Mengis
CAPITAL MANAGEMENT INC.

Mid-Quarter Newsletter

May 15, 2010

From My Corner

Jeff Mengis – President

Market Comments: Following the first market correction since the strong rally from the March 2009 lows, we wanted to review where our portfolios are focused. As is typical with the first year of a recovery, cyclicals and financial stocks led, P/E multiples expanded as earnings rebounded and investor confidence increased. At this point in the market cycle, we are overweight companies in the energy, health care and technology sectors that offer growth at a reasonable price. While there are certain financial companies we find attractive, our portfolios are underweight the sector because we believe that increased regulation and non performing assets will weigh on the industry for some time.

Our strategy when allocating capital has been to focus on the relative value of individual companies. Over the long-term, companies in the energy sector should benefit from rising energy prices as supply constraints converge with a more global economy. Even during the recent downturn, amid the worst recession in decades, capacity utilization of oil was at 95%. Once the economy has recovered, the price of energy is likely to increase. Recently, performance of this sector has been disappointing as a stronger dollar has driven the price of oil lower. In addition, the gulf oil spill has weighed on companies with drilling exposure. However, those fears have created opportunities in solid companies like Exxon Mobil (XOM), which has about $1.6 trillion in proven oil equivalent reserves.

We are also overweight in health care companies that should benefit from an aging demographic trend and provide some defense if the market were to double dip. A company like Abbott Laboratories (ABT) is trading near a 52-week low, primarily due to concerns about a weaker European Union impacting their sales. The pullback means an investor with a long-term view can buy Abbott at a historically low cash flow multiple and earn a 3.6% dividend yield while waiting for the stock price to improve.

Lastly, the fundamentals behind the technology sector reflect strength not seen since the late 1990's. An upgrade cycle driven by new software and strong demand from emerging economies should enhance profits in the industry. We favor a company like Intel, which is forecast to see record earnings in 2010 and pays a 3% dividend.

Investment Focus:

Marathon Oil (MRO) is the 4th largest integrated energy company based in the United States. About 70% of Marathon's revenues are derived from oil exploration and production, while about 30% is from refining and marketing division. Marathon is weighted more toward refining than most integrated oil companies. While it is a challenging environment for refineries, Marathon has a competitive advantage in that their geographic footprint in the Midwestern U.S. is not as vulnerable to imported fuel as coastal refiners. Marathon's oil exploration business provides the potential for upside. Production from a major platform in the Gulf of Mexico, combined with an oil sands project in Alberta will help to boost Marathon's cash flow by an estimated 12% by 2011. In addition, they have rights to about 336,000 net acres in the increasingly important North Dakota Bakken shale, which is currently estimated to produce 22,000 barrels of oil equivalent per day within 3 years. While this is a small part of their overall production, it provides a geopolitically safe, low cost source of oil.

Marathon currently trades at a discount to its peers because their exploration and production projects tend to have a higher cost per barrel of oil equivalent to produce, making the stock more tied to the price of oil. In addition, news of the gulf oil spill has created some pause around all deep water drilling. Realistically, given our countries tenuous energy position, we see little alternative but to drill in the gulf. Marathon's stock trades at about 4.5X 2010 forecast cash flow, allowing the company to pay a 3.3% dividend.

Focused Taxable Composite

MID-QUARTER NEWSLETTER
2nd Quarter 2010

Investment Strategy and Goal

The *Focused Taxable Composite* seeks long term capital appreciation by investing in companies which, in MCM's judgment, offer value relative to their long term potential and the market as a whole. Using a multi-cap approach, the composite is able to invest in companies of all sizes, although most companies have market capitalization in excess of $500 million. Our overall goal is to consistently outperform the S&P 500 index.

This information is presented as supplemental and complements the Annual Disclosure Presentation located at the bottom of this page

Top 10 Holdings (as of 03/31/10)

Intel	5.6%
Precision CastParts	5.0%
Philip Morris Intl	4.7%
Amgen	4.6%
Cisco Systems	4.6%
Teva Pharmaceutical	4.1%
3M	4.1%
Costco	3.6%
McDonald's	3.5%
Disney	3.1%

Data presented represents a percent of the total market value of the Focused Taxable Equity Composite, including cash. As of March 31, 2010, cash represented 4.7% of the total composite. This information is presented as supplemental and complements the Annual Disclosure Presentation located at the bottom of this page.

Performance

	Year-to-Date	*5 Year**	*Since Inception** *10/1/98*
Focused Taxable Composite	4.51%	2.36%	7.57%
S&P 500 Index	5.39%	1.92%	3.01%

* Past performance does not guarantee future results. Please see additional performance disclosures at the end of this presentation. Numbers are net of fees. 5 year and inception percentages are annualized figures.

Mengis Capital Management, Inc., has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS®). Mengis Capital Management, Inc. is a registered investment advisor. The firm maintains a complete list and description of composites, which is available upon request. Performance prior to November 28, 2001 occurred while the portfolio manager was employed at a prior firm and was the only individual responsible for selecting the securities to buy and sell. A review of this track record for compliance with the portability requirements of the GIPS standards was conducted by Ashland Partners & Company LLP. Compliance with the Association for Investment Management and Research Performance Presentation Standards (AIMR-PPS®, the predecessor to GIPS) was verified at the prior firm, beginning February 1, 1998. As represented by management, the performance from the predecessor firm conforms to the GIPS guidelines with regard to portability of investment results. Focused Taxable Equity Composite contains fully discretionary taxable equity accounts and for comparison purposes is measured against the S&P 500 Index. Sector weightings observed in the Focused Taxable accounts vary significantly from those in the S&P 500 Index. In addition, from time to time, the Focused Taxable accounts will generally have 20-30 holdings as compared to the S&P 500 Index (composed of 500 different stocks). For certain time periods, the composite may be more concentrated than the benchmark. Due to the limited number of holdings relative to this index, the investment risks associated with concentration are significantly greater for the Focused Taxable accounts than it is for the index used for comparison. For periods shown prior to January 1, 2006, the minimum account size for this composite is $50 thousand. Effective January 1, 2006, the minimum account size has been change to $150 thousand. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. As of 12/31/2009, there are 10 accounts being managed consistent with the discipline referred to as "Focused Taxable." Mengis Capital Management, Inc. currently manages over 200 other portfolios on a discretionary basis. These portfolios are not managed according to the Focused Taxable methodology and the results in these accounts will vary, both positively and negatively, from those experienced by the Focused Taxable accounts. Information regarding the performance achieved in these accounts is available upon request. The U. S. dollar is the currency used to express performance. Returns are presented gross and net of management fees and include the reinvestment of all income. Net of fee performance was calculated using actual management fees. Prior to January 1, 2002, accounts in the composite were charged an all inclusive wrap fee. Gross returns for this period are shown as supplemental information and are stated gross of all fees and transaction costs; net returns are reduced by all actual fees incurred. The standard management fee is a maximum of 2.00% on all assets. Mengis Capital Management, Inc. has been verified for the periods November 28, 2001 through March 31, 2010 by Ashland Partners. In addition, a performance examination was conducted on the Focused Taxable Equity Composite beginning November 28, 2001. A copy of the verification report is available upon request. Additional information regarding policies for calculating and reporting returns is available upon request. There has been no material change in personnel responsible for the investment management of this composite. The Focused Taxable Equity Composite was created October 1, 1998. Past performance is not indicative of future results. Investments are subject to market fluctuations and investors could lose some or all funds invested.

	Total Firm Assets (thousands)	Composite Assets		Accounts	Asset-Weighted Annual Return			
		US Dollars (thousands)	% of Firm Assets	at Year End	Gross	Net	S&P 500	Annual Composite Dispersion
2009	103,436	9,968	10%	10	25.33%	24.10%	26.46%	1.9%
2008	92,666	7,021	8%	13	(33.80%)	(34.45%)	(37.00%)	1.5%
2007	121,952	17,970	15%	14	8.29%	7.20%	5.49%	2.5%
2006	97,596	15,637	16%	16	14.66%	13.50%	15.80%	1.1%
2005	89,242	15,206	17%	12	9.55%	8.49%	4.88%	1.1%
2004	85,368	11,016	13%	9	17.70%	16.51%	10.88%	1.2%
2003	86,803	8,414	10%	13	30.04%	28.79%	28.69%	1.1%
2002	61,896	4,072	7%	10	(24.82%)	(25.44%)	(22.10%)	2.2%
2001*	45,728	1,848	4%	8	(9.74%)	(11.16%)	(11.88%)	4.4%
2000*		1,404	2%	6	35.90%	33.49%	(9.11%)	N.A.
1999*		481	1%	5 or fewer	25.13%	22.35%	21.04%	N.A.
1998*		137	<1%	5 or fewer				

- N.A. - Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year.

*- *Information presented pertains to portfolios managed by the portfolio manager while affiliated with a prior firm. Their presentation conforms to AIMR-PPS guidelines (the predecessor to GIPS) regarding the portability of investment results.*

- S&P 500 Index performance returns reflect gross dividends reinvested into index. S&P Index performance returns through September 30, 2001, were obtained from Bloomberg; index performance returns for periods after September 30, 2001, were calculated using data from FT Interactive Data.

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