CAPITAL MANAGEMENT OBJECTIVES, POLICIES AND PROCEDURES**

Capital management consists in maintaining the balance between risk-adjusted capital, regulatory capital ratios that satisfy the minimum requirements for a well-capitalized financial institution, as defined by the Office of the Superintendent of Financial Institutions (the “Superintendent”), and production of a competitive return on shareholders’ equity.

Each year, the Board of Directors, on the recommendation of the ARMC, approves a detailed capital management policy and the Bank’s capital plan. This policy sets out the principles and practices the Bank incorporates into its capital management strategy and the basic criteria it adopts to ensure that it has sufficient capital at all times and prudently manages such capital in view of its future capital requirements. The capital plan sets operational targets and takes into account expected levels for risk-weighted assets, determined under the regulatory approach. Moreover, the capital plan presents an analysis of the different strategies that are available to the Bank to optimize capital management, including the issuance and repurchase of equity securities and subordinated indebtedness and the dividend policy.

CAPITAL MANAGEMENT

The capital ratio is the ratio, expressed as a percentage, of regulatory capital to risk-weighted assets. The definition adopted by BIS distinguishes between three types of capital: Tier 1 capital, or base capital, which consists of common shareholders’ equity, non-cumulative preferred shareholders’ equity and non-controlling interests in subsidiaries, less goodwill; and Tier 2 capital, or supplementary capital, which consists of the book value of other preferred shares, the eligible portion of subordinated debentures and the general allowance for credit risk. In accordance with BIS rules, the Superintendent defines a third tier of capital intended specifically to cover market risk, which must also be covered by Tier 1 capital. Total regulatory capital, or total capital, is the sum of the various types of capital less investments in companies subject to significant influence and first-loss protection with respect to asset securitization.

On November 1, 2007, the Bank adopted the requirements of the new Basel II capital standards framework. These new rules, established in 2004 by the BIS in Basel, Switzerland, and adopted by many countries around the world, including Canada, amend the capital adequacy rules introduced in 1988.

Since November 1, 2007, the Bank has been using the standardized approach for credit risk. This approach is almost identical to the one used as at October 31, 2007. Beginning in fiscal 2010, the Bank will adopt the Advanced Internal Ratings-Based Approach, which provides for enhanced sensitivity of capital to the credit risk of borrowers and counterparties with which the Bank does business. The Bank has been using the standardized approach for operational risk since November 1, 2007. This approach imposes a capital charge to cover operational risk.

The Superintendent considers financial institutions to be well-capitalized if they maintain a Tier 1 capital ratio of 7% and a total capital ratio of 10%. The Bank maintained ratios that satisfied these requirements both in the fourth quarter of 2007 and in the first quarter of 2008.

In addition to regulatory capital ratios, banks are expected to meet an assets-to-capital multiple test. The assets-to-capital multiple is calculated by dividing a bank’s total assets, including specified off-balance sheet items, by its total capital. Under this test, total assets should not be greater than 23 times total capital. The Bank met the assets-to-capital multiple test both in the fourth quarter of 2007 and in the first quarter of 2008.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)

(unaudited) (millions of dollars)

4 – Capital Disclosure (cont.)

REGULATORY CAPITAL	Basel II	Basel I
	January 31, 2008	October 31, 2007
Tier 1 capital		
Common shares	1,590	1,575
Contributed surplus	33	32
Retained earnings	2,941	2,793
Unrealized foreign exchange gains and losses, net of hedging activities included in <i>Accumulated other comprehensive income</i>	(158)	(181)
Non-cumulative permanent preferred shares	400	400
Innovative instruments ⁽¹⁾	721	509
Non-controlling interest ⁽²⁾	18	18
Trading in short positions of own shares	(1)	(1)
Gross Tier 1 Capital	5,544	5,145
Goodwill	(702)	(703)
Net Tier 1 Capital	4,842	4,442
Gains on sales recorded upon securitization	(27)	–
Adjusted Net Tier 1 Capital	4,815	4,442
Tier 2 capital		
Subordinated debentures	1,644	1,641
Eligible general allowance for credit risk	308	308
Accumulated net after tax unrealized gains on available for sale equity securities included in <i>Accumulated other comprehensive income</i>	48	80
Excess Tier 1 qualifying innovative instruments ⁽¹⁾	205	–
Other deductions	(377)	(355)
Adjusted Tier 2 capital	1,828	1,674
Total capital	6,643	6,116

(1) 300,000 preferred shares, Series A, exchangeable, non-cumulative dividends issued by NB Capital Corporation and 400,000 NBC CapS II – Series 1 issued by NBC Asset Trust presented in non-controlling interest and the \$225 million deposit from NBC Capital Trust

(2) Excluding 300,000 preferred shares, Series A, exchangeable, non-cumulative dividends, issued by NB Capital Corporation, 400,000 NBC CapS II – Series 1 issued by NBC Asset Trust, mutual funds and other entities consolidated pursuant to the application of AcG-15

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***5 – Carrying Values of Financial Assets and Financial Liabilities by Category**

Financial assets and liabilities are recognized in the Consolidated Balance Sheet at fair value, cost or amortized cost according to the categories determined by the accounting framework for financial instruments. The carrying values for each category of financial asset and liability are presented in the table below.

As at January 31, 2008

	Held for trading	Designated as held for trading	Available for sale	Loans and receivables	Financial liabilities at cost or amortized cost	Derivative financial instruments designated as cash flow hedges	Derivative financial instruments designated as fair value hedges
FINANCIAL ASSETS							
Cash	262	–	–	–	–	–	–
Deposits with financial institutions	–	–	493	3,622	–	–	–
Securities							
Available for sale	–	–	6,634	–	–	–	–
Held for trading	36,396	–	–	–	–	–	–
Securities purchased under reverse repurchase agreements	–	–	–	8,855	–	–	–
Loans	–	–	–	47,562	–	–	–
Other							
Customers' liability under acceptances	–	–	–	4,533	–	–	–
Fair value of derivative financial instruments	4,031	–	–	–	–	37	165
Other assets	–	–	–	4,943	–	–	–
Total financial assets	40,689	–	7,127	69,515	–	37	165
FINANCIAL LIABILITIES							
Deposits							
Personal	–	–	–	–	31,522	–	–
Business and government	–	333	–	–	34,952	–	–
Deposit-taking institutions	–	–	–	–	6,090	–	–
Deposit from NBC Capital Trust	–	–	–	–	225	–	–
Other							
Acceptances	–	–	–	–	4,533	–	–
Obligations related to securities sold short	18,355	–	–	–	–	–	–
Securities sold under repurchase agreements	–	–	–	–	3,193	–	–
Fair value of derivative financial instruments	3,242	–	–	–	–	44	28
Other liabilities	–	–	–	–	8,470	–	–
Subordinated debentures	–	–	–	–	1,656	–	–
Total financial liabilities	21,597	333	–	–	90,641	44	28

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***5 – Carrying Values of Financial Assets and Financial Liabilities by Category (cont.)**

As at October 31, 2007

	Held for trading	Designated as held for trading	Available for sale	Loans and receivables	Financial liabilities at cost or amortized cost	Derivative financial instruments designated as cash flow hedges	Derivative financial instruments designated as fair value hedges
FINANCIAL ASSETS							
Cash	283	–	–	–	–	–	–
Deposits with financial institutions	–	–	836	2,209	–	–	–
Securities							
Available for sale	–	–	8,442	–	–	–	–
Held for trading	30,828	–	–	–	–	–	–
Securities purchased under reverse repurchase agreements	–	–	–	5,966	–	–	–
Loans	–	–	–	47,960	–	–	–
Other							
Customers' liability under acceptances	–	–	–	4,085	–	–	–
Fair value of derivative financial instruments	4,702	–	–	–	–	2	179
Other assets	–	–	–	5,194	–	–	–
Total financial assets	35,813	–	9,278	65,414	–	2	179
FINANCIAL LIABILITIES							
Deposits							
Personal	–	–	–	–	30,215	–	–
Business and government	–	297	–	–	33,500	–	–
Deposit-taking institutions	–	–	–	–	6,561	–	–
Deposit from NBC Capital Trust	–	–	–	–	225	–	–
Other							
Acceptances	–	–	–	–	4,085	–	–
Obligations related to securities sold short	16,223	–	–	–	–	–	–
Securities sold under repurchase agreements	–	–	–	–	2,070	–	–
Fair value of derivative financial instruments	3,319	–	–	–	–	85	216
Other liabilities	–	–	–	–	7,541	–	–
Subordinated debentures	–	–	–	–	1,605	–	–
Total financial liabilities	19,542	297	–	–	85,802	85	216

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***6 – Total Income from Trading Activities**

Total income from trading activities comprises net interest income from trading activities, trading revenues recognized as *Other income* and the impact of non-controlling interest.

Net interest income comprises interest and dividends relating to financial assets and liabilities associated with trading activities, net of interest expenses and interest income related to the financing of these financial assets and liabilities.

Other income comprises the realized and unrealized gains and losses on securities held for trading, income from derivative financial instruments held for trading purposes and the change in fair value of financial liabilities designated as held for trading.

The impact of non-controlling interest takes into account trading revenues and losses attributable to third parties.

TOTAL INCOME FROM TRADING ACTIVITIES

Quarter ended January 31	2008	2007
Net interest income	116	(39)
Other income	(68)	131
Non-controlling interest	62	(1)
Total	110	91

7 – Available for Sale Financial Assets

Financial assets classified as available for sale comprise securities and certain negotiable certificates of deposit.

As at January 31, 2008

	Cost or unamortized cost	Gross unrealized gains	Gross unrealized losses	Carrying value
Securities issued or guaranteed by:				
Canada	2,135	5	(16)	2,124
Provinces	864	5	-	869
Municipalities or school boards	1	-	-	1
U.S. Treasury and other U.S. agencies	40	-	(1)	39
Other debt securities	2,327	10	(7)	2,330
Equity securities	1,198	121	(48)	1,271
Total available for sale securities	6,565	141	(72)	6,634
Other available for sale financial assets	493	-	-	493
Total available for sale financial assets	7,058	141	(72)	7,127

Financial assets classified as available for sale are measured periodically to determine whether there is objective evidence of an other-than-temporary impairment in value. Gross unrealized losses on equity securities are mainly caused by market price fluctuations or foreign exchange movements. The Bank has the ability and intent to hold these securities for a period of time sufficient to allow for any recovery of their fair value. As at January 31, 2008, the Bank concluded that the gross unrealized losses were temporary.

Available for sale securities presented at cost

The Bank holds equity securities such as mutual fund units and other securities that are classified as available for sale but are presented at cost because they are not traded in an active market. These available for sale securities presented at cost in the Consolidated Balance Sheet totalled \$468 million. The fair value of some of these securities could be estimated. The difference between the estimated fair value and the cost of these securities totalled a gain of \$51 million.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***7 – Available for Sale Financial Assets (cont.)****Asset-backed commercial paper**

On December 23, 2007, the Pan-Canadian Investors Committee for Third-Party Structured Asset Backed Commercial Paper approved an agreement in principle to restructure 43 series of asset-backed commercial paper (ABCP) issued by 20 trusts. The restructuring plan will extend the maturity of the ABCP to provide for a maturity similar to that of the underlying assets. Trusts with ABCP supported in whole or in part by synthetic assets will pool their assets. Floating rate notes will be issued in exchange for their existing ABCP, with maturities based upon the maturities of the underlying pooled assets which are expected to be an average of seven years. Trusts with ABCP supported solely by traditional securitized assets will be restructured on a series-by-series basis, with each trust or series maintaining its separate assets. Noteholders will receive floating rate notes with maturities based upon the maturity of the underlying assets which will amortize and be repaid as assets mature or are sold. Trusts with ABCP supported by “ineligible” assets for which the credit quality is uncertain, principally as a result of exposure to sub-prime or home equity loan mortgages in the United States, will be restructured on a series-by-series basis, with each series maintaining its separate exposure to its own assets. Noteholders will receive floating rate notes with maturities based upon the maturity of the underlying assets which will amortize and be repaid as assets mature or are sold.

Taking into account this additional information and the higher probability of a successful restructuring of the ABCP, the Bank adjusted its valuation approach in order to assess the fair value of the ABCP it was holding as at January 31, 2008. For most of the ABCP held, the Bank considered the very high quality of the underlying assets and determined the fair value using a discounted cash flow analysis. The main assumptions pertain to the expected coupons, the expected maturity of the floating rate notes received in exchange of the ABCP, the expected rating and an appropriate discount rate taking into account risks of future losses. The expected discount rate is determined based on observable market inputs for comparable securities.

For ABCP that is not restructured or not under the Pan-Canadian Investors Committee process, as well as for ABCP supported by ineligible assets, observable market inputs for comparable securities from independent pricing sources were used to assess the fair value of each class of assets in the trusts.

To determine the value of the ABCP it holds, the Bank established a range of estimated fair value. Since the carrying value of the ABCP held by the Bank as of October 31, 2007 is within the range of the estimated fair value established as of January 31, 2008, no change was made to the carrying value as of January 31, 2008. The carrying value of the ABCP held by the Bank, as of January 31, 2008, was \$1,707 million of which \$1,580 million was classified in *Available for sale securities* and \$127 million was classified in *Held for trading securities*.

The Bank's valuation was based on its assessment of the conditions prevailing as at January 31, 2008, which may change in subsequent periods. Determining the fair value of ABCP is complex and involves an extensive process that includes the use of quantitative modeling and relevant assumptions. Possible changes that could have a material effect on the future value of the ABCP include (1) changes in the value of the underlying assets, (2) developments related to the liquidity of the ABCP market, (3) the outcome of the restructuring of the conduits and (4) a slowdown in economic conditions in North America.

8 – Transfers of Receivables**NEW SECURITIZATION ACTIVITIES***Insured mortgage loans*

The Bank securitizes insured residential mortgage loans by creating mortgage-backed securities. The pre-tax gain or loss from securitization transactions, net of transaction fees, is recognized in the Consolidated Statement of Income under *Securitization revenues*.

Securitization activities for the quarter ended

	January 31, 2008	October 31, 2007	January 31, 2007
Net cash proceeds	1,204	968	918
Retained interests	29	22	27
Retained servicing liability	(7)	(5)	(5)
	1,226	985	940
Receivables securitized and sold	1,208 ⁽¹⁾	980 ⁽²⁾	926
Gain before income taxes, net of transaction fees	18	5	14
Mortgage-backed securities created and retained included in <i>Securities available for sale</i>	455	74	–

(1) Includes \$181 million in receivables securitized in previous fiscal years

(2) Includes \$45 million in receivables securitized in the third quarter of 2007 and in previous fiscal years.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***8 – Transfers of Receivables (cont.)****MATURITY***Credit card receivables*

Certificates totalling \$400 million, issued by a trust during fiscal 2003 under a securitization program and backed by credit card receivables of the Bank, matured in January 2008. As a result, gross outstanding securitized credit card receivables decreased from \$1.2 billion as at October 31, 2007 to \$800 million as at January 31, 2008.

IMPACT OF SECURITIZATION ACTIVITIES ON CERTAIN ITEMS IN THE CONSOLIDATED STATEMENT OF INCOME**Securitization revenues for the quarter ended January 31**

	Gains on sale of assets		Servicing revenues		Other		Total	
	2008	2007	2008	2007	2008	2007	2008	2007
Insured mortgage loans	18	14	5	4	–	–	23	18
Credit card receivables ⁽¹⁾	13	17	6	4	4	9	23	30
Total	31	31	11	8	4	9	46	48

*(1) Revolving securitization transactions***KEY ASSUMPTIONS**

The key assumptions used to measure the fair value of retained interests as at the securitization date for transactions carried out during the quarter ended January 31, 2008 were as follows.

	Insured mortgage loans	Credit card receivables
Weighted average term (months)	29.2	–
Payment rate (per month)	–	24.8%
Prepayment rate	17.0%	–
Excess spread, net of credit losses	1.1%	10.9%
Expected credit losses	–	3.7%
Discount rate	4.2%	17.0%

9 – Financial Assets Transferred but Not Derecognized

As part of its operations, the Bank concludes transactions in which it transfers financial assets to a third party but which are presented in the Consolidated Balance Sheet because they do not meet the criteria for derecognition.

The carrying values of these transferred financial assets are presented in the table below:

	January 31, 2008	October 31, 2007
Securities sold under repurchase agreements	3,078	1,921
Loaned securities	5,458	4,103

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***10 – Held for Trading Financial Liabilities**

Certain deposits with one or more embedded derivatives are designated as held for trading. These deposits are included under liabilities in *Deposits* in the Consolidated Balance Sheet.

The fair value of these deposits totalled \$333 million as at January 31, 2008. The \$21 million change in fair value for the quarter was recorded as a gain in *Trading revenues* in the Consolidated Statement of Income. This change was entirely caused by factors other than changes attributable to credit risk.

The amount at maturity, which the Bank will be contractually required to pay to the holders of these deposits, may vary and will be different from the fair value as at January 31, 2008.

11 – Non-Controlling Interest

	Denominated in foreign currency	January 31, 2008	October 31, 2007
400,000 NBC CapS II – Series 1 issued by NBC Asset Trust ⁽¹⁾		400	–
300,000 preferred shares, Series A, exchangeable, non-cumulative dividends, issued by NB Capital Corporation ⁽²⁾	US 300	301	284
Mutual funds consolidated in accordance with AcG-15		23	26
Other entities consolidated in accordance with AcG-15		922	630
Other		18	20
Total		1,664	960

(1) On January 22, 2008, the Bank issued 400,000 non-voting transferable trust units called *Trust Capital Securities – Series 1* or “NBC CapS II – Series 1” through its subsidiary NBC Asset Trust (the “Trust”), a closed-end trust established under the laws of Ontario. These securities are not redeemable or exchangeable for Bank preferred shares at the option of the holder. The \$400 million in gross proceeds from the investment was used by the Trust to finance the acquisition of mortgage co-ownership interests from the Bank.

The non-cumulative fixed cash distribution per NBC CapS II – Series 1 payable on June 30, 2008 will be \$31.715. Thereafter, this distribution will be \$36.175 (representing a per annum yield of 7.235% of the \$1,000 initial issue price) to be paid by the Trust semi-annually from December 31, 2008 to June 30, 2018, inclusive. Each distribution made after June 30, 2018 will be determined by multiplying \$1,000 by one-half of the sum of the applicable bankers’ acceptance rate in effect plus 3.79%. No cash distributions will be payable by the Trust on NBC CapS II – Series 1 if the Bank fails to declare regular dividends on its preferred shares or, if no preferred shares are then outstanding, on its outstanding common shares. In this case, the net distributable funds of the Trust will be paid to the Bank as the sole holder of the special trust securities, representing the residual interest in the Trust. Should the Trust fail to pay the semi-annual distributions in full on the NBC CapS II – Series 1, the Bank will withhold from declaring dividends on any of its preferred and common shares during a determined period.

On or after June 30, 2013, or prior to that date upon the occurrence of a predetermined regulatory event or tax event, the Trust may, at its option, redeem the NBC CapS II – Series 1 in whole without the consent of the holders, with prior written notice and with Superintendent approval.

On or after January 22, 2013, the Trust may, with Superintendent approval, purchase the NBC CapS II – Series 1, in whole or in part, in the open market or by tender or private contract at any price. The NBC CapS II – Series 1 purchased by the Trust will be cancelled and will not be reissued.

Each NBC CapS II – Series 1 will be exchanged automatically, without the consent of the holders, for 40 First Preferred Shares, Series 19 of the Bank upon the occurrence of one of the following events: i) proceedings are commenced for the winding-up of the Bank; ii) the Superintendent takes control of the Bank; iii) the Bank posts a Tier 1 capital ratio of less than 5% or a total capital ratio of less than 8%; or iv) the Superintendent has directed the Bank to increase its capital or to provide additional liquidity and the Bank elects to cause such automatic exchange or the Bank does not comply with such direction to the satisfaction of the Superintendent. The First Preferred Shares, Series 19 of the Bank will pay semi-annual, non-cumulative cash dividends and will be redeemable at the Bank’s option, with Superintendent approval, as of June 30, 2013, but will not be redeemable at the option of the holders. Upon an automatic exchange, the Bank will hold all capital securities outstanding of the Trust.

For regulatory capital purposes, the NBC CapS II – Series 1 in the amount of \$400 million qualify as innovative instruments and are eligible as Tier 1 capital. According to the guidelines of the Superintendent, innovative instruments may consist of a portion representing up to 15% of net Tier 1 capital and an additional portion of 5% eligible as Tier 2B capital.

(2) Annual dividend of 8.35% payable quarterly on March 30, June 30, September 30 and December 30. These preferred shares do not have voting rights. They have been redeemable at the issuer’s option since September 3, 2007. The preferred shares, whose liquidation price is US \$1,000 per share, are traded on the New York Stock Exchange in the form of depository shares representing 1/40 of each share. Each preferred share will automatically be exchanged for a new First Preferred Share, Series 2 of the Bank if one of the following events occurs: (i) the Bank defaults on the dividend payment for its first preferred shares; (ii) the Bank’s Tier 1 capital ratio is less than 4% or its total capital ratio is less than 8%; or (iii) at the request of the Superintendent, in accordance with subsection 485(3) of the Bank Act (Canada).

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)

(unaudited) (millions of dollars)

12 – Capital Stock**Shares outstanding and dividends declared as at January 31, 2008**

	Number of shares	Shares \$	Dividends \$	Dividends per share
First Preferred Shares				
Series 15	8,000,000	200	3	0.3656
Series 16	8,000,000	200	2	0.3031
	16,000,000	400	5	0.6687
Common Shares	158,141,407	1,590	98	0.6200
		1,990	103	

REPURCHASE OF COMMON SHARES

On January 28, 2008, the Bank announced that it had filed a normal course issuer bid for the repurchase and cancellation of up to 4,700,000 common shares over a 12-month period beginning on February 1, 2008 and ending no later than January 30, 2009. Repurchases will be made on the open market at market prices through the facilities of the Toronto Stock Exchange.

On February 1, 2007, the Bank had filed a normal course issuer bid for the repurchase and cancellation of up to 8,102,000 common shares over a 12-month period ending no later than January 31, 2008. On January 23, 2006, the Bank had filed a normal course issuer bid for the repurchase and cancellation of up to 8,278,000 common shares over a 12-month period ending no later than January 22, 2007. Repurchases were made on the open market at market prices through the facilities of the Toronto Stock Exchange. Premiums paid above the average book value of the common shares were charged to *Retained earnings*. During the quarter ended January 31, 2008, the Bank did not repurchase any common shares. During the quarter ended January 31, 2007, the Bank had repurchased 717,000 common shares at a cost of \$46 million, which had reduced *Common share capital* by \$7 million and *Retained earnings* by \$39 million.

13 – Pension Benefits and Other Employee Future Benefits

Quarter ended	January 31, 2008	October 31, 2007	January 31, 2007
Pension benefit expense	9	16	15
Other employee future benefit expense	3	3	3

14 – Stock-Based Compensation**STOCK OPTION PLAN**

During the quarter ended January 31, 2008, the Bank awarded 2,260,036 stock options (2007: 1,493,504) with a fair value of \$9.21 per option (2007: \$11.32).

As at January 31, 2008, a total of 7,571,221 stock options were outstanding.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)*

The fair value of the options awarded was estimated on the award date using the Black-Scholes model. The following assumptions were used:

Quarter ended	January 31, 2008	January 31, 2007
Risk-free interest rate	4.40%	4.05%
Expected life of the options	6 years	5 years
Expected volatility	25.3%	22.5%
Expected dividend yield	4.6%	3.3%

Quarter ended	January 31, 2008	October 31, 2007	January 31, 2007
Compensation expense recorded for the stock options	2	2	5

15 – Collateral Management**PLEGGED ASSETS**

In the normal course of business, the Bank pledges securities and other assets as collateral for various liabilities it contracts. A breakdown of assets pledged as collateral is provided in the following table. These transactions were concluded under standard terms and conditions for such transactions.

	January 31, 2008	October 31, 2007
Assets pledged in relation to		
Derivative financial instrument transactions	434	948
Borrowing, securities lending and securities sold under repurchase agreements	20,838	17,227
Direct clearing organizations and other	5,389	5,619
Total	26,661	23,794

FINANCIAL ASSETS RECEIVED AS COLLATERAL

As at January 31, 2008, the fair value of financial assets received as collateral that the Bank was authorized to sell or repledge totalled \$31 billion (October 31, 2007: \$27 billion).

These financial assets received as collateral were obtained as a result of transactions involving securities purchased under reverse repurchase, borrowing and securities lending agreements and derivative financial instrument transactions.

These transactions were concluded in accordance with standard terms and conditions for such transactions.

16 – Litigation

In the normal course of business, the Bank is a party in legal proceedings, many of which are related to lending activities and arise when the Bank takes measures to collect delinquent loans. The Bank is also sometimes named as a defendant or joined in class action suites filed by consumers contesting, among other things, certain transaction fees and unilateral increases in their credit card limits or who wish to avail themselves of certain provisions of consumer protection legislation. The Bank's investment dealer subsidiary, National Bank Financial, is also a party in various legal proceedings in the normal course of business. Most of these proceedings concern Individual Investor Services and generally relate to the suitability of investments made by investors relying on the advice of their respective advisors. In the opinion of Management, based on available information and past experience, the related aggregate potential liability will not have a material unfavourable impact on the Bank's financial position.

As a result of the events that occurred in the asset-backed commercial paper (ABCP) market in August 2007, the Bank and its subsidiaries have received inquiries, complaints and formal demands from some of their clients, and are the subject of a lawsuit relating to the role of the Bank and its subsidiaries in ABCP-related transactions. On the basis of the arguments advanced by ABCP holders to date, Management is of the opinion that the Bank and its subsidiaries have strong defenses. At this stage, however, it is not possible to determine the outcome of such client requests, complaints, formal demands and legal action.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***17 – Segment Disclosures**

Quarter ended January 31	Personal and Commercial		Wealth Management		Financial Markets		Other		Total	
	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007
Net interest income ⁽¹⁾	342	344	34	33	150	(9)	(98)	(92)	428	276
Other income ⁽¹⁾	204	196	182	190	72	302	43	25	501	713
Total revenues	546	540	216	223	222	293	(55)	(67)	929	989
Operating expenses	309	312	153	156	173	168	(3)	20	632	656
Contribution	237	228	63	67	49	125	(52)	(87)	297	333
Provision for credit losses	44	43	–	–	–	–	(12)	(14)	32	29
Income (loss) before income taxes (recovery) and non-controlling interest	193	185	63	67	49	125	(40)	(73)	265	304
Income taxes (recovery) ⁽¹⁾	63	62	20	21	40	41	(56)	(68)	67	56
Non-controlling interest	–	–	2	2	(64)	1	5	5	(57)	8
Net income (loss)	130	123	41	44	73	83	11	(10)	255	240
Average assets	51,078	47,441	693	644	84,256	83,802	(13,174)	(12,041)	122,853	119,846

Personal and Commercial

The Personal and Commercial segment comprises the branch network, intermediary services, credit cards, insurance, business banking services and real estate.

Wealth Management

The Wealth Management segment comprises full-service retail brokerage, direct brokerage, mutual funds, trust services and portfolio management.

Financial Markets

The Financial Markets segment encompasses corporate financing and lending, treasury operations, including asset and liability management for the Bank, and corporate brokerage.

Other

This heading comprises securitization transactions, certain non-recurring elements, and the unallocated portion of centralized services.

Taxable Equivalent

(1) The accounting policies are the same as those presented in the note on accounting policies (Note 1), with the exception of the net interest income, other income and income taxes (recovery) of the operating segments, which are presented on a taxable equivalent basis. Taxable equivalent basis is a calculation method that consists in grossing up certain tax-exempt income by the amount of income tax that would have been otherwise payable. For all of the operating segments, net interest income was grossed up by \$23 million (2007: \$44 million) and other income by \$25 million (2007: \$21 million). An equivalent amount was added to income taxes (recovery). The impact of these adjustments is reversed under the Other heading.

CONSOLIDATED FINANCIAL STATEMENTS | Notes to the consolidated financial statements (cont.)*(unaudited) (millions of dollars)***18 – Disposal**

On January 3, 2008, the Bank, through one of its wholly owned subsidiaries, finalized the sale of all of its common shares in National Bank of Canada (International) Ltd. to Crédit Agricole (Suisse) SA. As a result of this transaction, the Bank recorded a gain of \$32 million, net of related charges of \$1 million, in the Consolidated Statement of Income. An additional gain of \$6 million will be recognized in the Consolidated Statement of Income, provided a certain level of assets under management is maintained.

INFORMATION FOR SHAREHOLDERS AND INVESTORS

Investor Relations

Financial analysts and investors who want to obtain financial information on the Bank are asked to contact the Investor Relations Department.

600 de La Gauchetière West, 7th Floor
 Montreal, Quebec H3B 4L2
 Toll-free: 1-866-517-5455
 Fax: 514-394-6196
 E-mail: investorrelations@nbc.ca
 Website: www.nbc.ca/investorrelations

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 General inquiries: telnat@nbc.ca

Quarterly Report Publication Dates for Fiscal 2008

Second quarter: May 29, 2008
 Third quarter: August 28, 2008
 Fourth quarter: November 27, 2008

Disclosure of First Quarter 2008 Results

Conference Call

- A conference call for analysts and institutional investors will be held on February 28, 2008 at 1:00 p.m. ET.
- Access by telephone in listen-only mode: 1-866-542-4236 or 416-641-6127
- A recording of the conference call can be heard until March 6, 2008 by calling 416-695-5800 or 1-800-408-3053. The access code is 3252080#.

Webcast

- The conference call will be webcast live at www.nbc.ca/investorrelations.
- A recording of the webcast will also be available on the Internet after the call.

Financial Documents

- The quarterly financial statements are available at all times on National Bank's website at www.nbc.ca/investorrelations.
- The Report to Shareholders, Supplementary Financial Information and a slide presentation will be available on the Investor Relations page of National Bank's website shortly before the start of the conference call.

Transfer Agent and Registrar

For information about stock transfers, address changes, dividends, lost certificates, tax forms and estate transfers, shareholders are requested to contact the transfer agent, Computershare Trust Company of Canada, at the address or telephone number below.

Computershare Trust Company of Canada

Share Ownership Management
 1500 University, 7th Floor
 Montreal, Quebec H3A 3S8
 Telephone: 1-888-838-1407
 Fax: 1-888-453-0330
 Email: service@computershare.com
 Website: www.computershare.com

Direct Deposit Service for Dividends

Shareholders may elect to have their dividend payments deposited directly via electronic funds transfer to their bank account at any financial institution that is a member of the Canadian Payments Association. To do so, they must send a written request to the transfer agent, Computershare Trust Company of Canada.

Dividend Reinvestment and Share Purchase Plan

National Bank offers holders of its common shares a Dividend Reinvestment and Share Purchase Plan through which they can invest in common shares of the Bank without paying a commission or administration fee. Participants in the Plan may acquire shares by reinvesting cash dividends paid on shares they hold or by making optional cash payments of at least \$500 per payment, to a maximum of \$5,000 per quarter. For additional information, please contact the registrar, Computershare Trust Company of Canada, at 1-888-838-1407.

Dividends

The dividends declared by the Bank constitute eligible dividends pursuant to the *Income Tax Act* (Canada).



**NATIONAL
BANK**

FINANCIAL GROUP

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