MFM HATHAWAY FUND
AUTHORISED INVESTMENT ADVISER'S REPORT

For the year ended 30 September 2011

Percentage change and sector position to 30 September 2011

	Six months	1 year	3 years	Since 4 January 2008**
MFM Hathaway Fund	-7.87%	-0.53%	14.42%	6.74%
Quartile Ranking	1	1	3	1

*Based on ranking within Balanced Managed Sector
**Changed IMA Sector on 04.01.2008 (launched 04.11.02)
External Source of Economic Data: Morningstar (bid to bid, net income reinvested)

Performance as against the market averages and performance benchmark

We have pleasure in presenting our annual report on our *equity and bond* unit trust, which posted an overall *decline* in the half year of 0.5%, being a 0.48p decrease in *accumulation* units (which class records the fund's *total return*) against *minus* 2.9% from the stock market (*minus* 3.1% from blue chips) and +6.6% from gilts; since launch in November 2002, those units have advanced from 50p to 87.69p – equivalent to annual compounding of approximately 6.5%.

This being our seventeenth interim/annual report, we record only our fourth negative period return, the table below illustrating the longer term comparative *data*, including pretty much keeping pace with our performance benchmark, that being a demanding guideline which tells us roughly where we ought to be (see also the "Notes" at the end of this report). We also show our targets, constituents and the related FTSE 100.

Year	MFM Hathaway Fund	Performance Benchmark (30% gilts,70% equities)	FTSE 100 (equities)	FTSE All Share (equities)	FTSE All Stocks (gilts)
2002/2010	+76.3%	+79.1%	+77.0%	+88.8%	+55.2%
2010/2011	- 0.5%	- 0.2%	- 3.1%	- 2.9%	+ 6.6%
Cumulative	+75.4%	+78.7%	+71.5%	+83.3%	+65.4%

We have favoured bonds to as much as 45% of the fund at times since 2002 and so, to have achieved 104% of the return from large cap stocks (FTSE 100) and 86% or so of that from general equities (FTSE All Share) over the last nine years, while therefore taking materially less risk, which represents both a gratifying performance 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).

Also, to have achieved 114% of the returns on gilts, alongside that equity return, over the 106 months since we started, is both encouraging and solid evidence of the merits of our *value investing* philosophy, particularly when you consider the notes below.

Performance as against our peers

The *Morningstar* table at the start of this report places us above average over one year and well above average since the Investment Management Association ("IMA") changed our sector in 2008 and, also, over the last six months. We were actually just in the bottom half over three years and, in percentage terms near the average in that time.

After last year's very strong showing, it was inevitable that we would post a more consolidating performance, and of course the stock market retreated heavily over the summer, but the short term and secular performance as against equities generally, shows the class of the companies in our portfolio.

To summarise: it is the quality of our company shares - well ahead of the stock market since launch (schoolboy algebra confirms that) – which has enabled us also to hold bonds for safety and stability and to deliver our unit holders superior, evergreen, returns. Over the long term we have therefore, so far, met the goal set out in Note 3 below.

Investing activities

Despite short term travails, our equity collection still looks well-placed and we continue to receive healthy business reports from our investees; even BP continues gradually to strengthen. We remain happiest in businesses where a healthy dividend and conservative balance sheet offset the risk of short term price falls (or, occasionally, where the growth potential is demonstrably strong in any case).

Therefore, aside from just reading the annual reports of companies, industry *data* etc, we carried out just two small purchases in the second half – Yule Catto and Marston's.

Outlook

As we said in the spring, generally, conditions for investors are something of a Curate's egg - good in parts. Low interest rates buttress equity values and business conditions for stable international companies are reasonably (and surprisingly) benign. Above all, UK blue chips (the biggest companies) have remarkably strong balance sheets and hold plenty of cash, but the bond market is challenging and inflation is gathering.

UK government bonds represent a capital trap which is set to spring – Treasury 8% 2021 for example (a standard ten year maturity) is now priced at almost 150p and yields about half the rate of inflation. As its wider peer group have returned up to 23% in the last year, we consider that, whilst the gilt bubble has shown surprising resilience, it is only a matter of time before it bursts and we wish to hold our unit holders harmless from the effects of that.

Gilts remind us of Benjamin Franklin's famous quote, which we amend slightly: those that give up long term returns (*i.e.* from equities) for the perceived security of gilts, deserve neither good returns nor safety.

The Euro zone crisis however dominates – what one observer called "risk on, risk off" as it lurches from one crisis to another short term solution; we sit reasonably favourably on the periphery of all this. Meanwhile to paraphrase Mark Twain (again), reports of America's death have been exaggerated. It is currently in a shambles, but expect it to be well on its way to self-sufficiency in fuel and energy within five years – they are already the top producer of natural gas (from shale – which will have people reaching for the atlas to see where North Dakota is).

The US/China trade see-saw is about to shift back in favour of the former as Chinese wage inflation catches up; America's strength in managing a single currency, having good demographics and 16 of the top 20 world universities will help. Although progress will be slow, this century may turn out also to be Uncle Sam's too.

Finally, as ever, we would remind our investors to keep their expectations to a sensible level (continuing turmoil with sovereign debt should make that easy) and to remember that all securities markets are two way streets; expect turbulence, and that we still won't buy any Greek government bonds for the fund (nor Spanish, Italian, Portuguese…). Equity prices still remain fairly full.

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

Graham Englefield;
Robert Bogle;
Graham Shaw;
07.11.11

www.hathawayinvestment.com

Notes

1. Statistical sources: the performance 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, also, 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 stock market") 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 performance 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 performance benchmark.

3. The performance 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 list might be constructed.

   Our most meaningful goal then, long term, is to get the same or a better return, from our overall portfolio, than from equities (the toughest test long term), while taking materially less risk than the stock market (if possible) over a market cycle. Therefore a target minimum performance (given that equities outpaced bonds) would be to match that return which the proportion (and type) of equities which we have actually held would have produced.

4. The cumulative figures in the last line of the second table very accurately show the *total return* from 25.11.02 to 30.09.11; 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.