Nexus Notes

July 2022
Vol. 27, No. 2

Featuring:

Invest *Thoughtfully*™

NEXUS

Our market-resilient investment strategy focuses on long-term results, providing investors with peace of mind through all stages of life.

Building Value for Clients

Since its establishment in 1988, Nexus has pursued an investment approach which concentrates on real growth in client wealth over the long term.

The chart illustrates the impact of this long-term investment thinking – a $100 investment in a balanced portfolio in 1989 has grown to $1,585 at June 30, 2022.

NEXUS

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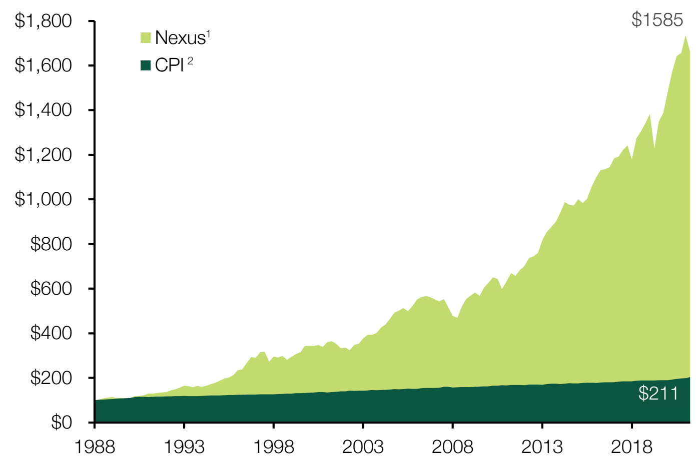
$100 Investment with Nexus in 1989



1 "Nexus" reflects the performance of a composite of Nexus accounts managed to a balanced mandate (until September 30,1997) and the Nexus North American Balanced Fund (thereafter). Returns shown prior to the deduction of investment management fees.

2 CPI is the "all-items" Consumer Price Index for Canada, not seasonally adjusted.

FROM THE EDITOR

The Bright Side

I recently read that the most popular song played at funerals in the UK was Monty Python's "Always Look on the Bright Side of Life." It's a song described as relentlessly optimistic, whose lyrics implore you to look at the positives in your life no matter what is happening.

A lot has been happening this year, but most of the headlines seem far from encouraging. Stock markets around the globe have been on a steady decline as the year has progressed. Inflation continues to be high, and supply chain problems are stubbornly persistent. There is still war in Ukraine, and let's not forget this is all happening under the umbrella of an ongoing global pandemic. Moreover, current events seem to be described with some version of "the worst in decades." At times like this, being told to grin at your troubles doesn't feel like sound advice.

But remaining hopeful that better times are coming is an essential part of being a long-term investor. People tend to assume that what's happened most recently will continue to happen. And when recent events have been negative, we develop a pessimistic outlook for the future. But when you look at events on a much longer timeline, you can see that things perhaps aren't so grim.

Last year at our annual client event, we had the good fortune to have Matt Ridley as a guest speaker, and like Monty Python, he's a product of the UK. He's the author of several books, including his most famous, "*The Rational Optimist.*" One of Matt's underlying messages is that not only has the world been getting better, but also the trend will continue in the future. And he outlines a compelling case for how innovation has been a cornerstone for those improvements. We can see this unfolding even now. As disheartening as current events seem, let's not forget that the course of the pandemic and its effects could have been much worse if a vaccine hadn't been created, and in record time no less. This is a great example of how innovation has a positive impact on the problems of the world, but also how great progress can get overrun by gloomy headlines.

While Ridley does argue that things are getting better rather than worse, his optimism for the future doesn't mean that everything in the world is fine, or that there aren't some areas or countries where things are getting worse. His view of optimism is on a global basis, rather than at a local level. But as individuals, how do we incorporate this viewpoint when assessing our own situations? One perspective is to focus on the things that we can control. This can be as simple as what we spend our money on or how much we set aside as savings. At Nexus, we can't predict the future and are faced with making investment decisions in an uncertain world. What we can control is our ability to stick with our investment discipline of investing in high-quality stocks that we believe are well-positioned for the long term. While this sometimes can feel like a waiting game, we are confident in this proven approach. And if you didn't have a chance to attend the Matt Ridley presentation last year, I recommend you view the recording on our website.

John Stevenson's most recent blog, "*The Long and Winding Road*" delves deeper into the current environment. Also, in this issue, Devin Crago describes some of the challenges in ESG investing, and Denys Calvin provides more information on upcoming changes known as the "Client Focused Reforms".

We are happy to welcome two more members to Nexus. Julie Crothers joins us as Vice President of Client Service and Business Development. And Ashleigh Oucharek joins our administrative team as a Portfolio Administrator. We are excited to welcome them to the team, and you can read more about both in our Inside Nexus section.

Brad Weber
CPA, CA, CFP

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To download a copy of this issue, or to access more resources go to: nexusinvestments.com/insights/nexus-notes-quarterly/

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The Long and Winding Road

by John C.A. Stevenson, CFA

Reading the newspaper is an unsettling activity these days. In almost every facet of life there is a concern that can rattle even the most stoic individual. Perhaps the most widespread of these is the surge of inflation. It is felt by us all when we stare at the total on the gas pump or look at our bill from the grocery store.

A year ago, central bankers were uniformly sanguine and insisted that price increases were "transient". But recently, prices have been rising at the fastest rate in 40 years and the increases are proving to be more persistent than anyone expected a year ago. A consequence is that a recent survey by the University of Michigan showed consumer confidence to be the lowest on record despite high levels of employment and excess savings.

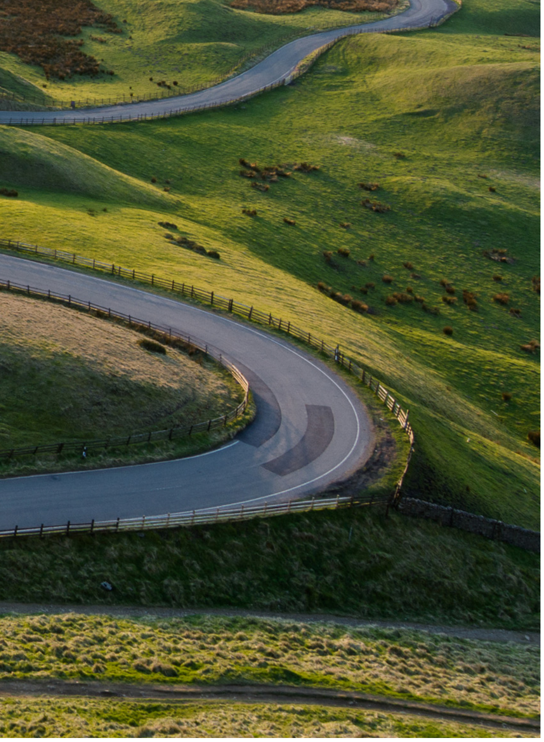
If inflation isn't sufficiently worrisome, there are many other concerns. In order to rein in inflation, central banks have become increasingly aggressive about raising interest rates. Higher interest rates present a significant headwind for house prices. Much of the extraordinary rise of wealth in Canada and the U.S. over the last several decades has come from the unrelenting increase in the value of houses, the largest asset in almost every person's portfolio. Equally worrisome is the possibility that if central banks raise interest rates too high too quickly, the resulting decline in demand for goods and services would plunge our economy into recession. Reflecting these concerns, the S&P 500 recently slipped into bear market territory.

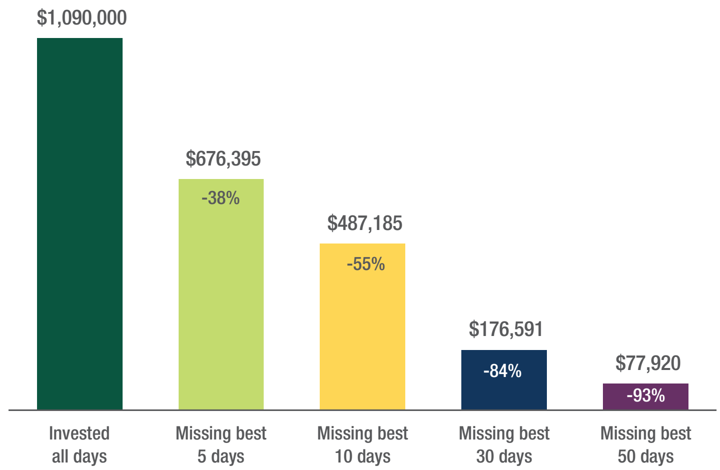
Of course, the human tragedy unfolding in Ukraine, and the related concerns about global peace and security, have many of us on edge. Similarly, lockdowns in some of China's biggest cities and renewed worries about its precarious real estate sector present a serious threat to global growth and financial stability. I could go on, but I expect that you get the point.

Any one of these factors would be a serious concern, but the confluence of them creates an outlook with great uncertainty. Surely, a prudent investor ought to tread cautiously with their investment decision-making. Perhaps some of your friends and neighbours have sold all their stocks and are taking solace in the cash they have accumulated. No doubt they feel good about their decision in the face of all these grave economic and geo-political issues.

Human instinct is to "do something" when the future is uncertain. This is a topic that we have addressed several times in the past but, given current circumstances, it seems appropriate to discuss again. Clearly, if one could predict exactly when a major market downturn was about to occur and predict exactly when an uptrend was about to start, one could make a lot of money trading out and then back into the market. However, getting lucky once or twice with such a prediction is insufficient. One needs to be able to accurately predict market movements repeatedly in order to succeed with the strategy over the long term. History has shown that human beings are remarkably ill-suited to do this.

Investors all know that the principle of "buy low and sell high" results in investment success. However, the evidence shows that investors do exactly the opposite – they buy high and sell low. It feels good to be buying when times are good and stocks are soaring. It feels smart to be selling when the news is bad and stocks are slumping – as is occuring right now.





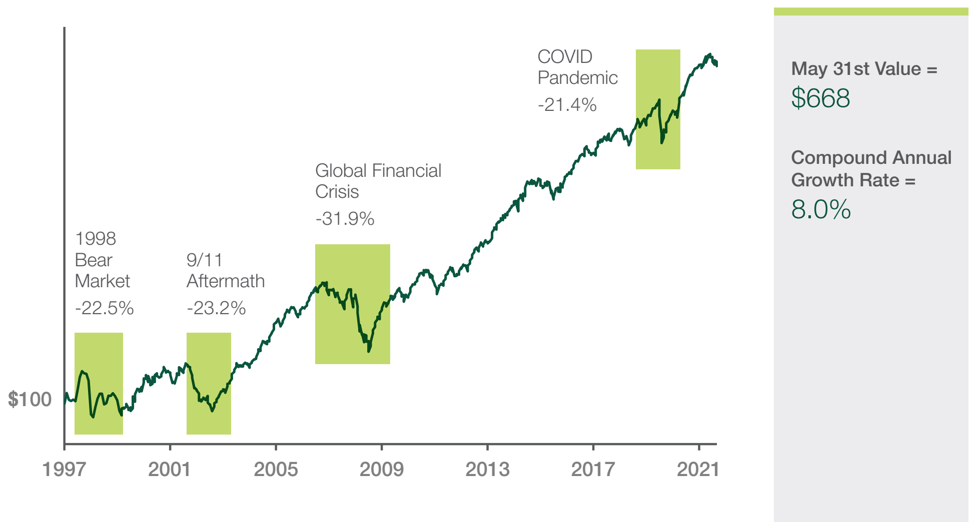
The Importance of Staying Invested[1]

We believe that long-term investment success comes from time *in* the market, not tim*ing* the market. If we accept the fact that we cannot consistently predict the future, the only approach that makes any sense is to buy and hold good quality stocks through good times and bad. A simple but powerful chart was recently printed in *Barron's* based on an analysis done by Fidelity Investments. It looks at the fantastic returns that accrued to those who invested in the U.S. stock market over the 40+ years between January 1, 1980 and March 31, 2021. Over that period, a hypothetical $10,000 invested in the S&P 500 turned into $1.09 million. Over the course of those years, investors endured many disasters: the stock market crash in 1987, the Asian currency crisis in 1998, the tech bubble collapse in 2000, the Global Financial Crisis in 2008/2009, and many other bear markets and temporary meltdowns. What the chart shows so powerfully is how devastating it is to long-term returns to miss out on a few good days of market rallies. Moreover, these best days in the market often come as a bounce in the middle of a downturn, or a strong recovery just as the market bottoms – both points in time when our market timing friends are likely to be sitting on the sidelines.

The history of Nexus also demonstrates how sticking with our holdings benefits our clients over the long term. We've endured many gut-wrenching set-backs, all of which felt awful at the time. You can see these highlighted in the following chart. But each set-back was followed by a strong recovery. The long-term record is clear.

This message is not new, but it is one that is useful to remember at challenging times like the present.

The moral of the story is that patience is one of the key virtues in the investment world. Investing is a long and winding road. There will be ups and downs. There will be moments of fear and moments of euphoria. Remaining disciplined and not letting emotions get the better of you is one of the greatest challenges that investors face. Use time as your ally and you will be rewarded… in time. Those who react to the latest headline eventually will be frustrated. As Warren Buffett has so famously observed, "investing is simple, but not easy."



Nexus Equity Fund Value, Starting at $100[2]

1 $10,000 invested in the S&P 500 from January 1, 1980 to March 31, 2021. From Barron's May 30, 2022, based on Fidelity Investments research.

2 Value of $100 invested in the Nexus North American Equity Fund at inception on August 31, 1997, presented on a logarithmic scale. Returns used for calculation are before deduction of investment management fees and after custody fees and fund expenses. Past performance is not indicative of future results.

The Imperfect Art of ESG

In addition to the devastation, the senseless war in Ukraine has revealed some awkward facts about the composition of some Environmental, Social and Governance (ESG) funds – in particular their holdings of Russian energy companies.

by
Devin Crago, CFA

According to research from CIBC, at the end of last year, many of the world's largest ESG funds had twice as much invested in Russia's oil and gas companies as they did in Canada's. The current problem for these funds is that Russia's biggest energy firms have, on average, lost 85% of their value since the invasion of Ukraine.

This begs the question "Why did ESG funds favour Russian holdings?" The answer seems to be because they had lower carbon intensity, which means the greenhouse gas (GHG) emissions released per barrel of oil equivalent produced are lower. They are large companies, so the absolute quantity of carbon emitted is greater than Canadian companies. But they emit less carbon per barrel produced. It may also be worth noting that Saudi Arabian barrels are less carbon intensive as well. But they come from a country that has received international censure for its poor track record on human rights issues.

This brings us back to an issue we've written about previously (in the article "*Nexus and the ESG Integration Approach*"), that the world of ESG comes with complications. Simple answers to what's "good" and what's "bad" are few and far between. Tradeoffs are required.

In this particular case, the tradeoffs made by those investing in Russian energy stocks have not worked well, to put it mildly. It appears that ESG investors sought out the reward of a superior GHG emissions profile, but they were swamped by the risks – now apparent in the harsh light of war – of bad governance and country-level risk in Russia. As the CIBC researchers articulate the situation, ESG "in aggregate, appears to place an overwhelming focus on carbon emissions to the neglect of other social and governance issues... Clearly, the concept of aligning investments with the values and ethics of responsible corporate citizens was significantly outweighed by simple, backwards-looking carbon metrics."

In contrast, Canadian energy stocks have performed well. On average, the biggest Canadian energy firms (Enbridge, Canadian Natural Resources, TC Energy and Suncor) have gained 20% while their Russian counterparts have fallen 85%.

This is not to say that Canadian energy firms are perfect. They have a higher GHG emissions intensity profile compared to some international competitors. That is an inherent challenge of oil sands operations, leaving their performance in the E part of ESG with room for improvement. But the need to improve has been acknowledged and Canada's big energy firms have announced a variety of emission reduction targets and underlying plans:

- Enbridge plans to achieve net zero greenhouse gas emissions by 2050, with an interim target to reduce emissions intensity by 35% by 2030.
- TC Energy also targets net zero emissions by 2050, with an interim target of reducing emissions intensity by 30% by 2030.
- Canadian Natural and Suncor, along with other oil sands producers, created the "Oil Sands Pathways to

Net Zero" initiative with the goal of also achieving net zero greenhouse gas emissions from their oil sands operations by 2050.

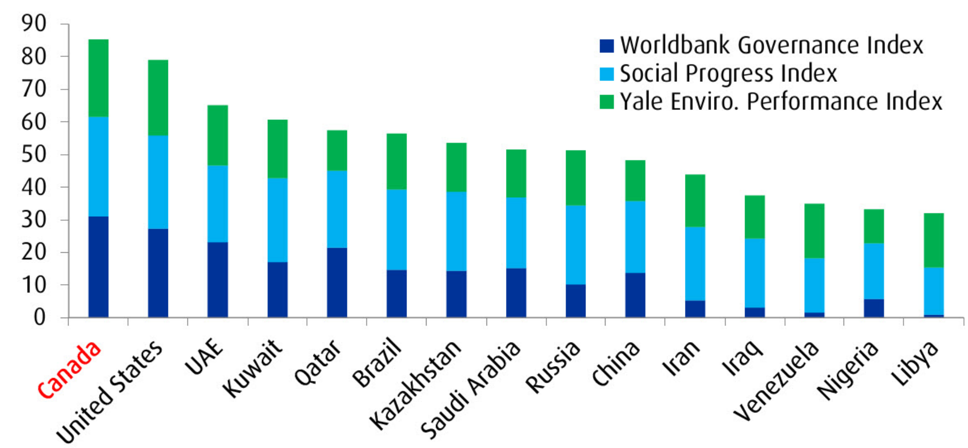
While Canadian energy firms are not global leaders when it comes to the carbon intensity of their operations, we anticipate continuous improvement in the years ahead as a result of these plans.

Like all other energy firms, they also face the challenge of managing and reporting on what's known as "Scope 3" emissions – the GHG emissions that come from the end-use consumption of their products (mostly gasoline and other fossil fuels). This challenge is further removed from each company's operations, but will need to be addressed. Unfortunately, Scope 3 emissions are beyond the direct control of the energy producer and a material reduction in the emissions that come from our burning of fossil fuels will require participation from all parts of society – individuals, corporations and governments – as well as innovation in clean energy technology.

Despite the environmental hurdles, Canadian energy firms do rank better in other ESG categories, particularly those related to social and governance considerations. What's more, they benefit from operating in Canada – a stable political jurisdiction that ranks well across the board on ESG metrics. While there are many ways to measure our nation's success on ESG, we find this exhibit from The Bank of Montreal to be illustrative of Canada's leading ESG position among the world's top oil reserve holders.

The recent divergent performance of Russian and Canadian energy stocks highlights the importance of each of the E, the S, and the G. Fixation on the E has led to losses for many of the world's largest ESG funds. Due consideration needs to be given to important social and governance considerations as well. And this, of course, is in addition to the traditional corporate strategy and financial considerations that go into a robust analysis of the merits and risks of an investment. Building ESG into our investment process is at the heart of our approach of "ESG integration" which you can read more about in the blog *"Nexus and the ESG Integration Approach*".

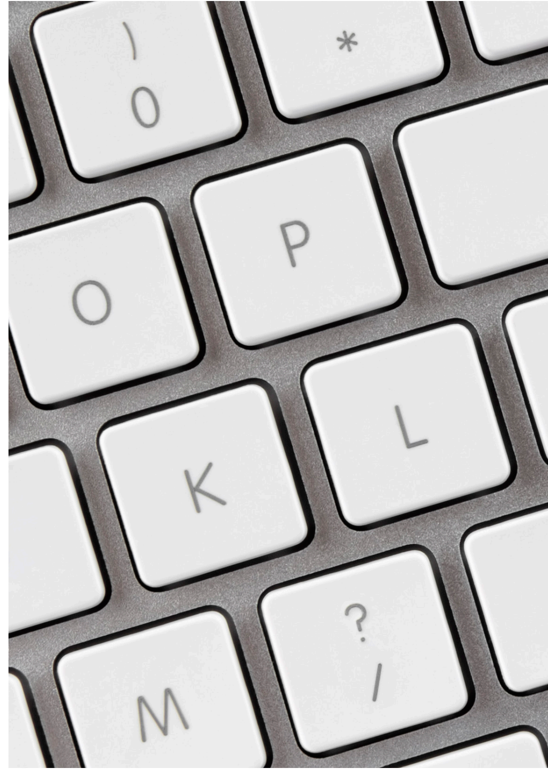
As we've written before, ESG analysis and implementation remains a work in progress. Nexus believes strongly in the underling principles, but we also recognize that ESG is not a silver bullet that can easily solve the complex problems of sustainability. This latest debacle is a clear example how much remains to be done to bring ESG investing into "prime time". Excellent long-term investment returns result from investing in companies with sustainable businesses. Perhaps what this latest episode suggests as much as anything is that a focus on ESG can't come at the expense of common sense.



Source: Yale Environmental Performance Index (EPI); Social Progress Imperative; World Bank Governance Indicators

Canada #1 in All Categories vs. Top Reserve Holders

Chart Source: BMO Capital Markets, "Building a Sustainable Future: ESG in Canadian Oil & Gas", November 2021.



Is Our Information About You Still Current?

by R. Denys Calvin, CFA

New regulations, known as the "Client Focused Reforms", now apply to all firms that are registered to give investment advice and trade in securities.

No doubt you know that scene in the movie where the protagonist jumps into a taxi and shouts "Follow that car!" While it makes for exciting cinema, and may be fine for a chase, it's Hollywood, not reality. And it surely wouldn't work for a long trip. In the real world, the driver needs more to go on than breathless exhortations from someone in hot pursuit.

It's the same in our business. A client who hands over some capital and tells the portfolio manager "just don't lose money" isn't giving the "driver" much to go on. Fortunately, most clients are quite open about themselves and what they're trying to accomplish by engaging a portfolio manager. For sure the manager wants to understand the client and their circumstances, to have a clear picture of the client's financial objectives, and, importantly, not to miss a meaningful change in the client's situation because "it didn't come up" in the normal back-and-forth between manager and client. And it's best for both if the information exchange is efficient, and there are no glaring gaps or misunderstandings.

Going back to the taxi example, when it comes to information exchange, Uber's got it down pat. Through an app, Uber has all the relevant information: the passenger's cellphone, email, credit card, and usual destinations (mine are "Home" and "Work"), to list the most obvious. There's even a place for something called "trusted contacts" – people who are allowed to see my location in real-time when I'm in an Uber.

In our business, we've always sought to make the information exchange between client and Nexus efficient. But it's hardly been "Uber-like". However, as regulators are raising the bar, and now require us to confirm with clients at least annually that the client information we have on file remains accurate, we've had to come up with a more streamlined approach – one that's not a burden on clients or on us. Unlike Uber, however, we can't herd everyone onto a smartphone app. Our approach has to be more tailored than that.

To accomplish this, starting later this spring, Nexus will begin rolling out an "update questionnaire". Each year, we'll provide the client with the information they've told us previously – including such things as their expected pattern of portfolio contributions and withdrawals, their employment situation and income, summary information about non-Nexus financial accounts and assets, and their professional advisers and "trusted contacts". The client can revise the things that have changed, and tick "No change" beside those that remain the same. However, there is no way to avoid the fact that the first time the questionnaire is completed it will take some time as clients help fill in some gaps in our records. In subsequent years, it should only take a few minutes.

Not everyone will get the same questions. A retired person would be justifiably irritated to be asked "When do you expect to retire?" Similarly, questions about changes in signing officers and decision-makers are important for a large

charitable organization, but don't really make sense to ask a married couple. While both spouses are welcome to complete separate questionnaires, in most households the "family CFO" will probably respond on behalf of the couple.

Much of the questionnaire will be familiar to clients who have had a financial plan prepared by Nexus. But someone who hasn't looked at a financial advisor's "know your client" form in the last 10 years will probably find that some questions have become a little more specific since then. Suffice it to say that we're asking only questions that are required by regulation or which will yield information that we know from experience enable us to best serve clients.

We anticipate that most people will prefer to complete something like this on-line – on their computer or tablet. To quote Apple, we'll "have an 'app' for that" (complete with the sensible data security features you might expect). No doubt some will prefer paper. There will probably also be situations where it works best if the Nexus partner jots down the answers while in conversation with the client.

Suffice it to say, we've thought carefully about how to make the information exchange as seamless and useful for clients and Nexus alike. With luck it will be nearly as convenient as Uber, but in a much nicer "vehicle"!

More on the Client Focused Reforms:

New regulations, known as the "Client Focused Reforms", now apply to all firms that are registered to give investment advice and trade in securities. Among other things, these reforms address conflicts of interest and disclosure. While Nexus has always provided our clients with the proper disclosures, we do welcome the regulators' efforts to create standards that apply consistently to all participants in our industry for the benefit of all Canadian investors.

As outlined above, the most noticeable effect of these reforms for clients will be the additional information we are now required to gather (and confirm annually) about our clients' personal and financial circumstances. Those who have used our wealth planning services will be familiar with these types of questions. Your Nexus relationship manager may spend some more time with you during your next meeting on some of these questions, and we thank you in advance for your understanding.

Nexus Client Insights Survey

by Alexandra Jemetz, CIM

Thank you to all of our clients who participated in our recent survey!

This spring, Nexus launched a survey asking our clients about their experience with our firm. The survey was anonymous, but we want to pass on our appreciation to those of our clients who responded.

You may also recall that we had pledged to make a charitable donation of $25 for each completed survey. Thanks to the overwhelming response, we have donated more than $9,000 to the Canadian Red Cross Ukrainian Humanitarian Crisis Appeal. We are delighted to have received so many responses and to have been able to make a donation like this.

We look forward to sharing the key results with you when they become available

The Nexus *Growth Spurt* *(Pandemic Edition)* Continues!

Nicole (Weiss) Louthe

As Nexus continues to grow, we remain committed to maintaining the highest levels of client service. This requires an ongoing investment in talent and experience. Throughout the pandemic we have added 6 new members to the Nexus team, two of whom we are excited to introduce here.

The hybrid work environment brought about by the pandemic continues to present challenges for integrating even the most experienced professionals onto the team. So, we will be introducing our new team members both virtually and in-person. This means that we'll be including them in a variety of client meetings and interactions when we can.

All of us are looking forward to meeting in person and hosting larger client functions again soon. Hopefully at that time you'll meet Julie and Ashleigh "live", as well as the team's other "pandemic hires" (in chronological order: Preethi, Tom, Lily and Ian).

In April, Julie Crothers, MBA, CIM, CFP joined our Client Service and Business Development team as a Vice President. Julie's role will be to assume responsibility for some current client relationships as well as develop her own. Julie has over 20 years of experience in the investment management industry, where she has had senior leadership roles in relationship management and client service. In those roles, she has advised clients on their wealth plans, implemented investment strategies and overseen a range of portfolios. In addition, Julie has extensive experience in working with not-for-profits and foundations. Like many other members of our team, she has also served on charitable boards and their respective investment committees.

Julie holds the Chartered Investment Manager and Certified Financial Planner designations and has a Master of Business Administration from the Rotman School of Management at the University of Toronto.

Outside of the office, Julie enjoys working on her tennis game, having picked up the sport during the pandemic. (Maybe we'll see a Nexus match in the future against our resident pro Devin Crago!) Julie also spends her time reading, going to the theatre and experiencing different cultures around the world through her travels.

You can read more about Julie in her bio on our website.

In May, Ashleigh Oucharek joined our administrative team as a Portfolio Administrator. Ashleigh focuses on supporting the portfolio managers and their clients. She will be involved in processing client documentation, forms and reporting, as well as facilitating trades with the portfolio management system. Ashleigh joins us from another firm in the investment industry, and we are looking forward to her becoming an integral part of our team.

Ashleigh enjoys staying active through kickboxing, creating art with her daughter, and during the summer months, she spends quality time with her family (and pup!) lakeside on Georgian Bay.

You can read more about Ashleigh in her bio on our website.

Worth a Thousand Words…

A little humour makes the world a better place.

A regular feature in Nexus Notes is the inclusion of a topical and insightful editorial cartoon. While some may address more serious or controversial issues, we particularly delight in amusing reflections on our current society. We hope you enjoy.

"The testing requirement is gone—you could've travelled with her."

Image used with permission: Ali Solomon, The Cartoon Bank/ The New Yorker Collection

Invest
Thoughtfully™

At Nexus, we offer thoughtful wealth planning and investment management with unparalleled personalized service to private clients and foundations.

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