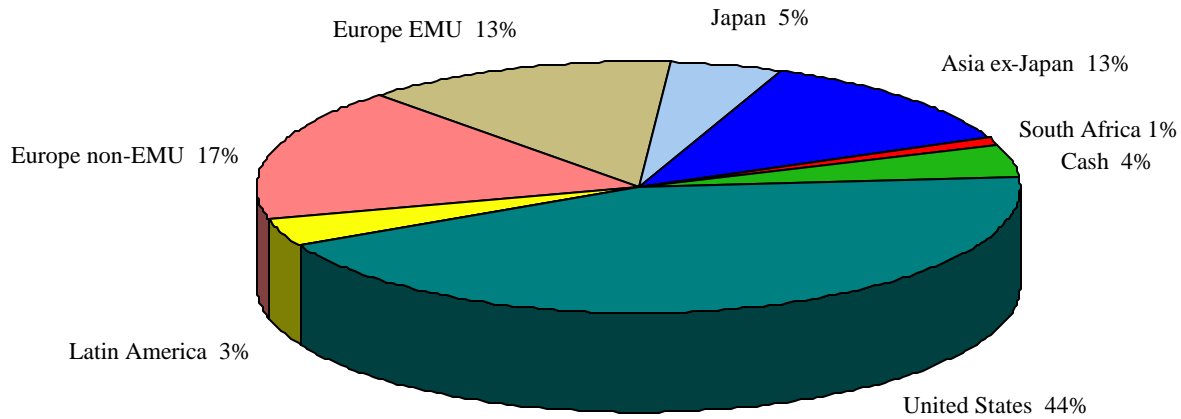


# HARDING, LOEVNER MANAGEMENT, L.P.

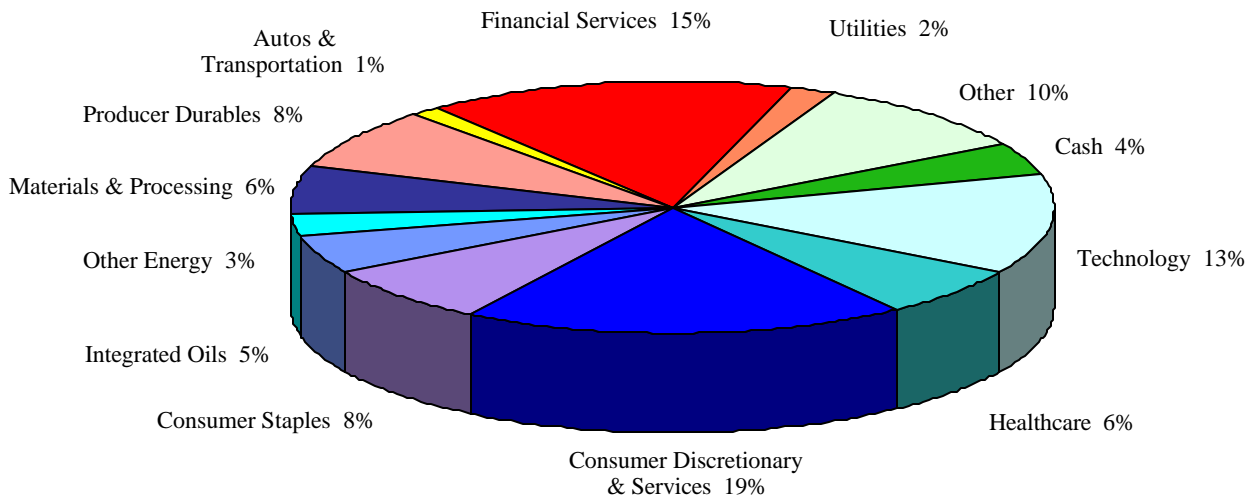
## 1999 Second Quarter Report

### GLOBAL EQUITY

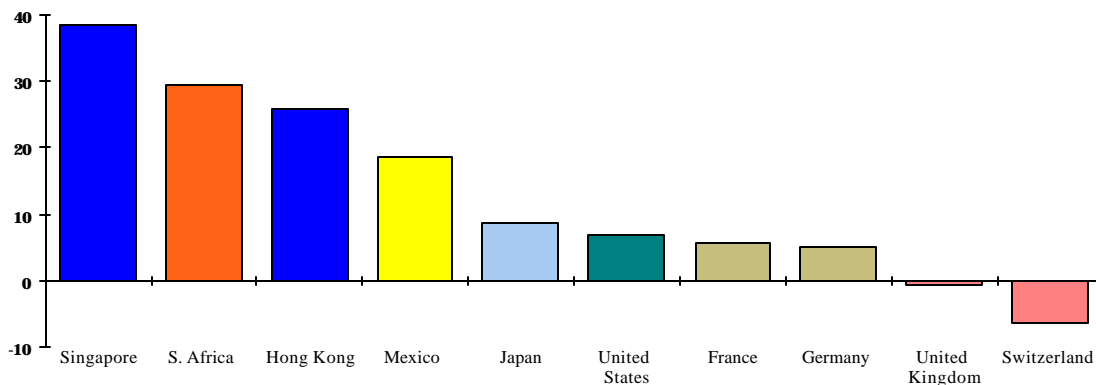
#### Geographic Distribution



#### Sector Distribution



#### 1999 Second Quarter Performance of Selected Stock Markets in US\$



The charts above provide a 'snapshot' of the Portfolio at June 30, 1999. See inside for details of performance.

## Performance

The portfolio returned 10.6% in the second quarter of 1999, gross of fees. This compares favorably with the 5.9% rise of the MSCI All Country World Index, and the 6.6% rise of the Lipper Global Fund Index.

In many ways, this past quarter was extraordinary. In style terms, market leadership shifted, almost violently, from 'growth' stocks to 'value' stocks. In geographic terms, leadership shifted from West to East. And, in size terms, leadership shifted from the very largest capitalization stocks to medium and smaller sized companies.

The shifts in style, regional and capitalization preference were triggered by positive economic news — particularly from Asia. Deflationary fears stemming from the financial crisis of the late summer of 1998 now are seen to be overdone. Most commodity prices — copper, crude oil & aluminum — have moved sharply higher, reflecting expectations of broad-based recovery in demand. Asian economies have rebounded faster and stronger than had been forecast at the end of 1998. For example, Korea's economy is now estimated to grow at a 7% rate this year, versus a prior estimate, as recently as the end of 1998, of 3%. The Singaporean economy is now estimated to grow at 4% this year, well ahead of the 2% prognostication at year-end. Finally, further supporting the expectation of faster, more inclusive, global growth was the US Fed's 25 basis point increase in interest rates at the end of the quarter. Satisfied that the global financial structure is now stable and that inflation-fighting is once again their first priority, Mr. Greenspan and the Fed Reserve governors have begun to claw back some of the 75 basis points worth of easing that provided salutary relief to financial markets last fall.

The rejuvenation of Asian economies and prospective resumption of more rapid, more widespread growth is incompatible with the enormous valuation gap that has developed between the largest 'growth' companies and the remainder of the global stock market. Growth stocks, particularly in Europe and the US, have been extraordinarily highly priced because, in a deflationary 'ice-age' environment with very low interest rates, their growing earnings stream would be rare and valuable. Conversely, industrial, commodity-related and other 'cyclical' stocks have been lowly priced on the expectation that global economic growth would be anemic.

This growth versus value price dichotomy, established over the course of two years, culminated in the extreme price gap that reached its peak in the first quarter. When the market's advance was confined to a narrow list of highly priced 'mega-cap' stocks, our insistence on broad diversification hindered our portfolio's performance. Moreover, as the price gap widened, our valuation-based investment discipline led us to reduce investments in large growth companies, and to increase investments in medium-size companies and in those with more economic sensitivity. Above all, it led us to maintain and, more recently, increase our commitment to companies operating directly or indirectly in emerging economies.

In the second quarter, these valuation trends reversed. The 'value' component of the MSCI All Country World Index outperformed its 'growth' counterpart by over 700 basis points in the quarter; in the US alone value outperformed growth by over 900 basis points. Worldwide, medium- and small-capitalization companies outperformed large companies by 315 basis points. Finally, the Pacific Basin, currently the most sensitive barometer of global economic sentiment, outperformed Europe and the US by over 1000 basis points and 340 basis points, respectively. Despite the size of these differentials, they retrace but a fraction of the prior, multi-year price movements. The price gap remains very large, as does the opportunity for the price-sensitive investor to exploit it.

This rotation accrued to the benefit of the portfolio. The portfolio's substantial representation in US industrial companies and in Southeast Asian companies was particularly favorably affected. Above all, our adherence to traditional valuation metrics and maintenance of a well-diversified portfolio was rewarded amidst the general re-appraisal of the sources and beneficiaries of global growth.

## Portfolio Review

In reviewing the price performance of the portfolio's holdings, the shared characteristics of the biggest 'winners' are obvious: cyclical and/or Asian exposure. This generalization, however, ignores the importance of company-specific business developments — to price performance, and as demonstration of how our portfolio companies are adapting themselves in a changing environment in order to serve their customers better, define more closely their core competencies

and, ultimately, grow their revenues and earnings faster. Three examples amongst the portfolio's largest gainers — **Johnson Electric**, **Singapore Press** and **AlliedSignal** — will illustrate the continual struggle to establish and maintain competitive advantage:

Hong Kong-based Johnson Electric (+47% in the quarter) is the world's #2 producer of mini-motors. It sells primarily to the automobile industry, and the kitchen & home appliance industry. Customers include all the US and European automobile producers, as well as companies such as Black & Decker and Cuisinart. We have followed this company since it became public in the mid-1980s and have owned it since the formation of our firm, some 10 years ago. Johnson's initial competitive advantage was cheap and productive labor in Hong Kong, used to spin copper wire around spindles by hand. The number of mini-motors in automobiles — to power everything from windshield wipers to seats to door locks — grew rapidly. Over time, rising labor costs in Hong Kong prompted the company to shift production to mainland China and Thailand. It retained engineering and development in Hong Kong, and established a research facility in Switzerland, taking advantage of that nation's tradition of mechanical miniaturization. By 1998 Johnson's production capacity had grown to 1.6 million motors per day, and annual sales of \$300 million.

In May of this year, Johnson took another evolutionary step, by purchasing United Technologies' automotive motor business. The acquisition, for less than 1x sales, will double Johnson's revenues. More critically, it gives it manufacturing capacity in the US, Italy and Mexico, allowing it to be geographically closer to its customers — who increasingly insist upon close physical proximity to their suppliers as a means of managing inventory better. This acquisition is the latest step in Johnson's evolution from a low-cost Asian manufacturer of commodity goods to a critical supplier of sophisticated components to some of the world's most demanding customers. Good management by the controlling shareholder family, a constant throughout, has enabled the company to change constantly and gradually, in response to the shifting demands of its market.

Singapore Press (+52% in the quarter) is the dominant publisher of English, Chinese and Malay language newspapers in Singapore. Newspaper advertising accounts for 75% of total revenues with the balance from circulation, magazines and other businesses. For many years that we followed the company, we were

attracted by the near-monopoly nature of the company's franchise but repelled by its apparent disregard for the interests of shareholders. Specifically, Singapore Press was using its copious free cash flows from the newspaper and magazine business to buy property, rather than increasing the dividend or considering repurchasing shares.

Chastened by the withdrawal of capital from the region during the financial crisis of 1997-98, the company has changed its stripes. We purchased shares in September 1998, in the midst of the crisis, when the value of the company had sunk more than 50% below its level 18 months earlier. Last fall, it was the first Singaporean company to eliminate the dual structure of separate shares for foreigners and locals. When the dual shares were merged, the company also carried out a share buyback and a dividend increase. A second share buyback has been authorized. The company is leveraging its valuable core media assets and, explicitly, the business is now being managed with an objective of increasing returns to its shareholders. The company is diversifying beyond its core newspaper business but has carefully defined its focus to include media and communications businesses that are related to its existing competencies. Having previously invested in cable TV and wireless communications businesses, Singapore Press' website is already one of Asia's most heavily visited 'portals'. The share price has appreciated more than three-fold since our investment.

The portfolio has held AlliedSignal (+27%), soon to be Honeywell, since 1996. AlliedSignal is a diversified manufacturing and technology company with concentrations in aerospace, automotive and engineered materials. Since moving from GE to become Allied's CEO in 1991, Larry Bossidy has transformed the company. He has sold non-core, low-returning businesses, aggressively reduced manufacturing costs, and increased productivity by 6% each year. Operating margins have increased from under 5% in 1991 to 13% in 1998 — especially impressive in light of the fact that Allied has been operating in an environment of steadily declining prices in its three core businesses. Bossidy's achievements at Allied must surely make his old boss Jack Welch proud.

Still, despite 28 consecutive quarters of EPS growth of 12% or more, analysts have been skeptical about Allied's ability to continue growing earnings without growing the top-line faster. The announcement in early

June of Allied's merger with Honeywell addresses these concerns. Honeywell's core controls and systems businesses share many aerospace and automotive clients with Allied. Its operating margins are already at Allied's 13% level. Management is targeting \$500 million in cost savings for the first year, and we expect to see margins for the new company climb towards 15% as these synergies are realized. Bossidy is scheduled to retire next April and has appointed Honeywell CEO Michael Bonsignore to succeed him. Bossidy will leave a company transformed from an ill-fitting collection of cyclical industrial businesses and a management acceptant of wide fluctuation in earnings, to a business focused on three business segments, unified by a culture driven to increase productivity relentlessly and grow earnings steadily.

Just as we described the shared characteristics of the 'winners', we could say that the portfolio's 'losers' performed poorly simply because they were large-cap growth stocks in a period when growth stocks were as popular as ants at a picnic. However in looking at the ten stocks that were the portfolio's worst performers this quarter, there are some company-specific issues that go beyond the 'falling out of fashion' of large cap growth.

**Pfizer** (-21%) has been a portfolio holding since 1997. The company has had a string of successes in new pharmaceutical launches this decade, including billion dollar drugs Norvasc (for hypertension), Zithromax (an anti-infective), Zoloft (for depression), and last year's well publicized launch of Viagra. Along with the products that have come from Pfizer's own laboratories, the company has grown its marketing and sales capabilities such that it has become the industry's marketing partner of choice. Pfizer's marketing strength has been a critical factor in the success of Warner Lambert's Lipitor and Monsanto's Celebrex.

Pfizer shareholders have been well rewarded for their company's successes. The shares have far outdistanced the S&P 500 and Pfizer's market cap of \$140 billion is second only to Merck's in the sector. It appreciated over 200% in 1997 and 1998, a return three-fold higher than that of the S&P 500. Beyond the question of growth valuation, two other factors contributed to the stock's poor recent performance. First, political debate over reimbursement policies, Medicare and healthcare reform is expected to intensify as the 2000 election draws closer, bringing increased uncertainty about long-term earnings growth rates for the pharmaceutical sector. Second, Pfizer suffered a setback in June when

the FDA limited use of the company's powerful new antibiotic Trovan to life-threatening cases, due to concern over the association of liver toxicity with the drug in a small number of instances.

We remain committed to Pfizer. With a \$2.3 billion R&D budget for 1999, Pfizer has the largest commitment to new drug development in the industry. While there is an element of serendipity in the discovery of successful new drug compounds — Viagra was a failed cardiovascular drug before its other effects were discovered! — we regard Pfizer's successful past record as strong evidence of the efficacy of its development efforts, and indicative of likely future results. This, coupled with the company's marketing muscle and our favorable view of the secular growth of healthcare expenditures, gives us confidence in Pfizer's future growth, notwithstanding its recent travails.

UK-based **Rentokil Initial** (-35%) has been a shareholding since 1995. The company is engaged in a variety of service businesses including pest control, hygiene services, non-armed security and tropical plant care. It employs some 140,000 blue-collar workers in forty countries. As befitting the nature of these service industries, Rentokil's revenues are fairly steady through business cycles. The company has grown organically, as well as through acquisitions. Rentokil has been able to increase the margins of acquired businesses by implementing best management practices, and by eliminating redundant overhead costs. Rentokil has been brilliantly managed, growing earnings at a 20% annual rate for the last twenty years — until this year. In May, the company announced that earnings growth would fall short of the 20% target this year and instead grow at a rate of 10 to 15%, due to subdued inflation, weaker contributions from Asia, and the strength of sterling. We had been expecting only 14% earnings growth and thus were not unduly surprised at the announcement. What *did* surprise us was the plunge in the share price that followed it.

In early June we added to our position in the company. Rentokil's management can fairly be criticized for having neglected revenue growth at the expense of increasing margins. The fall in the share price was such that it was discounting future annual earnings growth of only 9% over the next eight years — well below our adjusted estimate of 12%, which we believe to be conservative. Top-line growth should accelerate over the next few years, both organically and via acquisition. The businesses in which Rentokil operates

are by their nature fragmented, and therefore offer abundant acquisition opportunities. Continued outsourcing should drive organic growth, as companies define their core businesses more strictly and exit those businesses that do not fall within that core. Cash flows from the business are strong, and the company will buy back stock if it feels as though that is the best use of shareholders' funds. We believe that the characteristics that attracted us to this business initially are still intact. It is rare to find a business services company with good growth prospects at such an attractive valuation.

## Transactions

During the quarter, we bought:

**Goldman, Sachs**, one of the world's premier investment banks. Rarely do we buy IPO's because we cannot hope to become familiar enough with a company in the two- or three-week 'road show' to feel confident enough to buy it. Goldman, Sachs is an exception. Having done business with them for over twenty years, we know the company very well and believe its capabilities in trading and banking to be unsurpassed among its peers. Asset management is the third leg of their business, and should be the fastest growing of the three over the next few years. An acquisition in asset management is probable, in our opinion. The structure of the deal aligns the interests of outside shareholders and the employees of Goldman, Sachs by forbidding the sale of any shares by employees or the former general partners for three to five years.

**Grupo Televisa**, the dominant television and radio network in Mexico, operating four TV channels. The company is also the world's largest producer of

Spanish language TV programming. The company aims to maintain its dominant (>65%) market share in Mexico but also to export its programs to other Spanish TV markets, not only in Latin America but also the US, Spain and more than 70 other countries. The combination of both media distribution and content is rare and valuable. The new management team lead by Emilio Azcarraga, the son of the founder, intends to optimize the company's wide range of assets well beyond his father's vision.

We added to UK business service company **Rentokil Initial**, as previously mentioned. The price had dropped sharply, as the market's unrealistic expectations for earnings were not met. Our expectations were already lower and our confidence in this long-held company unshaken. The lower price was a good opportunity to buy back the partial position we sold at higher prices last year.

We sold:

**Societe Generale de Surveillance**, the Swiss testing and inspection company, completing the sale begun last quarter.

**Siam Cement**, Thailand's largest industrial conglomerate on price grounds. The share price had risen five-fold since last September, reflecting hopes that Thailand's economy had bottomed, and that Siam Cement, as the market leader, would emerge stronger than it was before the downturn. We think this is discounted in the share price at current levels.

Finally, we sold the warrants in **Scania**, which were expiring, and reduced the holding in **Royal Dutch**, the global integrated oil company.

## Portfolio Holdings as of June 30, 1999

Company	Country	Weight	Description
Allied Capital	US	3.3%	Financial institution making equity-linked loans to small businesses
Singapore Press	SING	3.2%	Dominant newspaper publisher in Singapore
Colgate	US	3.1%	Leading global consumer products company
Hutchison Whampoa	HK	3.0%	Conglomerate involved in container terminals, housing, energy, telecoms, & retailing
Royal Dutch Pet ADR	NETH	2.9%	Premier oil company operating worldwide
Gaz et Eaux	FRA	2.9%	Investment company in Lazard Group
Schlumberger	US	2.8%	Premier supplier of technical services & equipment to petroleum industry
Johnson Electric	HK	2.8%	Manufacturer of small precision motors used in cars & consumer products
Baxter International	US	2.7%	Leading medical products supplier focused on blood transfusion & kidney dialysis
Jardine Strategic	SING	2.7%	Investment holding company of Jardine Group Asian investment
WPP Group	UK	2.6%	World's largest advertising & marketing services company
Allied Signal	US	2.6%	Aerospace, auto, chemical & fiber manufacturing company
Pearson	UK	2.5%	UK print & broadcast media company
Rio Tinto	UK	2.3%	One of world's largest & most diversified mining companies
Investor	SWE	2.3%	Holding company for Wallenberg family interests in Swedish industrial concerns
Sun Microsystems	US	2.3%	Leading beneficiary of move to Internet computing
Thermo Electron	US	2.3%	World leader in environmental monitoring, analysis instruments & biomedical products
Rentokil Initial	UK	2.3%	Provider of wide range of services to commercial sector
American Int'l Group	US	2.3%	Insurance holding company offering insurance, risk management & agency services
Pfizer	US	2.1%	US pharmaceutical, veterinary, specialty chemicals & toiletries company
Exxon	US	2.1%	Premier global oil company
Wolters Kluwer	NETH	2.0%	Dutch publisher of legal, tax, medical, & business information
Wells Fargo	US	1.9%	California's largest commercial bank
Intel	US	1.9%	Global leader in semiconductor manufacturing
ABB	SWITZ	1.9%	Leading worldwide capital goods company
Wrigley, Wm. Jr.	US	1.8%	World's largest producer of chewing gum
Nestlé	SWITZ	1.8%	World's largest food company
Atlantis Japan	JAP	1.7%	Closed-end fund invested in smaller Japanese companies
Air Products	US	1.7%	Leading industrial gas company
Deere & Co.	US	1.6%	World's leading producer of farm equipment
Mitsubishi Corp	JAP	1.6%	One of Japan's largest trading companies
Dover	US	1.6%	Diversified capital goods manufacturer
Fannie Mae	US	1.6%	Government-sponsored agency that buys & repackages mortgages
Quintiles	US	1.5%	Outsourcing partner for healthcare companies
Hirose Electric	JAP	1.5%	Japanese manufacturer of electrical connectors & components
Bic	FRA	1.4%	World's leading producer of disposable razors, writing implements & lighters
Wisconsin Central	US	1.3%	Railroad operator in US & overseas
Monsanto	US	1.2%	Life sciences company with leadership position in genetic engineering
Luxottica	ITA	1.2%	World's largest & lowest cost producer of high-quality eyeglass & sunglass frames
Telefonos de Mexico	MEX	1.1%	Mexico's dominant provider of telecommunications services
Grupo Televisa GDR	MEX	1.1%	Largest media company in Spanish-speaking world
Li & Fung	HK	1.0%	Hong Kong-based trading & logistics company
CBT Group	IRE	1.0%	Leader in computer-based software training
SAP ADR	GER	0.9%	Global leader in packaged enterprise software
MCI Worldcom	US	0.9%	Global provider of fully-integrated local, long distance, international & internet services
UBS Reg.	SWITZ	0.9%	Europe's largest bank, & world's largest asset management firm
Zurich Allied	SWITZ	0.9%	Global provider of insurance & asset management services
Kimberly-Clark Mex	MEX	0.8%	Mexican subsidiary of US-based Kimberly-Clark Corporation
Allianz	GER	0.7%	One of world's largest general insurance companies
Quilmes	ARG	0.7%	Leading producer of beer & soft drinks in Latin America
Goldman Sachs	US	0.7%	Premier global investment bank
Liblife Strategic Inv.	S AFR	0.6%	Investment holding company with equity interest in Standard Bank
Aspen Technology	US	0.3%	Leading provider of process optimization software

## Global Equity Composite Performance Summary as of June 30, 1999

	Annualized Returns for Trailing Periods (%)					Volatility
	1 Year	3 Years	5 Years	9 Years	Since Inception*	Annual Standard Deviation (%)
<b>HLM Global Equity Composite</b>	<b>6.1</b>	<b>10.4</b>	<b>12.4</b>	<b>12.8</b>	<b>13.9</b>	<b>12.4</b>
<i>FT World Index</i>	16.4	18.0	16.3	12.1	10.7	14.9
<i>MSCI All Country World Index</i>	17.1	17.4	16.0	12.1	10.8	14.1
<i>Lipper Global Fund Index</i>	9.5	14.8	14.0	11.3	11.4	12.6

\*Inception Date: 11/30/89

	Calendar Year Returns (%)									
	YTD 1999	1998	1997	1996	1995	1994	1993	1992	1991	1990
<b>HLM Global Equity Composite</b>	<b>12.2</b>	<b>2.3</b>	<b>11.0</b>	<b>17.3</b>	<b>19.0</b>	<b>0.0</b>	<b>24.3</b>	<b>8.9</b>	<b>29.4</b>	<b>7.9</b>
<i>FT World Index</i>	9.5	23.0	15.4	13.2	19.6	5.9	22.6	-5.1	19.6	-17.0
<i>MSCI All Country World Index</i>	10.2	21.7	14.7	13.1	18.2	5.4	25.5	-4.3	19.5	-17.2
<i>Lipper Global Fund Index</i>	9.3	14.6	14.0	16.3	14.0	-2.2	32.8	0.1	20.3	-9.1

	Composite Information									
	YTD 1999	1998	1997	1996	1995	1994	1993	1992	1991	1990
Number of accounts included in the composite	10	11	15	13	17	16	14	12	†	†
Total market value of accounts included in composite (\$M)	\$182.8	\$176.9	\$251.1	\$188.0	\$146.7	\$112.4	\$80.2	\$63.3	\$41.3	\$15.3
% of total firm assets represented by composite	14.5%	12.9%	16.5%	15.1%	23.4%	30.5%	31.8%	39.3%	30.0%	26.6%
Internal dispersion: standard deviation of calendar year returns	NA	1.7%	1.5%	0.8%	2.0%	1.4%	6.5%	2.1%	2.5%	†

†Five or fewer accounts

Harding, Loevner Management, L.P. ("HLM") has prepared and presented this report in compliance with the Performance Presentation Standards of the Association for Investment Management Research ("AIMR-PPS™"). AIMR has not been involved with the preparation or review of this report. HLM is compliant with AIMR-PPS since 10/31/89. This composite has been verified compliant, one quarter in arrears, at Level II by Ashland Accounting LLC.

### NOTES:

- Harding, Loevner Management, L.P. is an independent registered investment adviser.
- Composite includes all US\$ based, fee-paying global equity accounts under discretionary management, including accounts no longer in existence. Accounts are included from the first full month following the date on which the account is deemed to be fully invested. No subsector or segment of a larger portfolio is included.
- Returns shown are time-weighted total returns in US\$, and reflect reinvestment of dividends and interest. Returns include the effect of foreign currency exchange rates. Returns are weighted by account size in the composite.
- All cash equivalents, bonds and/or convertible securities used in place of equities are included in return calculations.
- Composite returns are presented after brokerage commissions but before management and custodial fees and foreign withholding taxes. Management fees are described in our Form ADV Part II. Inclusion of management fees result in composite returns for trailing periods, as follows: 1 yr 5.5%, 3 yrs 9.5%, 5 yrs 11.6%, 9 yrs 11.9%, since inception 13.0% .
- Returns of all indices (except Lipper) are presented before foreign withholding taxes, and do not reflect commissions or fees that would be incurred by an investor in the index portfolios. Lipper Index returns are reported after all fees and expenses. Additional information regarding benchmarks, including the percentage of the composite invested in countries not included in the benchmarks, is available upon request.
- Annual standard deviations of returns (volatility) is estimated from monthly returns using a continuous return model to derive annual periodic standard deviation.
- A complete list and description of the firm's composites is available upon request.
- Past performance is not indicative of future results.

### Annualized Returns for Trailing Periods (%)

