



# Quarterly Investment Review

February 15, 2024

**NEXUS**

# Agenda

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1. Inside Nexus
2. Current Environment
3. Portfolio Overview
4. Investment Performance

# Inside Nexus

We continue to build our capability to support our clients and our vision



<sup>(1)</sup> Calculated as the average annual retention rate from December 31, 2013 to December 31, 2023.

# Current Environment

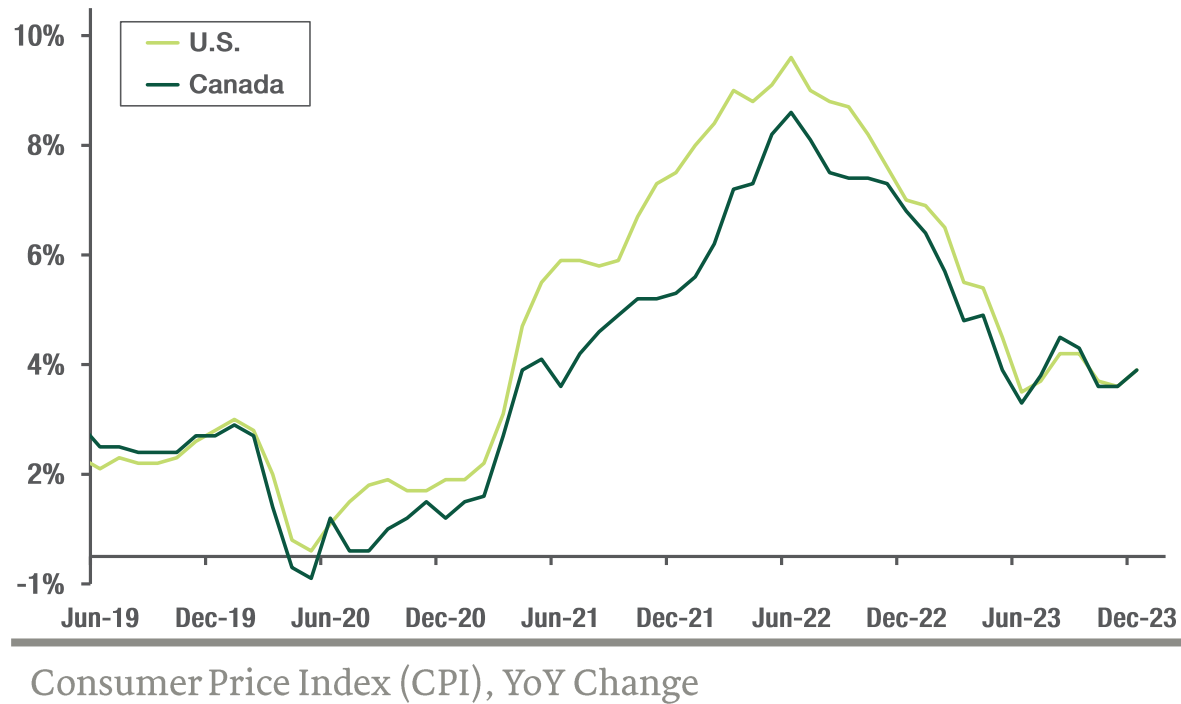
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Despite a better-than-expected 2023, significant economic challenges remain

- Tighter monetary conditions are having an effect
  - Inflation has been trending lower for some time
  - Excess cash in the economy mutes the effect of higher rates
  - Nonetheless, economic growth has remained resilient
- Labour market is pivotal to soft landing thesis
- Central banks must weigh multiple risks when determining the timing of rate cuts
- “Risk assets” reflect an optimistic outlook
  - Stock Market
  - Credit Spreads

# Current Environment

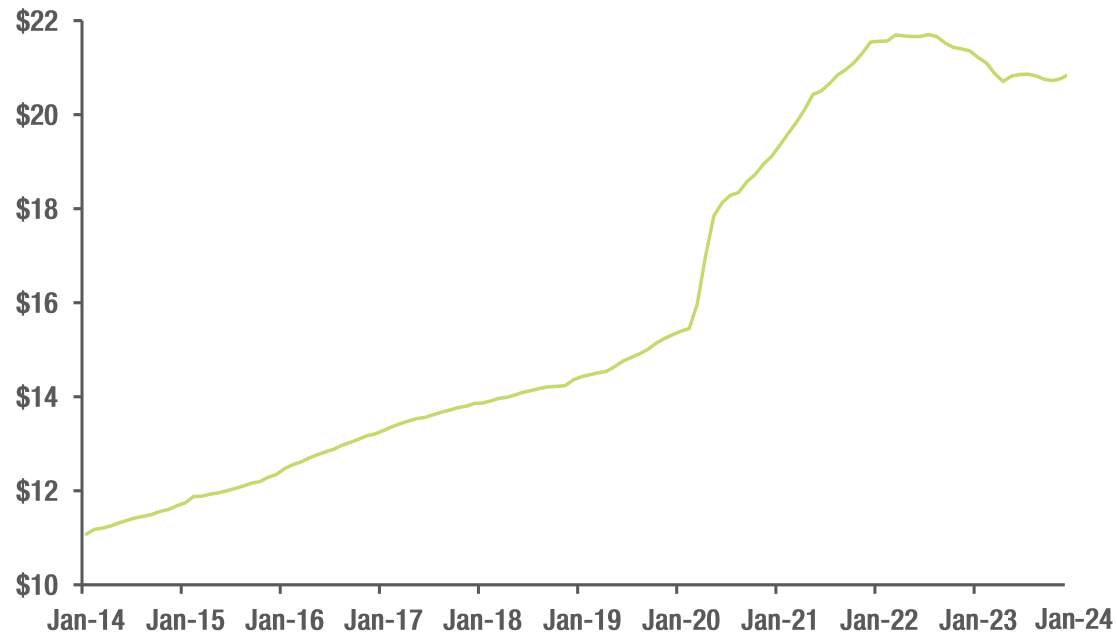
Inflation has been trending lower for some time



- Inflation levels have stabilized around 3%, but inflation not yet defeated
- “Where to from here?” depends on several factors, including:
  - Labour market developments
  - Corporate response to margin pressure
  - Consumer spending behaviour
  - Commodity prices
  - Further supply chain disruption

# Current Environment

## Excess cash in the economy mutes the effect of higher rates

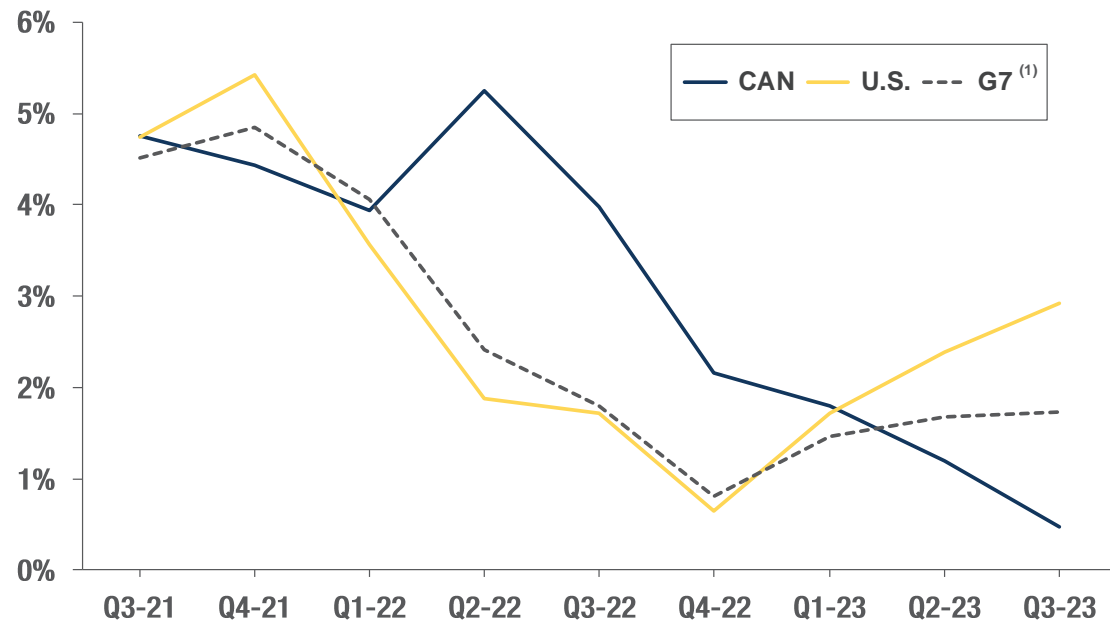


U.S. Money Supply<sup>(1)</sup> (U.S. \$trillions)

- Money supply expanded sharply in 2020 and has not yet contracted
- Central bank bond purchase programs increased bank lending, which added to M2.
- Surplus cash in the economy lessens the need to borrow funds, reducing the restrictive effect of higher rates

# Current Environment

## Economic growth has outpaced expectations

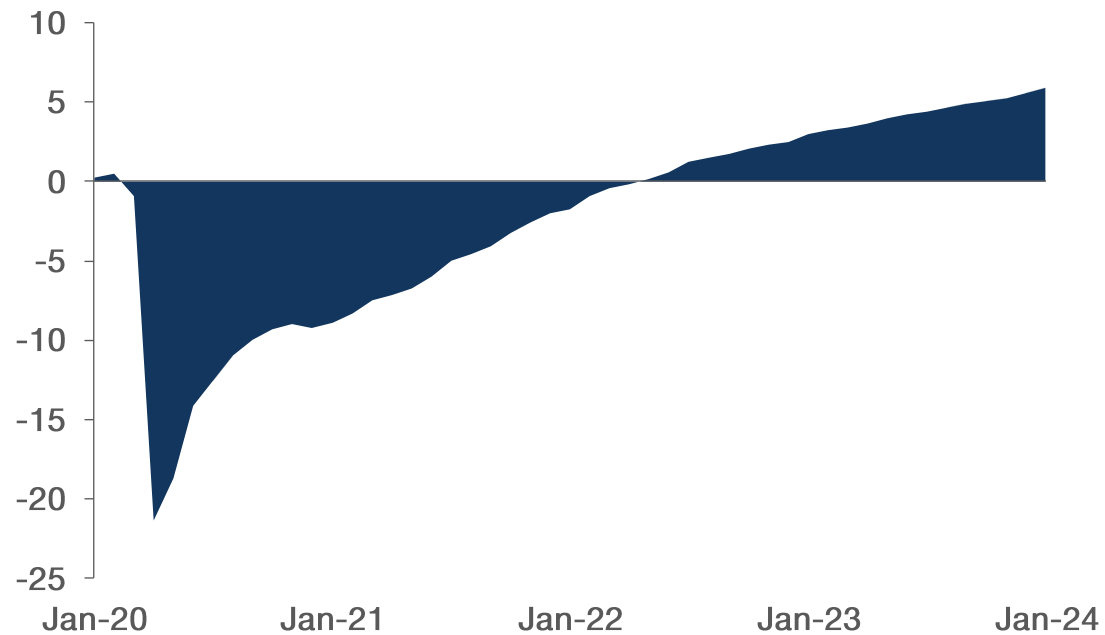


Quarterly GDP Growth (YoY%)

- At the beginning of 2023, an economic recession was widely anticipated
- Growth has slowed, but a recession has been avoided so far
- Canadian economic growth has lagged the U.S.

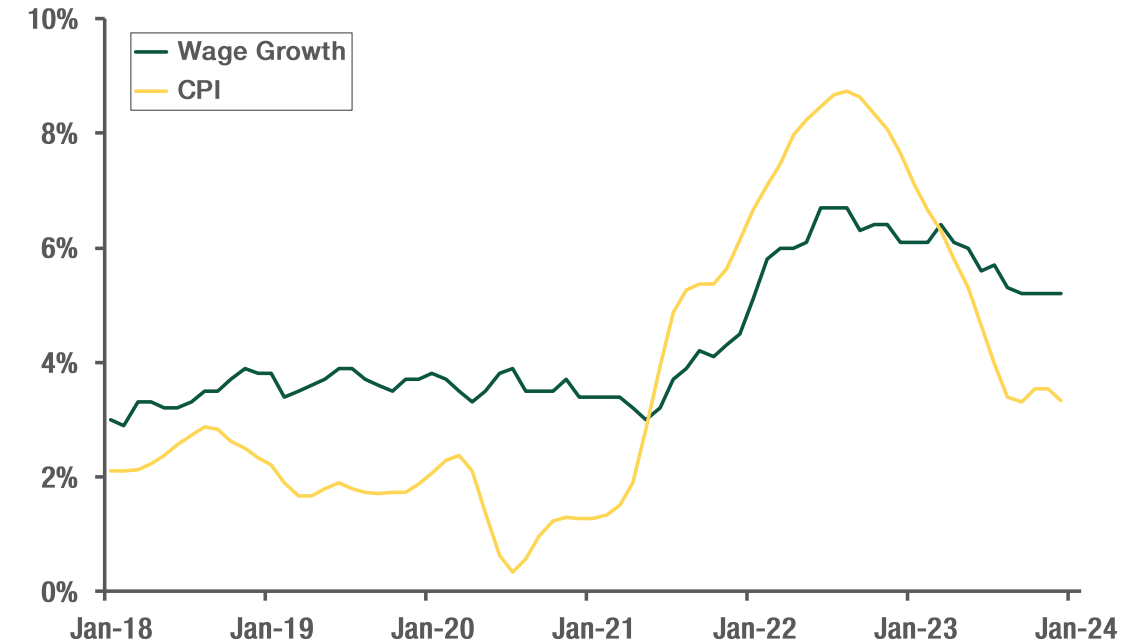
# Current Environment

## Labour markets remain strong



U.S. Cumulative Non-Farm Payroll Jobs (millions)

- The U.S. labour market added 2.7 million jobs in 2023 and the Canadian labour market added 430K jobs
- Public sector hiring more than offset technology sector layoffs in 2023

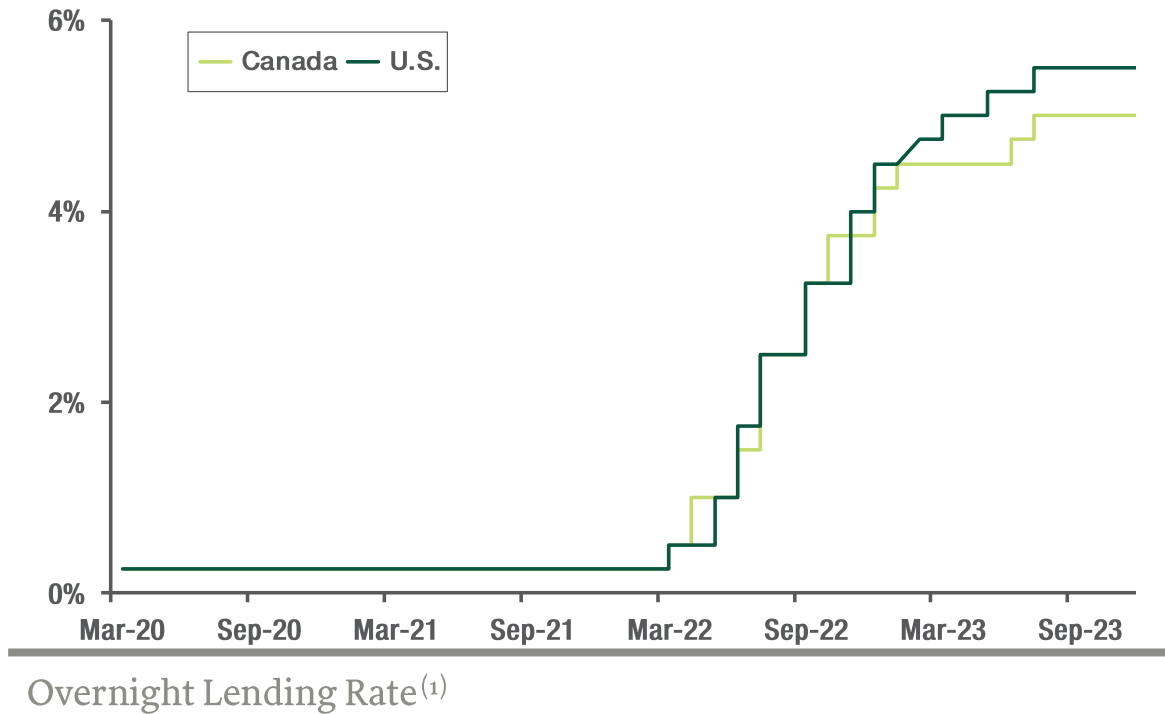


U.S. Monthly Wage Growth and CPI <sup>(1)</sup>

- Wages are catching up after lagging inflation
- “Soft landing” for economy depends on ongoing labour market strength

# Current Environment

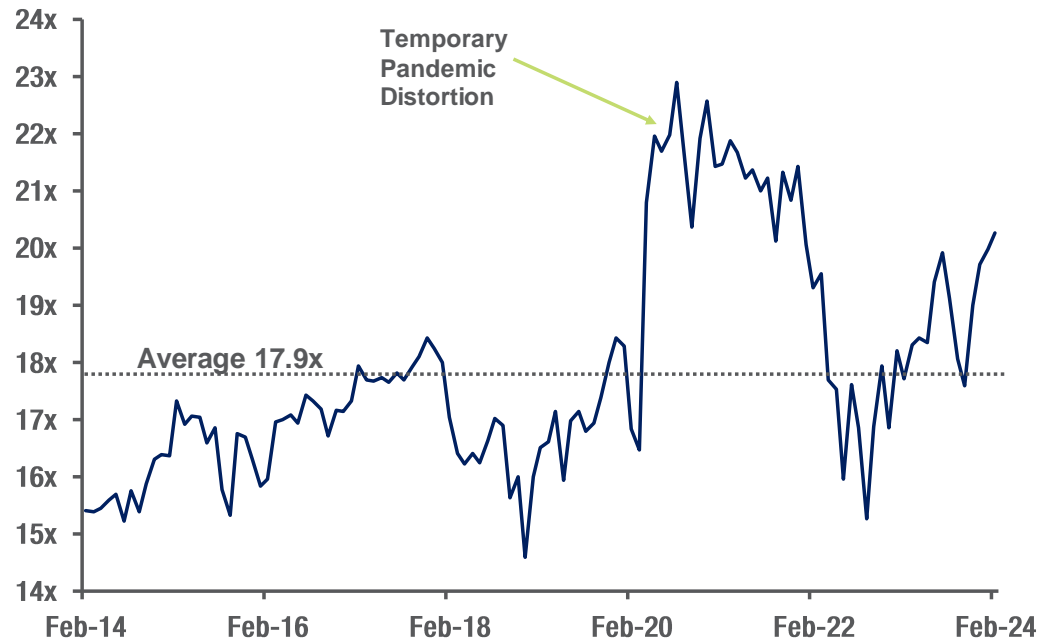
Central banks must weigh multiple risks when considering rate cuts



- Aggressive cuts could fuel a rebound in spending, housing prices or wages and, in turn, inflation
- Delayed cuts could dampen businesses and consumer sentiment

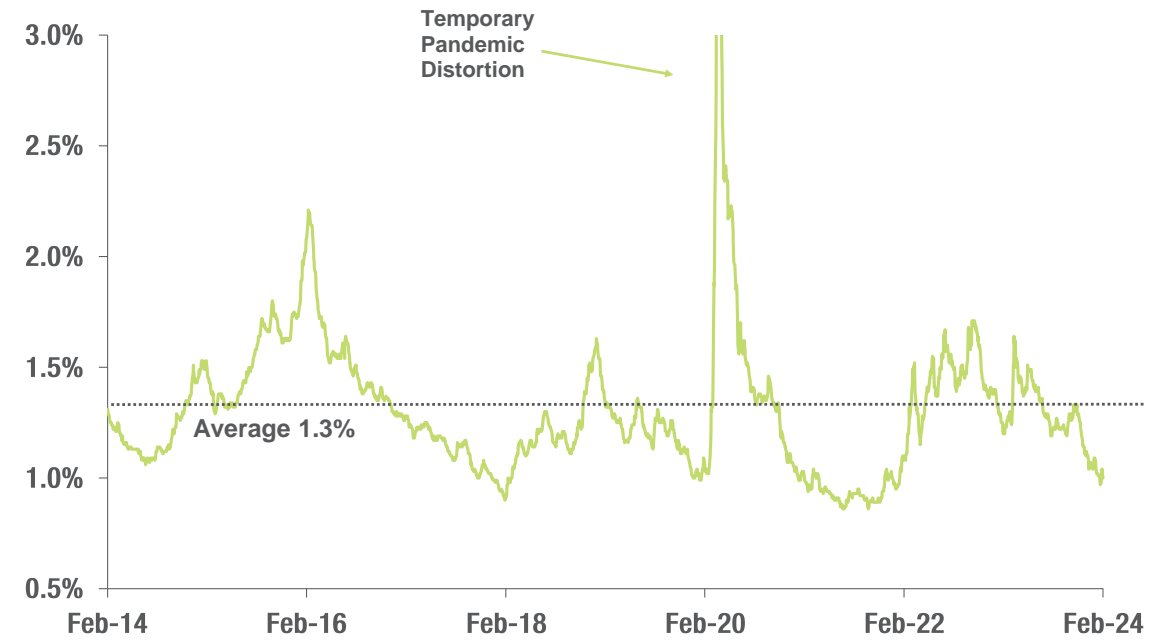
# Current Environment

Investors are optimistic about both the stock and bond market



S&P 500 Index Forward P/E Ratio <sup>(1)</sup>

- Equity valuations are well above the 10-year average



U.S. Investment Grade Credit Spreads <sup>(2)</sup>

- Historically low credit spreads indicate that investors are not worried about credit risk

Source: Bloomberg

<sup>(1)</sup> The forward price/earnings ratios are based on Bloomberg consensus earnings estimates for the next 12 months

<sup>(2)</sup> As represented by the ICE BofA U.S. Corporate Index Option-Adjusted Spread

# Current Environment

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2023 served as a reminder that market timing is difficult – 2024 will likely hold surprises too

- Economic, stock and bond performance all outperformed expectations in 2023
- Investors who remained in cash and GICs missed out
- Unlikely that 2024 will be any more predictable
  - Geopolitical pressures remain heated
  - U.S. election years are always volatile
- At Nexus we don't try to time markets; we favour a long-term approach with quality investments

# Portfolio Overview

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## Sticking to our knitting, despite go-go markets

- Only a handful of stocks drove most of last year's U.S. equity market gains
- In this narrow bull market, Nexus's equities didn't keep pace
- Since the financial crisis, we have kept up with our benchmark
  - A surprising result, given the dominance of Growth over Value during this period
  - Growth is unlikely to outperform Value indefinitely
- Overall equity allocations are near our long-term guidelines
- Fixed income portfolios remain concentrated in shorter-duration bonds

# Portfolio Overview

2023 Review

## 2023 was a year of dramatic events

- **Interest rate hikes** – fastest pace since the 1980s
- **“Fed pivot”** – dovish central bank commentary
- **Inflation** – U.S. rate slowed from 6.5% to 3.4% <sup>(1)</sup>
- **Regional bank crisis** – Silicon Valley Bank, Signature Bank
- **Surge in strikes** – 354 strikes in U.S. involving 500,000 workers <sup>(2)</sup>
- **War** – Ukraine and Gaza
- **China** – economic slowdown, real estate problems
- **Rapid innovation** – AI, ChatGPT, GLP-1 weight loss drugs



Canada Wildfires



Spy Balloon



Lost Titanic Submarine



FTX Failure



U.K. Coronation



Swift/Kelce Romance

Source: Bloomberg, Wall Street Journal, iStock (images used with permission)

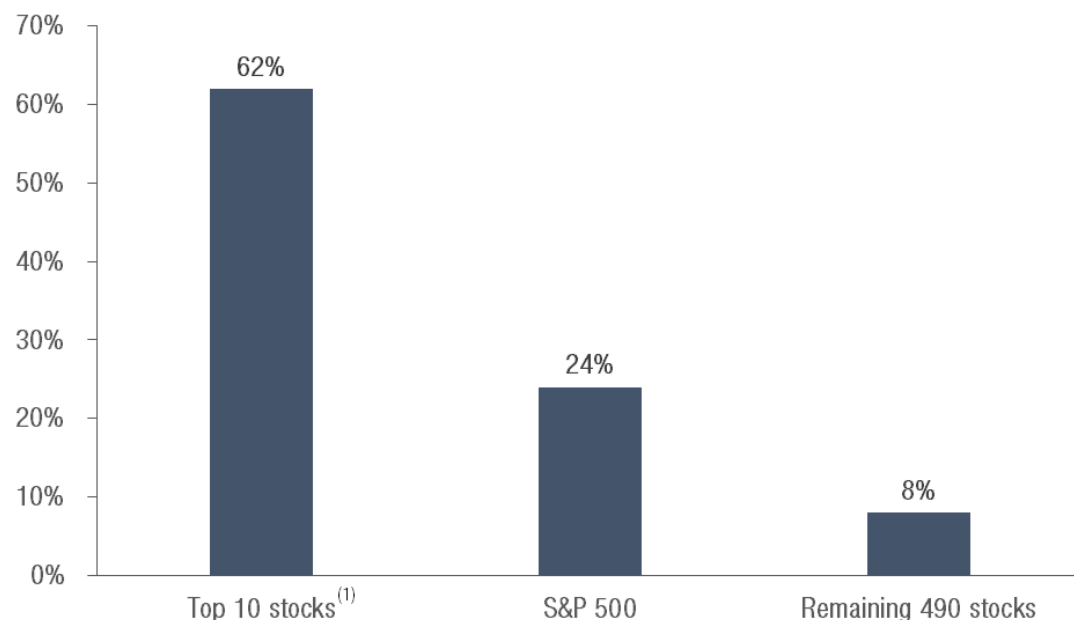
<sup>(1)</sup> United States Consumer Price Index (CPI). The year-over-year increase was 6.5% in December 2022 and 3.4% in December 2023

<sup>(2)</sup> Cornell University School of Industrial and Labor Relations, Labor Action Tracker, as of October 31, 2023

# Portfolio Overview

2023 Review

Last year's U.S. market gains were driven by only a handful of stocks



2023 Price Returns of S&P 500 constituents in US\$

- Investing in the S&P 500 Index is currently a big bet
  - Concentration risk*: the top 10 stocks account for 32% of the index – highest since 1972
  - Valuation risk*: the top 10 stocks have a price/earnings (P/E) ratio of 26.9x, while the other 490 stocks have a P/E ratio of 17.1x
- Similar situation in Canada: a single stock (Shopify) produced 30% of the TSX's price return

As at December 31, 2023

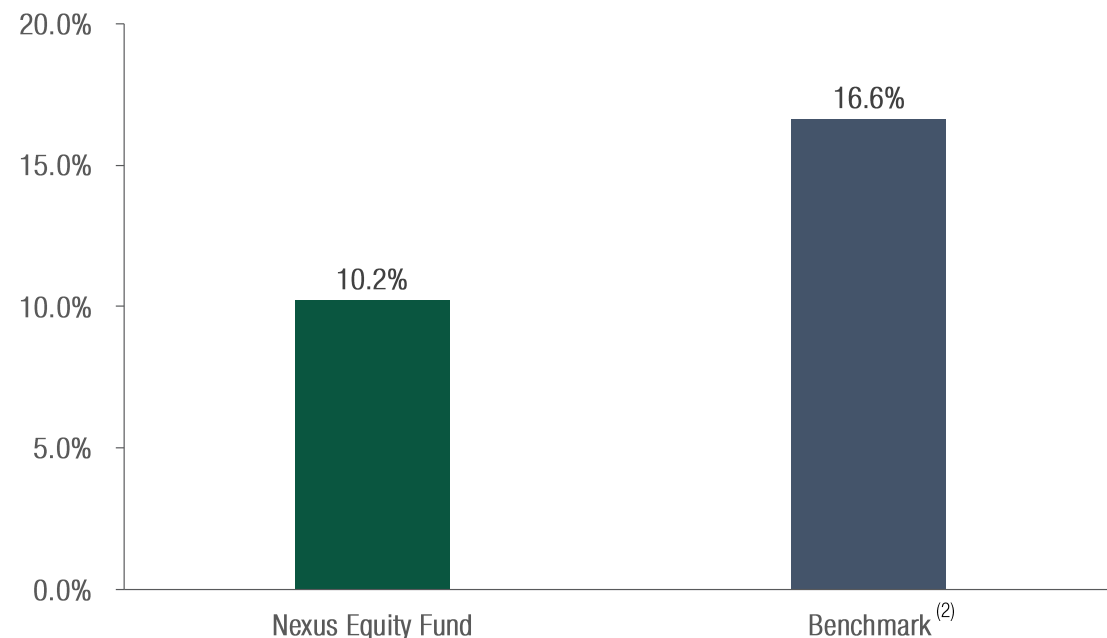
Source: J.P. Morgan Asset Management

<sup>(1)</sup> The top 10 companies represent the largest index constituents at the beginning of 2023. They were Apple, Microsoft, Alphabet, Amazon, Tesla, Meta Platforms, Nvidia, Berkshire Hathaway, Exxon Mobil and UnitedHealth Group

# Portfolio Overview

2023 Review

In this narrow bull market, Nexus's equities didn't keep pace



2023 Total Returns in C\$<sup>(1)</sup>

- Enthusiasm for Growth stocks – particularly those with an AI angle – supercharged the benchmark return last year
- Dividend-oriented stocks had a difficult year
- Nexus returns were solid, but trailed our benchmark

Source: Bloomberg

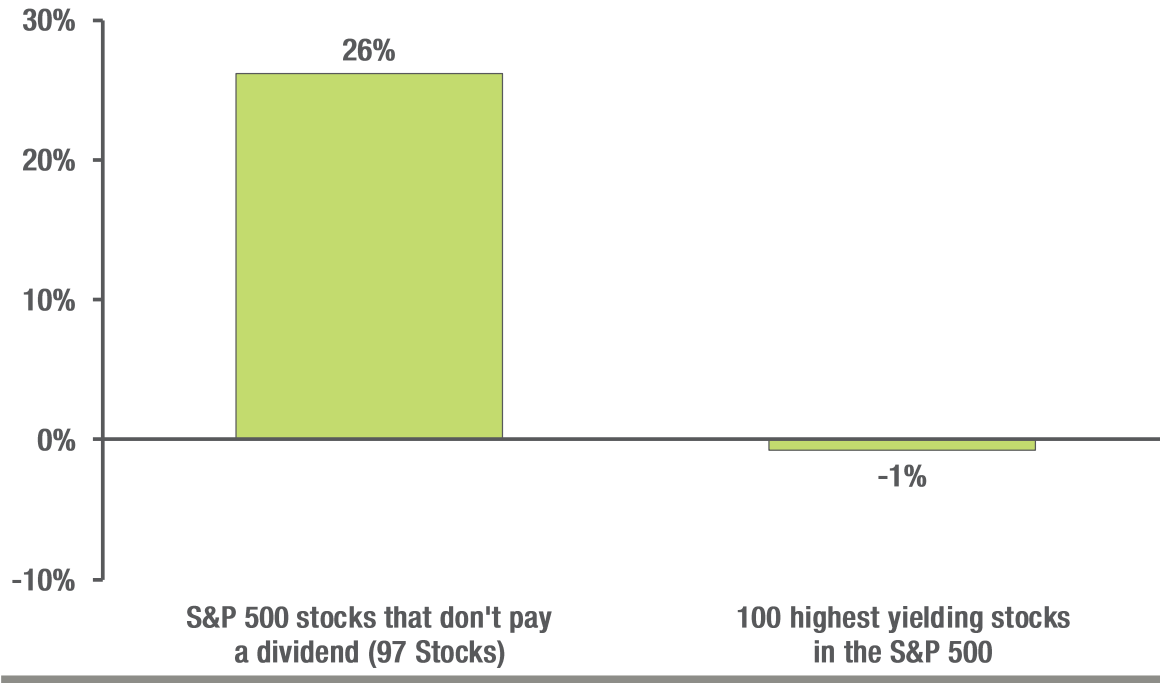
12 months ended December 31, 2023

<sup>(1)</sup> Nexus returns are compound annual average, time-weighted, total rates measured in Canadian dollars and calculated after deducting such direct and indirect costs as applicable withholding taxes, trading commissions, custody fees and other fund/account expenses, but without deducting Nexus's management fees (which are charged to client accounts and vary by client). Returns for market indices and benchmarks are presented on the same basis, but without any such deductions. Blended benchmark weightings are rebalanced monthly. Past performance is not indicative of future results.

<sup>(2)</sup> Benchmark is 5% FTSE Canada 91 Day T-Bill Index, 50% TSX, and 45% S&P 500 (in C\$); rebalanced monthly. For more information about benchmarks, please refer to <https://tinyurl.com/NexusOnBenchmarks>.

# Portfolio Overview

## Dividend-paying stocks have lagged

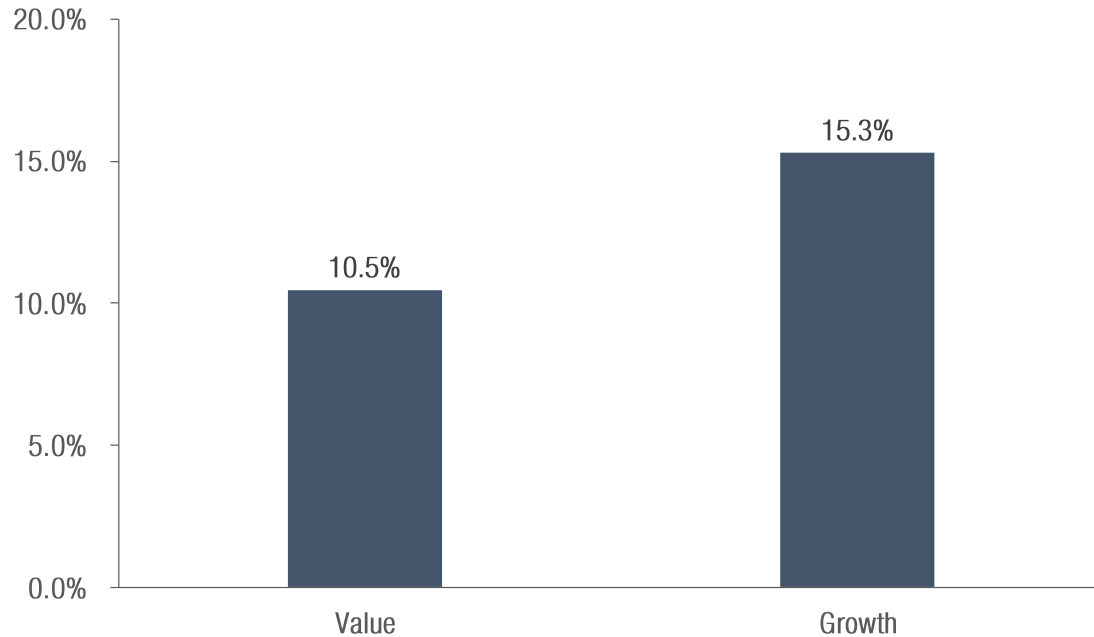


2023 Average Total Returns <sup>(1)</sup>

- Dividend payors are currently out of favour
- However, they have an excellent historical track record over the long term

12 months ended December 31, 2023

## Since the financial crisis, Growth has substantially outperformed Value



2009 - 2023 Total Returns in US\$ (%)<sup>(1)</sup>

- Despite Growth stocks dominating, Nexus has virtually kept pace during this period <sup>(2)</sup>
- Over longer periods, Value has outperformed Growth
  - On average, value stocks have outpaced growth stocks by 4.2% annually in the U.S. since 1927 <sup>(3)</sup>
- Growth is unlikely to outperform indefinitely
  - After a long winning streak for growth, mean reversion is likely
  - Stick with disciplined approach to capture the long-term opportunity

Source: Bloomberg, Kenneth R. French Data Library

<sup>(1)</sup> Annualized total returns (price changes + dividends), before withholding tax, for the Russell 1000 Growth Index and the Russell 1000 Value Index from Dec 31, 2009 to Dec 29, 2023, in US\$

<sup>(2)</sup> The C\$ total return of the Nexus Equity Fund has trailed the benchmark by 0.3% annually since 2009

<sup>(3)</sup> Measured as the average of the annual difference of returns of the Fama/French US Value Research Index and the Fama/French US Growth Research Index, in US\$, from 1927 to 2023

# Portfolio Overview

## Equity Portfolio Changes

Equity turnover remains low – some trimming to address overweight stocks

<b>Buy</b>	<b>Sell</b>
—	—
<b>Add</b>	<b>Trim</b>
Allied Properties	ARC Resources

Canadian Equities

<b>Buy</b>	<b>Sell</b>
American Electric Power	BMW
<b>Add</b>	<b>Trim</b>
—	Alphabet Meta Platforms Microsoft

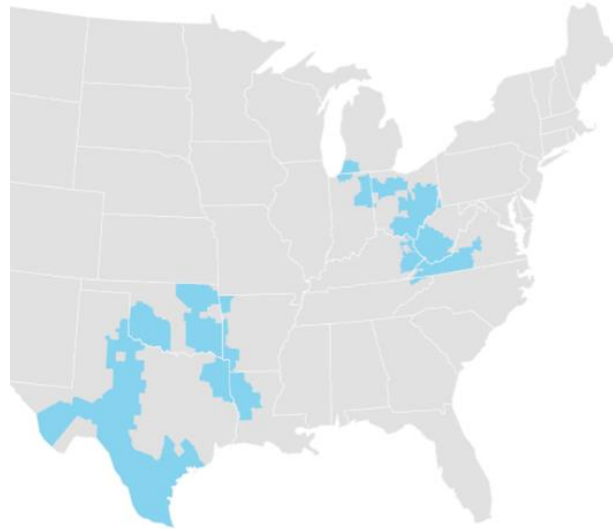
Foreign Equities

12 months ended January 31, 2024

# Portfolio Overview

## American Electric Power

American Electric Power (AEP) is one of the largest regulated electric utilities in the U.S.



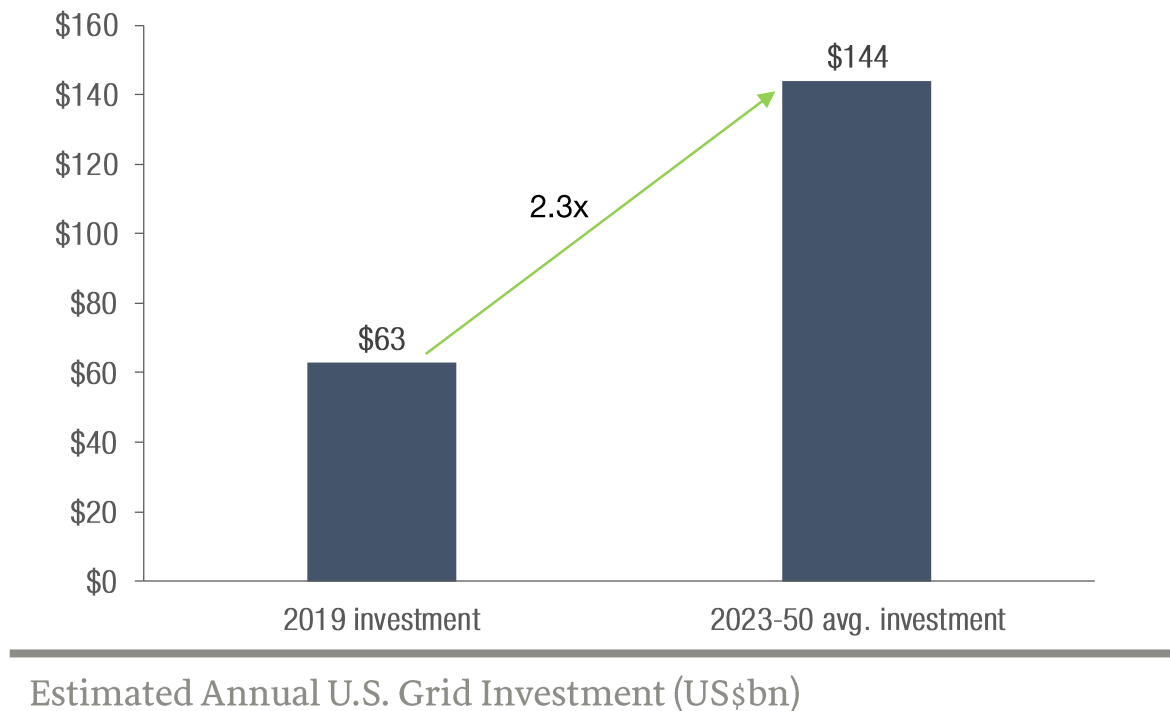
- AEP generates, transmits and distributes electricity to 5.6 million customers in 11 states
- AEP's assets include
  - 225,000 miles of distribution lines
  - 40,000 miles of transmission lines – the nation's largest system
  - 23 Gigawatts of regulated electricity generation assets
- Fiscal 2022 revenue of \$19.6bn

# Portfolio Overview

American Electric Power

AEP offers a combination of steady growth and an attractive dividend

- Electric utility with defensive characteristics
  - Earns regulated returns on its capital investments
  - Has delivered steady earnings growth over time
- Long runway of growth driven by secular trends
  - Electrification of the economy
  - Improving grid reliability and resilience
  - Growth in renewables to decarbonize
  - U.S. is expected to spend \$4 trillion on its grid by 2050
- Sustainable and growing dividend
  - Dividends every quarter for 113 years
  - Five-year annualized dividend growth rate of 5.9%
- Trades at an attractive valuation
  - U.S. Utility sector declined by 10.2% in 2023 <sup>(1)</sup>
  - Purchased at a forward Price/Earnings ratio of 14.3x <sup>(2)</sup>



Source: Bloomberg, AEP, Bernstein

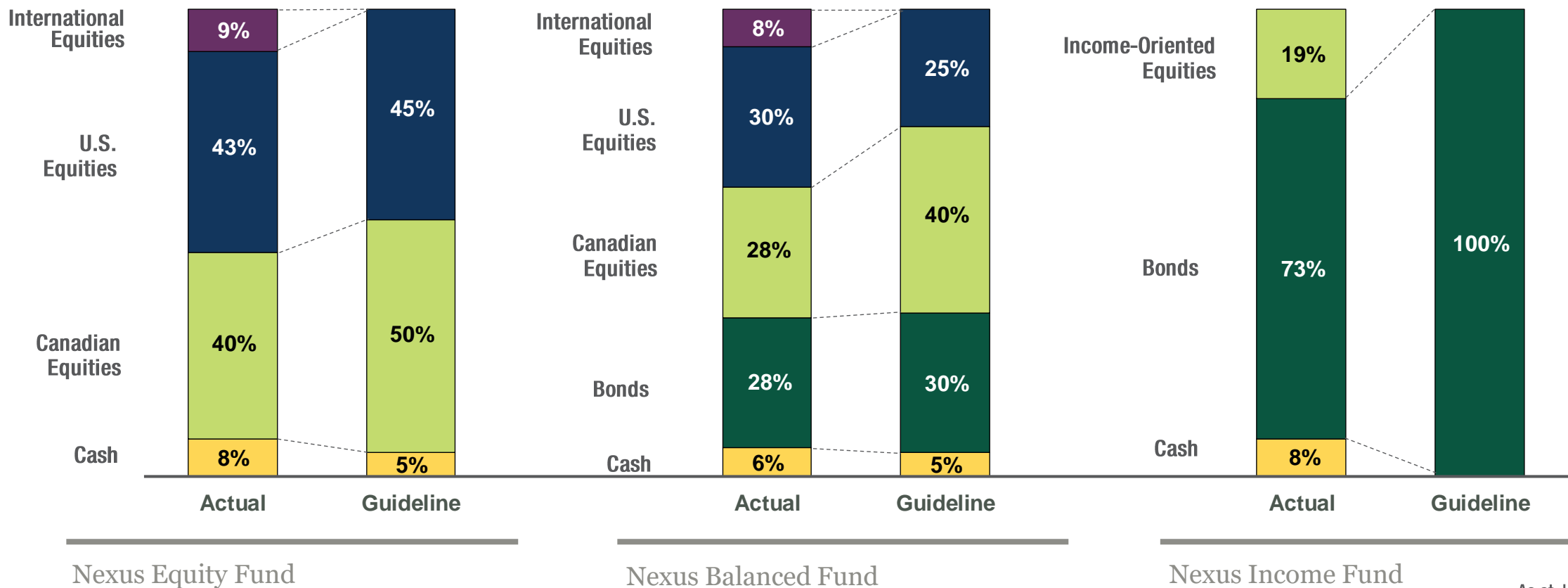
<sup>(1)</sup> Price return of the S&P 500 Utilities Sector Index

<sup>(2)</sup> The forward price/earnings ratios are based on Bloomberg consensus estimates for earnings in the next 12 months as of November 7, 2023

# Portfolio Overview

## Asset Allocation

Overall equity allocations are close to long-term guidelines



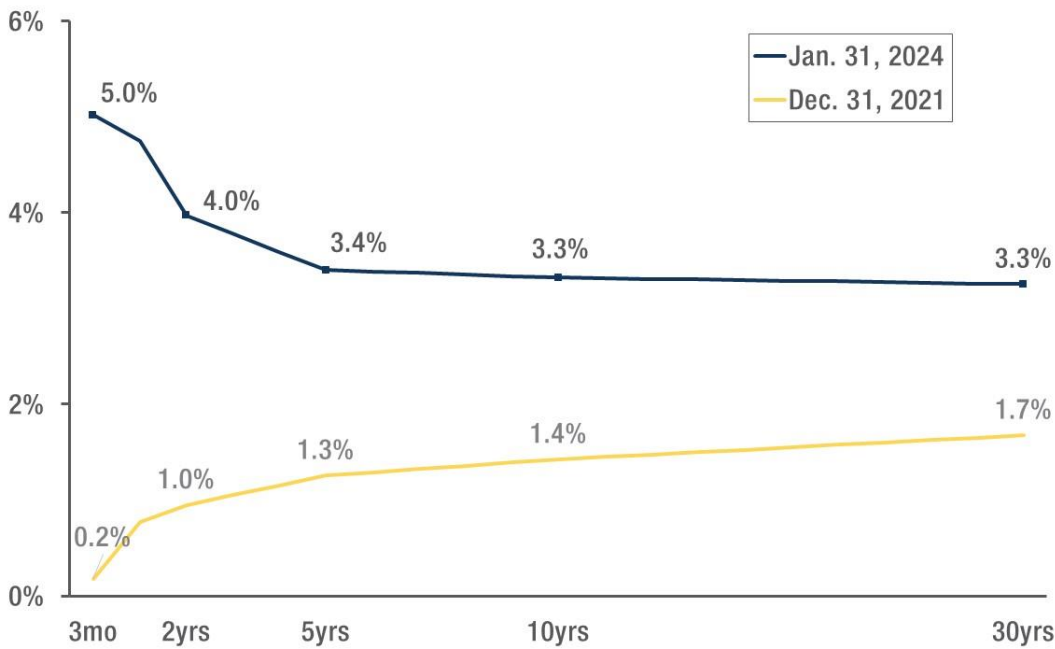
As at January 31, 2024

- Our portfolios are thoughtfully diversified across asset classes, geographies and sectors

# Portfolio Overview

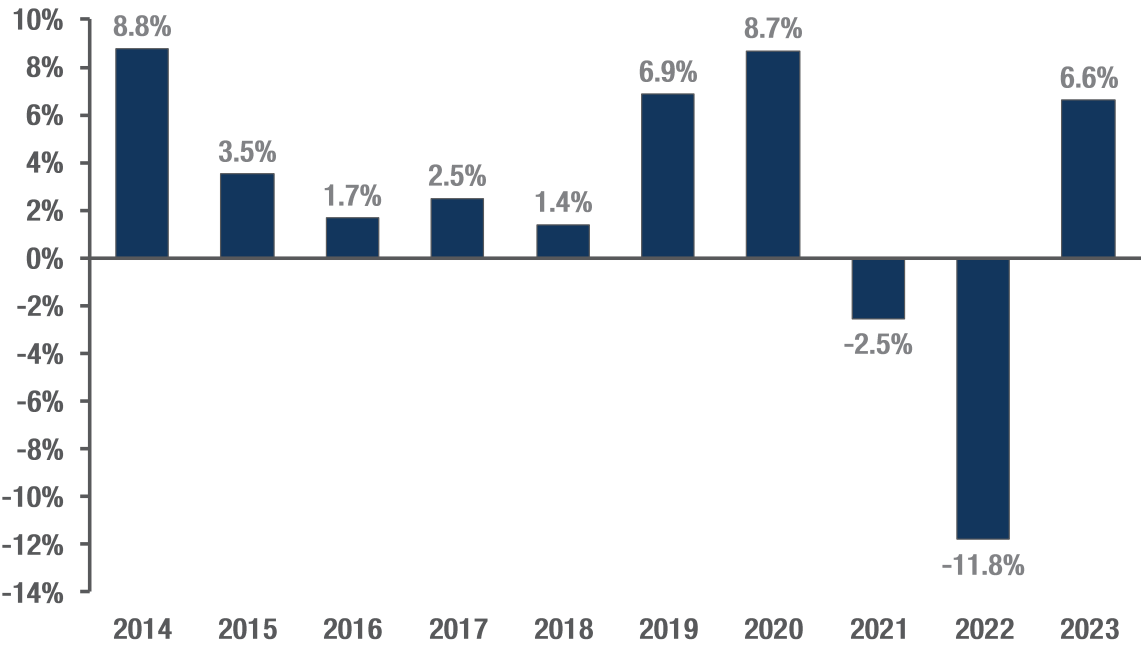
## Fixed Income

Fixed income is no longer the calm asset class that it once was



Government of Canada Yield Curve

- Despite a big move in shorter-dated rates, the yield curve continues to reflect expectations for aggressive rate cuts and muted inflation



Canadian Bond Market Performance<sup>(1)</sup>

- Volatility in the bond market has increased

Source: Bloomberg, FTSE Russell

<sup>(1)</sup> Canadian bond market represented by the FTSE TMX Universe Bond Index

# Investment Performance

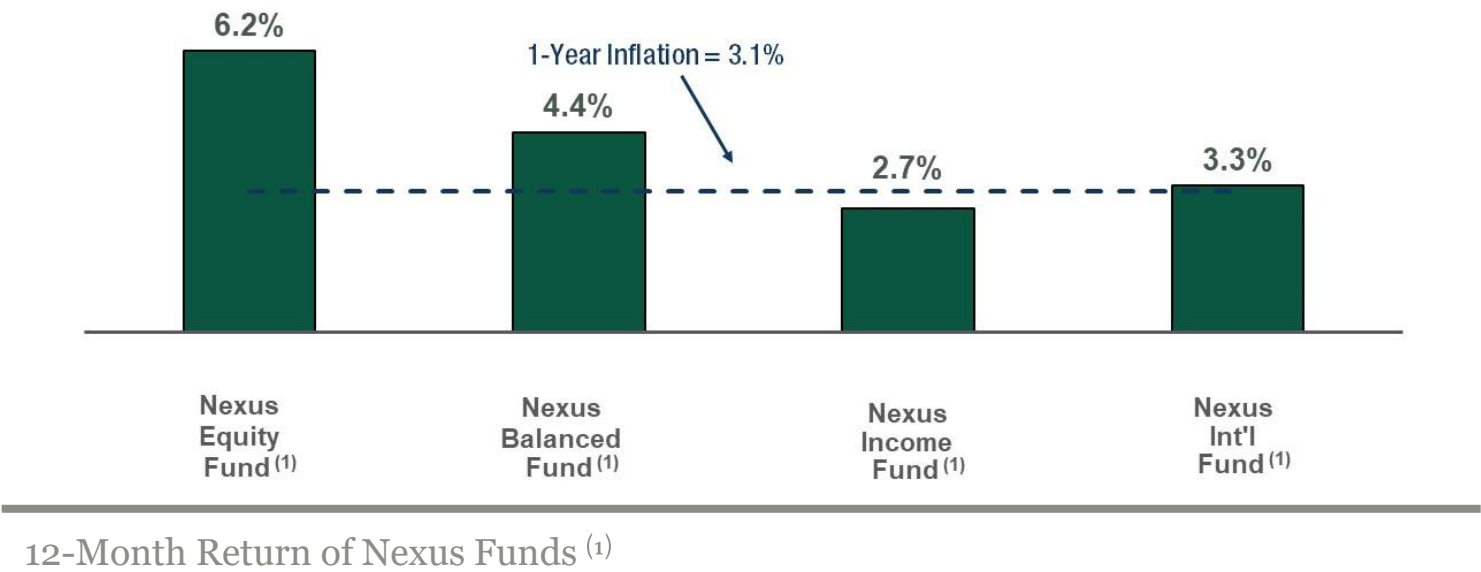
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## The strong finish to 2023 continued into January

- Robust gains in the last three months resulted in positive 12-month returns
  - Our bond portfolio significantly outperformed the bond index
  - Canadian stocks were a notable weak spot
  - U.S. and International stocks (other than China) enjoyed the strongest gains
  - Nexus gains not as robust as benchmarks – gains in most stock markets concentrated in very few stocks
- Longer-term risk / return characteristics are attractive
- Our approach differs from the indices – performance will inevitably diverge at times

# Investment Performance

One-year equity returns are solid, but trailed the high-flying stock market index returns

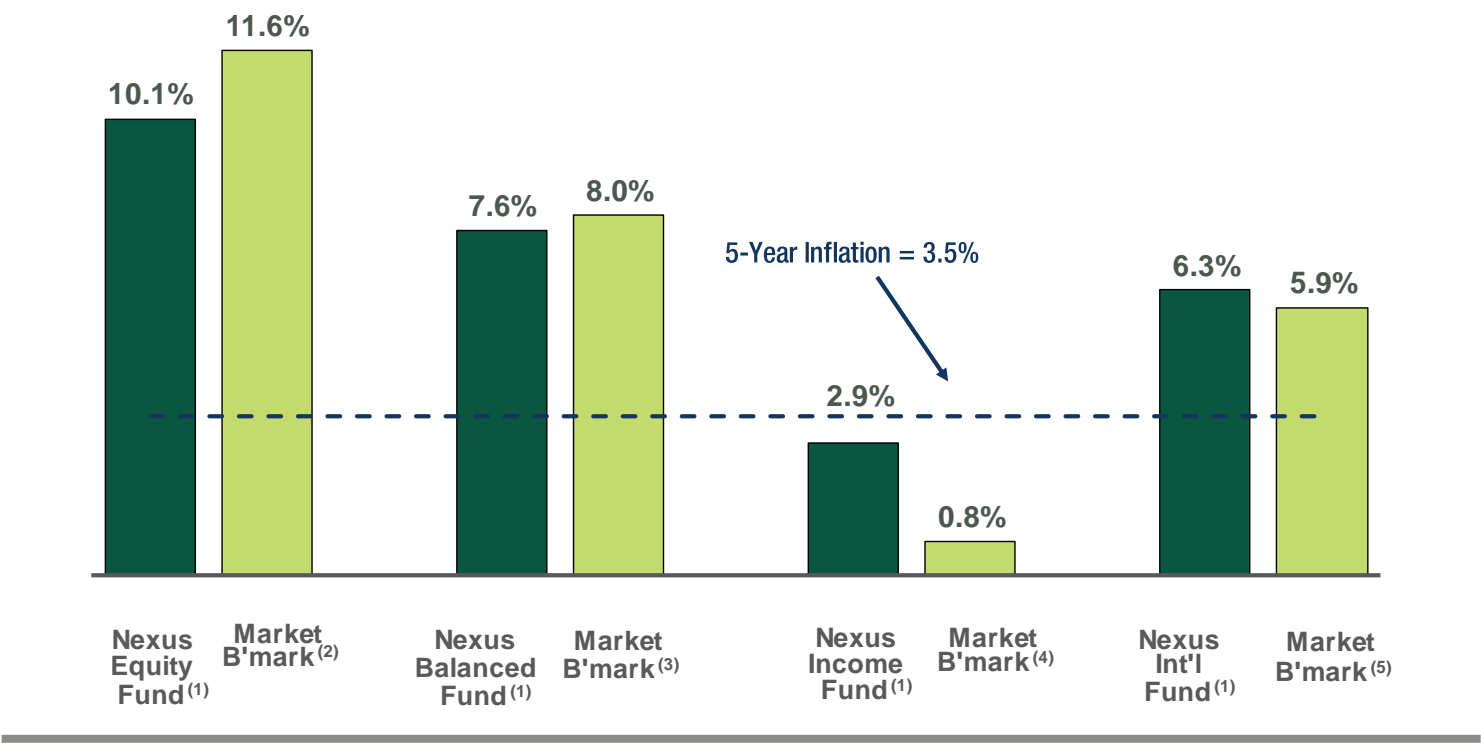


12 months ended Jan 31, 2024

<sup>(1)</sup> All Nexus returns are compound annual average, time-weighted, total rates measured in Canadian dollars and calculated after deducting such direct and indirect costs as applicable withholding taxes, trading commissions, custody fees and other fund/account expenses, but without deducting Nexus's management fees (which are charged to client accounts and vary by client). Past performance is not indicative of future results.

# Investment Performance

Five-year returns remain attractive, led by substantial gains in equity markets



5-Year Annualized Return

<sup>(1)</sup> All Nexus returns are compound annual average, time-weighted, total rates measured in Canadian dollars and calculated after deducting such direct and indirect costs as applicable withholding taxes, trading commissions, custody fees and other fund/account expenses, but without deducting Nexus's management fees (which are charged to client accounts and vary by client). Returns for market indices and benchmarks are presented on the same basis, but without any such deductions. For more information about benchmarks, please refer to <https://tinyurl.com/NexusOnBenchmarks>. Past performance is not indicative of future results.

<sup>(2)</sup> Equity Fund market benchmark is 5% FTSE Canada 91 Day T-Bill Index, 50% TSX, and 45% S&P 500 (in C\$); rebalanced monthly.

<sup>(3)</sup> Balanced Fund market benchmark is 5% FTSE Canada 91 Day T-Bill Index, 30% FTSE Canada Universe Bond Index, 40% TSX, and 25% S&P 500 (in C\$); rebalanced monthly.

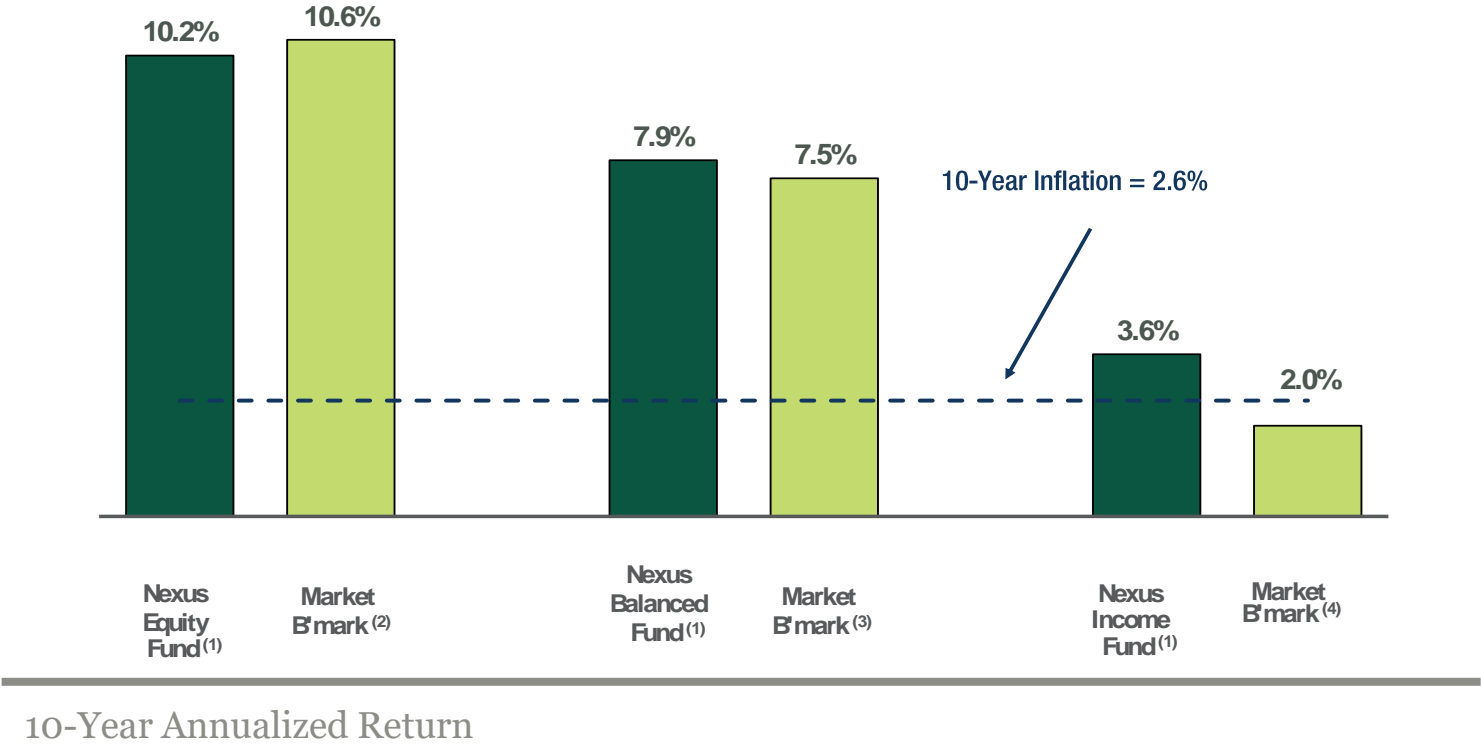
<sup>(4)</sup> Income Fund market benchmark is the FTSE Canada Universe Bond Index. Note that in addition to bonds, up to 20% of the Income Fund portfolio may be invested in equity securities.

<sup>(5)</sup> International Equity Fund market benchmark is 75% MSCI EAFE and 25% MSCI Emerging Markets indices (both in C\$); rebalanced monthly.

5 Years ended January 31, 2024

# Investment Performance

10-year returns remain attractive



<sup>(1)</sup> All Nexus returns are compound annual average, time-weighted, total rates measured in Canadian dollars and calculated after deducting such direct and indirect costs as applicable withholding taxes, trading commissions, custody fees and other fund/account expenses, but without deducting Nexus's management fees (which are charged to client accounts and vary by client). Returns for market indices and benchmarks are presented on the same basis, but without any such deductions. For more information about benchmarks, please refer to <https://tinyurl.com/NexusOnBenchmarks>. Past performance is not indicative of future results.

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10 Years ended January 31, 2024

# Outlook

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## Our portfolio is positioned for long-term investment success

- North American equity portfolio is comprised of quality stocks with attractive prices
  - Established, dividend-oriented stocks
  - Attractive valuations provide good long-term upside with a margin of safety
  - Well-positioned for a higher inflation environment
- Nexus Income Fund is constructed to emphasize quality and reduce price risk
  - Credit quality is high, average bond maturities are short
  - Higher interest rates will benefit bond investors over time
  - Income-oriented equities add long-term growth and inflation protection
- International equities continue to add diversification
  - Higher dividend yields and lower valuations than North America

# Appendix

# Portfolio Overview

## Equities

Our North American equities combine defensiveness and growth



As at December 31, 2023

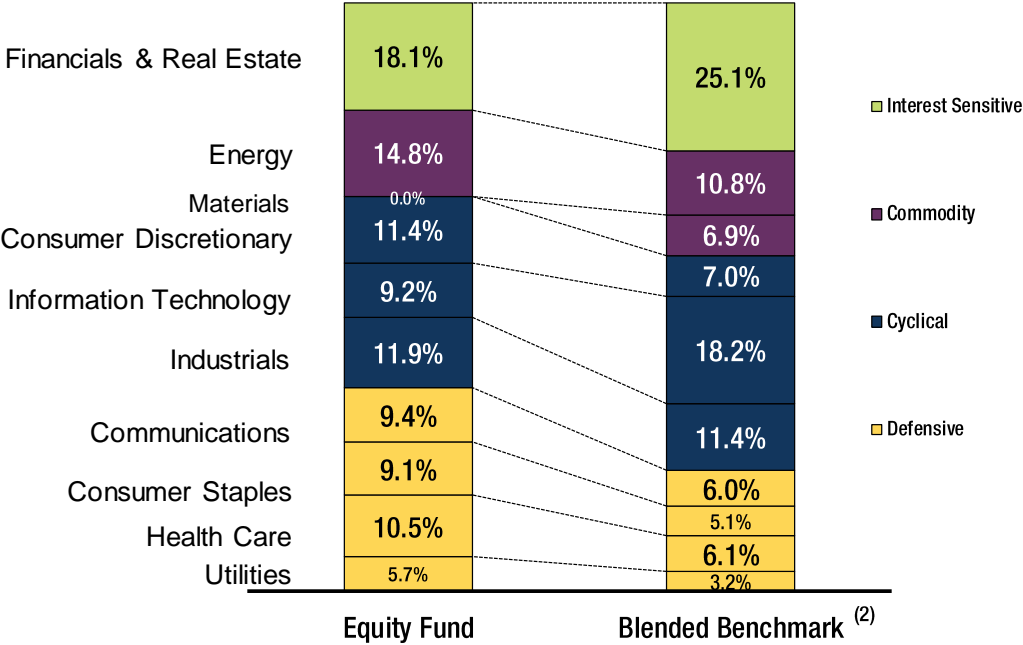
Source: Bloomberg.

<sup>(1)</sup> The “forward” year is the current fiscal year estimate for each company. Average P/E and Price/NAV multiples on this page are calculated using a weighted harmonic mean.

# Portfolio Overview

## Diversification

Our high-quality equity portfolio is diversified, different from the benchmark, and reasonably valued



	S&P 500	TSX	Nexus Equity Fund
Forward Price / Earnings	19.8x	13.7x	13.0x
Price / Book	4.4x	1.8x	1.6x
Dividend Yield	1.5%	3.2%	3.0%

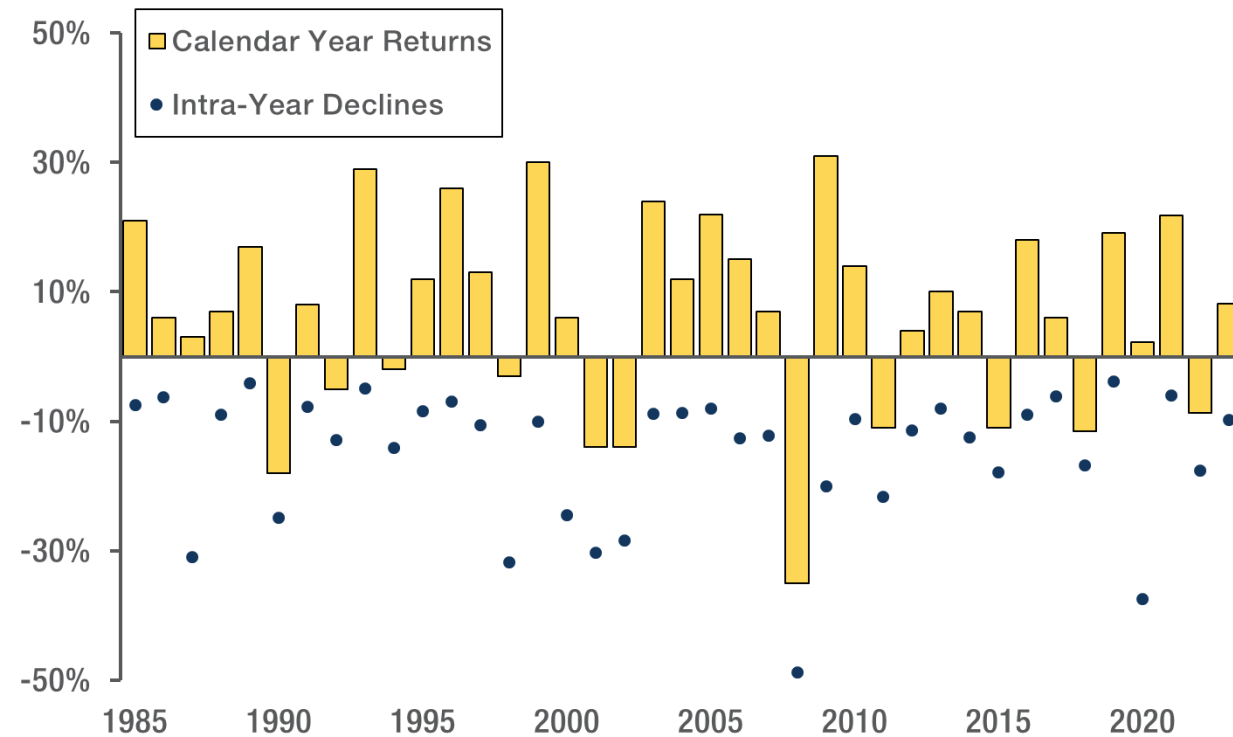
Nexus Equity Sector Allocation <sup>(1)</sup>

Comparable Valuation Metrics <sup>(3)</sup>

# Portfolio Overview

## Equities Deliver Over Time

Intra-year drawdowns are the norm – this can obscure the long-term rewards from equities



- Despite average intra-year declines of 15%, annual returns were positive in 28 of 39 years

S&P/TSX Composite Intra-Year Declines vs. Calendar Year Returns <sup>(1)</sup>

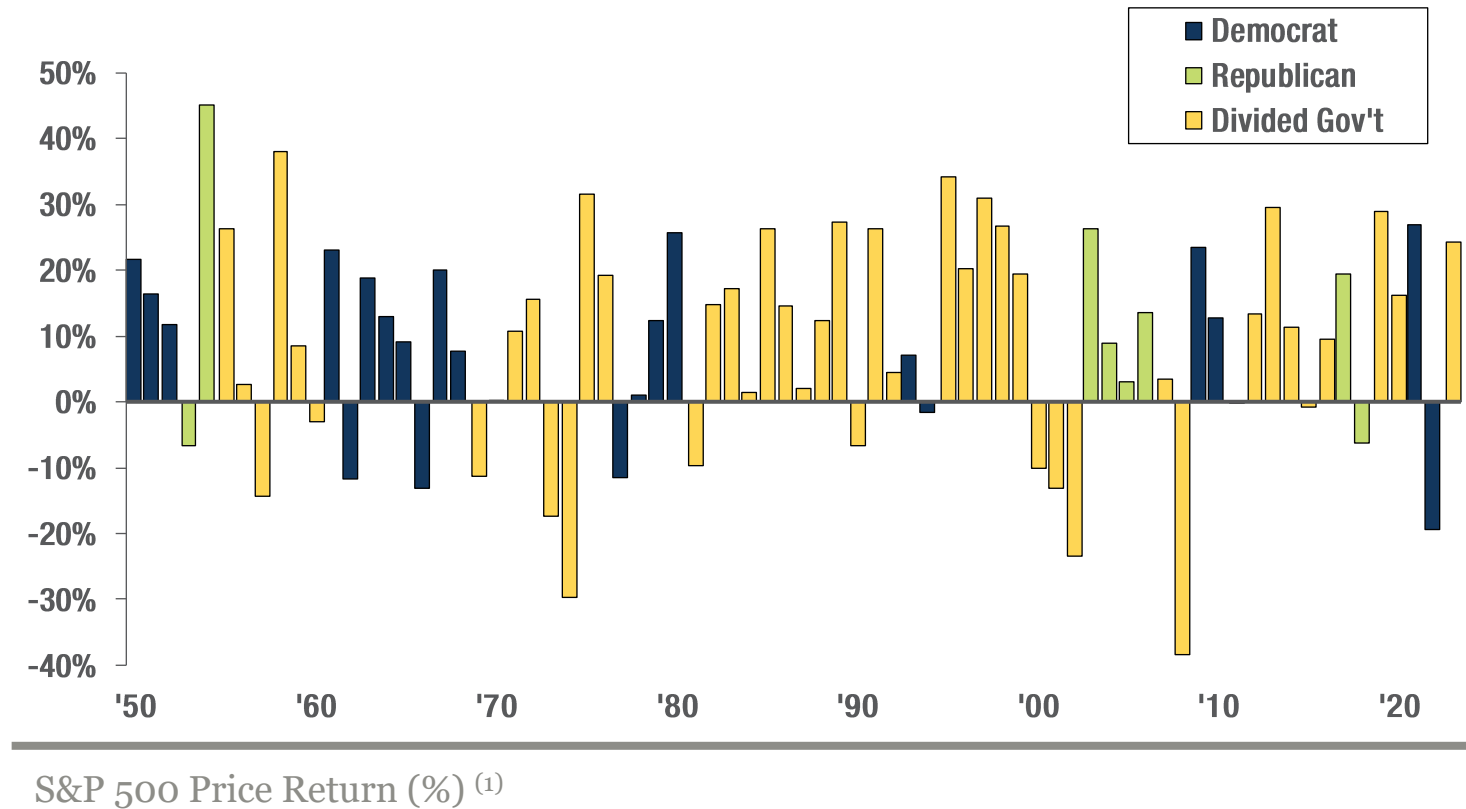
Source: Bloomberg.

<sup>(1)</sup> Returns are compound annual average, time-weighted, price-only rates measured in Canadian dollars and calculated without deducting any fees or expenses. Past performance is not indicative of future results. As of December 31, 2023.

# Portfolio Overview

## U.S. Election Outcome

Election outcomes have had little influence on long-term equity returns in the U.S.



- “Bull markets and bear markets come and go, and it’s more to do with business cycles than presidents.”

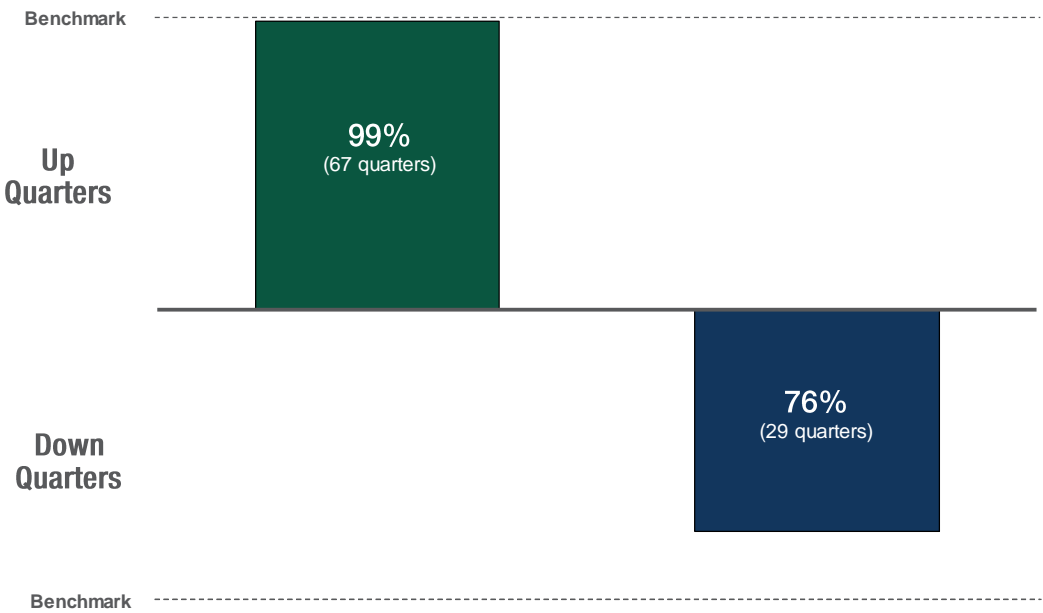
- Jeremy Siegel

<sup>(1)</sup> The chart represents the annual S&P 500 price return under different political scenarios. Green bars denote periods when the Republicans controlled both the White House and Congress; the blue bars represent periods of Democratic control over both the White House and Congress; and the yellow bars show instances of a dividend government, where one party controlled the White House, while the other held control over one or both houses of the Congress.

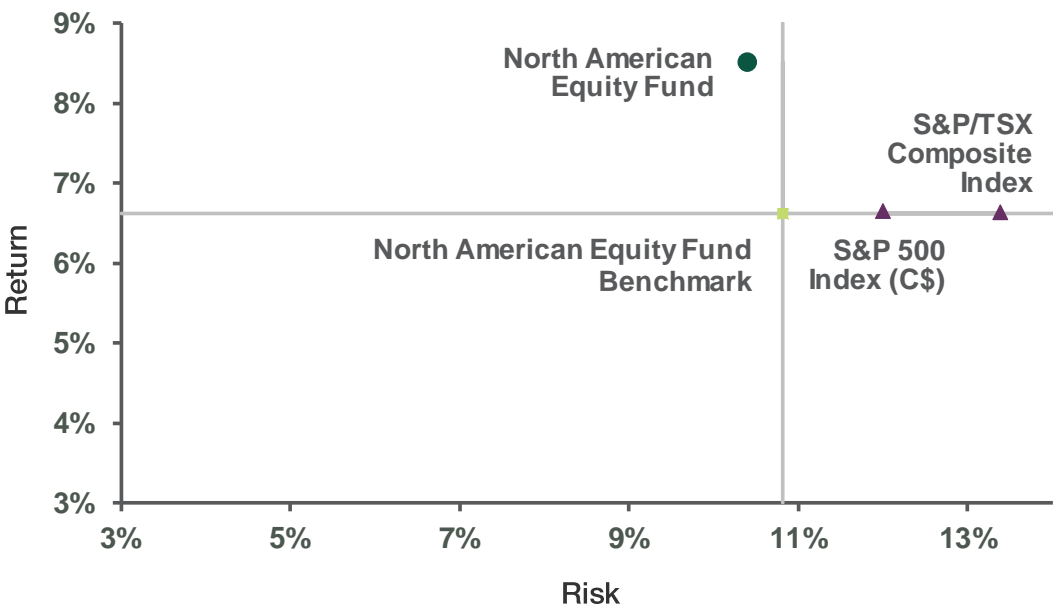
# Investment Performance

Equity Fund

Our approach has worked over the long term, with good downside protection



Equity Fund Up- & Down-Market Capture Ratios <sup>(1,2,3)</sup>



Risk / Return Profile Since January 1, 2000 <sup>(2,3,4)</sup>

<sup>(1)</sup> Each quarter since January 1, 2000 is defined as an “up” or “down” quarter based on whether the benchmark return for the quarter was positive or negative. For up (down) quarters, the capture ratio is the ratio of compound average rates of return for the Fund and its benchmark for such quarters. For more information about benchmarks, please refer to <https://tinyurl.com/NexusOnBenchmarks>.

<sup>(2)</sup> All Nexus returns upon which these charts are based are time-weighted, total rates measured in Canadian dollars and calculated after deducting such direct and indirect costs as applicable withholding taxes, trading commissions, custody fees and other fund/account expenses, but without deducting Nexus’s management fees (which are charged to client accounts and vary by client). Underlying returns for market indices and benchmarks are presented on the same basis, but without any such deductions. Past performance is not indicative of future results.

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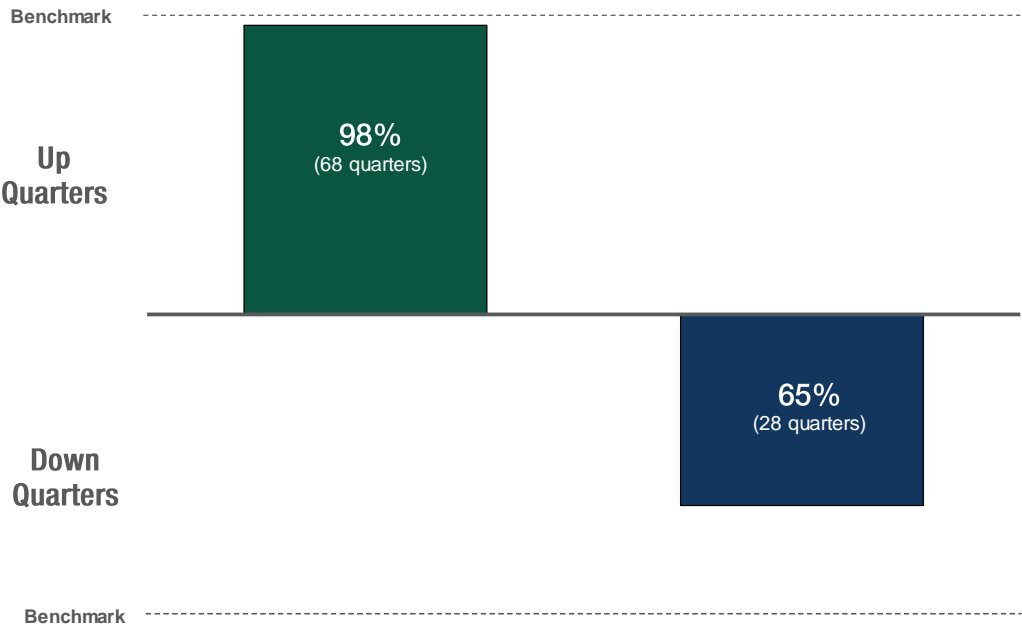
<sup>(4)</sup> Risk is calculated as the annualized standard deviation of monthly returns since January 1, 2000.

Period ending December 31, 2023

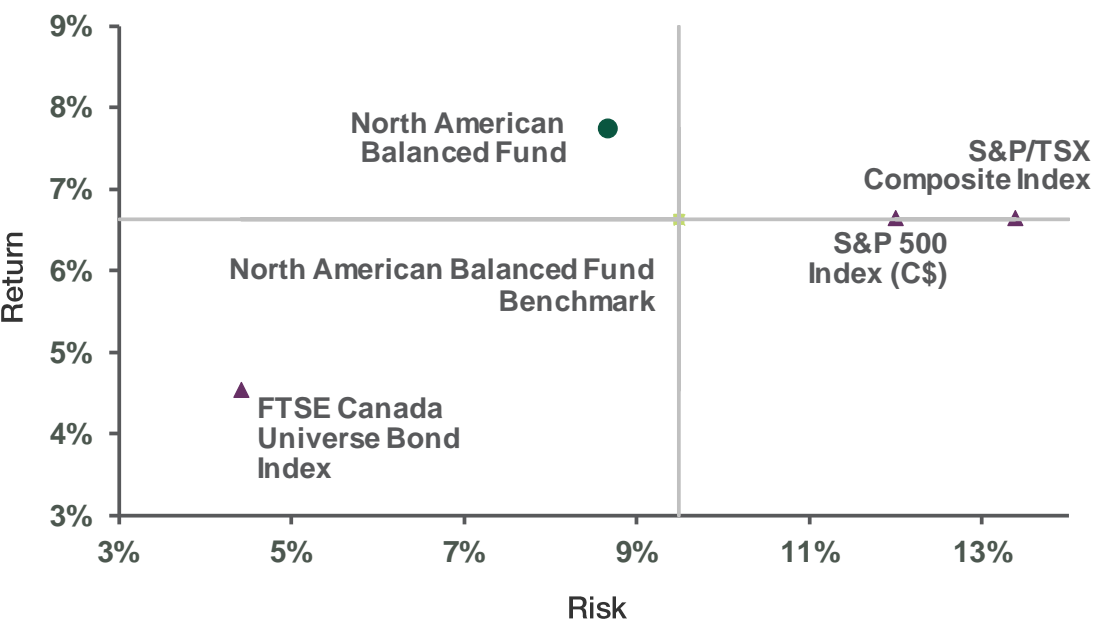
# Investment Performance

## Balanced Fund

Our approach has worked over the long term, with good downside protection



Balanced Fund Up- & Down-Market Capture Ratios <sup>(1,2,3)</sup>



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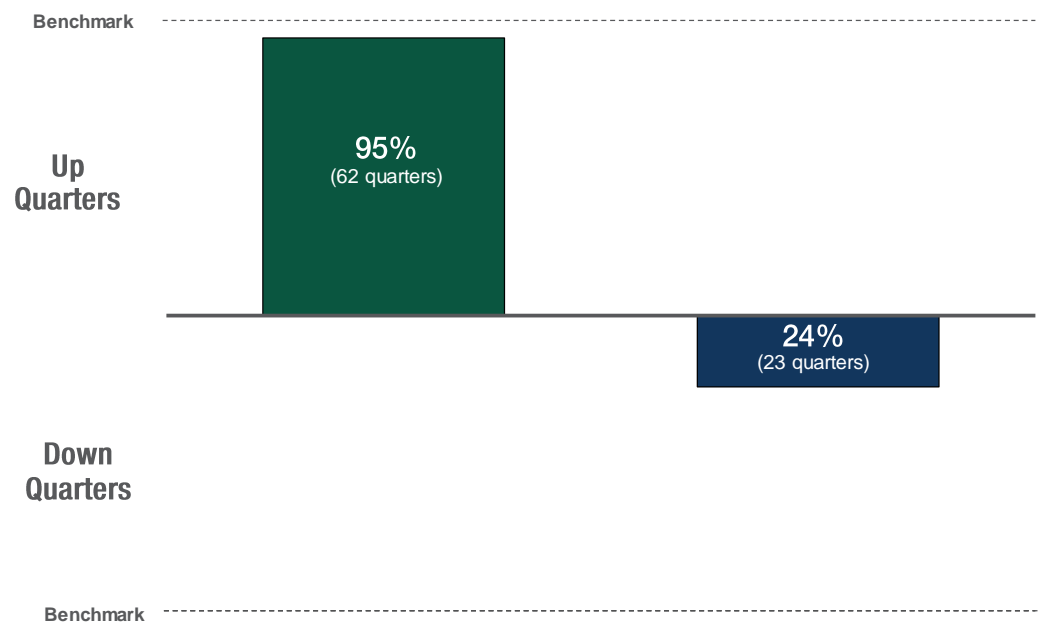
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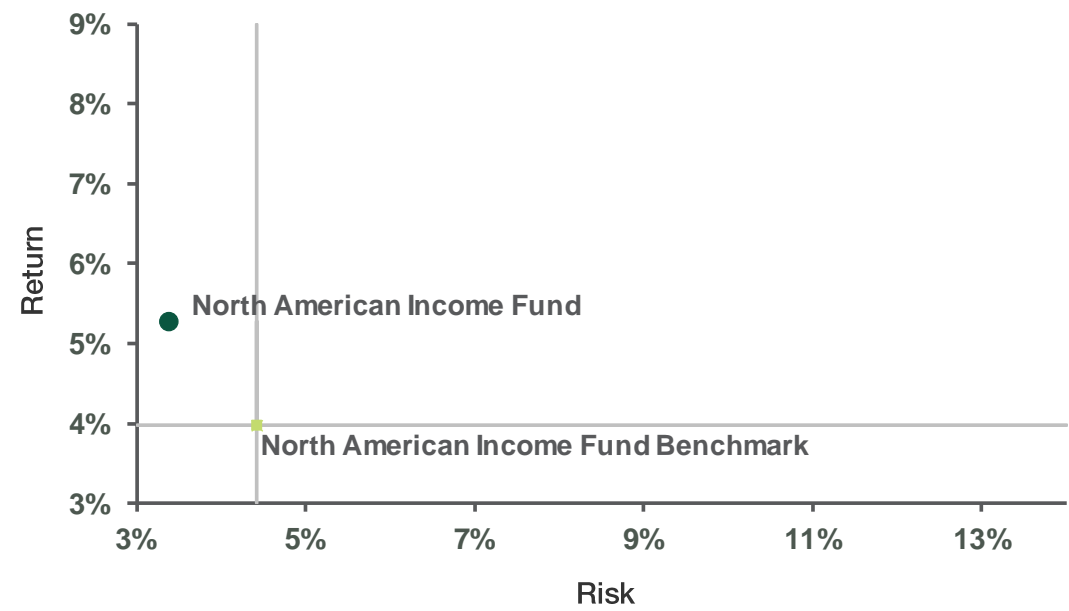
Period ending December 31, 2023

# Investment Performance

Our approach has worked over the long term, with good downside protection



Income Fund Up- & Down-Market Capture Ratios <sup>(1,2,3)</sup>



Risk / Return Profile Since October 1, 2002 <sup>(2,3,4)</sup>

<sup>(1)</sup> Each quarter since October 1, 2002 is defined as an “up” or “down” quarter based on whether the benchmark return for the quarter was positive or negative. For up (down) quarters, the capture ratio is the ratio of compound average rates of return for the Fund and its benchmark for such quarters. For more information about benchmarks, please refer to <https://tinyurl.com/NexusOnBenchmarks>.

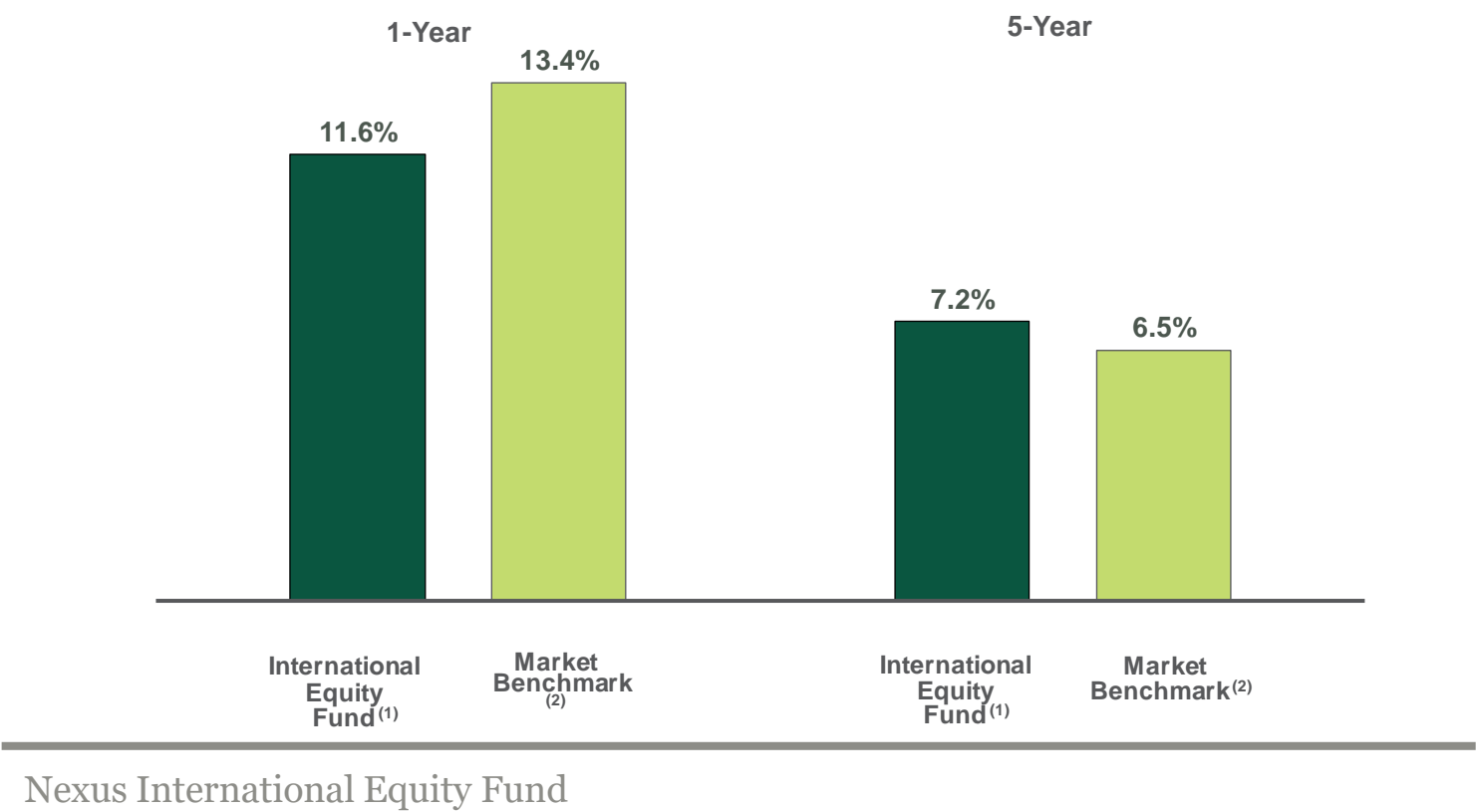
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# Investment Performance

Strong returns in the last year have helped the International Equity Fund rebound from a tough earlier period



Periods ended December 31, 2023

<sup>(1)</sup> All Nexus returns are compound annual average, time-weighted, total rates measured in Canadian dollars and calculated after deducting such direct and indirect costs as applicable withholding taxes, trading commissions, custody fees and other fund/account expenses, but without deducting Nexus's management fees (which are charged to client accounts and vary by client). Returns for market indices and benchmarks are presented on the same basis, but without any such deductions. Past performance is not indicative of future results.

<sup>(2)</sup> International Equity Fund market benchmark is 75% MSCI EAFE and 25% MSCI Emerging Markets indices (both in C\$); rebalanced monthly. For more information about benchmarks, please refer to <https://tinyurl.com/NexusOnBenchmarks>.

**NEXUS**

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