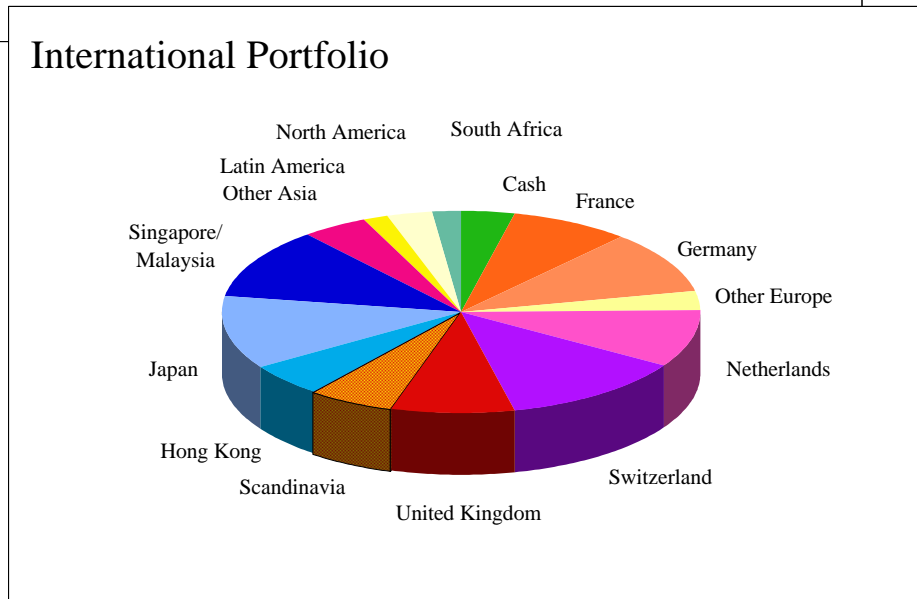
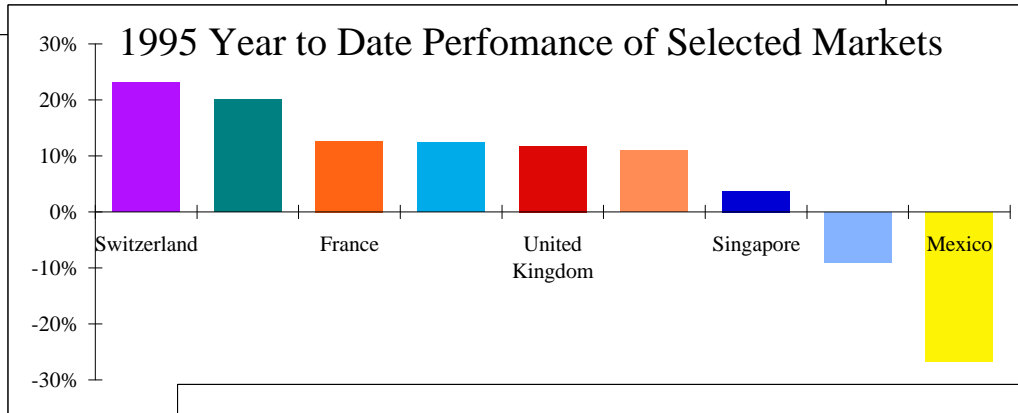
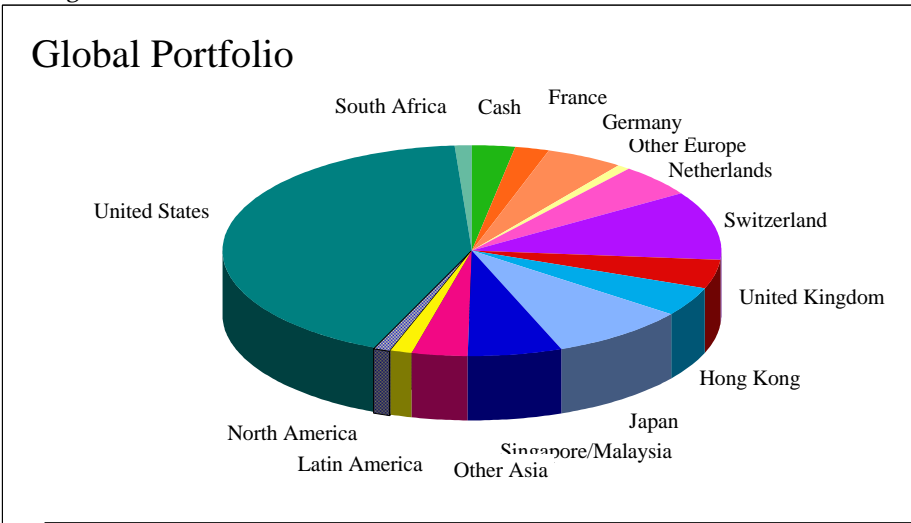


Harding Loevner Management Global and International Investing 1995 Second Quarter Report

The following material is excerpted from reports to equity clients of Harding, Loevner Management.



Overview of Portfolios

Harding, Loevner Management offers clients a choice of equity programs: *global equity*, which includes US-based companies, and *international equity*, which excludes US-based companies. Within each equity program, carefully selected companies are combined in portfolios that are broadly diversified by industry and by geography. The following table provides a 'snapshot' at June 30, 1995, of two representative portfolios:

	Global	International
Number of companies	49	43
Number of countries	16	18
% in cash	3%	4%
current yield	2.2%	2.5%
geographic allocation (%)		
<i>US</i>	42	N/A
<i>Europe</i>	28	57
<i>Japan</i>	9	12
<i>Other Asia</i>	12	21
<i>Emerging Markets</i>	10	14

Performance

HLM's global portfolios rose in value by 10.1%, on average, in the quarter, as against a 4.0% rise for the FT World Index and a 7.6% rise for the Lipper Index of global mutual funds. International portfolios rose by 8.8%, versus 0.8% for the FT World ex-US index and 5.1% for the Lipper International Index. The returns to the indices reflect the net effect of opposing movements of its largest constituents: the US and Europe, which rose by 9.5% and 6.4%, respectively; and Japan, which fell by 6.2%. Emerging markets recovered following sharp declines in January and February. Mexican stocks, for example, rose by 20.9%, while Malaysia was up by 9.1%.

	1995 YTD	Compound Annual Returns (%) for periods ending 6/30/95			
		1 year	3 years	5 years	Since Inception
HLM Global Equity Portfolio	13.7	14.6	13.9	13.8	14.9
FT World Index	8.1	9.3	12.7	7.4	5.7
S & P 500 Index	20.1	26.0	13.2	12.1	11.8
Global Fund Index (Lipper)	7.4	8.6	11.3	8.1	8.6
HLM International Equity Portfolio	6.9	7.5	17.3	12.0	12.6
FT World ex-US Index	1.7	0.8	12.5	4.8	2.6
MSCI World ex-US Index	3.1	2.6	12.8	5.0	3.2
International Fund Index (Lipper)	2.5	1.8	9.7	5.5	6.2

Note: The HLM performance data refer to its global and international equity composites, which are dollar-weighted averages of *all* HLM-managed global and international equity accounts, respectively. Inception date for global composite, 11/30/89; international composite, 9/30/89. HLM composite performance is presented before management and custody fees. See attached composite performance summaries for details.

Following the precipitous fall of the US dollar against the yen and central European currencies in the first quarter, exchange rate movements were more subdued in the second quarter. Stabilization of the dollar improved investor psychology toward shares of multi-national companies, which earn a large percentage of their revenues in dollars, a reversal of the phenomenon observed in the first quarter. Insofar as such global companies dominate the portfolios, returns were positively impacted, even after translation into stronger dollars.

Quarterly Review

The dramatic rise in the US stock and bond markets dominated the world financial stage in the recent quarter. Long-term US bond yields have fallen from 7.5% at the end of March, and 8.2% in November last year, to 6.6% now, despite the absence of very significant loosening of monetary policy. This interest rate movement has come as a consequence of mounting evidence that the rapid rate of economic growth seen in 1994 is abating, worldwide. Indeed, there is some evidence in the US, such as declining employment growth and falling manufacturer and consumer confidence, suggesting that a mild recession may be in store.

But despite this clouding of near-term prospects for corporate results, the long-term outlook for US companies and their shares has actually improved. Confounding the majority of prognosticators, inflation remains subdued, as it has been throughout this economic cycle. US companies are seeing, at last, the fruits of past investment in technology in the form of a sustained high rate of productivity growth—unusual in this maturing phase of the recovery cycle. The weaker dollar has enhanced the international competitive advantage of US producers, at least for the time being, and the US Administration has shown its determination to help them capitalize on this advantage by taking an aggressive line on trade barriers.

Perhaps the most powerful element in the enhancement of the long-term outlook is the rising prospect for reversal of the US economy's most enduring disability—its inadequate rate of domestic savings. There are a few encouraging signs that politicians of both parties may now give serious attention to the structural causes of the Federal deficit, such as Medicare. Rising demand for long-term investments from the baby-boom generation skeptical (sensibly) about the security of its social old age pension, suggests that the household sector may also contribute to a rise in aggregate savings. In the long run, it is the generation of adequate domestic savings, not 'competitiveness' or 'productivity,' that is the key to sustained growth with low inflation, balanced trade and a stronger dollar.

One need not quote from *The Madness of Crowds* to explain the current level of stock prices; they can be adequately justified on valuation grounds. In the view of investors, these favorable developments—improving productivity, quiescent inflation and higher savings—justify a lower 'risk premium' on equity investments. Lower interest rates and a smaller equity risk premium mean the discount rate that equity investors apply to future corporate profits and dividends in valuing equity investments has fallen. The net result, despite slowing near-term growth of profits, has been higher equity values and, accordingly, higher stock prices.

Against the backdrop of productivity gains and continued capital spending, and lower long-term interest rates, it should come as no surprise that the US market's rise was propelled by technology- and capital spending related stocks and interest-sensitive stocks. The global portfolio's US holdings, with their strong emphasis on capital goods and financial companies, performed particularly well in the quarter. Shares of electronic connector-maker **AMP**, instrument-maker **Thermo Electron** and diversified capital goods maker **Dover** appreciated strongly. Similar results were achieved by property catastrophe reinsurer **EXEL** and by the portfolio's US banking investments, **J.P. Morgan**, **Fannie Mae** and **First Fidelity**—the latter agreeing to a synergistic takeover bid by super-regional First Union Bank. Packaging leader **Crown, Cork & Seal's** price surged following the announcement of its intended acquisition of Europe's leading packaging company, Carnaud Metal Box.

Despite signs of an economic slowdown in Europe coming hard on the heels of its recent recovery, European bond and equity markets moved in sympathy with the US market's rise. In Germany, bond yields declined from 7.2% to 6.9%, and stocks rose reflexively. Yet, profit growth in Europe remains fragile. Exporters in the hard currency core—Germany, France, Switzerland—struggle against extraordinary competitive pressure from lower cost locales. On the periphery, governments in Italy, Belgium and Sweden are facing up to the need to shrink deficits by reducing spending.

Europe also remains handicapped in its economic organization relative to the US. Europe's labor markets are sclerotic with regulation, and state-sponsored enterprises lumber along with aid of explicit and implicit subsidies, introducing major competitive distortions. European firms have also been slower than their US counterparts to embrace new, productivity-enhancing technologies—perhaps because of the difficulty they face in shedding labor thereby made redundant. Historically, the consequences of these handicaps have been higher rates of unemployment relative to the US, and a greater reliance on exports to generate growth. We believe that Europeans are now acting to reduce these handicaps—through tax and labor law reform, through privatization, and through increased capital investment. Change will be fitful, but to the extent they are successful, the potential for improvement in economic and corporate performance is great.

Stock markets in Europe are not overtly expensive, but earnings growth rates are generally modest. Our European holdings are concentrated on companies that are able to grow much faster than their respective economies: through the pricing power provided by unusual business franchises, as in the case of UK commercial services company **Rentokil** and Dutch technical publisher **Wolters Kluwer**; by their position in young, growing industries, such as **Randstad**, a leading temporary employment agency; or by their commanding presence in emerging economies, such as **Brown Boveri**, which has been very successful in expanding its power generation business in Asia.

The US bull market has lifted stock markets elsewhere in the world—with the notable exception of Japan, where the stock market marches to the beat of its own drum. As elsewhere, Japanese bond yields have fallen—in the last three months alone, from 3.7% to 3.0%—but here, unlike elsewhere, the positive impact on stock valuations of lower interest rates has been overwhelmed by rising pessimism about the economic outlook and, specifically, fear for the health of the banking system.

Deflation is the phenomenon of falling prices, and 'price destruction' has become a household phrase in Japan. In a long-term sense, this is healthy—Japanese consumers have long been discouraged to spend and encouraged to save by laws and conventions devised to channel financial resources to manufacturers. We believe that the long-term interests of Japan *and* of its trading partners would best be served by unlocking pent-up consumer demand. Changes in retail laws, and the emergence of Western-style competitive and low-cost retailing outlets have begun that process.

This has a dark side, however, stemming from the policies that burst the 'bubble economy' of the late 1980s. The resulting slowdown in the economy, collapse in asset prices, and surge in defaulted loans has left the Japanese banking system dangerously short of capital. In past cycles, banks (and other entities) relied on sales of appreciated equity holdings to restore profits. With the collapse of stock prices, hidden reserves are nearly exhausted. Bad loans are staggering and are still rising—reasonable estimates put them at over \$600 billion, 10% of GDP. To date, the Government has been reluctant to mount a bail out. Use of public funds to support the equity market and to provide cash for the rescue of two regional banks earlier this year has proven deeply unpopular with the public. Moreover, the weak coalition Government is in no position to challenge the authority of the bureaucrats who steadfastly resist any move away from traditional fiscal conservatism.

The risk of a deflationary spiral sending asset prices tumbling again has been increased by the recent further appreciation of the yen. Japan's strongest companies, its exporters, have done an outstanding job in the last ten years in reducing their costs to remain competitive despite currency appreciation. Their response to renewed yen appreciation is to accelerate the relocation of manufacturing capacity to cheaper areas, notably to South East Asia and to address lagging productivity at the middle management level by

reducing headcounts and introducing information technology. At the individual company level, offshore manufacturing (the 'hollowing out' phenomenon) and corporate downsizing are positive steps for increasing profitability, but in the aggregate they have, in the near term, the effect of exacerbating the pervasive weakness in the domestic economy and further undermining the teetering banking system.

Our Japanese holdings are modest in relation to the size of the Japanese stock market and importance of its economy, and limited to companies whose valuation and prospects compare favorably with alternatives outside Japan. In general, Japanese stocks are cheap only in comparison with the immediate past—the bubble period. The five companies we hold are both agents of, and beneficiaries of, the changes that must occur in resolution of Japan's structural problems. **Canon Sales**, for example, is the distributor of office equipment made by **Canon** (another holding) as well as Apple Computer and independent software producers. The company will benefit from the massive investment in productivity-enhancing technology that is required for Japanese companies to reduce labor costs and to catch up with their US counterparts.

Ito Yokado, the country's largest retailer, operates both superstores and, through its subsidiary, Seven-Eleven, convenience stores. Its size and operational efficiency enables it to prosper at the expense of its weaker rivals in the increasingly competitive retailing sector. It is at the forefront of reducing prices to the consumer. **Nippon Denso**, a leading automobile component maker, has already established local manufacturing worldwide, in the US and other important markets for Japanese automobiles, to supply overseas plants of Toyota and its other traditional OEM customers, as well as non-Japanese automakers.

The rest of Asia continues to benefit from the industrial restructuring of Japan. The trickledown of investment from Japan, to take advantage of lower labor costs, combined with high savings rates, entrepreneurship and a highly productive workforce have led to the Asian economic miracle that is now a familiar theme. The recent strength of the yen assures us that this growth can continue. Our emphasis is on 'super-regional' diversified companies—**Keppel, Hutchison Whampoa**—and banks—**Bangkok Bank, DBS Bank**—that will benefit from economic growth in the region as a whole, as well as on companies such as Indonesian distributor **Wicaksana** and **Nestlé Malaysia** that are serving the needs of the rapidly-growing consumer sector. Currencies in this region are linked to the US dollar, at least implicitly. The decline in dollar interest rates has boosted valuations in stockmarkets throughout the region, and dollar depreciation against the European currencies has enhanced the competitive position of the region's exporters.

Portfolio Strategy

World stockmarkets are not cheap, but neither are they too dear. Stocks are not excessively expensive on a historical comparison: by measures such as price to book value, price to earnings, price to cash flow, or dividend yield (adjusted for stock buybacks), stock prices are well within the ranges seen in the last ten years. Neither are they excessively expensive against theoretical value if future dividends are discounted by today's interest rates and risk premia which, as we have argued above, are justifiably lower than in the past. And, while this observation owes much to the recent sharp drop in interest rates, real interest rates cannot be said to be abnormally low; they are also well within their range of the last dozen years—a remarkably tight 3-6% band. So long as inflation remains a non-problem, the environment for long-term equity investment appears sound.

Against this background, our portfolios are fully invested. As ever, holdings are companies with high financial and management quality, and durable competitive advantages. The portfolio's emphasis is on companies to which we attribute exceptional long-term growth prospects. At the valuations currently prevailing in stockmarkets generally, we can find no compelling reason to own second-quality companies, or those with mediocre growth prospects. Several adjustments to holdings were undertaken in the quarter, as described below. Currency turmoil at the end of the first quarter presented us with an opportunity to acquire several superior growth companies at prices that we felt did not adequately reflect their inherent value, and thus were likely to be transitory.

Portfolios

As illustrations of the investment programs pursued during the quarter, we have attached summaries of the global and international portfolios' holdings at June 30.

Transactions

In the second quarter, we bought shares in the following new companies:

- **Canon** is the world's leading producer of a wide range of visual image processing equipment with a globally-recognized brand name and reputation for quality. Canon has four main business areas: copiers, printers, steppers (used in manufacture of semiconductors) and cameras. 70% of Canon's sales are overseas. The company's commitment to research and development has given it a technological lead over competitors and enabled it to gain dominant share in new, fast growing segments of the office automation market such as laser printers and color copiers. Unlike many Japanese companies, Canon, despite its strong growth prospects, is valued at levels similar to leading US blue chip companies in terms of price to cash flow and price to book value.
- **Partner Re**, with more than \$1 billion in equity capital, is the largest Bermuda-based property reinsurer. The company, aided by its sponsorship by Swiss Re and the strength of its senior management team, has already become a leading provider of property catastrophe reinsurance—a market that is growing as a consequence of the recent higher frequency of occurrence of earthquakes, floods and storms, and the tremendous increases in construction and property values in the developing world, especially the Pacific Rim. Partner Re's shares are modestly valued at current levels, due to its brief corporate history. We believe Partner Re's Swiss pedigree and financial strength, lean expense ratios, superior pricing models, and the decline of competition from Lloyds auger for good earnings growth and a higher share valuation.
- For global portfolios, we bought **Motorola**, one of the world's leading electronics companies producing telecommunications equipment and semiconductors. Motorola pioneered and dominates many segments of the global telephony market, including switches and installed systems, cellular handsets, two-way radios and pagers. The rapidly growing usage of semiconductors outside of computers has been a boon to Motorola, with nearly 70% of production going to non-computer uses including consumer electronics, industrial controls and automotive industries. Motorola has long been a leader in technological innovation. In 1994 alone it spent over \$1.8 billion on R&D and received 940 US patents. Iridium, the company's multi-billion dollar low-altitude satellite system for global wireless communication, is emblematic of the vision and technological capabilities of Motorola.

For international portfolios, we also purchased:

- **IHC Caland** is the world's largest designer and builder of dredging equipment and related parts. The company is also active in the design, engineering and construction of single-point mooring terminals, specialized drilling ships, semi-submersibles, cranes and crane vessels. The company's products incorporate significant proprietary technological know-how, providing high barriers to entry, strong earnings growth and high returns on capital. Continued rapid development of the world's littoral regions, particularly in the Pacific Rim, creates conditions of strong demand for IHC Caland's products.
- **Imperial Oil**, a 70%-owned subsidiary of Exxon, is Canada's largest integrated energy company. Its proven oil reserves of 1.2 billion barrels equal 30 years of current production. Oil sands properties in

Alberta contain additional billions of barrels of probable reserves. Extraction costs are declining due to continuing investment in extraction technology, enhancing already considerable cash flow.

- **Astra** manufactures and markets local anesthetics, anti-infective medicines and medicines for the treatment of intestinal, respiratory and cardiovascular diseases. Prilosec, an ulcer medication and Pulmicort, an anti-inflammatory, are two of Astra's brand-name products. The company also has an important joint-venture with the American company, Merck. Astra is rapidly growing its way into the ranks of world class drug companies by virtue of its productive pharmaceutical R&D and its global marketing reach. The shares' modest price-earnings ratio reflects Astra's Swedish origins and some uncertainty about the introduction of leading asthma products into the US.

We also added to holdings in **Bangkok Bank convertible**, **DBS Bank**, **Gaz et Eaux**, **Krones**, **Rentokil** and, in global portfolios, **Cummins Engine**. Holdings of **Deutsche Bank warrants** were exercised to acquire common stock. Companies sold for fundamental reasons were:

- **Hong Kong and China Gas** was sold as a consequence of its announcement that it would participate in a large-scale property development project in conjunction with the company's controlling shareholder. We regarded this step as a significant departure from the company's traditional focus on energy distribution and a breach of faith with minority shareholders, who own Hong Kong Gas for its steady, predictable earnings growth—a characteristic incompatible with property investment. A substantial gain was realized on the sale, although, as explained, it was not undertaken for price reasons.
- **Makita**, Japanese manufacturer of power tools for homeowners and professionals, was sold in favor of Canon. Makita has been slower than Canon to adapt its manufacturing operations to the exigencies of a rising yen, and the result has been a succession of disappointing earnings results.

In global portfolios, we sold German forklift maker **Linde** to reduce excessive DM-bloc exposure of the portfolio. We also reduced the holdings in **Nylex Malaysia** and **Keppel**, which had become uncomfortably large after strong price appreciation this year. The only other sale was that of **US Industries**, a highly leveraged industrial holding company that was received as a spin out of **Hanson**.

HARDING, LOEVNER MANAGEMENT
Global Equity Performance Summary 6/30/95

	Calendar Year Returns					
	1995 6 mos.	1994	1993	1992	1991	1990
HLM Global Equity Composite	13.7	-0.1	24.2	9.1	31.6	3.6
<i>Financial Times World Index</i>	8.1	5.9	22.6	-5.1	19.6	-17.0
<i>Morgan Stanley Capital International World Index</i>	9.4	5.6	23.1	-4.7	18.7	-16.4
<i>S&P 500</i>	20.1	1.3	10.1	7.7	30.2	-3.1
<i>Lipper Global Fund Index</i>	7.4	-2.2	32.8	0.1	20.3	-9.1

	Average Annual Returns for periods ending 6/30/95			
	1 year	3 years	5 years	Since Inception*
HLM Global Equity Composite	14.6	13.9	13.8	14.9
<i>Financial Times World Index</i>	9.3	12.7	7.4	5.7
<i>Morgan Stanley Capital International World Index</i>	11.2	13.1	7.7	6.1
<i>S&P 500</i>	26.0	13.2	12.1	11.8
<i>Lipper Global Fund Index</i>	8.6	11.3	8.1	8.6

* Inception date: 11/30/89

Notes:

1. Returns shown are time-weighted total returns, and include reinvestment of dividends.
2. Returns from all cash reserve and equivalents, bonds and/or convertible securities used in place of equities are included in performance calculations.
3. Composite calculations have been weighted by account size.
4. Figures include all global equity accounts under discretionary management from their inception dates, including accounts no longer in existence.
5. No alterations of composites as presented here have occurred due to changes in personnel or other reasons at any time.
6. No selective periods of performance have been utilized.
7. Results are presented after brokerage commissions but before management and custodial fees. Management fees are described in our Form ADV Part II. Inclusion of standard management fees would reduce annual returns for global composite by approximately 1%.
8. Lipper Index performance is after fees and expenses.

Account summary information:

1. Number of accounts included in composite: 1989: 1; 1990: 4; 1991: 7; 1992: 14; 1993: 17; 1994: 17; 1995 (Q2): 11.
2. Total market value at year-end of accounts included in composite ('000): 1989: \$1,564; 1990: \$15,311; 1991: \$36,637; 1992: \$64,513; 1993: \$93,197; 1994: \$112,683; 1995 (Q2): \$122,415.

HARDING, LOEVNER MANAGEMENT
International (Non-US) Equity Performance Summary 6/30/95

	Calendar Year Returns					
	1995					
	6 mos.	1994	1993	1992	1991	1990
HLM International (non-US) Equity Composite	6.9	2.5	46.3	9.9	21.9	-12.9
<i>Financial Times World ex.-US Index</i>	1.7	8.4	32.1	-13.1	13.3	-23.1
<i>Morgan Stanley Capital International World Ex-US In</i>	3.1	7.6	32.6	-11.9	12.4	-22.8
<i>Lipper International Fund Index</i>	2.5	-0.9	39.2	-4.3	13.2	-12.4

	Average Annual Returns for periods ending 6/30/95			
	Since			
	1 year	3 years	5 years	Inception*
HLM International (non-US) Equity Composite	7.5	17.3	12.0	12.6
<i>Financial Times World ex.-US Index</i>	0.8	12.5	4.8	2.6
<i>Morgan Stanley Capital International World Ex-US Index</i>	2.6	12.8	5.0	3.2
<i>Lipper International Fund Index</i>	1.8	9.7	5.5	6.2

* Inception date: 9/30/89

Notes:

- Returns shown are time-weighted total returns, and include reinvestment of dividends.
- Returns from all cash reserve and equivalents, bonds and/or convertible securities used in place of equities are included in performance calculations.
- Composite calculations have been weighted by account size.
- Figures include all international equity accounts under discretionary management from their inception dates, including accounts no longer in existence.
- No alterations of composites as presented here have occurred due to changes in personnel or other reasons at any time.
- No selective periods of performance have been utilized.
- Results are presented after brokerage commissions but before management and custodial fees. Management fees are described in our Form ADV Part II. Inclusion of standard management fees would reduce annual returns for international composite by approximately 1%.
- Lipper Index performance is after fees and expenses.

Account summary information:

- Number of accounts included in composite: 1989: 1; 1990: 2; 1991: 3; 1992: 4; 1993: 5; 1994: 14, 1995 (Q2): 26.
- Total market value at year-end of accounts included in composite ('000): 1989: \$10,899; 1990: \$10,599; 1991: \$6,770; 1992: \$12,061; 1993: \$23,003; 1994: \$110,370; 1995 (Q2): \$271,971.