

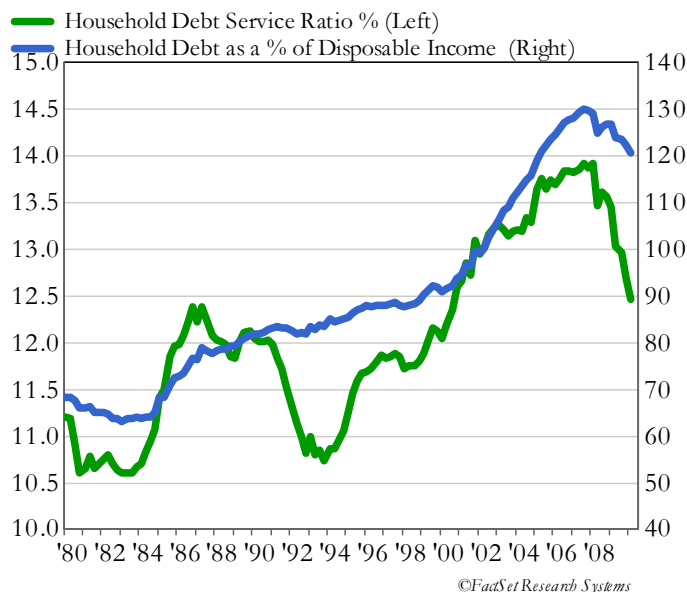
HVERFORD OUTLOOK



The third quarter was marked by volatile markets, shifting sentiment, and fears of a second recession. Since the economic recovery began, Haverford has forecasted only moderate growth in the developed world, offset by continued strength in emerging markets. Although we continue to foresee only tepid domestic economic growth in the near term, we also believe the foundation is being laid for a more durable economic expansion. Furthermore, we have identified several catalysts that could propel the stock market higher as we look toward 2011.

Economy: Slow Growth...For Now

Although the Federal Reserve has done a good job of restoring liquidity to the system in the wake of the financial crisis, economic growth has been lackluster due to deleveraging by consumers and businesses, as well as by the uncertainty associated with future tax rates and increased government regulation. These concerns will likely conspire to put a lid on economic growth in the coming quarters, but we anticipate better times ahead as we wring out the excesses of the past.



The Household Debt Service Ratio is an estimate of the ratio of debt payments (required payments on mortgage and consumer debt) to disposable personal income.

Deleveraging by the consumer is likely the largest impediment to stronger economic growth. Consumers continue to pay down debt *en masse*, which is diverting funds that would otherwise be used to purchase goods and services. While this has a negative impact on the economy in the short term, consumers will likely emerge stronger and our national savings rate will be higher, which is good for the economy and capital markets. This process of deleveraging is occurring at a faster pace than originally anticipated, as lower interest rates have reduced monthly payments on mortgages and other debt, increasing consumers' wherewithal to pay down principal.

Another drag on the economy is fiscal policy, which is growing increasingly restrictive. The cost of compliance with

numerous new regulations has resulted in a “shadow tax” that will likely temper companies’ ability to undertake new ventures and hire new employees. There is also a great deal of uncertainty regarding these shadow taxes since many of the regulations – those associated with healthcare and financial reform, to name just two pieces of legislation – have yet to be written. Furthermore, there is also much uncertainty related to the future tax code. The expiration of the Bush tax cuts is a subject of great debate, of course, but also lurking in Washington is a possible revamp of the corporate tax code, which could result in higher corporate tax rates to help pay for the extension of the tax cuts for the middle class.

By year end many of these uncertainties should give way to increased clarity, or, at the very least, they should become more quantifiable. To the extent that the midterm elections reduce political uncertainty, businesses will have a better opportunity to plan and budget, and then hopefully begin to hire permanent workers.

Although fiscal policy has grown more restrictive, the most influential policy lever – monetary policy – remains decidedly stimulative. The Federal Reserve is committed to a zero-percent interest rate policy for the immediate future, and has expressed its willingness to employ additional quantitative easing should the economy weaken further. Low short-term rates have resulted in a steep yield curve, which usually presages an expanding economy. In addition, low short rates are facilitating the rapid repairing of bank balance sheets while simultaneously providing inexpensive financing for creditworthy borrowers. With monetary policy so accommodative, barring an unpredictable external shock to the economy, we believe a double-dip recession remains a low probability.

Equities: Catalysts for Higher Stock Prices

With equities at the top end of their recent trading range, we believe several catalysts exist that could drive prices higher.

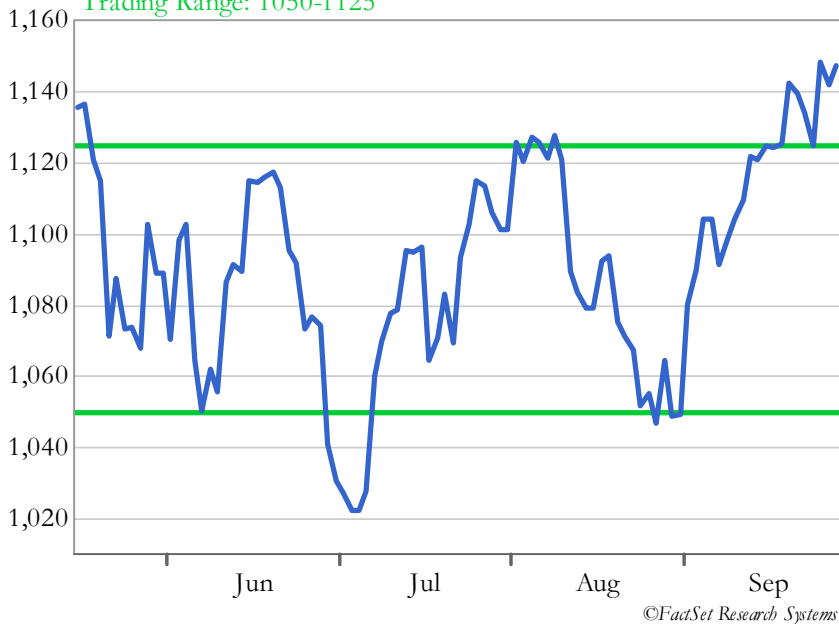
Obviously, stronger-than-expected economic growth would likely be a strong catalyst for higher stock prices. We witnessed this in September. Following August’s poor economic reports, better-than-expected data were the catalyst for the strong rally as investors worried less about a potential double-dip recession. Analyst estimates for GDP growth will likely rise if we experience further improvements in the trade deficit. Recall that second-quarter GDP was dragged down by a deteriorating trade deficit, but recent data have pointed to an improvement, which the market does not yet reflect.

September’s market strength may also be attributable to investors anticipating turnover in the midterm elections. A high level of political turnover will likely result in legislative gridlock, which has historically benefited equity markets since it reduces the possibility of any major new legislation and regulations. Insofar as investors view Washington as “anti-business,” restoring checks and balances will likely be viewed favorably.

Monetary stimulus in the form of additional quantitative easing may also ignite a further rally. At the FOMC’s September meeting, the Fed expressed willingness to implement quantitative easing if necessary and some expect that it might occur this November. Quantitative easing is a term that essentially means providing more liquidity to the system. Some of this cash would surely find its way into equities given attractive valuations, growing earnings, and attractive dividend yields.

S&P 500 Price Index - May 15 to Sep 28, 2010

Trading Range: 1050-1125



We believe several catalysts exist that could drive prices higher through the end of the year:

- *Rising GDP Estimates*
- *Mid-term Elections*
- *Quantitative Easing*
- *Mergers & Acquisitions*
- *Rising Dividends and Buybacks*
- *Reversal of Negative Sentiment*

Merger and acquisition activity has increased recently, which is a sign that corporate managers and directors have more confidence in the sustainability of the economic expansion and are thus willing to assume more risk.

Corporate balance sheets are

certainly flush with cash, giving companies plenty of flexibility to increase dividends and stock buybacks, and to increase M&A activity. An uptick in any of these activities would be welcome by investors, creating yet another catalyst for higher prices.

Finally, extremes in investor sentiment are often a contrary indicator for asset prices. By the end of August, sentiment had almost become as sour as it was in early March '09, reflecting high levels of fear and pessimism. In addition to the bull/bear and consumer confidence surveys, this dour sentiment is reflected in investors' continued exit out of equity mutual funds and into bond funds. As a result, many stocks currently have dividend yields greater than the yield of the ten-year Treasury note. The last time this occurred was in 1956 due to the vestiges of the Great Depression mentality in which investors required stocks to yield more than bonds because of the added risk. Any positive shift in sentiment could ignite a further rally in stock prices.

Given that many parts of the world are growing faster than the United States, we believe that companies with global economic exposure will outperform the overall market. We will also continue to hold highly predictable and less economically-sensitive companies to mitigate portfolio volatility and provide insurance in case our economic and market outlook proves too optimistic. With a great many stocks yielding more than Treasuries, and in some cases upward of four and five percent, we believe equities are extremely attractive relative to bonds.

Fixed Income: Strategies for a Zero-Rate Environment

The Federal Reserve's commitment to a zero-percent interest rate policy and willingness to implement additional quantitative easing will likely have a greater impact on Wall Street than on Main Street. We may also be perilously close to a point in the cycle where low interest rates are hurting investors more than they are helping borrowers. Despite these low rates, we believe there are various pockets of value within the market that deserve investors' focus.

U.S. Treasury yields continue to hover at all-time lows. The two-year note currently yields a record low of 0.42%, while the 10-year note yields only slightly above its recent low of 2.46%. Clearly, these rates benefit the Treasury as it finances ongoing deficits, but we continue to be very concerned

about deficits that total more than \$1 trillion per fiscal year. Even with the Federal Reserve reinvesting approximately \$200 billion of maturing holdings into Treasury issues over the next year, the market must absorb more than \$800 billion of new financing in addition to rolling over existing debt.

At these low rates, bond prices are very vulnerable to any increase in rates. An increase of 100 basis points in 10-year yields would only take the market back to the levels of mid-May, while the resulting price decline would approximate 8.3% of the bond's value. The bond's paltry 2.59% yield would only offset 30% of the price decline. This very possible scenario illustrates why we believe these low yields offer very little value for investors.

While low mortgage rates have been a boon to both home buyers and those able to refinance their mortgages, investors in mortgage-backed securities are subject to both reinvestment risk as principal payments are received and extension risk when rates begin to increase. In this environment we prefer mortgage-backed issues with lower volatility (such as those backed by 15-year mortgages as opposed to longer-dated 30-year collateral) and we similarly value seasoned issues over new production. Consistent with the Federal Reserve's policy to reinvest the proceeds of mortgage securities into other sectors, we are not reinvesting payments back into the mortgage-backed sector, thereby reducing over time our allocation to the mortgage-backed market.

Corporations have taken advantage of low yields to aggressively issue new debt. Lower absolute financing costs clearly help corporate cash flows, but this benefit is mitigated by already substantial cash balances earning virtually zero interest. For example, IBM issued \$1.5 billion in new 3-year notes with a 1% coupon. If the company had to pay 1% more, it would reduce annual earnings by \$0.01 per share. Conversely, IBM would earn an additional \$0.11 per share if interest rates on their cash balances were to rise by the same 1%. We continue to be comfortable owning the debt of large, high-quality corporations due to positive trends for both earnings and balance sheets.

State and local governments have taken advantage of low interest rates and strong investor demand to finance both operating deficits and new projects. Municipal finances have lagged the improvement in corporate earnings and low rates have exacerbated the strains resulting from already underfunded pension liabilities. This further delays credit improvement and necessitates even more borrowing. One strategy we have used to gain incremental yield in the municipal sector has been to purchase callable bonds in the secondary market. While most new issues do not adequately compensate investors for the risk of a bond being redeemed prior to maturity, we have been successful in uncovering opportunities in the secondary market that offer higher yields to maturity.

Conclusion

Similar to other economic recoveries, there is a great deal of anxiety and frustration with the pace of economic growth. This is especially true given the severity of the recent recession and the highest level of unemployment witnessed in many years. Although investors yearn for better times ahead, this is not an easy task given the incessant drumbeat of negative news that is now pervasive across all the 24-hours-per-day news networks.

In this environment, we believe it is essential that investors maintain a longer-term perspective, filtering out much of the negative noise. A closer look reveals many good things occurring, including strong and growing corporate earnings, solid balance sheets, and many catalysts on the horizon – the November elections, to name just one – that could well bring about much more constructive investor sentiment and higher stock prices.