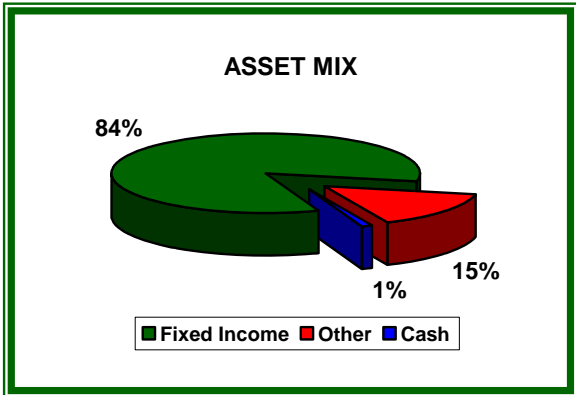


NEXUS NORTH AMERICAN INCOME FUND
QUARTERLY REPORT – September 30, 2009

Over the course of this quarter the global economy continued its unsteady recovery. On any given day, an economic release in one country might suggest further economic weakness, only to be followed by a release, perhaps in another part of the world, which held out hope that recovery was at hand. However, by any reasonable standard, the recovery remains as much anticipated as it is evident at this point in time. Where our hopes are highest for economic recovery are the emerging economies of China, Southeast Asia and South America, which now represent almost 30% of global GDP. For many years, growth in these economies derived either from growing exports to North America and Europe, or from capital investment in machinery and infrastructure. In this recent recovery, growth has been led in large part by local domestic demand, which arose from fiscal stimulus and low interest rates. As a consequence, the growth of these developing economies is likely to be more self-sustaining and less reliant on a recovery in the developed world.

In Europe and the U.K., the case that a durable recovery is underway remains speculative. Encumbered by a legacy of fiscal rectitude as well as the drag of an aging population, a co-ordinated policy response across all countries has been unsuccessful in generating an immediate economic recovery. Many measures of economic activity such as retail sales and industrial production remain weak, while certain forward indicators, such as business sentiment, suggest that there is some light at the end of the tunnel. What has been good news this quarter is that real estate prices across Europe, and particularly in the U.K., have begun to stabilize. There is clear improvement in this part of the world, but it should not be confused with a solid cyclical recovery just yet.

Discerning an economic trend in North America remains challenging. For better or worse, the U.S. continues to lead the world with aggressive fiscal and monetary stimulus. While business sentiment in both Canada and the U.S. has greatly improved, consumer confidence and spending suggests there are reasons to remain cautious. In particular, employment in the U.S. remains particularly worrisome. At a current level of 9.8%, unemployment continues to grow and this measure excludes the millions of Americans who have given up looking for work or who are 'under-employed'. Given the unprecedented degree of fiscal stimulus (now more than 13% of GDP) some rebound in economic activity ought to be taken for granted. The fact that the recovery so far is muted, suggests that the U.S. has significant structural challenges that still need to be dealt with. For example, the unavoidable de-leveraging of the over-indebted American consumer will act as a drag on growth for many years to come.



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Thankfully, this contrasts with the situation in Canada where there is evidence that weakness in the labour market is receding. The recovery in the emerging world has put a floor underneath commodity prices and Canadian consumers do not have the same structural de-leveraging ahead of them that is so prevalent in the U.S. Low interest rates and fiscal stimulus are generating the seeds of a recovery, but a strong currency and weak exports, particularly to the U.S., make a durable recovery here very much in question.

In short, our worst fears of economic calamity continue to recede but the dawn of a traditional cyclical recovery is still a hope rather than a reality.

Notwithstanding the uncertain economic picture, the Fund gained 4.1%¹ in the last quarter, and is up 11.7% in the last 12 months. The DEX Universe Bond Index gained 2.7% over the quarter and increased 10.3% since last September. Our bond performance continues to be excellent with our holdings continuing to run well ahead of the index.

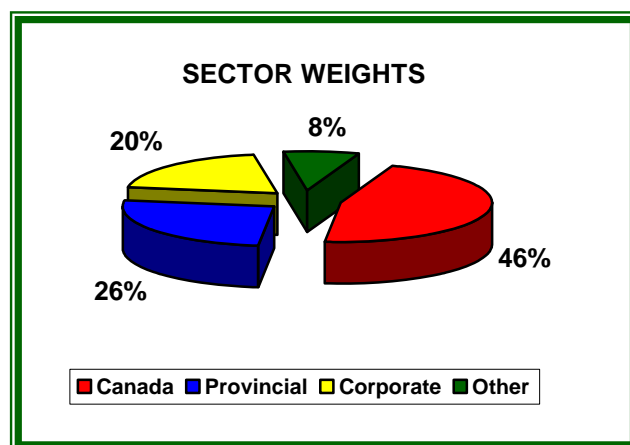
Asset Mix

We increased our allocation to 'other income-oriented securities' from 12% to 15% this quarter at the expense of our cash position which we have kept low. Our allocation to bonds is 84%, unchanged from last quarter and our holding of cash equivalents is now 1%.

Fixed Income Summary (84% of Assets)

Government of Canada interest rates have been unusually steady in 2009, and the Canada bond market has been an unexciting, but safe, haven for investors. The same is not true for investors in the corporate and provincial sectors of the bond market, where interest rate spreads between lesser quality credits and Canada bonds have compressed enormously. As a result, prices and returns in these sectors have greatly outpaced the Canada sector.

Put another way, divining Bank of Canada policy and predicting changes in the level of interest rates or the shape of the yield curve has been much less fundamental to investment success than has been having exposure to corporate and provincial bonds in a period where they greatly outperformed Canada bonds. In Canada, the corporate bond market is dominated by financial companies, particularly the major banks. At the start of this year the spread between bank deposit notes (the highest credit quality) and Canada bonds was 2.50%. At the end of the quarter this spread was only 0.60%. For issues of lesser quality the spread compression has been even more dramatic. Indeed, one class of bank debt known as hybrid notes has improved by almost 4.0%. The corresponding price appreciation of these securities has been more than 20% in many instances.



We have had a generous exposure to provincials and corporate bonds for much of the year, although we locked-in profits and reduced our exposure over the last quarter. By reducing our corporate exposure we have lessened the opportunity for gains should credit spreads tighten further or disappointment should credit spreads widen out again. These are hardly normal times, yet spreads are back to levels that pre-date the current crisis. Using a long look back at history, there is room for spreads to tighten further. But we prefer to navigate the coming period with higher quality and more liquid Canada and provincial bonds.

Although parsing the statements of central bank speakers or reviewing the minutes of the policy meetings of the Bank of Canada or the U.S. Federal Reserve has not been key to success yet this year, it's still necessary to pay attention. In both Canada and the U.S., headline inflation is significantly negative² and

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

² In August 2009, Canadian headline CPI was -0.8%, and U.S. headline CPI was -1.5%.

core inflation, a measure that excludes volatile food and energy prices, is running below 1.5%. The Bank of Canada explicitly targets inflation with both a lower and an upper band. At current levels, inflation is well below target and, as a result, we expect government bond rates to remain very low for some time yet. As for the U.S., Mr. Bernanke has been musing about the need to be prepared to drain liquidity from the banking system and tighten monetary policy. But the fragile economic fundamentals make us think that this is a remote possibility in the coming year.

As we stated last quarter, the wild card that could upset our rather dull interest rate outlook is the issue of international confidence in the value of the U.S. dollar. Massive deficits, as have been planned in the U.S., must be financed with foreign savings. There is a growing suspicion that future economic growth and / or increased taxes will be insufficient to pay down the debt burden that is currently planned. In such a case, servicing the debt and paying it off may require a devaluation of the U.S. dollar or a rise in inflation. The current administration seems much less concerned with a devaluation of the U.S. dollar and the risks that come with it than many international investors would like. Recent U.S. dollar weakness and commodity price strength could yet flare up into more serious problems.

The Fund's bond returns continue to be very satisfactory. The Fund's fixed income returns were +3.3% for the quarter and +12.3% in the last 12 months. By comparison, the DEX Universe Bond Index was +2.7%, and +10.3% for the same periods.

Other Income-Oriented Securities (15% of Assets)

We remain below our limit of a 20% allocation to this sector, although we did increase our allocation by 3% over the course of the quarter. We added no new names to our list of holdings, but increased our positions in nine different holdings. Perhaps the most notable change this quarter was that we sold our small position in Manulife Financial. Manulife was a reasonably new addition to the Fund, added at the start of the year when its price was depressed and its dividend yield very high. Over the course of the year, its price increased from what we had paid for it, but in August, in a move to preserve capital, it elected to reduce its dividend by 50%. Apart from substantially reducing the income generated by the holding, it became clear that the board and the new CEO were moving in a different strategic direction than we had previously assumed. Manulife remains a core holding at the Firm and likely has excellent long-term prospects for growth. However, we no longer consider it as an income-oriented security and feel more comfortable in this portfolio with it removed.

This quarter, our allocation to 'other income-oriented' securities again had a very positive impact on the Fund, rising 10.9%. We now own 13 different securities spread across 7 industrial sectors and continue to believe that an allocation to these securities will enhance long-term returns to unit-holders.

