MFM HATHAWAY FUND

INVESTMENT ADVISER'S REPORT

For the year ended 30th September 2007

To the unitholders of the MFM Hathaway Fund:

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 30th September 2007.

Amid faltering confidence in securities markets, our overall portfolio gain over the period under review was +5.5%, made up of a 4.38p increase in *accumulation* units, which reflect the *total return*. Since we started in November 2002, those units have grown from 50p to 84.035p, an approximate annualised compound rate of +11.0%, with the period return comprising a capital gain of + 2.5% plus dividends received at 3.0%.

The following table records the progress so far (see also the explanatory notes at the end):

Year	MFM Hathaway Fund	Benchmark (30% gilts, 70% equities)
2002/03	+ 13.1%	+ 6.7%
2003/04	+ 9.8%	+ 9.8%
2004/05	+16.4%	+19.7%
2005/06	+10.1%	+10.7%
2006/07	+ 5.5%	+ 8.4%
Cumulative	+68.1%	+68.2%

The table records that the fund remains in line with our "benchmark", although the fact that we have held an average of about 40% in gilts and cash in recent years, means that the statistics in the right column in fact overstate what our performance might have been, so in fact we remain slightly ahead of expectations.

Indeed, an adjustment to the benchmark to reflect our actual asset allocation (including our preference for large capitalisation stocks - so that we use the FTSE 100 Index and not the All Share for the equity element) means that it would have returned a cumulative figure of +50.7% as opposed to the +68.2% posted. We do not however propose to change how we prepare the test.

Suffice to say here, that our caution has led to our cumulative matching of the benchmark, but that our selection of individual equity securities has indeed proved wise, as we have beaten the stockmarket comfortably with them (as the table overleaf shows). Our overriding intention – as we have described before in these reports – is to achieve greater returns than the level of risk would indicate and cumulatively we have comfortably achieved that, as the tables above and overleaf show.

Our cautious approach continues

As we note, our levels of cash and bonds remain high (around 41%) as we demand an ever greater standard of safety from our overall portfolio following what we see as the considerably greater risk now carried by the stockmarket. Note that in 2002/03, conventional thinking was to invest almost all in bonds (since when they have produced, cumulatively, a total return of just 21%) but we then only placed about a quarter in that segment; now, the opposite prevails and we are more and more cautious about deploying the capital entrusted to us.

In summary, whilst we may so far appear to have been too cautious over the last few years, we reiterated in our half year report that the time for an investor to reign in his or her expectations, is when all the economic indicators are benign; since March, we have seen plenty to vindicate that stance (the example of Northern Rock neatly covering the position).

Security selection: MFM Hathaway Fund Equities vs FTSE 100 and FTSE All Share

Separately, in considering the merits of our selection of investments, we are ultimately interested in how our equities perform, since bonds generally produce lower returns (but at least at a reasonable rate of return while we patiently look to deploy capital in shares).

The table below therefore shows the average proportion of the fund held in shares since we started and then the *total return* performance of that portion (i.e. as if an isolated equity portfolio) as against the FTSE 100 and FTSE All Share indices; the statistics show the productivity of our decisions in choosing individual equities and funds and also record our reducing commitment to shares as they have risen. In both these contexts, it is gratifying to see over a 100% return on our equities so far.

Year	MFM Hathaway proportion in equities	MFM Hathaway equity return	FTSE 100 Index	FTSE All Share Index
2002/03	71%	+ 16.3%	+ 4.8%	+ 8.2%
2003/04	67%	+ 12.1%	+11.4%	+12.1%
2004/05	61%	+ 21.2%	+24.4%	+24.7%
2005/06	57%	+ 15.9%	+11.7%	+13.7%
2006/07	59%	+ 9.4%	+12.1%	+12.1%
Cumulative	--	+100.3%	+81.8%	+92.7%

Linking the two themes above together, our tasks are first to protect your capital (where caution comes in) and secondly to make it grow (security selection) and the results presented in this report bear witness to that. We will patiently exercise our judgement to find worthwhile investments to deliver the *absolute* and *relative* returns you have seen to date.

Turning to individual securities, we previously highlighted Wolseley (in plumbing and lumber), Tesco and Berkshire Hathaway (in insurance) and we note that the latter two are performing very well in business terms (although Berkshire is constrained in its sterling quote by the performance of the dollar); Wolseley has been hard hit by its largest market – the US – where clearly housing and house building is under pressure, but its semi-annual report last week (which included a 10% increase in the dividend to shareholders) underlined its strength, since it has done considerably better than the average in its market place.

Meanwhile, the robust interim statement from Lloyds TSB – over the summer – vindicates what we have said about it in these reports several times; its dividend increase buttresses our view.

Lastly, we previously highlighted Law Debenture Corporation as a first-class investment fund (for example, in 2004 its *net asset value* had advanced well ahead of the stockmarket, but its share price had lagged behind) and whilst it is gratifying to read the reports from the fund which show that it is still outperforming, its lack of popularity under current conditions leads the share price again to lag its sound performance – a phenomenon which will be reversed in due course, as it has before.

We look forward to reporting the half yearly performance in the spring, while more about our *value investing* philosophy and the current fund prices are on our website.

We should close by thanking Marlborough who, as managers and registrars, did a first-class job on the housekeeping and Barlow Andrews who do an impeccable job on the audit; both provide us with a standard to follow as investment advisers.

Graham Englefield
Robert Bogle
Graham Shaw

www.hathawayinvestment.com

Notes

1. Statistical source: the benchmark figures we quote in the table above are derived from statistics recorded in the Financial Times newspaper (and all are calculated on a *mid-to-mid* price basis, with net income reinvested); the MFM Hathaway Fund, equally, shows performance based on the mid-price of *accumulation* units, so that all figures in the table are on the same footing. Movements in the price of an *accumulation* unit, provide a complete record of performance, since accrued income is included alongside capital performance.

2. "Equities" means company shares and the FTSE All Share Index (what we generally mean by "the stockmarket") records the experience of a commitment to almost all quoted companies; "Gilts" means UK government bonds, while the FTSE All Stocks Index is an average of all those in issue and so we use that in preparing the bond part of the benchmark. The FTSE 100 Index covers just the largest quoted companies (the "blue chips").

3. The cumulative figures in the last line of the table very accurately show the *total return* from 25.11.02 to 30.09.07; any apparent discrepancy from a simple aggregation of annual and semi-annual statistics, is explained by rounding each year.

4. References to "year" in the tables, is to the fund year – October 1st to September 30th, except for 2002/03, which is for the period 25th November 2002 to 30th September 2003.