MFM HATHAWAY FUND

INVESTMENT ADVISER'S REPORT

For the year ended 30th September 2010

Performance

We have pleasure in presenting our annual report on the MFM Hathaway Fund – an *equity and bond* unit trust – which posted an overall portfolio advance in the year of +11.1%, resulting in an 8.815p increase in an *accumulation* unit (which class records exactly the *total return* on the fund) against a background of a return of +12.7% in the stock market (+12.1% from blue chips); since we started in November 2002, those units have advanced from 50p to 88.17p – equivalent to annual compounding of 7.5%.

It is gratifying to record our twelfth positive result – *i.e.* in *absolute* terms – from fifteen half yearly or annual reports and the table below illustrates that longer term record in comparative terms.

Year	MFM Hathaway Fund	Benchmark (30% gilts, 70% equities)	FTSE 100 (equities)	FTSE All Share (equities)	FTSE All Stocks (gilts)
2002/2009	+58.6%	+60.8%	+57.9 %	+67.6%	+42.8%
2009/2010	+11.1%	+11.4%	+12.1%	+12.7%	+8.7%
Cumulative	+76.3 %	+79.1%	+77.0%	+88.8%	+55.2%

The fund was therefore in line with its benchmark in the year and just behind since launch – the latter being a demanding guideline which tells us, long term, roughly where we ought to be (and more information about it are in the "Notes" at the end). However, that notional index is made up partly of the broader FTSE All Share Index (as to 70% in fact) so, given that our equities are mainly "blue chips", we have also included the FTSE 100 in the exhibit above and you can see that we remain up with the large capitalisation stocks which constitute that record.

Equally, we have previously described, at some length, how we have favoured bonds as to as much as 45% of the fund since we started (just now they are down to around 15% - 20%) and so, to achieve 99% of the return from large cap stocks and 86% or so of that from general equities over the last eight years, while taking materially less risk, represents both a fair performance so far and success in meeting our overriding goal – to achieve an appreciably higher return than that which the level of risk we have taken would indicate to be our due (a "cake and eat it" situation - as we have previously described it).

In simple terms, over the last 94 months, we made generous use of (what are generally accepted to be) lower risk/lower reward instruments – government bonds – but that anchor has not held us back; indeed, since we launched, we have achieved 138% of the returns on those securities and practically all that on large company shares, so it continues to be gratifying to see our philosophy holding its own.

No *hubris* though: the evaluation and valuation of risk is really what we see investing as all about and we will stick to this task with an *objective* eye rather than one clouded by past success, even though that be encouraging; our first job, will always be the *long term* safety of our unit holders' capital and rising asset values are once more making that task more challenging.

That brings us neatly on to the discrepancy between our performance in the first half of the year and the last six months. In March we were comfortably ahead of our benchmark over the first half and, at that time, gilts were actually in negative territory since last September. The summer though, marked a strong rebound in government bonds and our eschewing of them earlier this year looks preemptive. However, we are unrepentant about shifting from bonds to equities: to paraphrase Nathan Mayer Rothschild, we have left something for the speculators.

Equally, our equity performance in the second half was hit by the B.P. oil rig disaster and the weakening of the dollar (both now slowly reversing) but that was only in the *absolute* sense and, to put the small decline into perspective, it is encouraging to note that, at the time of signing off this report, our fund had reached a new high.

We are also pleased to see, from the first table above, that the fund's slip between March and September, left the annual exhibit relatively unaffected – we remained pretty much at the top of our peer group over the year.

Investing activities

Despite short term travails, our equity collection continues to look well-placed and, with the obvious exception of B.P. , we continued to receive healthy business reports from our investees (particularly from the stalwarts such as Tesco, Diageo (Gordon's Gin etc) and Kone (the lift maker); we remain happiest in businesses where a healthy dividend offsets the risk of short term price falls (or, occasionally, where the growth potential is demonstrably strong in any case). We continue to look closely at the amount of debt a business carries and we prefer enterprises with income streams either predominantly in sterling or across many currencies (effectively providing a hedge).

In investing, your decisions are always made under uncertain conditions, but adherence to the eternal verities tends to produce, at the very least, the prospect of satisfactory results. With that in mind, the record of Procter & Gamble (Pampers nappies through to Gillette razors), might sober up those still intoxicated by structured products, derivatives and the like: since 1890, it has paid an uninterrupted dividend to shareholders, and increased it for the last 54 consecutive years.

"P&G" – which we hold for the long term of course - neatly underscores why we made few changes to the portfolio in the year - the stock market quietly moves money from the active to the patient.

Outlook

We said two years ago that equities "are now set to deliver acceptable returns once again" and that has continued to prove accurate and we also remarked then that "the stock market…is likely to move higher well before the economy or sentiment demonstrably improve...the outlook is currently attractive" and that has also turned out to be right (although in both cases we had no insight as to *when* those statements might be proved correct, as of course we never try to guess market moves).

As ever, we do not (nor does anyone) have the faintest idea where general business or the stock market are going to go over the next year or two (fortunately for our investors we do not need to form a view), but we are nonetheless seeing some signs of an old – fashioned bull market and such developments rarely reverse quickly; in this environment, we will do our best to capture as much of the available returns, without compromising security. Indeed, on this last point, the yellow caution light on our desks is now fully on – indicating a need to be increasingly thoughtful about company shares as they continue to rise.

Finally therefore, we would remind our investors to keep their expectations to a sensible level (continuing turmoil in the international economy should see to that) and to remember that all securities markets are two way streets; expect turbulence, and that we won't buy any Greek government bonds for the fund.

We look forward to reporting the half-year performance in the spring, while more about our *value investing* philosophy and the current fund prices and performance are on our website. As ever, we close by thanking Marlborough - the fund's administration managers and registrars - and Barlow Andrews as auditors; both do a great job behind the scenes.

Graham Englefield
Robert Bogle
Graham Shaw
08.11.10
www.hathawayinvestment.com

Notes

1. Statistical sources: the benchmark figures we quote in the second table are derived from *data* 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 that exhibit are on the same footing. Movements in the price of an *accumulation* unit provide a complete record, 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 aggregate experience of 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 to prepare the bond part of the benchmark (as to 30% of it). The FTSE 100 Index covers just the largest quoted companies (the "blue chips" or "large capitalisation" or "large cap" stocks), so we instead use the first of these three indices (as to 70%) in calculating our benchmark.

3. The benchmark is intended as a rough guide to how adroitly the portfolio has been invested over any period (particularly the allocation between bonds and equities) reflecting how a typical conservative private investor's securities might be constructed; one reason why it is only an indicator though, is that it is impliedly continually rebalanced to 70:30 each day (as statistically it must be).

   Our most meaningful goal then, long term, is to get the same or a better return than equities (the toughest test long term), while taking materially less risk than the stock market (if possible) over a market cycle (so a bare minimum acceptable performance would be to match that return which the amount (and type) of equities which we have actually held would have produced (and that is approximately +60% so far)).

4. The cumulative figures in the last line of the first table very accurately show the *total return* from 25.11.02 to 30.09.10; any apparent discrepancy, from a simple aggregation of annual and semi-annual returns (either here or in previous reports), is explained by rounding each year in preparing the discrete statistics.

5. Any references to "year" (or, for example, "2002/2009") in the tables or the text, is to the fund year – October 1st to September 30th, except for 2002/03 (shown in previous reports, but contained in aggregate numbers here), which was for the period 25th November 2002 to 30th September 2003. The actual valuation dates for the unit trust (and therefore the comparative indices/benchmark) may, in some years, vary by a day or so from these dates, but we are consistent in then using them to commence subsequent periods and to utilising corresponding comparative statistics.