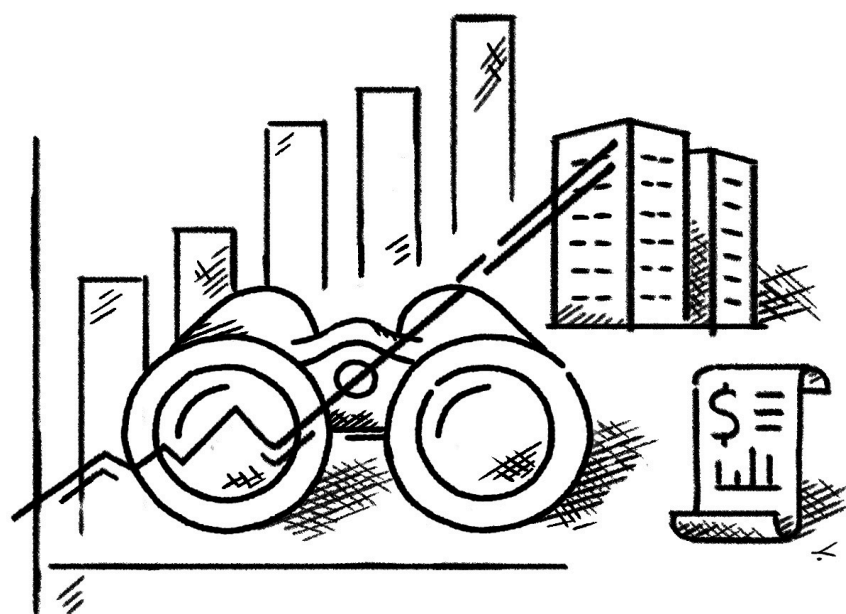


The Nexus Report

*Resilience in the Face
of Adversity*



Third
Quarter
2026

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Higher Rates, Higher Stocks

In the first quarter of this year, the main development for markets was the outbreak of the Iran war. In the second quarter, the market's attention shifted to AI and its opportunities and risks. By contrast, the third quarter brought to the forefront a less exciting development, but one that carries outsized consequences for the economy and markets: rising interest rates. Yet despite the sharp rise in rates, both Canadian and U.S. stock markets delivered solid gains.

To be sure, the topic of interest rates rarely competes with war, AI, or tariffs for attention at the Thanksgiving table. There is, after all, only so much enthusiasm for a surprise move in the 10-year Treasury yield. Nevertheless, for investors, interest rates matter enormously. They determine the cost of money throughout the economy and influence the value of everything from homes and businesses to stocks and bonds.

Why did interest rates move higher? While rising rates rarely have a single cause, one of the clearest connections this year has been among the Middle East conflict, energy prices, inflation, and interest rates. As oil prices moved higher, so too did concerns about inflation. Because oil is a key input in producing and transporting many goods, higher oil prices tend to ripple through the economy, raising costs, and, in turn, the prices paid by consumers. The prospect of higher inflation led investors to seek higher interest rates on long-term bonds. Simply put, if prices are expected to rise more quickly in the future, investors want to be paid more for lending money today. The result was an increase in long-term interest rates.

And the move was significant. The yield on the 10-year U.S. Treasury bond increased 87 basis points, its largest quarterly rise since 1994.¹ It finished the quarter at its highest level in more than two decades.² And to be clear, this is not just a U.S. phenomenon. During the quarter, yields on 10-year government bonds in the U.K. and Canada rose by more than 50 basis points.³ In France, the increase was even more dramatic at 125 basis points, a reminder that national fiscal

and debt considerations also influence bond markets alongside global forces such as energy prices and inflation.

One might have expected a difficult environment for equities given war, concerns about how AI may reshape industries and society, and rapidly rising interest rates. Instead, both Canadian and U.S. stock markets gained ground. The TSX Composite rose 1.6% in the quarter, bringing its year-to-date return to 13.0%, while the S&P 500 gained 2.3% in the quarter and 16.8% year-to-date.

The story was different in fixed income markets. As yields moved higher, bond prices moved lower, leaving most bond indices modestly negative year-to-date.

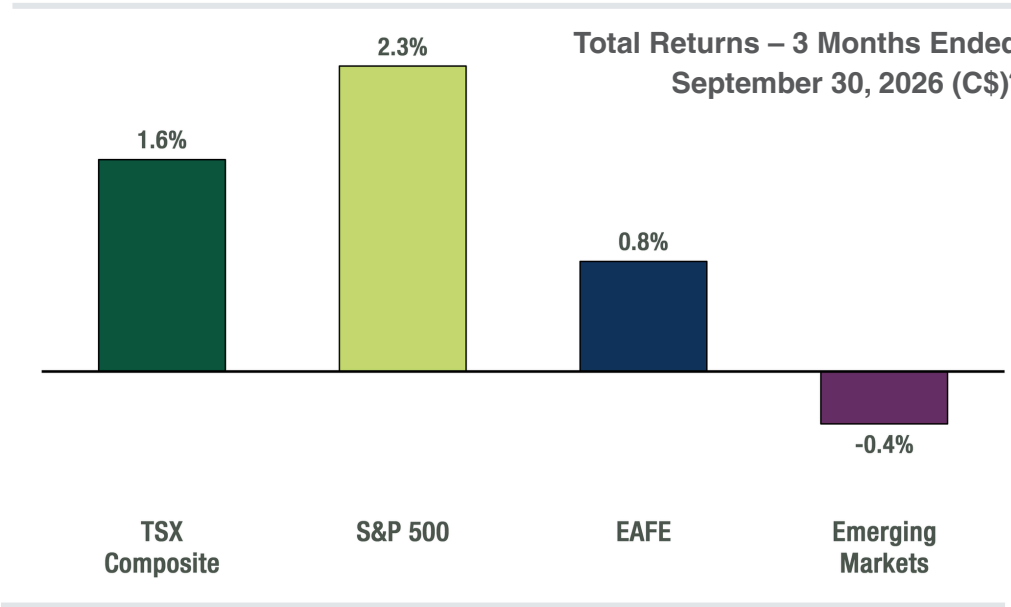
Yet some perspective is warranted. While today's interest rates are the highest investors have seen in years, they aren't particularly unusual by historical standards. Viewed through a longer historical lens, the ultra-low interest rate environment that followed the Global Financial Crisis may prove to have been the anomaly. A 5% U.S. Treasury yield may cause the talking heads to hyperventilate, but it's just not that unusual

to see interest rates at today's levels. That said, an economy financed at 5% behaves differently than one financed at 1%, with higher borrowing costs generally acting as a constraint on growth and investment.

Still Standing

So far, both the Canadian and U.S. economies have proven remarkably resilient despite this challenging backdrop.

Let's start with the data in Canada. Readers may recall that earlier this year, there was some discussion that Canada had entered a "technical recession," defined as two consecutive quarters of negative economic growth. As it turns out, that conclusion appears to have been premature. An initial estimate showing a slight contraction in first-quarter GDP briefly supported the recession theory, but by August the numbers had been revised to show the economy had actually expanded. Together, the first-quarter revision and a stronger-than-expected 3.3% annualized growth rate in the second quarter largely put to bed the recession debate. While growth remains modest, Canada's economy has proven more resilient than many had feared.



NOTE: Unless indicated otherwise, 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. Stock-specific returns are price-only returns, and for U.S.-listed stocks are in U.S. dollars. Past performance is not indicative of future results. For more information about benchmarks, please refer to nexusinvestments.com/benchmarks.

¹ Barron's, September 30, 2026.
² The Wall Street Journal, September 30, 2026.
³ Doug Porter, BMO Economics, October 2, 2026.
⁴ Bloomberg.

Market Outlook

Looking ahead, however, the more important question may be not simply how quickly Canada grows, but what drives that growth. In recent years, economic expansion has been driven in large part by adding more people. As population growth slows, headline economic growth may moderate. But if Canada can improve productivity and attract more capital, it could ultimately benefit from slower but higher-quality growth.

There are at least some encouraging signs in that direction. Our trade dispute with the United States has highlighted the risks associated with excessive dependence on a single trading partner. This has prompted efforts to diversify Canada's trade relationships and deepen economic ties elsewhere, including with Europe. At the same time, Canadian policymakers appear more focused on the need to improve productivity, attract investment, and strengthen our economic competitiveness. Recent efforts have included measures to encourage private-sector investment, attract international capital, and advance major infrastructure and energy projects intended to strengthen Canada's long-term economic capacity. Governments have a mixed track record when it comes to economic development, and big improvements in productivity are rarely achieved overnight. Nevertheless, we view the growing recognition of these challenges, and the efforts being made to address them, as constructive developments for Canada's long-term outlook.

Turning to the U.S. economy, the picture is somewhat mixed. Concerns about deficits and higher interest rates persist, while weak consumer confidence underscores that the benefits of economic growth are not being felt evenly across households, particularly lower-income households. Yet other core economic data continues to hold up relatively well. Layoff announcements remain below their long-term average, consumer spending has held up better than expected, and corporate profitability remains strong. U.S. corporate profits rose more than 20% year-over-year in the second quarter.⁵ Meanwhile, S&P 500 companies are on track to deliver a third straight quarter of earnings growth above 25%.⁶

At the beginning of this commentary, we noted how quickly the market's attention can shift. In the first quarter it was conflict in the Middle East. In the second quarter it was AI. In the third quarter it was interest rates. As we enter the final quarter of the year, attention is likely to shift once again, this time to the U.S. midterm elections.

Undoubtedly, there will be much angst and likely some market volatility before the contest and, once it's said and done, much ink spilled about what it all means for markets. Such concerns are understandable. Elections do matter, as they influence the policy direction of a country and can have meaningful consequences for individuals, businesses, and investors. However, historical experience provides some reassurance. According to the data, the S&P 500 has delivered positive returns in the year following a midterm election in 95% of instances dating back to 1938.⁷

One of the challenges of investing is that the source of uncertainty is always changing. Yet over time, market returns have been driven less by the headline of the day than by the ability of businesses to innovate, invest, grow, and create value. At Nexus, that is where our focus steadfastly remains.

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⁵ U.S. Bureau of Economic Analysis (BEA).

⁶ FactSet Earnings Insight, September 25, 2026.

⁷ "The Surprising Truth About Midterms and Stocks," *Fidelity Viewpoints*, August 12, 2026.

Choppier Beneath the Surface

Stocks ended the third quarter modestly higher, with the TSX Composite up 1.6% and the S&P 500 up 2.3%. But it was a tougher quarter than those numbers suggest, as the gains came from just a few sectors. In Canada, eight of the TSX's eleven sectors declined. Technology, led by Shopify, and Materials, led by gold miners, accounted for most of the gain, with Energy also contributing positively. Without them, the TSX would have finished lower. The U.S. told a similar story. Seven of eleven sectors declined, and the market's gains came mainly from large technology companies and the Energy and Health Care sectors.

Three forces shaped the quarter: oil, interest rates and AI. Renewed tensions in the Middle East and Ukrainian attacks on Russian refineries squeezed global energy supplies, pushing oil above \$100 a barrel and diesel prices to record highs. That was good news for oil producers and refiners, but it revived fears of inflation. Bond yields rose sharply in response, with the 10-year U.S. Treasury yield reaching a nearly 20-year high. Higher yields hit rate-sensitive stocks such as utilities, telecoms, pipelines and real estate. Consumer stocks fell too, on worries that higher prices and borrowing costs would squeeze household spending. Even the AI trade cooled, as chip stocks pulled back. But a handful of large technology companies more than offset that decline with strong AI-related results and new products.

North American Equities

Our Canadian holdings declined by 1.2%, giving back some of the prior quarter's extraordinary 11.2% gain. We lagged the TSX because we don't own gold stocks or Shopify. Each carries a large weight in the index, and together they drove most of its gains. Our energy holdings helped offset some of this, with Cenovus Energy and Suncor Energy each rising more than 25%. We pick stocks on their merits, not on how big they are in the index. So our results will sometimes look quite different from those of the index. This was one of those quarters.

In the U.S., that difference worked in our favour. Our U.S. stocks gained 5.1% in the quarter, well ahead of the S&P 500. Microsoft and Meta Platforms led the way, along with our healthcare holdings Thermo Fisher, Gilead and Pfizer. Ross Stores, a U.S. discount retailer similar to Winners, also posted strong gains despite the pressure on consumer stocks.

We made a few changes during the quarter. Early on, we added to Microsoft. The stock had fallen through the year on worries about AI disrupting its software business, a concern we felt was overdone. That concern faded after a strong earnings report in late July. We also trimmed Ross Stores. After a strong run, it had grown into a larger share of the portfolio than we wanted, so we took some profits to keep the position size in check.

We also bought a new position in The Southern Company, an electric and natural gas utility serving the southeastern U.S., mainly Alabama and Georgia. We like it for two reasons. The first is stability. Southern is the only provider in most of its territory, and regulators set its rates to earn a fair return on what it invests, which gives it steady and predictable earnings. It has also paid a dividend for nearly 80 years, raising it for the last 25. The second is an improving growth outlook, which is unusual for a utility. Increased demand from data centres powering AI has driven growth in electricity demand, and Southern is well placed to supply it.

International Equity Investments

International markets were mixed in the quarter. Developed markets posted a small gain, while emerging markets declined modestly. Japan was the standout among developed markets, supported by strong corporate earnings and ongoing governance reforms that continue to push companies to be more shareholder friendly. UK equities also finished higher, helped by their large exposure to energy and commodity-related sectors. On the other hand, continental European stocks lagged. Investors worried that rate hikes from the European Central Bank, rising bond yields and limited exposure to the AI theme would leave the region's earnings growth behind the rest of the world. Emerging markets took a breather after a strong first half of the year, as the AI-related semiconductor stocks that had powered the rally led the pullback this quarter.

We continue to hold two externally-managed international pooled funds.⁸ EQIT (international developed market equities) declined 0.1%, and EMEC (emerging market equities) declined 4.5%, both trailing the market in the quarter. During the quarter, we trimmed EMEC following its strong run this year and reinvested the proceeds in EQIT, where we see better value.

International equity exposure remains an important diversification tool within our portfolio. It provides us with essential access to a broader universe of companies with distinct growth profiles and attractive valuations. The macro factors that influence international markets are often unique to those regions, which provides uncorrelated performance and volatility characteristics that complement our North American holdings.

NOTE: The overall and geographic level return data in this section are for the Equity Fund. Equity returns within the Balanced Fund were similar. For specific performance, please refer to your own quarterly report.

⁸ Both pooled funds are managed by teams from J.P. Morgan Asset Management in the U.K. and are held in our International, Equity, and Balanced Funds.

Higher Yields Weigh on Returns

Canadian fixed income markets came under pressure in the third quarter as government bond yields rose sharply. The FTSE Canada Universe Bond Index returned -3.0%, while our bond holdings declined a more modest -1.4%. Over the past 12 months, our bonds returned +0.5%, compared with -1.1% for the benchmark.

The weakness in the quarter was primarily the result of higher government bond yields. Canadian government yields rose between 52 and 68 basis points during the quarter, with some of the largest moves occurring in two- and five-year bonds. The 10-year Government of Canada yield ended September at 3.99%, while the 30-year yield reached 4.30%. As bond prices move inversely to yields, this rapid adjustment pushed prices lower and weighed on returns.

We have written recently about how higher yields can provide a cushion against capital losses when interest rates rise. This quarter was a reminder that this cushion has its limits when rates move sharply over a short period. However, the increase in yields leaves bond investors better positioned today, with higher income providing a greater buffer against future rate volatility.

Canada’s Economic Climate

The economic picture remains mixed in Canada. GDP grew at an impressive 3.3%⁹ in the second quarter. Current estimates are for third quarter growth of approximately 1.9%, reflecting tariff-related headwinds that have led forecasts to be revised lower.

Inflation has remained stubborn. Headline CPI was 3.0% in August, above the Bank of Canada’s 2.0% target, while manufacturing input prices reached their highest level since July 2022 in September.

Together, modest economic growth and persistent inflation have complicated the outlook for interest rates.

The Bank of Canada

The Bank of Canada held its overnight rate at 2.25% in September for a seventh consecutive meeting. However, its messaging became more cautious about inflation, including the potential effects of tariffs and geopolitical developments. In a speech given in Halifax in September, Governor Macklem warned that policymakers do not want to be late in raising rates should inflationary pressures persist. This change in tone contributed to higher short-term bond yields and increased expectations that the Bank will raise rates before year-end.

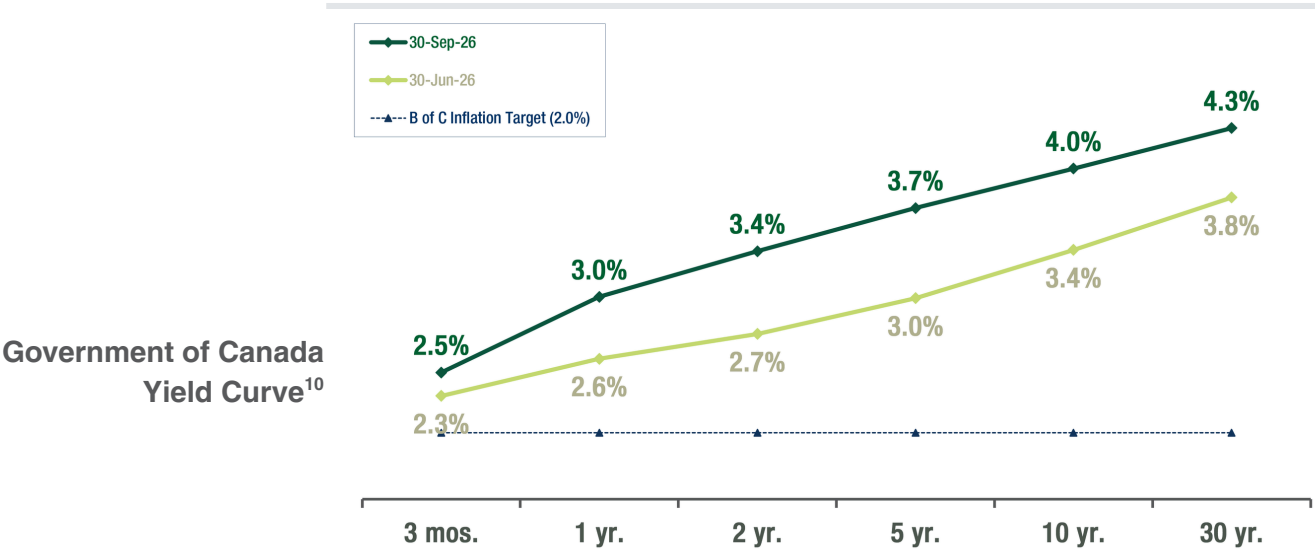
Canada Is Not the U.S.

While Canadian yields have risen meaningfully, the move has been relatively measured compared with the U.S. Canadian yields remain well below comparable U.S. yields, with the gap approaching historically wide levels. For context, the Canadian 10-year yield ended the quarter 135 basis points below its U.S. counterpart. This divergence reflects higher policy rates, higher inflation and economic growth in the U.S., as well as heightened concerns surrounding the country’s fiscal position.

Bonds Becoming Slightly More Attractive

The speed of the recent rise in Canadian yields is notable. Current yields may be justified by the economic and inflation backdrop, but they are also becoming increasingly attractive to investors. Should geopolitical tensions ease and oil prices decline, inflation concerns could moderate, creating an environment in which bond yields could move lower.

During the quarter, we extended portfolio duration slightly to 4.2 years, as we cautiously took advantage of the increase in yields. Our portfolio duration remains meaningfully shorter than the benchmark. We believe this continues to strike an appropriate balance of capturing higher yields while maintaining positioning that is reflective of our approach to fixed income investing.





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