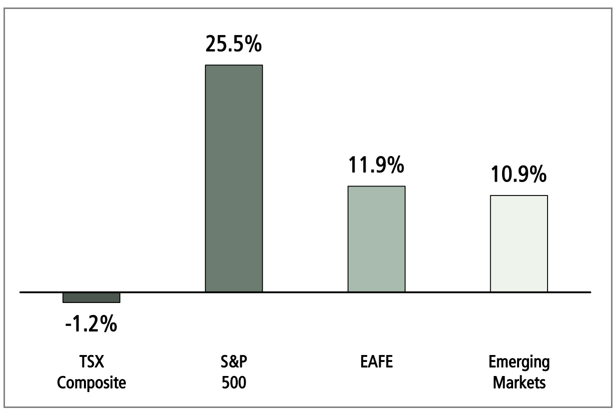
A Fading Bull Market

After a strong start to 2015, investment returns moderated in the past quarter. Many stock markets around the world posted small losses. For example, the principal Canadian stock market index, the TSX Composite, had a total return of -1.6%, strikingly similar to the return in the Canadian bond market of -1.7%. In the U.S., the S&P 500 stock index offered a return of -1.4% in Canadian dollars.[1] The story was much the same internationally. The MSCI EAFE Index (Europe, Australasia and the Far East) and the MSCI Emerging Markets Index each posted the identical return of -1.0% (in Canadian dollars).

Notwithstanding the decline in the second quarter, year-to-date and 12-month returns remain good. Principally, this is the result of strong performance by non-Canadian stocks. The sharp decline in the Canadian dollar in the first months of the year provided a significant tailwind for Canadian investors investing in foreign markets. Of course, the steep decline in energy prices also weighed on the Canadian market more heavily than others.



Total C$ Returns for Year Ended June 30, 2015

We predicted as we entered 2015 that, after a six-year bull market, investment returns were almost certain to be more modest going forward. Market returns in the quarter may well be a signal that heady returns are fading into the sunset.

Peloponnesian Problems

Typically, the Nexus Report begins with the most fundamental driver of our investment outlook – the economic environment in Canada and the U.S. However, Greece has stolen the spotlight in recent weeks. On July 5, the Greek people voted "No" to the proposition that Greece agree to further measures of fiscal austerity demanded by other European nations in exchange for additional liquidity for the Greek financial system. The "No" vote throws Greece into even greater crisis and raises the spectre that it could be forced to withdraw from the European Monetary Union. Greece would go back to the Drachma and the country would be thrown even deeper into economic depression.

We can't possibly predict how this will play out and the likely consequences for financial markets. We know for sure that Greece can never repay all the money it has borrowed. The good news is that the vast majority of the debt is now held by various governmental entities like the European Central Bank and the International Monetary Fund. There is little risk of a cascading series of bank failures such as might have occurred should Greece have defaulted on a massive amount of debt held by private entities. As well, it is important to remember that the Greek economy is about the same size as British Columbia's. A withdrawal from the Eurozone will be very bad for the Greek people, but it won't have much of a direct impact on global growth or global financial stability.

The more significant concern about Greece is the potential for secondary effects. Much larger European nations (like Italy and Spain) also owe staggering amounts of money. If Greece "gets away with" a default, maybe they can too? If Greece leaves the European Monetary Union, maybe they can too? What is of greatest concern is the precedent that could be set as the current Greek crisis is resolved. We are in unchartered waters. Also of concern is what would happen when or if Greece actually defaults on large quantities of its debts. Public entities like the European Central bank would suffer losses and its member countries would have to shore up the ECB's balance sheet. Inevitably, this would pressure interest rates higher across the Eurozone, a force that would not be positive for Europe's fragile economies. Perhaps some compromise will be reached, but the risk presented by the current crisis is real and rising.

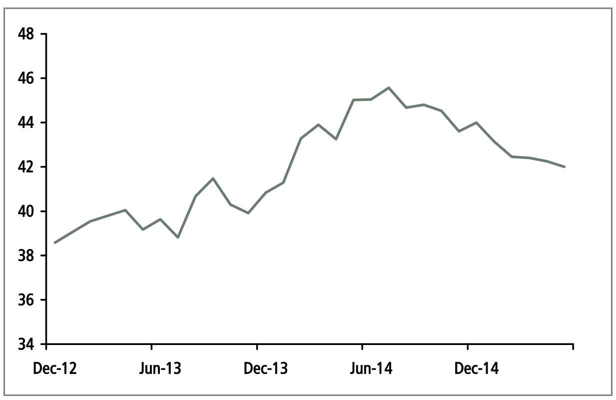
Recession Risk at Home

The burning question debated by Canadian economists at the moment is whether we will slide into recession. Late in March, Bank of Canada Governor Poloz warned that first quarter economic

[1] In US$ the S&P 500 total return was +0.3%. A modest recovery in the C$ turned the return negative when converted to C$.

performance in Canada was likely to be "atrocious". Investors were shocked by his blunt description, and taken by surprise by his dire outlook. Economic performance since then has been weak, but possibly less bad than Poloz imagined. Still, dark clouds loom over the Canadian economy at the same time as the Greek tragedy unfolds.

Recently, it was announced that Canada's trade deficit in May widened to $3.3 billion, the second worse deficit on record. Most of this was driven by a 0.6% decline in exports. We are an export-oriented nation and others are not buying as many of our goods as they were. It would be easy to blame this on the turmoil in energy markets, but energy exports actually increased 1.3% in May. It is significant weakness in forestry, machinery, electronics and metals that are leading the decline. In fact, over the last five months, non-energy exports have declined in four. In the context of this trade data, it seems very likely that second quarter GDP will contract. This would be the second quarter in a row for economic contraction, the technical definition of a recession.



Canada Total Exports (C$ billions)

While Canada's economy may well achieve the technical definition of a recession, we think a more pragmatic assessment would come to a different conclusion. Weakness has been focused in certain industries and in certain regions of the country (Alberta and Saskatchewan). There is not a broad-based decline in economic activity. Auto and home sales remain strong, and labour markets are generally healthy. While there is a growing consensus that the Bank of Canada will cut interest rates to support the economy, we maintain a slightly more sanguine view than some. The Canadian economy is likely to remain sluggish for some time but, especially with some improvement in the U.S., is not likely to endure a full-blown recession.

Better Days Ahead for the U.S.

The pace of the U.S. economic recovery remains disappointing. Last quarter we discussed how severe winter weather in the Northeast and a port strike in the West crimped domestic economic activity. The strong U.S. dollar weighed on the export sector. Undoubtedly, some of these headwinds have yet to abate. As a result, the U.S. labour report for June revealed that slightly fewer jobs were created than expected. As well, expected increases in average hourly earnings failed to materialize. Since labour markets have been generally good, this recent disappointment took investors by surprise. Some investors also were concerned by the decline in the labour force participation rate to 62.6%, the lowest level since October 1977.

Still, many economic indicators in the U.S. remain positive. Consumer confidence and home sales are strong, and while auto sales disappointed in June they remain at very healthy levels. We believe the U.S. economy is poised to be stronger in the second half of the year, which should allow the Federal Reserve to commence its long awaited normalization of interest rates.

Turbulent Times

Investors understandably are nervous about the period ahead. Weak economic performance in Canada and the U.S provides little insulation from a deepening Greek crisis. On the other side of the globe, the domestic Chinese stock market has collapsed, down 32% (at the time of writing) from its mid-June peak. While it is easy to dismiss this as an inevitable correction following a debt-fueled bubble created by Chinese retail investors over the last year, it certainly poses a risk to financial market stability in that part of the world. Perhaps bonds are a good place to ride out the storm? In our mind, bonds provide important short-term stability in a portfolio, but the paltry 0.68% yield on a Government of Canada 5-Year bond is not a sensible solution for a long-term investment portfolio.

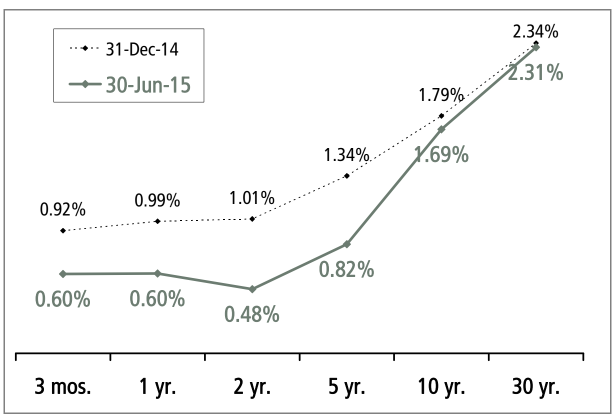
High quality equities remain the only real solution for long-term investors. Turbulence is a part of investing that we all must endure from time to time. After six years when markets have hardly corrected, it is easy to forget the financial crisis of 2008 and 2009. Yet periods like this should be expected, even if they can't be predicted. By sticking to a sensible investment strategy and with high-quality equity securities, clients will endure the current uncertainty just as securely as they have other periods of turmoil.

Asset Class Investment Review

Fixed Income

Fuelled by a surprise cut in the Bank Rate to start the year, bond yields had declined sharply in the first quarter. However, in the second quarter, yields of longer-maturity bonds drifted almost back to their starting levels at the beginning of the year, while rates of shorter-maturity bonds remained at multi-generational low levels. As a result, the yield curve has steepened (pictured below) and some of the first quarter's gains were given back in the second quarter as longer maturity bonds declined in value. In the quarter the FTSE TMX Bond Universe Index[2] (the Bond Index) returned -1.7%, resulting in a return of 2.4% for the year to date. Our returns, using the bonds in the Income Fund as a proxy, fared better. In the second quarter, the return was -0.6% and for the year-to-date our return has been +3.2%.

Longer-term yields drifted higher this quarter due to growing evidence of an improving U.S. economy which will necessitate a reduction in the amount of monetary stimulus that comes from ultra-low interest rates. Of particular note is the improvement in labour markets, housing activity and retail sales activity.[3]



Government of Canada Yield Curve

In anticipation that the U.S. Federal Reserve would respond to improving economic performance, investors paid close attention to both the official press release from the U.S. Federal Reserve following its June meeting, as well as Governor Yellen's press conference afterward. However, the Fed and Governor Yellen did a fine job of leaving open some uncertainty as to when the highly accommodative monetary policy might change. For our purposes, it really doesn't matter whether the first interest rate will come in September or December. We believe that over the next 18 months a growing recovery will ultimately drive a series of official interest rate increases, resulting in a less than rewarding return from bond investments. Accordingly, our portfolio remains concentrated in bonds of shorter maturity where the price effect of interest rate increases is more muted.

It's worth noting that the improvement we see in U.S. economic activity has not yet been matched in Canada. In fact, there is growing speculation that the Bank of Canada will again cut interest rates to add a further boost to our labouring economy. In our opinion, the primary cause of sub-optimal economic performance in Canada is low energy prices, an issue that can't really be addressed with even lower interest rates. So it would surprise us if this happens. In fact, there is a risk that lower rates will contribute to even higher personal debt levels that will create imbalances in housing and other asset prices that will be extraordinarily disruptive when unwound. Eventually, strong U.S. growth will make its effect felt on this side of the border and Canada's economy will improve. For now, we think another rate cut would be the wrong medicine. But the steepening of the curve, described above, is a direct result of anticipation that the Bank of Canada could cut rates yet again.

Our outlook for the balance of the year is unchanged from last quarter. We foresee a long-term trend to higher interest rates that should produce flat returns from bond investments. Our portfolio has a short duration (4.4 years) and we retain a bias to higher rated securities. We are positioned to redeploy our investments when longer term yields eventually are more attractive.

Equities

After a long strong run, the second quarter of 2015 was a period of indigestion for equity investors. The Canadian equity market was down 1.6%. The S&P 500's small positive return of 0.3% in U.S. dollars was a loss of 1.4% when measured in Canadian

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[2] Formerly the DEX Universe Bond Index.

[3] On July 2nd the BLS reported that the unemployment rate fell to 5.3%. In late June, despite the effect of lower energy prices, the year-over-year growth rate of retail sales accelerated to 2.7% and the National Association of Home Builders Index rose to its best level in almost ten years.

dollars (as the US dollar weakened against the the Canadian dollar over the quarter).[4]

As an indicator of performance, the Equity Fund was down 1.3%% in the quarter, but returned a very strong 13.9% over the past twelve months. The Fund slightly outperformed its benchmark in the quarter and was ahead by 3.5% for the last twelve months.[5]

Of note, the Canadian equity market has recently provided poor returns, down 1.2% in the last twelve months. This stands in stark contrast to the rest of the world. (Each of the S&P 500, International and Emerging Markets Indices were up double digits measured in Canadian dollars.) Now is a good time to reflect on the benefit of a well diversified equity approach. Our non-Canadian holdings (U.S., international and emerging markets) drove the Equity Fund's 13.9% overall return in a period where the typical Canadian-only equity investor experienced a loss.

As we have stated for some time, the relentless positive pace of the equity markets had to slow. It looks like it has. Regardless, we reiterate that we believe that "time in the markets" with a quality equity portfolio will beat "timing the markets" over the long term.

Canadian Equities

Nexus Canadian stocks were down 2.8% in the quarter and down 0.4% over the last twelve months. This was slightly behind the TSX Composite's -1.6% return for the quarter and slightly ahead of the TSX's -1.2% for the twelve months.

The poor Canadian equity market return reflects Canada's high exposure to the poorly performing energy and materials sectors, and the knock-on effect on other sectors of the economy.

For our holdings, the quarter reflects a mix of relatively small ups and downs. Over the twelve months, the main drag on our portfolio has been our energy holdings, but thankfully they are only a small component of the Canadian equity portfolio and smaller yet in the context of clients' overall portfolios.

During the quarter, we added to ATCO and trimmed Enbridge, principally due to the substantial valuation difference between the two. We sold one small position, Trican Well Service, which has been severely damaged by the slowdown in the energy sector. We had intended to hold the stock through the trough, but sold as it became apparent that the uncertainty presented by the energy royalty review of the new NDP government in Alberta will delay any recovery.

U.S. Equities

Nexus U.S. equities were close to break-even in the quarter, down 0.2%. After a strong run, the weaker U.S. dollar in the past 3 months reduced our U.S. equity returns by about 1.7% points in Canadian dollars. The twelve month return on our U.S. equity stocks has been exceptionally strong, up 31.6%, and well ahead of the S&P 500 return of 25.5%.

In the quarter, our financial holdings did well. Indeed, we feel that many of the headwinds that have impeded the U.S. banks – litigation, regulatory change, and slow economic growth – are abating. In the second quarter we established a new holding, M&T Bank, a "Main Street" bank in the U.S. northeast. M&T has a strong record of profitability, growth and capital strength. Indeed, it has not experienced a quarterly loss since 1976 and was one of only two major U.S. banks that did not cut its dividend in the credit crisis. M&T's take-over offer for Hudson City Bancorp has been delayed and there is a chance that it will not be completed. This presents both risk and opportunity (in the form of a lower than usual valuation) and we made a calculated decision to invest.

International Equities

We continue to hold two non-North American equity investments within our Balanced and Equity Funds. These are two externally-managed pooled funds called EQIT (international developed market equities) and EMEC (international emerging market equities).[6]

EQIT was up 0.5% in the second quarter and EMEC was down 3.7%. They were +15.6% and +8.4% respectively over the twelve months.

[4] Except where indicated, U.S. and international returns are measured in Canadian dollars.

[5] All the return data in the Equities section are for the Equity Fund. Equity returns within the Balanced Fund were similar. For more specific performance, please refer to the Fund reports in this document or your client-specific report.

[6] Both funds are managed by teams from JPMorgan Asset Management based in London, England.

Pooled Fund Reports

Nexus North American Equity Fund

After a good start in the first 3 months of the year, the Nexus North American Equity Fund had a weak quarter, declining 1.3%. This result was marginally better than our benchmark which declined 1.4% for the same period. Thankfully, returns for longer periods remain excellent. The Fund returned 13.9% in the last 12 months, nicely ahead of the 10.4% return of our benchmark. More importantly, the Fund continues to provide attractive relative and nominal returns for longer holding periods. Over the last ten years, the Fund has generated an annual average return of 8.4%, well above the 7.4% return from the benchmark. More detail of the Fund's performance is laid out in the table below.

Much of the weakness this quarter came in June as uneasiness regarding Greece affected capital markets. However, because Greece's status in the Eurozone is unlikely to affect global economic growth, we believe that investors with a long-term view have moved past worrying that its fundamental budgetary and fiscal imbalances would derail the global economic recovery or have a major lasting effect on the Eurozone economy. In fact, bringing the crisis to a head, such as has been created by the referendum, is probably a necessary step in getting people past the event.

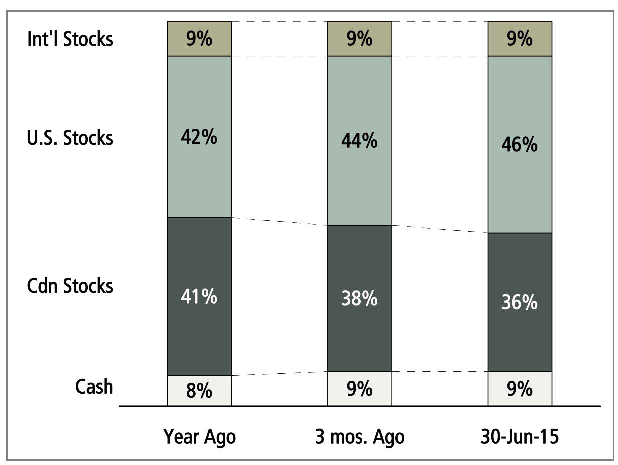
Somewhat counter-intuitively, another drag on markets were growing signs of economic recovery in the U.S. Conventionally, economic expansion is associated with revenue and earnings growth and acts as a support for equity valuations. But at present, it will also be associated with a move away from the ultra-easy monetary policy that has been pursued by the U.S. Federal Reserve for many years. Low interest rates have provided a powerful underpinning to equity prices. So investors, particularly those with a short-term orientation, were unnerved by the growing consensus that the Fed would begin to raise the target rate for federal funds before the end of 2015. A more detailed explanation of developments in equity markets appears earlier, in the Asset Class Review section of this report.

Our cash position is 9%, the same as it was at the end of the prior quarter and above our notional target of 5%. We remain in no particular hurry to get capital deployed. In the current environment, we want to be sure that we emphasize quality and long-term growth potential with our selections. At 36%, our allocation to Canadian stocks is just below where it was when we last reported, and our U.S. allocation is up slightly to 46%. The balance of 9% is invested outside of North America through our holdings of EQIT and EMEC.

	Equity Fund	Cdn Stocks	U.S. Stocks	Int'l Stocks
Quarter				
Fund	-1.3%	-2.8%	-0.2%	-1.5%
Benchmark	*-1.4%*	*-1.6%*	*-1.4%*	
One Year				
Fund	13.9%	-0.4%	31.6%	12.1%
Benchmark	*10.4%*	*-1.2%*	*25.5%*	

Returns are presented before deduction of management fees. Benchmarks are (a) for the Fund: 5% FTSE TMX 91-Day T-Bill, 50% TSX, and 45% S&P 500 (in C$) (rebalanced monthly); (b) for Cdn Stocks: TSX; and (c) for U.S. Stocks: S&P 500 (in C$).

Investment Returns – As at June 30, 2015



Equity Fund Asset Mix

Nexus North American Balanced Fund

After a good start in the first 3 months of the year, the Nexus North American Balanced Fund had a weak quarter, declining 1.1%. This result was better than our benchmark, which declined 1.4% for the same period. Thankfully, returns for longer periods remain excellent. The Fund returned 11.4% in the last twelve months, nicely ahead of the 7.5% return of our benchmark. More importantly, the Fund continues to provide attractive relative and nominal returns for longer holding periods. More detail of the Fund's performance is laid out in the table below.

In the bond market, we continue to emphasize a portfolio of shorter-dated, higher-quality bonds. As such, our holdings were less affected than was the Bond Index by the increase in interest rates which occurred this quarter. Returns for this portion of the Fund were -0.6%, disappointing on an outright basis, but ahead of the Bond Index loss of -1.7%. This quarter, we adjusted our holdings in two ways to increase our emphasis on quality. We have reduced our exposure to Alberta bonds, believing that the policy priorities of the new NDP government will undermine the financial condition of Alberta and that it will be a more frequent borrower in public debt markets. As well, we reduced our already small allocation to BBB credits in order to increase the liquidity of our holdings. A more detailed explanation of developments in bond markets appears earlier in the Asset Class Review section of this report.

Equity markets were weak this quarter. In Canadian dollar terms, Canadian, U.S. and international indices all declined over the period. Much of the blame was associated with Greece's precarious status in the Euro zone. In our opinion, investors with a long-term view have moved past worrying that Greece's budgetary and fiscal imbalances would derail the global economic recovery or have a major lasting effect on the Eurozone economy. In fact, bringing the crisis to a head, whether through the referendum process or by missing a € 1.6 billion loan repayment to the IMF, is actually a necessary step to bring this issue to a conclusion.

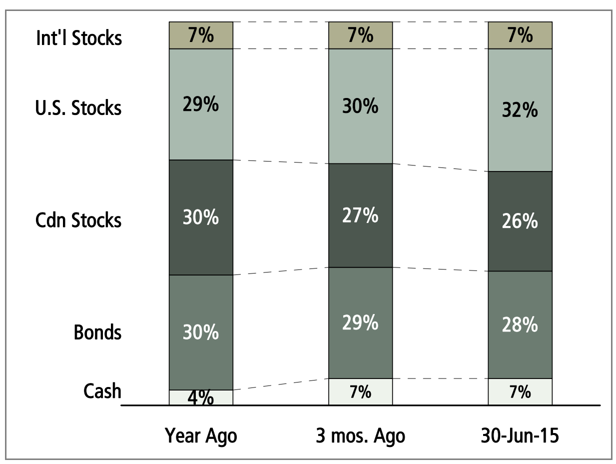
Somewhat counter-intuitively, another drag on markets were growing signs of economic recovery in the U.S. Conventionally, economic expansion is associated with revenue and earnings growth and acts as a support for equity valuations. But at present, it will also be associated with a move away from the ultra-easy monetary policy that has been pursued by the U.S. Federal Reserve for many years. Low interest rates have provided a powerful underpinning to equity prices. So investors, particularly those with a short-term orientation, were unnerved by the growing consensus that the Fed would begin to raise the target rate for federal funds before the end of 2015. A more detailed explanation of developments in equity markets appears earlier in the Asset Class Review section of this report.

Our asset allocation changed only modestly from last quarter. The cash position is 7%, bonds are 28% and the balance, 65%, is in stocks. Within equities, our holdings are more heavily weighted outside of Canada.

	Balanced Fund	Bonds	Cdn Stocks	U.S. Stocks	Int'l Stocks
Quarter					
Fund	-1.1%	-0.6%	-2.8%	-0.5%	-1.0%
Benchmark	*-1.4%*	*-1.7%*	*-1.6%*	*-1.4%*	
One Year					
Fund	11.4%	5.8%	-0.2%	30.5%	13.0%
Benchmark	*7.5%*	*6.3%*	*-1.2%*	*25.5%*	

Returns are presented before deduction of management fees. Benchmarks are (a) for the Fund: 5% FTSE TMX 91-Day T-Bill, 30% FTSE TMX Universe Bond, 40% TSX, and 25% S&P 500 (in C$) (rebalanced monthly); (b) for Bonds: FTSE TMX Universe Bond; (c) for Cdn Stocks: TSX; and (d) for U.S. Stocks: S&P 500 (in C$).

Investment Returns – As at June 30, 2015



Balanced Fund Asset Mix

Nexus North American Income Fund

A correction in prices of longer-dated bonds produced an uncommon quarter of negative returns in the bond market. The Nexus North American Income Fund declined 0.9% this quarter, but has returned +2.8% in the year-to-date. This compares favourably to the performance of the Fund's benchmark, the Bond Index which declined 1.7% over the quarter and is up 2.4% for the year to date. More detail of the Fund's performance is laid out in the table below.

We continue to emphasize a portfolio of shorter-dated, higher-quality bonds. Our maturities are concentrated between two and seven years. With a portfolio duration of 4.4 years, we have substantially less interest rate exposure than does the Bond Index, which has a duration of 7.4 years. After the bond market saw record low yields late in the first quarter, yields of longer maturity bonds have drifted higher. It is our belief that we are in the earliest stages of a trend to higher rates, driven by improving economic performance in the United States as well as Europe and much of the rest of the world. A more detailed explanation of developments in bond markets appears earlier, in the Asset Class Review section of this report.

This quarter, we adjusted our holdings in two ways to increase the emphasis on quality. For many years, Alberta bonds have traded at a tighter spread to Canada bonds than other provinces' bonds. This owed both to its credit standing and because its bonds had "scarcity value". With the recent election of an NDP government, we made the decision to replace almost all of our Alberta exposure with bonds issued by Canada Housing Trust. Combined with the effects of lower energy prices, we think the policy priorities of the new government will undermine the financial condition of Alberta and that it will be a more frequent borrower in public debt markets.

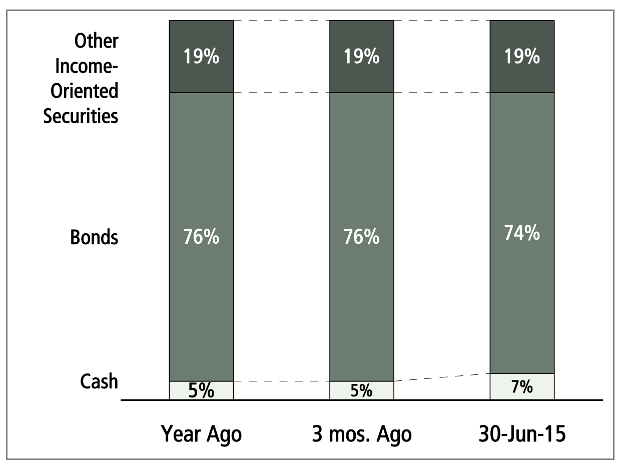
A lingering concern of ours is that liquidity in the bond market will suffer when investors, who have used the bond market as a safe haven, decide they want to re-allocate to "riskier" securities such as equities. In many instances these investors have emphasized higher-yielding, lower-credit quality bonds as a means of positioning. This quarter, we decided to reduce our already small allocation to BBB credits in order to increase the liquidity of our holdings. We do not forecast a liquidity problem, but we would like to favour the side of caution in the event that the situation changes.

Looking at asset mix, there is almost no change from the previous quarter. We remain almost fully invested in the "Other Income-Oriented" sector, with an allocation of 19%, our core bond holdings represent 76% of the Fund, and cash makes up the balance at 5%.

	Income Fund	Bonds	Cdn Stocks	U.S. Stocks
Quarter				
Fund	-0.9%	-0.6%	-4.1%	3.9%
Benchmark	*-1.7%*	*-1.7%*		
One Year				
Fund	6.5%	5.9%	5.2%	32.4%
Benchmark	*6.3%*	*6.3%*		

Returns are presented before deduction of management fees. Benchmarks are (a) for Fund: FTSE TMX Universe Bond; (b) for Bonds: FTSE TMX Universe Bond.

Investment Returns – As at June 30, 2015



Income Fund Asset Mix

Financial Market Summary

Market Levels

Canada	June 30, 2015	December 31, 2014
TSX Composite Index	14,553	14,632
91-Day T-Bill Yield	0.58%	0.91%
30-Year Government of Canada Bond Yield	2.30%	2.33%
Prime Rate	3.00%	3.00%
Exchange Rate (US$ per C$)	0.8006	0.8620

United States		
Dow Jones Industrial Average	17,620	17,823
Standard & Poor's 500 Index	2,063	2,059
30-Year U.S. Treasury Yield	3.12%	2.75%

Market Returns for Periods Ended June 30, 2015 [1]

	Last Quarter	Last 12 Months	Last 5 Years [2]	Last 10 Years [2]
FTSE TMX 91-Day T-Bill Index	0.2%	0.9%	0.9%	1.8%
FTSE TMX Universe Bond Index	-1.7%	6.3%	5.1%	5.0%
TSX Composite Index	-1.6%	-1.2%	8.3%	6.9%
S&P 500 Index (in C$)	-1.4%	25.5%	21.2%	8.1%
MSCI EAFE Index (in C$)	-1.0%	11.9%	13.2%	5.3%
MSCI Emerging Markets Index (in C$)	-1.0%	10.9%	7.1%	8.3%

Notes:

[1] Market returns represent total returns, including income and capital appreciation (or depreciation).
[2] Market returns are compound annual rates for periods of more than 1 year, but are not annualized for shorter periods.