MFM HATHAWAY FUND

INVESTMENT ADVISER'S REPORT

For the year ended 30 September 2005

We have pleasure in presenting the Investment Adviser's report on the MFM Hathaway Fund – an *equity and bond* unit trust – for the year ended 30 September 2005.

Since we started our work, launching the fund in November 2002, the mid-price of an *accumulation* unit has risen from the starting point of 50p to 72.355p at the end of the period under review, a gain of over 13% compounded annually.

During a year of more robust confidence in securities markets, our unit trust continued to consolidate gains made in the first two years of its life; the fund *total return* performance came in at +16.4% over the twelve months, continuing the progress toward our long-term aim of exceeding the return on the stockmarket.

Year*	MFM Hathaway Fund*	Benchmark	FTSE All Share Index (Equities)*	FTSE All Stocks Index (Gilts)*
2002/3	+13.1%	+ 6.7%	+ 8.2%	+ 3.3%
2003/4	+ 9.8%	+ 9.8%	+12.1%	+ 4.4%
2004/5	+16.4%	+19.7%	+ 24.7%	+ 8.2%
Cumulative	+44.7%	+40.2%	+ 51.4%	+16.7%

In the twelve months, the fund lagged our "benchmark" which returned +19.7% (that gauge – as recorded in the second column above – being the amalgam of the two indices beside it, reflecting our actual asset allocation), illustrating what often happens in sharply rising stockmarkets – speculatory fever breaks out – in the face of which our *value investing* philosophy leads us both to be ever more sceptical and not to try to participate in that hazardous development.

Indeed, the actual business growth, of the companies driving the rise in the stockmarket, underperformed the hike in their shares, confirming the speculative nature of those price advances (there was no game of "catch-up" to be played); accordingly, our levels of cash and short-dated bonds remained high during the year.

The advantage of our philosophy was illustrated to our investors, when company shares fell quite sharply (*minus* 4.6%) in the month of October, since our fund only fell half as far in that time; our risk-averse stance and use of bonds to provide a *margin of safety*, again came into its own and of course we have always said that it is in a falling market that you set yourself up to achieve long-term superiorities over the average.

The fund's outperformance of our benchmark, since we launched the fund in 2002, is again wide – at the date we drafted this report – buttressing our confidence in the *value investing* philosophy and qualifying the statistical showing recorded above.

Equally, we are pleased to see that, since launch, our equity commitments have returned approximately +57% (an advance which has increased since that fund year-end figure), well ahead of the stockmarket, so continuing the outperformance of our chosen companies, as highlighted in our interim report in the spring; our growing list of investors have therefore generally received (depending, in the short term, on when they joined us), greater rewards than the level of risk they have run so far would indicate, which is our long-stated goal.

We continued to receive satisfactory reports from our investee companies and funds during the period (we have previously observed, of course, that only business performance can justify an investment and not some stockmarket quotation the next day, week or month), while the upward spike in the equity market was of no help to us and our caution grew at the same rate as the desire for risk of the average investor; we continued to remain highly patient during the period and our only demonstrable effort was to keep reading and looking at security values.

Indeed, we said in the interim report in the spring of 2004, that we prefer falling security prices in order that we can acquire long-term values at sensible prices and, as we say above, those conditions simply did not prevail in the year, to any degree and there were few, if any, interesting investments to be made in the equity sector although we keep looking (the only changes were caused by corporate reconstructions or redemptions).

We would again single out – as particularly gratifying – the business reports from Wolseley (in plumbing and lumber), while Lloyds TSB continues to make progress (and to pay out a handsome dividend to shareholders) in the face of long-standing pessimism in the financial press, which does not accord with our view of the enterprise; sooner or later the stockmarket confirms the quality of a company, a process which occurred some time ago with the former, while the quality of the latter appears at last to be appreciated by investors.

As ever, we would ask unitholders to keep their expectations within reasonable parameters and, whilst we have exceeded them so far, we do not necessarily expect always to do so; we look forward however to reporting our performance at the interim stage in the spring and we know that we will do so while incurring a level of risk, as we noted above, considerably below the average equity investor (on any measure) and also from the standpoint of a highly competitive charging structure on the fund, with our annual fee of 1% being well below the mean (according to an article in the "Financial Times" in September), which average stands at 1.4%.

Finally, we close by again thanking Marlborough who, as managers and registrars, did a first-class job on the housekeeping, exceeding our expectations and providing us with a gold standard for administration, which we try to replicate in our investment work.

Unitholders wishing to see more of our philosophy or to note the current fund price, may wish to view our web-site at www.hathawayinvestment.com.

Graham Englefield
Robert Bogle
Graham Shaw
04.11.05

*Source, the index statistics are from the Financial Times (and they are calculated on a mid-to-mid price basis, with income reinvested); the MFM Hathaway Fund, therefore shows performance based on the mid-price of *accumulation* units, so that all figures are on the same footing.

Notes: 1. "Equities" means company shares and the FTSE All Share Index shows the general experience of a commitment to almost all quoted companies (the statistic in the sixth paragraph refers to this record); "Gilts" means UK government bonds.

2. Paragraphs six and seven cover a short period after the fund year-end, but they are included since they lead to a greater understanding of the performance in the twelve months under review and of the MFM Hathaway Fund generally.