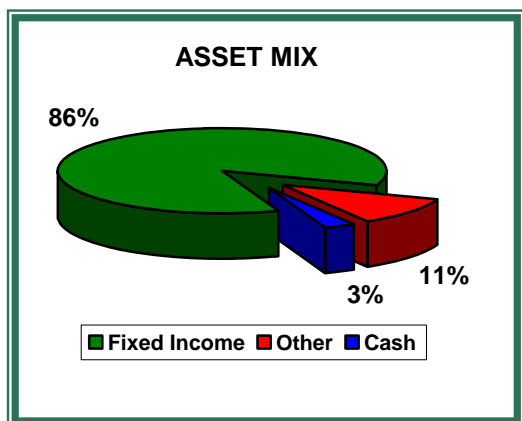


NEXUS NORTH AMERICAN INCOME FUND

QUARTERLY REPORT – June 30, 2008

The worry that characterized capital markets in late 2007 and early 2008 continues. Investor sentiment began the latest quarter with the hope that the well-documented economic woes (particularly in housing and the financial sector) would be contained. However, sentiment has changed for the worse over the course of the quarter and worry that the troubling issues that face the economy are unresolved and may have deteriorated is now beginning to be reflected in asset prices. The problems of the financial sector have now clearly spread to the wider economy and economic activity around the globe is decelerating. In North America, and particularly the United States, many harbingers of a traditional recession are in plain view. Unemployment is rising, consumers are spending less and industrial activity is operating below full capacity. After a long period of economic expansion, we have moved into an environment that, if not contracting, is certainly much less buoyant than recent history. This sort of experience is unsettling, but it is part of a natural cycle of economic activity.

If there is anything this time that seems different from the previous experience with the natural rhythms of the economy, it is that accompanying this period of economic slowdown there has been a pick-up in the measured rate of inflation around the globe. In North America, the decline in the value of the U.S. dollar, combined with robust resource demand in emerging markets has fueled price increases in a number of basic commodities, particularly energy. In the developing world, where spending for basic necessities, particularly food makes up a higher proportion of personal income, food price inflation has also risen sharply. At this time, it is unclear whether inflationary prices will be limited to the change in commodity prices, or whether it is more pervasive and will be passed through to other goods and services.



A mix of slowing economic performance and higher prices reminds investors of the debilitating period of 'stagflation' that was experienced in the late 1970s. It is a comparison that is not well founded, as present circumstances differ substantially from the situation back then. Nonetheless, the Bank of England, the European Central Bank, the U.S. Federal Reserve and the Bank of Canada have each announced that staying ahead of the pernicious effects of inflation remains a top priority and we would expect them to follow with tighter monetary policies should commodity price pressures flow through to higher prices for finished goods and services - a possibility, but not a probability in our estimation. For now, there is little evidence that companies in North America are able to

increase the prices for consumer goods and services. Instead, companies continue to absorb higher input costs with lower profit margins. Likewise, workers are not 'winning' inflationary wage increases. In fact, unit labour costs are well controlled and productivity has been improving as the economy sheds jobs. In the coming months, we expect measured headline inflation will remain at elevated levels with energy prices continuing to pressure prices higher. However, a soft economy and declining prices for 'bigger ticket' items such as cars, appliances and even shelter (housing) will mitigate the effects.

Canada has enjoyed a period of relative stability in 2008. On a year-over-year basis, headline inflation released in May was 2.2% and the core rate was only 1.5% - enviable circumstances as compared to the experience in the U.S. and Europe. Equity markets have rebounded from their March lows and despite a weak month of June, are still 6% ahead of where they began the year. Although they have

moved higher over the course of the quarter, interest rates remain low in absolute terms, and fixed income returns have been positive for the year-to-date. This relatively benign capital markets experience belies a far different experience for many Canadians. In fact, the issues of imbalance between regions and industrial sectors is as acute now as it has been since we first worried about the 'Dutch disease' more than three years ago. The disparity between the economic performance in the resource-rich western provinces and the manufacturing and export-oriented provinces of Ontario and Quebec has likely never been larger. The new Bank of Canada Governor, Mark Carney, likely wanted to establish his inflation fighting credentials when the Bank defied market expectations and left the Bank Rate unchanged at 3% in early June. However, in the absence of a pick-up in the core rate of inflation, we expect that economic conditions will lead to reductions in short-term interest rates between now and the end of the year.

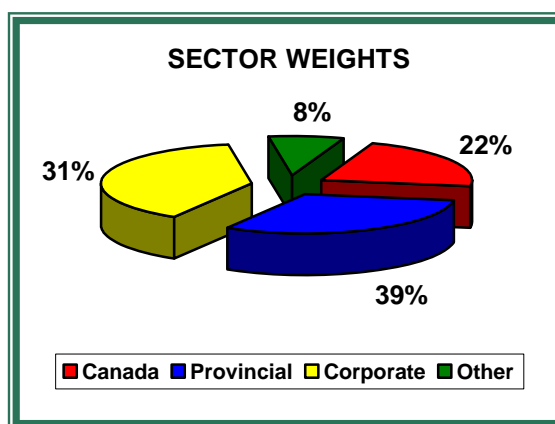
Due to the increase in interest rates, the Fund declined 0.9%¹ in the last quarter, and is now up 1.2% for the year-to-date. The DEX Universe Bond Index (DUBI) was lower by 0.7% for the quarter and increased 2.2% so far this year. While our bond results remain ahead of the DUBI this year, a decline in the value of our holdings of "other income-producing securities" is the cause of our trailing performance in 2008. The Fund continues to maintain its out-performance relative to the DUBI over longer time periods.

Asset Mix

Our asset mix has remained basically unchanged over the quarter. Our allocation to traditional fixed income is high at 86%, our holdings of cash equivalents is low at 3% and the balance of 'other income-producing' securities remains at 11%.

Fixed Income Summary (86% of Assets)

Since the middle of 2007, when investors became aware that serious issues existed in the global financial system, there has been widespread expectations that Central Banks around the globe, in order to discourage any further seizing-up of the financial system, would lower official interest rates. Between November 2007 and March of 2008 the Bank Rate was lowered from 4.5% to 3.5%. In the United States, where the financial crisis was more extreme, the Federal Funds rate was pushed to 2.25%. However, it is now clear that low interest rates alone will not solve the problems of economic malaise and financial system quality, and that expectations for lower policy rates had become too widespread. We believe that the remedy of dramatically lower interest rates has been contributing to a devaluation of the U.S. dollar and a rise in commodity prices denominated in U.S. funds. At this time the necessary fiscal and monetary policy prescriptions to address the economic slowdown and market dislocations requires little more in the way of interest rate decreases.



In late April, the Bank of Canada followed through with a widely expected cut to the Bank Rate which brought the level to 3%. Likewise, the U.S. Federal Reserve lowered its target rate for Federal Funds to

¹ Fund returns are shown before the deduction of management fees but after the deduction of direct expenses.

2.0%. Both central banks have since passed on opportunities to adjust their rates further and have issued press releases to underscore their current 'wait and see' approach to the unfolding economic picture. As a result, there has been some modest disappointment in bond markets that the days of very easy money may be behind us. Interest rates have risen across the yield curve, most noticeably for shorter maturities where the effect of central bank policy has the greatest influence. Canadian 2 year bonds have risen 0.63% from 2.62% to 3.25%, while 10 year bonds have risen almost 0.30% from 3.44% to 3.74%. We continue to maintain a position that reflects our two main points of view. The first is that interest rates for longer-term maturities are not particularly attractive, except in the instance of extremely unlikely dire economic developments. The second opinion we hold is that further reductions in Canadian short-term interest rates may be necessary as the effects of a slowdown in economic activity in the U.S. continue to work their way through our economy. The consequence of this view is that we expect that interest rates for shorter maturities could actually decline somewhat between now and the end of the year, but that interest rates for longer dated bonds could yet move higher. Most importantly, the order of magnitude of these changes should be small. The bond markets will continue to be a reasonably unexciting asset class, offering safety and modest returns over the coming months.

The spreads between the interest rates paid by well-rated bond issuers and the interest rates on Canada bonds continues to remain wide. In Canada, the corporate bond market has long been dominated by bonds of companies in the financial services industry. Given the worries regarding financial industry solvency, these spreads are expected to remain wide. Even with the many issues facing the Canadian banking industry, it is in far better shape than its counterparts in Europe or the United States. Over the course of this quarter we have reduced our corporate bond exposure and added to provincial and Canada bonds. In the interest of diversification, we have also reduced our concentration in certain corporate names such as GE Capital Canada and added to holdings of previously unrepresented issuers, such as Manulife and Sun Life.

Other Income-Oriented Securities (11% of Assets)

Last quarter we noted that in the interest of maintaining quality, we had sold our holdings of the Bank of Montreal and purchased the shares of the BNS, TD and the Royal Bank. This quarter, we also sold our holding in Bank of America as well as Wells Fargo. Bank of America had held up reasonably well compared to other large U.S. banks, but we felt that given the scope and breadth of its operations (it holds 10% of the US banking industry deposits) it had become a proxy for the US banking sector. Despite an attractive valuation, it wasn't plausible that at its size it could perform meaningfully differently than the entire industry. Since selling it, it has declined a stunning 37% and now yields more than 10%. At these levels, we are watching it carefully to see if it could be re-introduced to the portfolio. For now we are waiting until the issues of the U.S. banking industry become clearer to us. Similarly, despite the fact that Well Fargo has a great long-term track record, it seemed increasingly improbable that a major home mortgage lender, based in markets such as California, where home prices have been very badly affected, could continue to avoid a major write-down. Both of these institutions will be long term industry survivors, but given that each has serious issues of their own to deal with, neither will be able to take advantage of the inevitable strategic opportunities that will inevitably arise as the industry sorts itself out.

Our investments in this sector remain concentrated in banks and utilities, as well as four stable income trusts. While they have had a negative impact on the Fund in the year to date and the last quarter, we continue to believe that an allocation to this sector will enhance long-term returns to unit holders.

