ANNUAL REPORT 2011

Premium Income Corporation

strathbridge
ASSET MANAGEMENT

Letter to Shareholders

We are pleased to present the 2011 annual report containing the management report of fund performance and the audited financial statements of Premium Income Corporation.

During the year ended October 31, 2011, the Fund paid distributions of $0.86 per Preferred share and $0.81 per Class A share. The net asset value per Unit decreased from $22.56 per Unit (on a post-Class A share consolidation basis) to $20.81 per Unit during this period. For a more detailed review of the operations of the Fund, please see the Results of Operations and the Portfolio Manager Report sections.

In connection with the special redemption right approved by shareholders at a special meeting on September 29, 2010, the Class A shares were consolidated on November 1, 2010 on the basis of 0.738208641 new shares for each old share resulting in a higher Class A net asset value per share. This was done in order to maintain an equal number of Preferred shares and Class A shares outstanding subsequent to the special redemption.

On April 28, 2011, the Fund issued 9,523,493 warrants to Class A shareholders of record on May 6, 2011 on the basis of one warrant for each Class A share held. Two warrants entitle the holder to subscribe for one Unit (consisting of one Class A share and one Preferred share) of the Fund at a subscription price of $23.65 until the expiry date of December 15, 2011. The offering was designed to provide the Fund with additional capital that can be used to take advantage of attractive investment opportunities in shares of Canadian banks, increase the trading liquidity of the Class A shares and the Preferred shares and reduce the ongoing management expense ratio of the Fund.

We thank all shareholders for their continued support and encourage shareholders to review the more detailed information contained within this annual report.

John P. Mulvihill
Chairman & CEO,
Strathbridge Asset Management Inc.

The Fund

The Fund is a split share corporation designed to provide Preferred shareholders with cumulative preferential quarterly cash distributions of $0.22 per share, to provide Class A shareholders with quarterly cash distributions of $0.20 per share (on a post-Class A share consolidation basis) and to return the original issue price to holders of both Preferred shares and Class A shares upon windup of the Fund. Once the net asset value ("NAV") per Unit exceeds $25.00, the Class A share distribution will be based on 8.0 percent per annum of the NAV of the Class A share. The shares are listed on the Toronto Stock Exchange under the ticker symbols PIC.PR.A for the Preferred shares, PIC.A for the Class A shares and PIC.WT for the warrants. A Unit of the Fund consists of one Preferred share and one Class A share. To accomplish its objectives, the Fund invests primarily in common shares issued by:

- Bank of Montreal
- The Bank of Nova Scotia
- Canadian Imperial Bank of Commerce
- Royal Bank of Canada
- The Toronto-Dominion Bank.

The Fund employs a proprietary investment strategy, Strathbridge Selective Overwriting ("SSO"), to enhance the income generated by the Portfolio and to reduce volatility. In addition, the Fund may write cash covered put options in respect of securities in which it is permitted to invest.

The SSO strategy is a quantitative, technical based methodology that identifies appropriate times to write and/or close out option positions compared to continuously writing and rolling options every thirty days. This proprietary process has been developed over many years through various market cycles. The Manager believes the primary benefit to investors is to maximize the total return of the particular portfolio while reducing the level of volatility of the portfolio, thereby increasing the risk-adjusted return.

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Management Report of Fund Performance

This annual management report of fund performance contains the financial highlights for the year ended October 31, 2011 of Premium Income Corporation (the "Fund"). The annual financial statements of the Fund are attached.

Copies of the Fund's proxy voting policies and procedures, proxy voting disclosure record or quarterly portfolio disclosure may be obtained by calling 1-800-725-7172 toll free, or by writing to the Fund at Investor Relations, 121 King Street West, Suite 2600, Toronto, Ontario, M5H 3T9, or by visiting our website at www.strathbridge.com. You can request semi-annual or annual reports at no cost by using one of the above methods.

Investment Objectives and Strategies

The Fund's investment objectives are to:

(1) provide Preferred shareholders with cumulative preferential quarterly cash distributions of $0.22 per share,

(2) provide Class A shareholders with quarterly cash distributions of $0.20 per share (on a post-Class A share consolidation basis), and;

(3) return the original issue price to holders of both Preferred shares and Class A shares upon windup of the Fund.

Once the net asset value ("NAV") per Unit exceeds $25.00, the Class A share distribution will be based on 8.0 percent per annum of the NAV of the Class A share.

To accomplish its objectives the Fund invests primarily in common shares of Bank of Montreal, The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Royal Bank of Canada, and The Toronto-Dominion Bank.

The Fund employs a proprietary investment strategy, Strathbridge Selective Overwriting, to enhance the income generated by the Portfolio and to reduce volatility. In addition, the Fund may write cash covered put options in respect of securities in which it is permitted to invest.

Risk

Risks associated with an investment in the securities of the Fund are discussed in the Fund's 2011 annual information form, which is available on the Fund's website at www.strathbridge.com or on SEDAR at www.sedar.com. There were no changes to the Fund over the year that materially affected the risks associated with an investment in the securities of the Fund.

Results of Operations

Distributions

For the year ended October 31, 2011, cash distributions of $0.81 per share were paid to Class A shareholders compared to $0.60 per share (equivalent to $0.81 per share on a post-Class A share consolidation basis) a year ago. During the same period, cash distributions of $0.86 per share were paid to Preferred shareholders, unchanged from the prior year. Since the inception of the Fund in October 1996, the Fund has paid total cash distributions of $18.91 per Class A share and $13.15 per Preferred share.

Revenue and Expenses

The Fund's total revenue was $0.83 per Unit for the year ended October 31, 2011, down $0.04 per Unit compared to the prior year. The difference in income per Unit was mainly due to the timing for recognizing certain dividend income at the end of fiscal 2010, rather than at the beginning of fiscal 2011. Despite the unfavourable impact of the Ontario harmonized sales tax and additional costs associated with the warrant offering, total expenses for 2011 were down $0.04 per Unit compared to a year ago. In 2010, total expenses were $0.32 per Unit which included a special resolution expense of $0.07 per Unit pertaining to the fund extension. The Fund had a net realized and unrealized loss of $0.61 per Unit in 2011 as compared to a net realized and unrealized gain of $2.35 per Unit a year earlier.

Net Asset Value

The net asset value per Unit of the Fund decreased 7.8 percent from $22.56 per Unit (on a post-Class A share consolidation basis) at October 31, 2010 to $20.81 per Unit at October 31, 2011. The aggregate net asset value of the Fund decreased $94.2 million, from $292.3 million at October 31, 2010 to $198.1 million at October 31, 2011, largely attributable to the Unit retractions (totalling $77.6 million) and cash distributions (totalling $16.0 million) on Class A and Preferred shares during the year.

During the year ended October 31, 2011, the annual total return of the Fund was negative 0.4 percent reflecting a general decline in the value of the securities in the portfolio. The S&P/TSX Diversified Banks Index (the "Banks Index") total return during the same period was 0.1 percent. As a result of the Fund being limited to a specific universe of stocks and utilizing a covered call writing strategy to generate income, comparison with a market index may not be appropriate. The Banks Index is calculated without the deduction of management fees and fund expenses, whereas the performance of the Fund is calculated after deducting such fees and expenses.

Recent Developments

In connection with the special redemption right approved by shareholders at a special meeting on September 29, 2010, the Class A shares were consolidated on November 1, 2010 on the basis of 0.738208641 new shares for each old share resulting in a higher Class A net asset value per share. This was done in order to maintain an equal number of Preferred and Class A shares outstanding subsequent to the special redemption.

On April 28, 2011, the Fund issued 9,523,493 warrants to Class A shareholders of record on May 6, 2011 on the basis of one warrant for each Class A share held. Two warrants entitle the holder to subscribe for one Unit (consisting of one Class A share and one Preferred share) of the Fund at a subscription price of $23.65, until the expiry date of December 15, 2011. The offering was designed to provide the Fund with additional capital that can be used to take advantage of attractive investment opportunities in shares of Canadian Banks, increase the trading liquidity of the Class A shares and the Preferred shares and reduce the ongoing management expense ratio of the Fund.

On October 3, 2011, Mulvihill Capital Management Inc. ("MCM"), the Manager and Investment Manager of the Fund, announced a name change to Strathbridge Asset Management Inc. ("Strathbridge") reflecting a revitalized focus and commitment to the closed-end fund business.

Future Accounting Policy Changes

The Manager has developed a changeover plan to meet the timetable published by the Canadian Institute of Chartered Accountants ("CICA") for changeover to International Financial Reporting Standards ("IFRS").

The changeover plan was prepared to address the requirements and includes disclosures of the qualitative and quantitative impact, if any, of the changeover to IFRS in the 2011 financial statements and the preparation of the 2012 financial statements in accordance with IFRS with comparatives. However, the Canadian Accounting Standards Board approved a two year deferral from IFRS adoption for investment companies applying Accounting Guideline 18 - Investment Companies ("AcG-18"). As a result, the Fund will adopt IFRS for its fiscal period beginning November 1, 2013 and will issue its initial financial statements in accordance with IFRS, with comparative information, for the semi-annual period ending April 30, 2014.

As at October 31, 2011, some anticipated changes to financial reporting include:

- Compliance with the full body of IFRS without industry specific exemptions. Unlike Canadian Generally Accepted Accounting Principles ("Canadian GAAP") where investment fund accounting was based upon guidance in AcG-18,
- Changes to the presentation of shareholder equity to consider puttable instruments,
- Presentation of comparative information, and;
- Additional financial statement note disclosures on the recognition and classification of financial instruments.

Based on the Manager's current understanding and analysis of IFRS to the accounting policies under Canadian GAAP, the Manager does not anticipate that the transition to IFRS will have a material impact on the Fund's net assets per Unit, systems and processes, and it is expected that it will mainly result in additional note disclosure in the financial statements.

Related Party Transactions

Strathbridge, as the Investment Manager of the Fund, manages the Fund's investment portfolio in a manner consistent with the investment objectives, strategy and criteria of the Fund pursuant to an Investment Management Agreement made between the Fund and MCM dated October 17, 1996 and amended as of October 8, 2010.

Strathbridge is the Manager of the Fund pursuant to a Management Agreement made between the Fund and MCM dated October 17, 1996 and amended as of October 8, 2010. As such, Strathbridge is responsible for providing or arranging for required administrative services to the Fund.

Strathbridge is paid the fees described under the Management Fees section of this report.

Independent Review Committee

National Instrument 81-107 - Independent Review Committee for Investment Funds ("NI 81-107") requires all publicly offered investment funds to establish an independent review committee ("IRC") to whom the Manager must refer conflict of interest matters for review or approval. NI 81-107 also imposes obligations upon the Manager to establish written policies and procedures for dealing with conflict of interest matters, maintaining records in respect of these matters and providing assistance to the IRC in carrying out its functions. Members of the IRC are Robert W. Korthals, Michael M. Koerner and Robert G. Bertram.

On March 2, 2011, the Manager presented to the IRC a proposal of the Fund to issue warrants to Class A shareholders to subscribe for additional Units of the Fund. Each Unit consists of one transferable, redeemable Class A share and one transferable, redeemable Preferred share. The exercise of warrants by holders will provide the Fund with additional capital and is also expected to increase trading liquidity and reduce the management expense ratio of the Fund. The IRC reviewed the proposal and approved the warrant offering as it achieved a fair and reasonable result for the Fund.

Financial Highlights

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for the past five years. This information is derived from the Fund's audited annual financial statements.

The net assets per Unit presented in the financial statements differs from the net asset value per Unit calculated weekly, primarily as a result of investments being valued at bid prices for financial statement purposes and at closing prices for weekly net asset value purposes.

Years ended October 31

	2011	2010	2009	2008	2007
THE FUND'S NET ASSETS PER UNIT					
Net Assets, beginning of year (based on bid prices)(1)	**$ 22.53(5)**	$ 19.15	$ 19.16	$ 26.16	$ 26.40(4)
INCREASE (DECREASE) FROM OPERATIONS					
Total revenue	**0.83**	0.87	0.70	0.89	0.95
Total expenses	**(0.28)**	(0.32)	(0.21)	(0.25)	(0.30)
Realized gain (loss) for the period	**1.43**	0.82	(3.65)	(1.40)	1.78
Unrealized gain (loss) for the period	**(2.04)**	1.53	3.97	(4.48)	(0.61)
Total Increase (Decrease) from Operations(2)	**(0.06)**	**2.90**	**0.81**	**(5.24)**	**1.82**
DISTRIBUTIONS					
Preferred Share					
From capital gains	**–**	–	–	–	(0.05)
From net investment income	**(0.84)**	(0.86)	(0.86)	(0.86)	(0.82)
Non-taxable distributions	**(0.02)**	–	–	–	–
Total Preferred Share Distributions	**(0.86)**	**(0.86)**	**(0.86)**	**(0.86)**	**(0.87)**
Class A Share					
From capital gains	**–**	–	–	(0.90)	(1.20)
From net investment income	**–**	(0.60)	(0.45)	–	–
Non-taxable distributions	**(0.81)**	–	–	–	–
Total Class A Share Distributions	**(0.81)**	**(0.60)**	**(0.45)**	**(0.90)**	**(1.20)**
Total Annual Distributions(3)	**(1.67)**	**(1.46)**	**(1.31)**	**(1.76)**	**(2.07)**
Net Assets, as at October 31 (based on bid prices)(1)	**$ 20.79**	**$ 20.56**	**$ 19.15**	**$ 19.16**	**$ 26.16**

(1) Net Assets per Unit is the difference between the aggregate value of the assets of the Fund and the aggregate value of the liabilities excluding the Redeemable Preferred Share liability of the Fund on that date and including the valuation of securities at bid prices divided by the number of Units then outstanding.
(2) Total increase (decrease) from operations consists of interest and dividend revenue, realized and unrealized gain (loss), less expenses, excluding Preferred share distributions, and is calculated based on the weighted average number of Units outstanding during the year. The schedule is not intended to total to the ending net assets as calculations are based on the weighted average number of Units outstanding during the year.
(3) Distributions to shareholders are based on the number of shares outstanding on the record date for each distribution and were paid in cash.
(4) Net Assets per Unit has been adjusted for the change in accounting policy relating to the calculation of net asset value based on bid prices versus closing prices prior to 2007.
(5) Net Assets per Unit has been adjusted for the consolidation of the Class A shares effective the opening of trading on November 1, 2010. Each shareholder received 0.738208641 new Class A shares for each Class A share held. The total value of a shareholder's investment did not change, however, the number of Class A shares reflected in the shareholder's account declined and the Net Assets per Class A share increased proportionately.

	2011	2010	2009	2008	2007
RATIOS/SUPPLEMENTAL DATA					
Net Asset Value, excluding the Redeemable Preferred Share liability ($millions)(1)	**$ 198.09**	$ 292.34	$ 279.70	$ 352.11	$ 497.18
Net Asset Value ($millions)(1)	**$ 55.33**	$ 79.25	$ 60.95	$ 76.36	$ 211.31
Number of Units outstanding(1)	**9,517,553**	14,206,046	14,575,324	18,345,439	18,995,200
Management expense ratio(2)	**1.15%**	1.44%	1.07%	1.08%	1.04%
Portfolio turnover rate(3)	**81.29%**	93.32%	74.20%	11.51%	109.89%
Trading expense ratio(4)	**0.06%**	0.09%	0.08%	0.04%	0.07%
Net Asset Value per Unit(5)	**$ 20.81(6)**	$ 20.58	$ 19.19	$ 19.19	$ 26.17
Closing market price - Preferred	**$ 14.58**	$ 15.00	$ 14.90	$ 12.60	$ 15.25
Closing market price - Class A	**$ 6.03**	$ 5.84	$ 4.57	$ 5.30	$ 10.10

(1) This information is provided as at October 31. One Unit consists of one Preferred share and one Class A share.
(2) The management expense ratio ("MER") is the sum of all fees and expenses, including federal and provincial sales taxes and capital tax but excluding transaction fees, income taxes and Preferred share distributions, charged to the Fund divided by the average net asset value excluding the Redeemable Preferred Share liability. The MER for 2011 includes warrant offering costs and special resolution recovery. The MER for 2011 excluding warrant offering costs and special resolution recovery is 1.13%. The MER for 2010 includes the special resolution expense. The MER for 2010 excluding the special resolution expense is 1.10%. The MER, including Preferred share distributions, is 5.02%, 5.60%, 5.81%, 4.99% and 4.26% for 2011, 2010, 2009, 2008 and 2007 respectively.
(3) Portfolio turnover rate is calculated based on the lesser of purchases or sales of investments, excluding short-term investments, divided by the average value of the portfolio securities. The Fund employs an option overlay strategy which can result in higher portfolio turnover by virtue of option exercises, when compared to a conventional equity mutual fund.
(4) Trading expense ratio represents total commissions expressed as a percentage of the daily average net asset value during the year.
(5) Net Asset Value per Unit is the difference between the aggregate value of the assets of the Fund and the aggregate value of the liabilities excluding the Redeemable Preferred Share liability of the Fund on that date and including the valuation of securities at closing prices divided by the number of Units then outstanding.
(6) Net Asset Value per Unit has been adjusted for the consolidation of the Class A shares effective the opening of trading on November 1, 2010. Each shareholder received 0.738208641 new Class A shares for each Class A share held. The total value of a shareholder's investment did not change, however, the number of Class A shares reflected in the shareholder's account declined and the Net Asset Value per Class A share increased proportionately.

Management Fees

Strathbridge, as the Investment Manager of the Fund, is entitled to fees under the Investment Management Agreement calculated monthly as 1/12 of 0.80 percent of the net asset value of the Fund at each month end. Services received under the Investment Management Agreement include the making of all investment decisions and writing of covered call options in accordance with the investment objectives, strategy and criteria of the Fund. Strathbridge also makes all decisions as to the purchase and sale of securities in the Fund's portfolio and as to the execution of all portfolio and other transactions.

Strathbridge, as the Manager of the Fund, is entitled to fees under the Management Agreement calculated monthly as 1/12 of 0.10 percent of the net asset value of the Fund at each month end. Services received under the Management Agreement include providing or arranging for required administrative services to the Fund.

Mulvihill Fund Services Inc. (the predecessor Manager or "Mulvihill") amalgamated with Mulvihill Capital Management Inc. (the predecessor Investment Manager or "MCM") on September 1, 2010. As successor, MCM became the Manager as well as the Investment Manager of the Fund. Subsequently, on October 3, 2011, MCM announced a name change to Strathbridge Asset Management Inc. ("Strathbridge").

Past Performance

The following chart sets out the Fund's year-by-year past performance. It is important to note that the:

(1) information shown assumes that all distributions made by the Fund during these periods were reinvested in the Fund,

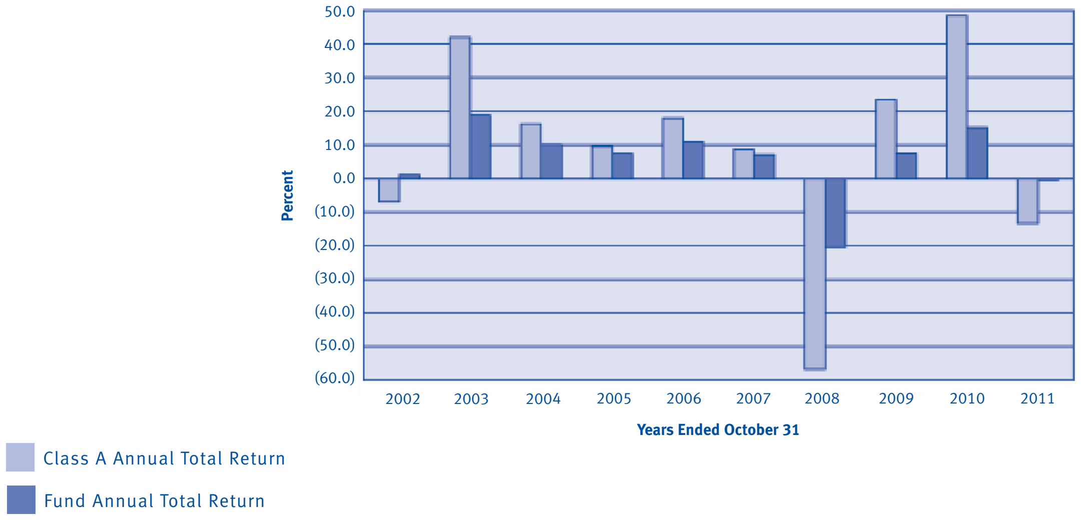
(2) information does not take into account sales, redemptions, distributions or other optional charges that would have reduced returns, and;

(3) past performance of the Fund does not necessarily indicate how it will perform in the future.

Year-By-Year Returns

The following bar chart illustrates how the Fund's annual total return varied from year to year for each of the past ten years. The chart also shows, in percentage terms, how much an investment made on November 1 in each year would have increased or decreased by the end of the fiscal year.

Annual Total Return



Annual Compound Returns

The following table shows the Fund's historical annual compound return (net of expenses) for the periods ended October 31, 2011, as compared to the performance of the S&P/TSX Diversified Banks Index.

	One Year	Three Years	Five Years	Ten Years
Premium Income Corporation	**(0.44)%**	7.20 %	0.96 %	5.16 %
Premium Income Corporation – Preferred	**5.88 %**	5.88 %	5.88 %	5.95 %
Premium Income Corporation – Class A	**(13.38)%**	16.67 %	(5.70)%	4.00 %
S&P/TSX Diversified Banks Index*	**0.11 %**	12.50 %	4.37 %	11.42 %

* The S&P/TSX Diversified Banks Index is a subset of the S&P/TSX Composite Index.

The equity performance benchmark shown here provides an approximate indication of how the Fund's returns compare to a public market index for similar securities. It is important to note that the Fund is not managed in order to match or exceed this index; rather, its objectives are to pay out quarterly dividends and return the original invested amount at the termination date. As a result, the Fund has, from time to time, maintained cash balances in an effort to provide greater net asset value stability and employs a covered option writing strategy to generate the distributions.

The use of options may have the effect of limiting or reducing the total returns of the Fund, particularly in a rising market since the premiums associated with writing covered call options may be outweighed by the foregone opportunity of remaining fully invested in the securities comprising the portfolio. The Manager believes that in a flat or downward trending market, a portfolio that is subject to covered call option writing will generally provide higher relative returns and lower volatility than one on which no options are written.

Portfolio Manager Report

After showing some signs of improvement in the first half of the fiscal year ending April 30, 2011, North American equity markets corrected in the second half as economic indicators weakened over the summer, negatively impacted by the high price of oil as well as the global supply chain interruption that resulted from the horrendous tsunami that hit Japan in March. Global economic indicators were also deteriorating at the same time as several Eurozone countries had to implement significant spending reductions to reduce record deficits. Volatility levels picked up in late July as the deadline for the U.S. Congress vote on the debt ceiling limit on August 2nd was approaching and remained elevated after Standard & Poor's downgraded the rating of U.S. Government debt. All of these factors weighed on equity markets into early October, but then stabilized and rallied into year-end on the probability that the European Central Bank along with other European Union countries would help bailout Greece. The Canadian economy has proven to remain relatively strong with employment and housing conditions much stronger than most developed countries and the government enjoying a much stronger fiscal position. After raising the benchmark overnight rate by 25 basis point increments three times in 2010, the Bank of Canada remained on hold during the period due to slower than expected growth and a relatively stable Canadian dollar which increased by 2.3 percent relative to the U.S. dollar.

The Canadian banks reported mixed earnings growth over fiscal 2011 on solid retail banking and better than expected loan loss provisions offset by weaker than expected trading revenues. Capital ratios continued to remain strong with Tier 1 ratios up slightly from the previous year. The Canadian banks continued to return capital to shareholders during the period as every bank increased its dividend in 2011, with the exception of the Bank of Montreal. Record low interest rates are likely to remain for the foreseeable future until economic growth is believed to be sustainable. In light of current low interest rates, the valuations of the Canadian banks remain at attractive levels when measured by price to earnings ratios and current dividend yields and this should continue to act as major support for the share prices. As regulatory requirements become clearer in 2012, the banks are likely to continue to return capital to shareholders in the form of increased dividends and share repurchases.

The total return for the S&P/TSX Diversified Banks Index for the year was 0.1 percent which modestly outperformed the broader S&P/TSX Composite Index which declined 0.8 percent. The five banks that make up the portfolio experienced varying returns over the period with The Toronto-Dominion Bank leading the group, up 5.9 percent while the Royal Bank of Canada lagged the group, down 7.1 percent due to weaker than expected trading revenues.

The annual total return of the Fund, including reinvestment of distributions, for the year ended October 31, 2011 was negative 0.4 percent. The Fund modestly underperformed the S&P/TSX Diversified Banks Index for the year due to some covered call writing in the month of February, when the five banks within the portfolio increased 7.8 percent on average. The Fund maintained its invested position during the majority of the year and ended 2011 with a cash position of 1 percent compared to 24 percent at the end of 2010 that was increased in order to finance the special redemption right offered in conjunction with the fund extension. Due to the increase in the level of volatility in the Canadian banks during the second half of the year, the Fund increased its selective covered-call writing activity as the higher volatility did compensate the Fund enough to justify this activity. The Fund ended 2011 with approximately 31 percent of the portfolio subject to covered calls.

The Canadian banks are expected to improve profitability and capital ratios in 2012 due to improving credit, good expense control and leverage to an economic recovery. Consequently, Canadian banks are likely to continue to return capital to shareholders in the form of dividend growth and share buybacks.

Summary of Investment Portfolio

The composition of the portfolio may change due to ongoing portfolio transactions of the Fund. A quarterly update is available on our website at www.strathbridge.com.

Asset Mix

October 31, 2011

	% OF NET ASSET VALUE*
Financial Institutions	100 %
Cash and Short-Term Investments	1 %
Other Assets (Liabilities)	(1)%
	100 %

*The Net Asset Value excludes the Redeemable Preferred Share liability.

Portfolio Holdings

October 31, 2011

	% OF NET ASSET VALUE*
Canadian Imperial Bank of Commerce	21 %
Bank of Montreal	20 %
The Bank of Nova Scotia	20 %
The Toronto-Dominion Bank	20 %
Royal Bank of Canada	19 %
Cash and Short-Term Investments	1 %

*The Net Asset Value excludes the Redeemable Preferred Share liability.

Forward-Looking Statements

This report may contain forward-looking statements about the Fund. Forward-looking statements include statements that are predictive in nature, that depend upon or refer to future events or conditions, or that include words such as “expects”, “anticipates”, “intends”, “plans”, “believes”, “estimates” or negative versions thereof and similar expressions. In addition, any statement that may be made concerning future performance, strategies or prospects, and possible future Fund action, is also forward-looking. Forward-looking statements are based on current expectations and projections about future events and are inherently subject to, among other things, risks, uncertainties and assumptions about the Fund and economic factors.

Forward-looking statements are not guarantees of future performance, and actual events and results could differ materially from those expressed or implied in any forward-looking statements made by the Fund. Any number of important factors could contribute to any divergence between what is anticipated and what actually occurs, including, but not limited to, general economic, political and market factors, interest and foreign exchange rates, global equity and capital markets, business competition, technology change, changes in government regulations, unexpected judicial or regulatory proceedings, and catastrophic events.

The above-mentioned list of important factors is not exhaustive. You should consider these and other factors carefully before making any investment decisions and you should avoid placing undue reliance on forward-looking statements. While the Fund currently anticipates that subsequent events and developments may cause the Fund’s views to change, the Fund does not undertake to update any forward-looking statements.

Management's Responsibility for Financial Reporting

The accompanying financial statements of Premium Income Corporation (the "Fund") and all the information in this annual report are the responsibility of the management of Strathbridge Asset Management Inc., (the "Manager"), and have been approved by the Fund's Board of Directors (the "Board").

The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and include certain amounts that are based on estimates and judgments. Management has ensured that the other financial information presented in this annual report is consistent with the financial statements. The significant accounting policies which management believes are appropriate for the Fund are described in Note 4 of the annual financial statements.

The Manager is also responsible for maintaining a system of internal controls designed to provide reasonable assurance that assets are safeguarded and that accounting systems provide timely, accurate and reliable financial information.

The Audit Committee meets periodically with management and the independent auditor to discuss internal controls, the financial reporting process, various auditing and financial reporting issues, and to review the annual report, the financial statements and the independent auditor's report. Deloitte & Touche LLP, the Fund's independent auditor, has full and unrestricted access to the Audit Committee and the Board.

John P. Mulvihill
Director
Strathbridge Asset Management Inc.
November 30, 2011

John D. Germain
Director
Strathbridge Asset Management Inc.

To the Shareholders of Premium Income Corporation

We have audited the accompanying financial statements of Premium Income Corporation, which comprise the statement of investments as at October 31, 2011, the statements of financial position as at October 31, 2011 and 2010, and the statements of operations and deficit, changes in net assets and of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Premium Income Corporation as at October 31, 2011 and 2010, and the results of its operation, its changes in the net assets, and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants
Licensed Public Accountants
November 30, 2011
Toronto, Ontario

Statements of Financial Position

As at October 31

	2011	2010
ASSETS		
Investments at fair value (cost - $202,600,690; 2010 - $211,399,043)	**$ 194,975,346**	$ 223,326,075
Short-term investments at fair value (cost - $1,995,707; 2010 - $24,668,841)	**1,995,707**	24,668,841
Cash	**364,217**	621,501
Interest and dividends receivable	**887,028**	1,042,335
Due from brokers - investments	**–**	43,697,903
TOTAL ASSETS	**$ 198,222,298**	**$ 293,356,655**
LIABILITIES		
Accrued management fees	**$ 151,637**	$ 223,648
Redemptions payable	**123,629**	–
Accrued liabilities	**64,951**	131,503
Special resolution payable	**–**	972,841
Redeemable Preferred shares (Note 6)	**142,763,295**	213,090,690
	143,103,512	**214,418,682**
EQUITY		
Class A and Class B shares (Note 6)	**130,878,706**	144,207,687
Deficit	**(75,759,920)**	(65,269,714)
	55,118,786	**78,937,973**
TOTAL LIABILITIES AND EQUITY	**$ 198,222,298**	**$ 293,356,655**
Number of Units Outstanding (Note 6)	**9,517,553**	**14,206,046**
Net Assets per Unit		
Preferred Share	**$ 15.00**	$ 15.00
Class A Share - Basic	**5.79**	5.56
Net Assets per Unit (Note 5)	**$ 20.79**	**$ 20.56**
Net Assets per Class A Share - Diluted	**$ 5.79**	**n/a**

On Behalf of the Board of Directors

John P. Mulvihill, Director

Robert W. Korthals, Director

Statements of Operations and Deficit

Years ended October 31

	2011	2010
REVENUE		
Interest	$ 74,919	$ 108,565
Dividends	7,829,802	12,301,677
	7,904,721	12,410,242
Net realized gain on investments	9,056,123	13,317,955
Net realized gain (loss) on derivatives	4,619,566	(1,526,860)
Total Net Realized Gain	13,675,689	11,791,095
TOTAL REVENUE	21,580,410	24,201,337
EXPENSES (Note 7)		
Management fees	1,905,694	2,662,660
Administrative and other expenses	130,469	152,460
Transaction fees (Note 10)	135,967	278,347
Custodian fees	47,579	53,532
Audit fees	36,040	35,225
Director fees	21,835	21,520
Independent review committee fees	8,457	6,536
Legal fees	6,696	11,620
Shareholder reporting costs	41,519	49,816
Capital tax	(213)	60,000
Federal and provincial sales taxes	205,613	192,006
Subtotal Expenses	2,539,656	3,523,722
Warrant offering costs (Note 6)	150,633	–
TOTAL EXPENSES	2,690,289	3,523,722
Net Realized Income before Special Resolution Expense and Distributions	18,890,121	20,677,615
Special resolution recovery/(expense) (Note 2)	112,774	(1,018,079)
Net Realized Income before Distributions	19,002,895	19,659,536
Preferred share distributions (Note 9)	(8,214,013)	(12,309,165)
Net Realized Income	10,788,882	7,350,371
Net change in unrealized appreciation/depreciation of investments	(19,552,376)	21,912,993
Amortization of premium on issue of preferred shares (Note 4)	–	123,132
	(19,552,376)	22,036,125
NET INCOME (LOSS) FOR THE YEAR	$ (8,763,494)	$ 29,386,496
NET INCOME (LOSS) PER CLASS A SHARE - BASIC		
(based on the weighted average number of Class A shares outstanding during the year of 9,562,135; 2010 - 14,317,528)	$ (0.92)	$ 2.05
NET LOSS PER CLASS A SHARE - DILUTED	$ (0.92)	n/a
DEFICIT		
Balance, beginning of year	$ (65,269,714)	$ (87,630,291)
Net allocations on retractions of Class A shares (Note 6)	6,013,602	1,536,979
Net income (loss) for the year	(8,763,494)	29,386,496
Distributions on Class A shares	(7,740,314)	(8,562,898)
BALANCE, END OF YEAR	$ (75,759,920)	$ (65,269,714)

The notes are an integral part of the Financial Statements.

Statements of Changes in Net Assets

Years ended October 31

	2011	2010
NET ASSETS – CLASS A AND B SHARES, BEGINNING OF YEAR	**$ 78,937,973**	$ 60,325,346
Net Realized Income before Distributions	**19,002,895**	19,659,536
Amortization of Premium on Issue of Preferred Shares	**–**	123,132
Class A Share Capital Transactions		
Value for Class A shares redeemed (Note 6)	**(7,315,379)**	(2,210,971)
Distributions (Note 9)		
Preferred Shares		
From net investment income	**(7,973,332)**	(12,309,165)
Non-taxable distributions	**(240,681)**	–
Class A Shares		
From net investment income	**–**	(8,562,898)
Non-taxable distributions	**(7,740,314)**	–
	(15,954,327)	(20,872,063)
Net Change in Unrealized Appreciation/Depreciation of Investments	**(19,552,376)**	21,912,993
Change in Net Assets during the Year	**(23,819,187)**	18,612,627
NET ASSETS – CLASS A AND B SHARES, END OF YEAR	**$ 55,118,786**	$ 78,937,973

Statements of Cash Flows

Years ended October 31

	2011	2010
CASH AND SHORT-TERM INVESTMENTS, BEGINNING OF YEAR	**$ 25,290,342**	$ 10,956,151
Cash Flows Provided by (Used In) Operating Activities		
Net Realized Income before Distributions	**19,002,895**	19,659,536
Adjustments to Reconcile Net Cash Provided by (Used In) Operating Activities		
Purchase of investment securities	**(166,802,154)**	(255,400,631)
Proceeds from disposition of investment securities	**189,276,196**	344,358,610
Net (gain)/loss on sale of investments (including derivatives)	**(13,675,689)**	(11,791,095)
(Increase)/decrease in interest and dividends receivable and due from brokers - investments	**43,853,210**	(44,047,897)
Increase/(decrease) in accrued management fees, accrued liabilities and special resolution payable	**(1,111,404)**	1,044,783
	51,540,159	34,163,770
Cash Flows Provided by (Used In) Financing Activities		
Distributions to Preferred shares	**(8,214,013)**	(12,309,165)
Distributions to Class A shares	**(7,740,314)**	(8,562,898)
Preferred share redemptions	**(70,238,295)**	(14,033,280)
Class A share redemptions	**(7,280,850)**	(4,583,772)
	(93,473,472)	(39,489,115)
Net Increase/(Decrease) in Cash and Short-Term Investments During the Year	**(22,930,418)**	14,334,191
CASH AND SHORT-TERM INVESTMENTS, END OF YEAR	**$ 2,359,924**	$ 25,290,342
Cash and Short-Term Investments comprised of:		
Cash	**$ 364,217**	$ 621,501
Short-Term Investments	**1,995,707**	24,668,841
CASH AND SHORT-TERM INVESTMENTS, END OF YEAR	**$ 2,359,924**	$ 25,290,342

The notes are an integral part of the Financial Statements.

Statement of Investments

As at October 31, 2011

	Par Value/ Number of Shares/ Number of Contracts	Average Cost/ Proceeds	Fair Value	% of Portfolio
SHORT-TERM INVESTMENTS				
Bankers' Acceptances				
The Bank of Nova Scotia, 1.07% - November 30, 2011	950,000	$ 948,689	**$ 948,689**	
The Bank of Nova Scotia, 1.13% - January 17, 2012	1,050,000	1,047,018	**1,047,018**	
Total Bankers' Acceptances		**1,995,707**	**1,995,707**	**100.0 %**
Accrued Interest			**988**	**0.0 %**
TOTAL SHORT-TERM INVESTMENTS		**$ 1,995,707**	**$ 1,996,695**	**100.0 %**
INVESTMENTS				
Canadian Common Shares				
Bank of Montreal	671,000	$ 39,901,565	**$ 39,515,190**	
Canadian Imperial Bank of Commerce	565,000	43,274,755	**42,431,500**	
Royal Bank of Canada	771,000	42,731,393	**37,486,020**	
The Bank of Nova Scotia	739,500	40,395,720	**38,742,405**	
The Toronto-Dominion Bank	516,000	37,717,840	**38,715,480**	
Total Canadian Common Shares		**$ 204,021,273**	**$ 196,890,595**	**101.0 %**
Options				
Purchased Put Options (100 shares per contract)				
Bank of Montreal - November 2011 @ $59	1,035	**$ 278,829**	**$ 79,999**	**0.0 %**
Written Covered Call Options (100 shares per contract)				
Bank of Montreal - November 2011 @ $58	(3,450)	(489,900)	**(425,023)**	
Canadian Imperial Bank of Commerce - November 2011 @ $74	(2,800)	(481,600)	**(730,951)**	
The Bank of Nova Scotia - November 2011 @ $50	(1,898)	(370,110)	**(562,081)**	
The Toronto-Dominion Bank - November 2011 @ $74	(1,290)	(276,060)	**(277,193)**	
Total Written Covered Call Options		**(1,617,670)**	**(1,995,248)**	**(1.0)%**
Total Options		**$ (1,338,841)**	**$ (1,915,249)**	**(1.0)%**
Adjustment for transaction fees		**(81,742)**		
TOTAL INVESTMENTS		**$ 202,600,690**	**$194,975,346**	**100.0 %**

The notes are an integral part of the Financial Statements.

1. Corporate Information

Premium Income Corporation (the "Fund") is a mutual fund corporation incorporated under the laws of the Province of Ontario on August 27, 1996. On September 29, 2010, the shareholders approved a reorganization effective on November 1, 2010 to extend the term of the Fund for an additional seven years. All shares outstanding on November 1, 2017 will be redeemed by the Fund on that date subject to an automatic extension of the term for an additional seven years.

On September 1, 2010, Mulvihill Capital Management Inc. ("MCM") amalgamated with Mulvihill Fund Services Inc. As successor, MCM became the Manager as well as the Investment Manager of the Fund. Subsequently, on October 3, 2011, MCM announced a name change to Strathbridge Asset Management Inc. ("Strathbridge").

2. Reorganization

On September 29, 2010, shareholders approved a reorganization effective on November 1, 2010 to extend the term of the Fund an additional seven years to November 1, 2017. As part of the reorganization, shareholders were given a special retraction right to retract their Class A shares or Preferred shares at the net asset value ("NAV") of the Fund on November 1, 2010. This resulted in the Class A shares being consolidated on the basis of 0.738208641 new shares for each old share in order to maintain an equal number of Preferred shares and Class A shares outstanding subsequent to the special retraction. The Fund also made changes to its authorized share capital by adding new classes of shares issuable in series, changing the monthly retraction prices for the Preferred shares and the Class A shares so that they are calculated by reference to market price in addition to NAV and changing the dates by which notice of monthly retractions needs to be provided and by which the retraction amount will be paid. The Fund will also allow for the calculation of a diluted NAV in the event the Fund should ever issue warrants or rights to acquire additional Preferred shares or Class A shares.

In 2010, there was a special resolution expense of $1,018,079 pertaining to the fund extension of which $112,774 was recovered in 2011 as unclaimed solicitation fees.

3. Investment Objectives of the Fund

Effective November 1, 2010, the Fund's investment objectives were changed to:

(i) provide Preferred shareholders with cumulative preferential quarterly cash distributions of $0.22 per share,

(ii) provide Class A shareholders with quarterly cash distributions of $0.20 per share (on a post-Class A share consolidation basis), and;

(iii) return the original issue price to holders of both Preferred shares and Class A shares upon windup of the Fund.

Once the net asset value ("NAV") per Unit exceeds $25.00, the Class A share distribution will be based on 8.0 percent per annum of the NAV of the Class A share.

To accomplish its objectives the Fund invests primarily in common shares of Bank of Montreal, The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Royal Bank of Canada, and The Toronto-Dominion Bank.

The Fund employs a proprietary investment strategy, Strathbridge Selective Overwriting, to enhance the income generated by the Portfolio and to reduce volatility. In addition, the Fund may write cash covered put options in respect of securities in which it is permitted to invest.

4. Summary of Significant Accounting Policies

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"), which include estimates and assumptions by management that may affect the reported amounts of assets, liabilities, income and expenses during the reported periods. Primary estimates include valuation of investments. While management believes that the estimates used in preparing its financial statements are reasonable and prudent, actual results could differ from these estimates.

Financial Instruments – Disclosures

The Fund uses a three-tier hierarchy as a framework for disclosing fair value based on inputs used to value the Fund's investments. See additional note disclosures in Note 12.

The significant accounting policies of the Fund are as follows:

Valuation of Investments

Investments are recorded in the financial statements at their fair value determined as follows:

Securities are valued at fair value, which is determined by the closing bid price on the recognized stock exchange on which the securities are listed or principally traded. If no bid prices are available, the securities are valued at the closing sale price.

Short-term investments are included in the statement of investments at their cost. This value together with accrued interest approximates fair value at bid price.

Listed options are valued at fair values as reported on recognized exchanges. Over-the-counter options are valued using the Black-Scholes valuation model.

Transaction Fees

Transaction fees have been expensed as incurred and included in the transaction fees line in the Statement of Operations and Deficit. Transaction fees are costs that are directly attributable to portfolio transactions which include fees and commissions paid to brokers and dealers.

Investment Transactions and Income

Investment transactions are accounted for on a trade date basis. Realized gains and losses on the sale of investments and change in unrealized appreciation/depreciation of investments are determined on an average cost basis. Realized gains and losses relating to written options may arise from:

(i) Expiration of written options whereby realized gains are equivalent to the premium received,

(ii) Exercise of written covered call options whereby realized gains or losses are equivalent to the premium received in addition to the realized gain or loss from disposition of the related investments at the exercise price of the option, and;

(iii) Closing of written options whereby realized gains or losses are equivalent to the cost of purchasing options to close the positions, net of any premium received.

Realized gains and losses related to options are included in net realized gain (loss) on derivatives.

Realized gains and losses relating to purchased put options may arise from:

(i) Expiration of purchased put options whereby realized losses are equivalent to the premium paid,

(ii) Exercise of purchased put options whereby realized gains or losses are equivalent to the realized gain or loss from disposition of the related investments at the exercise price of the option less the premium paid, and;

(iii) Sale of purchased put options whereby realized gains or losses are equivalent to the sale proceeds, net of any premium paid.

Option premiums received are reflected as deferred credits in investments so long as the options are outstanding. Any difference resulting from revaluation is included in change in unrealized appreciation/depreciation of investments. Premiums received on written put options that are exercised are included in the cost of the security purchased.

Dividend income is recorded on the ex-dividend date. Interest income is recorded daily as it is earned.

Redeemable Preferred Shares

Each Redeemable Preferred share is valued for financial statement purposes at the lesser of: (i) $15.00; and (ii) the net assets of the Fund divided by the number of Preferred shares outstanding.

Premium on Preferred Shares

Premium on Preferred shares net of issue costs is amortized over the remaining life of the Fund. The premium on Preferred shares retracted will be recognized on the date they are retracted.

5. Net Asset Value

The net asset value of the Fund is calculated using the fair value of investments as the close or last trade price. The net assets per Unit is calculated using the fair value of investments at the closing bid price. The net assets per Unit for financial reporting purposes and net asset value per Unit for pricing purposes will not be the same due to the use of different valuation techniques.

The difference between the net asset value per Unit for pricing purposes and the net assets per Unit reflected in the financial statements is as follows:

	2011	2010
Net Asset Value per Unit (for pricing purposes)	**$20.8130**	$20.5786
Difference	**(0.0217)**	(0.0220)
Net Assets per Unit (for financial statement purposes)	**$20.7913**	$20.5566

6. Share Capital

The Fund is authorized to issue an unlimited number of Preferred shares and Class A shares and 1,000 Class B shares. As a result of the reorganization on November 1, 2010, the authorized capital of the Fund was expanded to include an unlimited number of Class C shares, an unlimited number of Class D shares and an unlimited number of Class E shares, each issuable in series and an unlimited number of Class C Preferred shares, an unlimited number of Class D Preferred shares and an unlimited number of Class E Preferred shares, each issuable in series.

Preferred shares and Class A shares may be surrendered at any time for retraction at specified retraction amounts. Holders of Preferred shares and Class A shares may concurrently retract one Preferred share and one Class A share on an October 31 valuation date at their net asset values. Following the reorganization in 2010, the monthly retraction prices for shares retracted at any other valuation date or not retracted concurrently at an October 31 valuation date (collectively, a “Valuation Date”) are calculated as follows. Class A shares retracted on a Valuation Date will be entitled to receive a retraction price per share equal to the lesser of: (i) the Class A NAV retraction price; and (ii) 96 percent of the difference between (a) the Unit market price and (b) the cost to the Fund of purchasing a Preferred share in the market for cancellation. Preferred shares retracted on a Valuation Date will be entitled to receive a retraction price per share equal to the lesser of: (i) the Preferred NAV retraction price; and (ii) 96 percent of the lesser of (a) the Unit market price less the cost to the Fund of purchasing a Class A share in the market for cancellation and (b) $15.00.

Net allocations on retractions of Class A shares represent gains on retractions where the price paid upon retraction is less than the carry ing value of the retracted shares. Under the terms of a Recirculation Agreement, the Fund may, but is not obligated to, require the Recirculation Agent to use its best efforts to find purchasers for any Preferred shares and Class A shares tendered for retraction. The Preferred shares rank in priority to the Class A shares and the Class A shares rank in priority to the Class B shares with respect to the payment of dividends and repayment of capital on the dissolution, liquidation or winding up of the Fund.

The holders of Class B shares are not entitled to receive dividends. The Class B shares are retractable at a price of $1.00 per share. Strathbridge owns all of the issued and outstanding Class B shares.

Class B shares are entitled to one vote per share. Preferred shares and Class A shares are entitled to vote on certain shareholder matters.

The Fund's Preferred shares have been classified as liabilities in accordance with Canadian GAAP. Accordingly, net income for the year is stated after Preferred share distributions.

During the year, 4,688,493 (2010 - 369,278) each of Preferred shares and Class A shares were redeemed with a total retraction value of $77,642,774 (2010 - $7,750,141).

Issued and Outstanding

	2011	2010
9,517,553 Preferred shares (2010 - 14,206,046)	**$ 142,763,295**	$ 213,090,690
9,517,553 Class A shares (2010 - 14,206,046)	**$ 130,877,706**	$ 144,206,687
1,000 Class B shares (2010 - 1,000)	**1,000**	1,000
	$ 130,878,706	$ 144,207,687

In December 2010, the Toronto Stock Exchange ("TSX") accepted a normal course issuer bid filed by the Fund. Under the terms of the normal course issuer bid, the Fund proposes to purchase, if considered advisable, up to a maximum of 947,069 Class A shares and 947,069 Preferred shares or approximately 10 percent of the Fund's public float as of December 7, 2010 as determined in accordance with the rules of the TSX commencing December 21, 2010. One Unit consists of one Class A share and one Preferred share. The Fund may not purchase more than 190,470 of its Units (representing approximately 2 percent of the Fund's issued and Units as of December 7, 2010) in any 30-day period under the bid. The purchases made pursuant to the normal course issuer bid will be made in the open market through the facilities of the TSX. The normal course issuer bid will remain in effect until the earlier of December 20, 2011, the termination of the bid by the Fund or the Fund purchasing the maximum number of Units permitted under the bid. Class A shares and Preferred shares purchased by the Fund pursuant to the issuer bid will be cancelled. As at October 31, 2011, nil Units have been purchased by the Fund.

On April 28, 2011, the Fund issued 9,523,493 warrants to Class A shareholders, on the basis of one warrant for each Class A share held. Two warrants entitle the holder to subscribe for one Unit (consisting of one Class A share and one Preferred share) of the Fund at a subscription price of $23.65. The TSX approved the listing of the warrants under the symbol PIC.WT and they commenced trading on May 9, 2011 and will remain trading until the expiry date of December 15, 2011. Warrants may be exercised only on the expiry date. During the year, the Fund incurred a cost of $150,633 for the warrant offering.

7. Management Fees and Expenses

Strathbridge, as Manager under the terms of the Management Agreement and as Investment Manager under terms of the Investment Management Agreement, received fees payable at annual rates of 0.10 percent and 0.80 percent respectively of the Fund's net asset value, calculated and payable monthly, plus applicable taxes.

The Fund is responsible for all ongoing manager, legal, accounting and audit fees as well as all other expenses incurred by the Manager in the ordinary course of business relating to the Fund's operations. The Fund is also responsible for commissions and other costs of portfolio transactions and any extraordinary expenses of the Fund which may be incurred from time to time.

8. Income Taxes

The Fund is a "mutual fund corporation" as defined in the Income Tax Act (Canada) (the "Act") and is subject to tax in respect of its net realized capital gains. This tax is refundable in certain circumstances. Also, the Fund is generally subject to a tax of 33 1/3 percent under Part IV of the Act on taxable dividends received in the year. This tax is fully refundable upon payment of sufficient dividends. The Fund is also subject to tax on the amount of its interest income that is not offset by operating expenses and share issue expenses.

The Fund is also a "financial intermediary corporation" as defined in the Act and, as such, is not subject to tax under Part IV.1 of the Act on dividends received nor is it generally liable to tax under Part VI.1 on dividends paid on taxable preferred shares.

Under the dividend policy of the Fund, premiums received in respect of written options that are still outstanding at year end are not to be distributed in the year to the shareholders. The premiums retained by the Fund are subject to a refundable tax. This tax was nil for 2011 (2010 - nil).

Accumulated non-capital losses of approximately $5.9M (2010 - $5.9M) and capital losses of $33.5M (2010 - $46.3M) are available for utilization against net investment income and realized gains on sale of investments, respectively, in future years. The capital losses can be carried back for 3 years and carried forward indefinitely. The non-capital losses expire as follows:

Expiration Date	**Amount (in $M)**
2028	**$ 3.7**
2029	**2.2**
Total	**$ 5.9**

The Fund has offset the future tax liability for refundable taxes payable with the refund expected upon payment of capital gains or ordinary dividends. As a result, the future tax liability for refundable taxes payable is eliminated.

9. Distributions

Preferred shares are entitled to a cumulative preferential quarterly dividend of $0.215625 per share payable on the last day of January, April, July and October in each year.

Following the fund extension in November 2010, the capital gains dividend gross-up entitlement of $0.068 per Preferred share was eliminated due to changes in Canadian tax laws that came into effect subsequent to the Fund's initial public offering, specifically to the effective tax rates on capital gains. In addition, the Fund is now permitted to make distributions to holders of Class A and Preferred shares in the form of returns of capital. Return of capital distributions are generally not subject to tax. However, returns of capital reduce the adjusted cost base of the shares in respect of which they are paid.

10. Transaction Fees

Total transaction fees paid for the year ended October 31, 2011 in connection with portfolio transactions were $135,967 (2010 - $278,347). Of this amount $14,334 (2010 - $52,774) was directed to cover payment of research services provided to the Investment Manager.

11. Capital Disclosures

Canadian Institute of Chartered Accountants ("CICA") Handbook Section 1535, "Capital Disclosures" requires the disclosure of: (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data and qualitative information about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The Fund's objectives, policies and processes are described in Note 3, information on the Fund's shareholders' equity is described in Note 6 and Note 9, and the Fund does not have any externally imposed capital requirements.

12. Financial Instruments and Risk Management

The Fund's financial instruments consist of cash, investments, receivables, payables, Redeemable Preferred shares and certain derivative contracts. In accordance with CICA Handbook Section 3862, "Financial Instruments - Disclosures", the Fund uses a three-tier hierarchy as a framework for disclosing fair value based on inputs used to value the Fund's investments. The hierarchy of inputs is summarized below:

(i) Level 1 - for unadjusted quoted prices in active markets for identical assets or liabilities,

(ii) Level 2 - for inputs, other than quoted prices included in Level 1, that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices), and

(iii) Level 3 - for inputs that are based on unobservable market data.

The following is a summary of the inputs used as of October 31, 2011 in valuing the Fund's investments and derivatives carried at fair value:

	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Short-Term Investments	$ –	$ 1,996,695	$ –	**$ 1,996,695**
Canadian Common Shares	196,890,595	–	–	**$ 196,890,595**
Options	–	(1,915,249)	–	**$ (1,915,249)**
Total Investments	**$ 196,890,595**	**$ 81,446**	**$ –**	**$ 196,972,041**

The following is a summary of the inputs used as of October 31, 2010 in valuing the Fund's investments and derivatives carried at fair value:

	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Short-Term Investments	$ –	$ 24,681,606	$ –	**$ 24,681,606**
Canadian Common Shares	223,640,904	–	–	**$ 223,640,904**
Options	7,535	(322,364)	–	**$ (314,829)**
Total Investments	**$ 223,648,439**	**$ 24,359,242**	**$ –**	**$ 248,007,681**

There were no transfers between Level 1 and Level 2 during 2011 and 2010.

As a result, the Fund is exposed to various types of risks that are associated with its investment strategies, financial instruments and markets in which it invests. The most important risks include other price risk, liquidity risk, interest rate risk and credit risk.

These risks and related risk management practices employed by the Fund are discussed below:

Other Price Risk

Other price risk is the risk that the value of financial instruments will fluctuate as a result of changes in market prices (other than those arising from interest rate or currency risk), whether caused by factors specific to an individual investment, its issuer, or all factors affecting all instruments traded in a market or segment. The Portfolio consists primarily of equity securities of the major Canadian banks. Net Asset Value per Unit varies as the value of the securities in the Portfolio varies. The Fund has no control over the factors that affect the value of the securities in the Portfolio, including factors that affect all the companies in the global financial services industry. The Fund's market risk is managed by taking a long-term perspective and utilizing an option writing program.

Approximately 99 percent (2010 - 77 percent) of the Fund's net assets, excluding the Redeemable Preferred Share liability, held at October 31, 2011 were publicly traded equities. If equity prices on the exchange increased or decreased by 10 percent as at October 31, 2011, the net assets, excluding the Redeemable Preferred Share liability, of the Fund would have increased or decreased by $19.7M (2010 - $22.4M) respectively or 9.9 percent (2010 - 7.7 percent) of the net assets, excluding the Redeemable Preferred Share liability, all other factors remaining constant. In practice, actual trading results may differ and the difference could be material.

The Fund employs a proprietary investment strategy, Strathbridge Selective Overwriting, to enhance the income generated by the Portfolio and to reduce volatility. In addition, the Fund may write cash covered put options in respect of securities in which it is permitted to invest. The Fund is subject to the full risk of its investment position in securities that are subject to outstanding call options and those securities underlying put options written by the Fund, should the market price of such securities decline. In addition, the Fund will not participate in any gain on the securities that are subject to outstanding call options above the strike price of such options. The Fund may also purchase put options. The Fund has full downside risk on invested positions which may be partially mitigated by the use of purchased put options. The risk to the Fund with respect to purchased put options is limited to the premiums paid to purchase the put options.

Liquidity Risk

Liquidity risk is the possibility that investments in the Fund cannot be readily converted into cash when required. To manage this risk, the Fund invests the majority of its assets in investments that are traded in an active market and can be easily disposed of. In addition, the Fund aims to retain sufficient cash and short-term investments to maintain liquidity and to meet its obligations when due. Liabilities are payable within one year except the Redeemable Preferred Share liability which matures on November 1, 2017 (see Note 6).

Cash is required to fund redemptions. Following the reorganization of the Fund, shareholders must surrender shares at least 10 business days prior to a valuation date and receive payment on or before 10 business days following such valuation date. Therefore the Fund has a maximum of 20 business days to generate sufficient cash to fund redemptions mitigating liquidity issues.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of a financial instrument. The financial instruments which potentially expose the Fund to interest rate risk are the short-term fixed income securities. The Fund has minimal sensitivity to change in rates since they are usually held to maturity and short-term in nature.

Credit Risk

In entering into derivative financial instruments, the Fund is subject to the credit risk that its counterparty (whether a clearing corporation, in the case of exchange traded instruments, or other third party, in the case of over-the-counter instruments) may be unable to meet its obligations. The Fund manages these risks through the use of various risk limits and trading strategies.

The credit risk is mitigated by dealing with counterparties that have a credit rating that is not below the level of approved credit ratings as set out in National Instrument 81-102.

The following are the credit ratings for the counterparties to derivative instruments that the Fund dealt with during the current and prior year, based on Standard & Poor's credit rating as of October 31, 2011 and October 31, 2010:

Dealer	Long-Term Local Currency Rating	Short-Term Local Currency Rating
Canadian Dollar		
Bank of Montreal	A+	A-1
Canadian Imperial Bank of Commerce	A+	A-1
Citigroup Inc.	A	A-1
National Bank of Canada	A	A-1
Royal Bank of Canada	AA-	A-1+
The Toronto-Dominion Bank	AA-	A-1+

The following is the credit rating for short-term investments held by the Fund based on Standard & Poor's credit ratings as of October 31, 2011:

Type of Short-Term Investment	Rating	% of Short-Term Investments
Bankers' Acceptances	A-1+	100%
Total		**100%**

The following are the credit ratings for short-term investments held by the Fund based on Standard & Poor's credit ratings as of October 31, 2010:

Type of Short-Term Investment	Rating	% of Short-Term Investments
Government of Canada Treasury Bills	AAA	60%
Province of Ontario Treasury Bills	AA	20%
Bankers' Acceptances	A-1	20%
Total		**100%**

The carrying amount of these investments represents their maximum credit risk exposure, as they will be settled in the short-term.

13. Future Accounting Policy Changes

The Fund was required to adopt International Financial Reporting Standards ("IFRS") for the year beginning on November 1, 2011. However, the Canadian Accounting Standards Board approved a two year deferral from IFRS adoption for investment companies applying Accounting Guideline 18 - Investment Companies. As a result, the Fund will adopt IFRS for the year beginning on November 1, 2013 and will issue its initial statements in accordance with IFRS, with comparative information, for the semi-annual period ending April 30, 2014.

Statement of Corporate Governance Practices

The Board of Directors of the Fund is responsible for the overall stewardship of the Fund's business and affairs. The Fund has investment objectives and investment strategies that are set out in the prospectus of the Fund. The Fund's manager, Strathbridge Asset Management Inc. (the "Manager"), administers many functions associated with the operations of the Fund pursuant to a management agreement entered into at the time the Fund issued its shares to the public. Under this agreement the Manager is responsible for certain day to day operations of the Fund including the payment of distributions on its shares and attending to the retraction or redemption of its shares in accordance with their terms.

The Board consists of five directors, three of whom are independent of the Fund. The Board believes that the number of directors is appropriate for the Fund and only directors independent of the Fund are compensated. Amounts paid as compensation are reviewed for adequacy to ensure that they realistically reflect the responsibilities and risk involved in being an effective director. Individual directors may engage an outside advisor at the expense of the Fund in appropriate circumstances subject to the approval of the Board.

To assist the Board in its monitoring of the Fund's financial reporting and disclosure, the Board has established, and hereby continues the existence of, a committee of the Board known as the Audit Committee. The Audit Committee consists of three members, all of whom are independent of the Fund. The responsibilities of the Audit Committee include, but are not limited to, review of the annual financial statements and the annual audit performed by the independent auditor and oversight of the Fund's compliance with tax and securities laws and regulations. The Audit Committee has direct communication channels with the independent auditor to discuss and review specific issues as appropriate.

The Board is responsible for developing the Fund's approach to governance issues and, together with the Investment Manager, is evolving a best practices governance procedure.

The Fund maintains an Investor Relations line (toll-free: 1-800-725-7172 or email: info@strathbridge.com) and website (www.strathbridge.com) to respond to inquiries from shareholders.

Board of Directors

John P. Mulvihill
Chairman & CEO,
Strathbridge Asset Management Inc.

John D. Germain
Senior Vice-President & Chief Financial Officer
Strathbridge Asset Management Inc.

Michael M. Koerner[1,2]
Corporate Director

Robert W. Korthals[1,2]
Corporate Director

Robert G. Bertram[1,2]
Corporate Director

[1] Audit Committee Member
[2] Independent Review Committee Member

Information

Independent Auditor:
Deloitte & Touche LLP
Brookfield Place
181 Bay Street, Suite 1400
Toronto, Ontario
M5J 2V1

Transfer Agent:
Computershare Investor Services Inc.
100 University Avenue, 8th Floor
Toronto, Ontario
M5J 2Y1

Shares Listed:
Toronto Stock Exchange
trading under
PIC.A/PIC.PR.A

Custodian:
RBC Dexia Investor Services Trust
RBC Centre
155 Wellington Street West, 2nd Floor
Toronto, Ontario
M5V 3L3

Visit our website at www.strathbridge.com for additional information on all Strathbridge Investment Funds.

Investment Funds Managed by Strathbridge Asset Management Inc.

UNIT TRUSTS

Canadian Utilities & Telecom Income Fund
Core Canadian Dividend Trust
Gold Participation and Income Fund
Premier Canadian Income Fund
Top 10 Canadian Financial Trust

SPLIT SHARES

Premium Income Corporation
S Split Corp.
Top 10 Split Trust
World Financial Split Corp.

PRINCIPAL PROTECTED FUNDS

Government Strip Bond Trust

Head Office:

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Toronto, Ontario
M5H 3T9

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Toll Free: 1 800 725-7172
Fax: 416 681-3901
e-mail: info@strathbridge.com

Contact your broker directly for address changes.

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