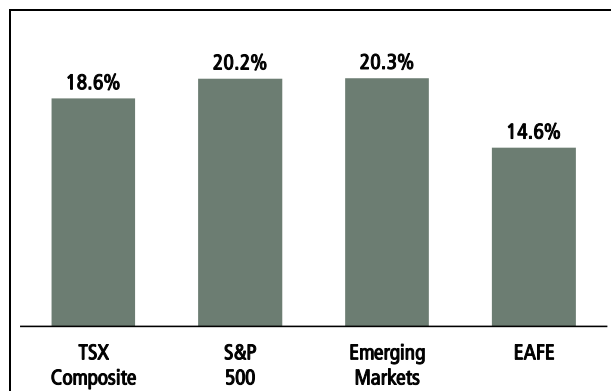


## Up, Up and Away

The first quarter of 2017 offered investors around the world much to smile about. Three months ago we wrote about how the U.S. stock market moved sharply higher after Donald Trump's surprise election victory – a reaction even more surprising than the election victory itself. The so-called "Trump Bump" continued through much of the past quarter and the S&P 500 Index posted a strong total return (in US dollars) of 6.1%. Moreover, the market environment throughout the quarter was both positive and relatively tranquil. The VIX, which is a measure of volatility and some see as a "fear gauge", posted its second lowest quarterly average ever recorded. Similarly, the daily average percent change for the Dow Jones Industrial Average was the lowest seen since 1965.

In comparison, first quarter returns in Canada were decent but more modest than in the U.S. The TSX Composite generated a total return of 2.4%. International stocks were the best of all as EAFE (international developed markets) generated a total return in Canadian dollars of 6.3% and Emerging Markets posted a 10.5% total return.

These solid quarterly rises capped off a wonderful 12-month period for stock markets around the world. As demonstrated in the chart below, what's not to like?



Returns for 12 Months Ended March 31, 2017<sup>1</sup>

## Good Economic News Abounds

To be sure, some of the rise in the U.S. stock market relates to optimism about Trump's proposals to lower taxes and loosen regulation, and the positive

impact that this is likely to have on corporate earnings. However, the bigger factor affecting the U.S. and other markets around the world is simply the clear improvement in economic fundamentals.

For several quarters, we've discussed the steady growth of the U.S. economy. At the heart of this strength has been the labour market, which continued to improve over the past quarter. Both January and February were strong months for job creation. While March's non-farm payroll report of 98,000 new jobs fell short of expectations, the three-month average of 178,000 new jobs per month is excellent. Moreover, the household survey for March suggested stronger job growth than the non-farm report, and the official unemployment rate fell to 4.5% even as more Americans joined the work force. By any measure, an unemployment rate this low reflects robust business conditions.

In addition to the strong labour market, many other "hard" economic statistics – such as housing – remain on a steadily improving trend. What has really accelerated, however, are the "soft" statistics, particularly various sentiment measures. For example, the National Association of Independent Business small business optimism survey recently hit its highest level in 12 years and the University of Michigan Consumer Confidence Survey recently hit its highest level in 17 years.

In Canada, the economic outlook is improving but remains a bit of a quandary. In contrast with the U.S., we've had a cautious outlook on the Canadian economy for some time. The downturn in the energy sector hit Canada hard and the tax and regulatory burden has caused many companies to think twice about investing here. Nonetheless, over the last few months, several economic indicators suggest Canada may be turning the corner.

For example, the 0.6% increase in GDP in January took investors by surprise and represents the strongest month-over-month growth rate since 2011. Over the last three months, Canadian GDP grew at a 6% annualized rate, and at a 4% annualized rate over the last six months. At this pace, Canadian economic growth is likely to be stronger than that in the U.S. in 2017, and may well be the strongest in the G7. Employment reports also offer much reason for optimism. Canada gained 19,400 new jobs in March as compared to expectations for 5,000. Over the last 12 months, an incredible 276,000 new jobs have been added.

<sup>1</sup> Total returns in Canadian dollars.

On the other hand, there remain several factors for concern for Canadian investors. Despite the booming job market, wage growth has been weak. Statistics Canada reported that year-over-year wage growth was 1.1% in March, the weakest since 1998. In fact, wage growth has been below 2% for nine straight months. As well, after several strong months, economists were shocked to learn that Canada had a \$972 million trade deficit for February – a far cry from the \$600 million surplus expected. A 2.9% decline in non-energy export volumes was responsible and took almost every analyst by surprise.

Many wondered why Bank of Canada Governor Poloz remained cautious after the dazzling January GDP report, but this more recent data suggests his caution may be warranted. His caution also seems appropriate in the face of the worrisome escalation of real estate prices in several cities, but most particularly in Toronto. We do believe that the Canadian economy is gaining traction, but there remain many challenges.

At the same time that economic conditions seem brighter in Canada and the U.S., there also is better news overseas. Concerns about a downturn in China's economy have subsided, and Europe continues to improve. Indeed, we may be on the cusp of the first period of synchronized global growth that we have enjoyed in a long time.

## Political Risk Rising

Just as the economic backdrop for investors is improving, there has been a considerable increase in political risk. In the U.S., for example, the market appears to reflect great optimism that Trump's domestic economic agenda will be implemented quickly and effectively and that corporate earnings will benefit. However, confusion and chaos are rampant in Washington. After the abrupt withdrawal of the healthcare reform bill there should be serious concern about how smoothly future policy initiatives will move through Congress. We also worry that Trump's policies on immigration could undermine the access to skilled labour for many U.S. companies, particularly those in the technology sector. Last, but not least, is the possibility of a government shutdown in late April as the debt ceiling is breached once again. In sum, the risks to the U.S. economic

recovery from political dysfunction may not be fully priced into the market.

It's a big election year in Europe and a range of populist and extreme candidates have attracted surprising levels of support. Fortunately, the Dutch election resulted in victory for a mainstream politician, but the French election looms in May, and the German election in the fall. The possibility of a shocking and disruptive election outcome is small, but real. As well, the United Kingdom officially started the process of leaving the European Union in March. This is uncharted water and we expect the path to be anything but smooth.

Finally, in the category of great imponderables, the circumstances in North Korea and in Syria continue to deteriorate. Time will tell whether the recent U.S. missile strike on military targets in Syria will aid or harm the prospect for peace. Ironically, however, it is one of the few initiatives of the new U.S. administration that has achieved widespread domestic and international support.

## Investment Outlook

As we enter the ninth year of the equity bull market, it would be natural to expect more modest investment returns. However, the outlook for improved global growth gives us optimism that 2017 will be another satisfactory year for client portfolios. Moreover, after a strong post-election rally good sense seemed to return to markets in March. In fact, one of the best contrary indicators in the investing world corrected quite nicely. The American Association of Individual Investors survey saw bullish sentiment fall 16 points to 30.2% and bearish sentiment rise 12 points to 37.4%. Typically, when individual investors are bearish that portends positive investment returns, and vice versa.

While we see political risk as being elevated there is no easy answer or clear step one should take with portfolios. Accordingly, we focus on our time-tested approach of emphasizing quality and value. We are confident that portfolios will prosper as earnings improve, and preserve capital in the inevitable periods of turbulence that occur in every market cycle.

## Asset Class Investment Review

### Fixed Income

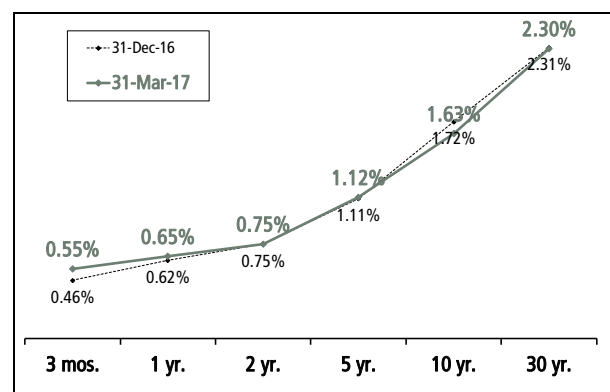
After yields had jumped sharply higher in the final quarter of 2016, this quarter the bond market lived up to its reputation as a boring subset of the capital markets. Benchmark 10-year Canada bonds began the year yielding 1.72% and traded in a range between 1.59% and 1.87%. They finished slightly stronger at a yield of 1.63%. Amazingly, the yield of 2-year, 5-year and even 30-year Canada bonds each closed within a few basis points of where they began the year (see chart). In an unsettled world, this might be just what is hoped for.

Conventionally, the U.S. Treasury market leads the Canadian bond market, and changes in U.S. Treasury yields typically come from unexpected strength (or weakness) in economic data or unexpected changes to central bank policy. However, yields are also heavily influenced by investor preference for risk (or safety). In uncertain times, bonds become more popular for their relative stability. Based on economic data, it might be argued that the U.S. economy was a bit stronger than expected and that interest rates should rise. In particular, labour market conditions were surprisingly strong<sup>2</sup>, as were surveys of business and consumer optimism that assess attitudes about future conditions. It's widely believed that the U.S. economic expansion is on a secure footing. If stronger economic data would have ordinarily pushed rates higher, investors' preference for safety in a time of political uncertainty probably kept rates lower than they might otherwise have been. Put another way, turmoil in Washington, Europe and in North Korea pressured yields lower than they might have been on economic fundamentals alone. As for central bank policy, in early February, the U.S. Federal Reserve met and made no changes to the fed funds rate. But in many speaking opportunities that came after, various Fed governors prepared the markets for a rate hike in March. Indeed, at their meeting that concluded on March 15th, the U.S. Fed raised the fed funds rate by a quarter of a point to a range of 0.75% to 1.00%. The bond market was well prepared for this "news" and bond prices hardly moved when it was announced.

<sup>2</sup> In each of January (238,000) and February (235,000) the increase in non-farm payroll employment was ahead of expectations and the unemployment rate remained at a level generally acknowledged to be full employment (about 5.0%).

In contrast, despite an encouraging January GDP report and strong labour markets<sup>3</sup>, Governor Poloz and the members of his governing council have used every opportunity to caution that Canada's economy faces several challenges and that no change to the Bank Rate should be expected. For now, we agree. Our economy depends on trade, particularly energy exports to the U.S. President Trump's protectionist rhetoric, combined with a large increase in domestic U.S. energy production, overhangs Canada's economic outlook. But if the protectionist fears do not play out, and energy prices continue to rebound, the case for exceedingly stimulative interest rates in Canada will fall away.

We still believe that interest rates in Canada will eventually drift higher. In preparation, the maturity profile in our bond portfolio remains shorter than the FTSE TMX Universe Bond Index (the Bond Universe). In the first quarter, both the Bond Universe and our portfolio returned 1.2%. In the last year, we outperformed modestly with our portfolio returning 1.8% as compared to the Bond Universe's return of 1.5%.



Government of Canada Yield Curve

### Equities

The first quarter of 2017 was a continuation of a very strong 2016 and, indeed, a very long and strong run that started in March, 2009 (as such, we are now 98 months into a bull market, and counting). As an indicator, the Equity Fund was up 4.0% in the

<sup>3</sup> After 26 consecutive months in deficit, the merchandise trade account was in surplus from October through to January and Canada's economy added more than 200,000 full-time jobs over the same period.

quarter and up 21.2% over the past 12 months.<sup>4</sup> In the quarter, all our equity asset classes – U.S., Canadian and international equities – did well, with stand-out performance from EMEC (11.4%) and EQIT (7.8%).

The Canadian dollar yo-yoed during the quarter, but, over the full quarter strengthened only slightly, up 1.0%, which modestly reduced the return on our U.S. equity holdings.<sup>5</sup> Over the last 12 months, our currency is weaker and had the effect of increasing the return of our U.S. equity holdings by 3 percentage points. Hopefully, one of these days we can stop reporting breathlessly on the antics of the Canadian dollar and go back to our regular programming.

### Canadian Equities

Nexus's Canadian stocks were up 3.6% in the quarter and 22.5% over the last 12 months. This was ahead of the TSX Composite's 2.4% return for the quarter and 18.6% for the 12 months.

For the quarter, our Utility holdings performed particularly well (ATCO and Brookfield Infrastructure Partners). Our Energy holdings were the weakest performers (all down noticeably), but so too was the entire Energy sector on the TSX, such that our limited exposure to Energy helped us relative to the TSX Index.

### U.S. Equities

Nexus's U.S. equities were up 4.0% in the quarter – on its own a good quarterly return, but we slightly trailed the S&P 500 return of 5.1%. The relative lag was largely due to stock-specific factors: PRA Group, Gilead, CarMax and GE were our weakest holdings in the quarter (all down), whereas our InfoTech holdings were strong and four of them had double digit returns. Our longer-term U.S. equity returns remain strong (20.0% annualized for 5 years and 10.3% annualized over 10 years.)

During the quarter we sold M&T Bank and Hewlett Packard Enterprise. M&T Bank has an excellent regional franchise in the U.S. Northeast, but its premium valuation and the tremendous run in all of our U.S. banks holdings over the past nine months (which resulted our having a heavy overweight in U.S. banks) led to the sale. Hewlett Packard

Enterprise has had a good recovery from earlier issues and, again, our big overweight in U.S. "value tech" was a key driver of the sale. As yet, we have not reinvested. While we are "okay" with the economic outlook, we are willing to remain disciplined. Investors in general have put a lot of faith in Trump and market valuations are full.

### Other Equity Investments

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

Anyone listening to the popular media may well think that Europe is crumbling, Trump is skewering trade with some emerging markets (China and Mexico), and others are collapsing due to domestic shenanigans (Turkey, Brazil, Russia, South Africa). In the face of this, EQIT was up 7.8% in the past quarter and has returned 18.6% over the last 12 months. EMEC has been even stronger, up 11.4% in the quarter and 23.3% for the 12 months. In recent quarters we have been reiterating our comfort with these investments and have bumped up our holdings within the Equity and Balanced Funds to what we think is around the limit within a North American mandate (the two holdings are now around 11% of our total equity exposure). Despite the recent run, both international developed markets and emerging markets have better dividend yields and substantially lower valuations than the S&P 500 and TSX Composite. Although they will remain prone to swings in investor sentiment, the prospects for these holdings remain strong. For more information on EQIT and EMEC, please see the Nexus International Equity Fund section of this report.

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<sup>4</sup> All the return data in the Equities section are total returns 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.

<sup>5</sup> Except where indicated, all U.S. and international returns are measured in Canadian dollars.

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<sup>6</sup> Both funds are managed by teams from JPMorgan Asset Management in London, England.

## Pooled Fund Reports

### Nexus North American Equity Fund

The Nexus North American Equity Fund generated a total return of 4.0% in the first quarter. This return compares to the 3.6% total return of the Fund's benchmark during the same period. In the last 12 months, the Fund has returned 21.2%, outpacing the benchmark return of 18.5%. From a longer-term perspective, our returns for the 2, 5 and 10-year periods remain at or above the benchmark and are very attractive on an outright basis.

More detail on the Fund's performance is presented in the table below.

In Canada, the equity market gained 2.4% in the quarter. Our Canadian holdings outperformed, delivering a 3.6% return. The main contributors to the Fund's relative performance in the first quarter were individual stocks, namely Brookfield Infrastructure Partners and ATCO. In addition, we avoided some of the weakness in the Energy sector during the quarter. On the negative side, we did not own any Materials stocks which detracted from performance as that sector performed well.

In the U.S., the equity market rose 5.1% in the quarter. Our U.S. holdings underperformed,

generating a 4.0% return. Our U.S. returns benefitted from our overweight positioning in the Information Technology sector and avoiding the Energy sector. Within Information Technology, Western Digital and Apple were both solid individual contributors. However, these positives were overshadowed by weak returns in the quarter from several individual U.S. stocks, including PRA Group, Gilead Sciences and CarMax.

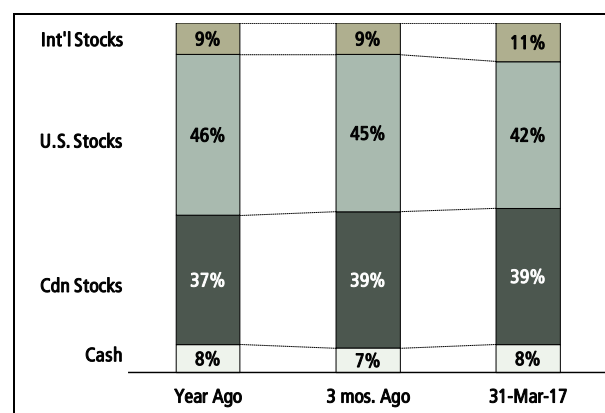
Our international holdings had a strong start to the year. The developed markets fund, EQIT, was up 7.8% this quarter and the emerging markets fund, EMEC, rose 11.4%.

At the end of the first quarter, the Fund's cash position was 8%. Our allocation to Canadian stocks was 39%, while U.S. stocks represented 42% of the mix. We have increased our allocation – to 11% – to markets outside North America and remain confident that this will provide important diversification to our North American investments.

	Equity Fund	Cdn Stocks	U.S. Stocks	Int'l Stocks
<b>Quarter</b>				
Fund	4.0%	3.6%	4.0%	9.2%
Benchmark	3.6%	2.4%	5.1%	
<b>One Year</b>				
Fund	21.2%	22.5%	25.7%	20.3%
Benchmark	18.5%	18.6%	20.2%	

Returns are presented before deduction of management fees. Benchmarks are (a) for the Fund: 5% FTSE TMX 91 Day TBill, 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 March 31, 2017



Equity Fund Asset Mix

## Nexus North American Balanced Fund

The Nexus North American Balanced Fund generated a total return of 2.9% in the first quarter. This return compares to the 2.6% total return of the Fund's benchmark during the same period. In the last 12 months, the Fund has returned 15.0%, exceeding the benchmark return of 12.8%. From a longer-term perspective, our returns for the 2, 5 and 10-year periods remain at or above the benchmark and are very attractive on an outright basis.

More detail on the Fund's performance is shown in the table below.

Our bond holdings returned 1.2% in the quarter, matching the return of the bond benchmark. Although the maturity of our bond portfolio remains shorter than the FTSE TMX Universe Bond Index, this positioning had little impact in the quarter as the yield of 2-year and 5-year Canada bonds each closed within a few basis points of where they began the year.

	Balanced Fund	Bonds	Cdn Stocks	U.S. Stocks	Int'l Stocks
<b>Quarter</b>					
Fund	2.9%	1.2%	3.3%	3.9%	8.8%
Benchmark	2.6%	1.2%	2.4%	5.1%	
<b>One Year</b>					
Fund	15.0%	2.1%	21.7%	24.3%	19.9%
Benchmark	12.8%	1.5%	18.6%	20.2%	

Returns are presented before deduction of management fees. Benchmarks are (a) for the Fund: 5% FTSE TMX 91 Day TBill, 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 March 31, 2017

In equities, our Canadian stocks outperformed their benchmark, led by strong returns from two stocks in the Utilities sector (Brookfield Infrastructure and ATCO). In contrast, our U.S. stocks lagged their benchmark, with PRA Group, Gilead Sciences and CarMax detracting from performance in the quarter.

Our international holdings delivered very strong performances to start the year. The developed markets fund, EQIT, was up 7.8% this quarter and the emerging markets fund, EMEC, rose 11.4%.

At the end of the quarter, cash represented 7% of the Fund's asset mix, bonds were 27% and stocks accounted for the remaining 66%. These asset allocations continue to remain close to the Fund's long-term guideline.

Int'l Stocks	6%	6%	7%
U.S. Stocks	34%	34%	33%
Cdn Stocks	26%	26%	26%
Bonds	29%	27%	27%
Cash	5%	7%	7%
	<b>Year Ago</b>	<b>3 mos. Ago</b>	<b>31-Mar-17</b>

Balanced Fund Asset Mix

## Nexus North American Income Fund

The Nexus North American Income Fund produced a total return of 1.7% in the first quarter. This compares to the 1.2% total return of the Fund's benchmark during the same period. In the last 12 months, the Fund has returned 5.6%, outperforming the benchmark return of 1.5%. From a longer-term perspective, our returns for the 2, 5 and 10-year periods remain at or above the benchmark and are very attractive on an outright basis.

More detail on the Fund's performance is displayed in the table below.

Our bond holdings produced a return of 1.2% in the quarter, matching the benchmark. Although the maturity of our bond portfolio remains shorter than

	Income Fund	Bonds	Cdn Stocks	U.S. Stocks
<b>Quarter</b>				
Fund	1.7%	1.2%	5.6%	1.7%
Benchmark	1.2%	1.2%		
<b>One Year</b>				
Fund	5.6%	1.8%	22.7%	24.0%
Benchmark	1.5%	1.5%		

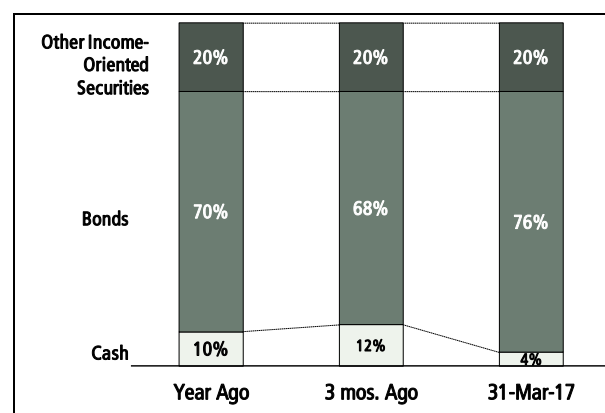
Returns are presented before deduction of management fees. Benchmarks are (a) for Fund: FTSE TMX Universe Bond; (b) for Bonds: FTSE TMX Universe Bond. In addition to bonds, up to 20% of the Fund's portfolio may be invested in equities.

Investment Returns – As at March 31, 2017

the FTSE TMX Universe Bond Index, this positioning had little impact in the quarter as the yield of 2-year and 5-year Canada bonds each closed within a few basis points of where they began the year.

The Fund benefitted from tailwinds provided by our Other Income-Oriented Securities: both our Canadian stocks (up 5.6%) and U.S. stocks (up 1.7%) delivered positive results in the quarter.

At the end of the first quarter, the Fund's cash position was 4%, Other Income-Oriented Securities accounted for 20% and the balance, 76%, was in our core bond holdings.



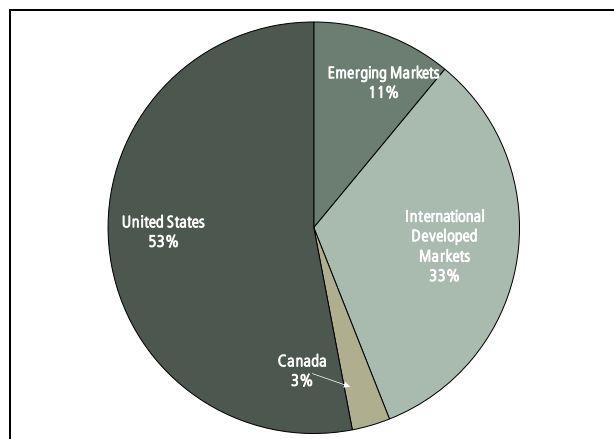
Income Fund Asset Mix

## Nexus International Equity Fund

The Nexus International Equity Fund (“NIEF”) holds two underlying funds: EQIT (invested in international developed market equities) and EMEC (invested in emerging market equities).<sup>7</sup>

In the first quarter, NIEF had a very strong return of 9.2% and was ahead of its blended benchmark return of 7.3%. This was comprised of a very good showing for EQIT (up 7.8%) and a strong return of 11.4% for EMEC. Over the past year, EQIT returned 18.6% and EMEC 23.3%.

Together, international developed markets and emerging markets are just under half of global equity markets.



Global Equity Market Capitalisation

There has been much negative news for international developed and emerging markets. In Europe, this includes Brexit, Greece, refugees and nationalist

movements. In Japan, figuratively, nothing is going on. In emerging markets, for some years now the strengthening US dollar has been materially reducing the dollar-denominated growth of emerging market companies’ earnings (the dollar is the common currency “lens” that emerging markets are typically viewed through by non-domestic investors). Finally, for some emerging market countries, terrorism, Trump’s trade rhetoric, corruption and fiscal deficits, have caused concerns.

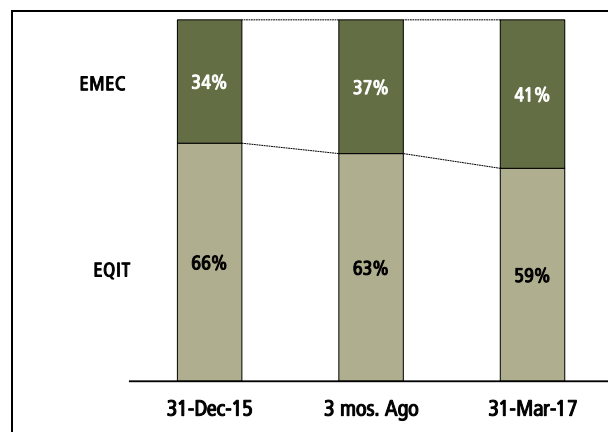
Despite the headlines, Europe is benefitting from a slow, but ongoing, decline in unemployment. Emerging markets are attractive due to their weak currencies. Today, this means that their exports are more competitive in developed markets. Longer term, if emerging market currencies strengthen over time, this will be a direct add-on to the investment return that foreign investors receive. JPMorgan analysis indicates that, if the basket of emerging market currencies reverted over time to their historic long-term *average* relative to the US dollar, this on its own would be a 33% total investor return measured in dollars, and this is before factoring in the higher rate of emerging market growth and its attractive valuation multiple. Emerging markets as a whole are trading just below their own long-term average valuation multiples and well below developed markets.

Over time we have bumped up the proportional holding of EMEC relative to EQIT. The proportions of EMEC and EQIT at the end of 2015 were 34:66, at the end of 2016 37:63, and are now at 41:59.

	International Equity Fund	EQIT	EMEC
<b>Quarter</b>			
Fund	9.2%	7.8%	11.4%
Benchmark	7.3%	6.3%	10.5%
<b>One Year</b>			
Fund	20.4%	18.6%	23.3%
Benchmark	16.1%	14.6%	20.3%

Returns are presented before deduction of management fees.  
 Benchmarks are (a) for Fund: 75% MSCI EAFE (in C\$) and 25% MSCI Emerging Mkts (in C\$) (rebalanced monthly); (b) for EQIT: MSCI EAFE (in C\$); and (c) for EMEC: MSCI Emerging Mkts (in C\$).

Investment Returns – As at March 31, 2017



International Equity Fund Asset Mix

<sup>7</sup> International developed markets or EAFE includes Europe, Australasia and the Far East. Emerging markets include 23 developing countries. EQIT and EMEC are managed by JPMorgan Asset Management in the UK.