September 1, 2005

SEPTEMBER NEWSLETTER

Executive Summary

Year-to-Date Total Returns – Most of the stock indices have had relatively flat returns through the first eight months of 2005. The mid and small capitalization stocks have performed better than the large capitalization stocks, and “value” stocks have out-performed “growth” stocks. Energy stocks and “defensive” sectors such as Utilities, Health Care and Consumer Staples have led the market.

Strong Second Quarter Earnings – Earnings per share of the Standard & Poor’s 500 companies increased a strong 13% in the second quarter of 2005. This rate of increase was only slightly less than the 14% increase in the first quarter and was over 2 percentage points higher than recent estimates. Energy companies led the way with a 41% average increase in the second quarter with companies in the Industrials, Materials and Telecommunications sectors contributing average increases of over 20%.

Earnings Outlook - Earnings per share for the Standard & Poor’s 500 Average are estimated to increase 15% in the third quarter and then slow to a 6% increase in the fourth quarter with similar single-digit increases throughout 2006. Most of the earnings deceleration is expected to occur from companies in the Energy, Materials and Industrials sectors due to lower expected increases in energy and commodity prices and slower economic growth. However, analysts expect earnings growth to accelerate in the Consumer Discretion, Consumer Staples, Health Care and Information Technology sectors.

Stock Valuations – Current average price/earnings ratios, based on 2005 and 2006 earnings estimates, are near or below the average low price/earnings ratio of the past five years in every Standard & Poor’s sector except Utilities. The current price/earnings ratio of the Standard & Poor’s 500 average is near the long-term historical average and appears to be under-valued when adjusted for current interest rates.

Investment Strategy - We continue to be constructive on the outlook for stock prices over the next several years, and we believe they offer better value than fixed-income alternatives at current prices. We believe that most of the uncertainties regarding rising interest rates, high energy prices and slowing economic growth are already largely discounted in the current prices of stocks. We recommend strong portfolio weightings in selected stocks in the Energy, Health Care, Consumer Discretion and Financial sectors for investors with a long-term investment horizon.

Year-to-Date Total Returns

The year-to-date returns in the U.S. stock markets have vacillated during 2005 between modest single digit increases and single digit declines. Through August 31, 2005, the Standard & Poor's 500 had a total return (price change plus dividends) of +1.6%, while the Dow Jones Industrials and the NASDAQ Composite had declines of -1.0% and -1.5%, respectively. The mid and small capitalization stocks have performed better than the large capitalization stocks, and "value" stocks have out-performed "growth" stocks during the first eight months of 2005. These returns are presented in Exhibit 1.

Only four of the 10 Standard & Poor's 500 economic sectors had a positive total return for the year-to-date period. Companies in the Energy sector led the market with an average total return of +27.9%, followed by Utility stocks with a +16.3% average total return for the period. The poorest performing sector was Materials, as investor concerns that many commodity prices may have peaked outweighed strong second quarter earnings results. Other than the Energy stocks, most of the positive returns came from so called "defensive" stocks. Utilities, Health Care and Consumer Staples stocks tend to have steady results through good and bad economic periods and investors have historically favored these stocks when they have concerns about slowing economic growth.

Exhibit 1
January 1, 2005 – August 31, 2005 Total Returns
(Price Change plus Dividends)

Stock Index	**Total Return**
Standard & Poor's 500	+1.6%
Standard & Poor's Midcap 400	+6.8%
Standard & Poor's Smallcap 600	+4.5%
Dow Jones Industrials	-1.0%
NASDAQ Composite	-1.5%
Russell 1000 Growth	+1.2%
Russell 1000 Value	+3.5%
Standard & Poor's Sector	
Consumer Discretion	-4.2%
Consumer Staples	+1.8%
Energy	+27.9%
Financials	-2.0%
Health Care	+3.8%
Industrials	-3.5%
Information Technology	-1.2%
Materials	-6.4%
Telecommunications	-3.8%
Utilities	+16.3%

Source: Baseline

Despite very strong earnings reports from many companies during the first and second quarters, investors appeared to be increasingly uncertain about the rate of growth in future economic activity and corporate profits. Part of this uncertainty was most likely due to the continual racheting up of short-term interest rates by the Federal Reserve from only 1% in mid-2004 to 3.5% currently. At some point, these higher rates could adversely impact consumer borrowing rates and lead to weaker auto sales, housing starts and home price appreciation, all of which have been important contributors to recent economic growth. However, on the positive side, longer-term interest rates (10 years and longer) have declined since mid-2004, due to modest inflation trends and strong investor demand.

Investors have also been concerned about rising energy prices and the impact that these could have on consumer discretionary income and corporate profit margins. It is no coincidence that the stock prices are weak on most days when energy prices are strong. We also believe that investors are impacted psychologically by the apparent intractability of the insurgency in Iraq and terrorism around the world. Finally, we believe that some investors have shifted money from the stock market to real estate due to the strong (but probably unsustainable) returns in real estate during the past five years.

Strong Second Quarter Earnings

Earnings per share of the Standard & Poor’s 500 companies increased a strong 13% in the second quarter of 2005 compared to the prior year’s quarter. This rate of increase was only slightly less than the 14% increase in the first quarter and was over 2 percentage points higher than recent estimates. Energy companies led the way with a 41% average increase in the second quarter with companies in the Industrials, Materials and Telecommunications sectors contributing average increases of over 20%. The robust increase in the earnings of Energy companies was no surprise given the strong increases in oil and gas prices during the quarter. The Materials companies benefited from both higher volumes and higher commodity prices compared to a year ago. Industrials were also beneficiaries of higher demand and firmer pricing. Telecommunications showed a recovery from very depressed results last year. The weakest sector was Consumer Discretion, which reported an earnings per share decline of 4% in the quarter. Other sectors that reported weaker than average earnings gains included Financials, Utilities and Consumer Staples. Consumer stocks were pulled down by weak results at some of the retailers as high energy prices and abnormally hot weather in much of the country discouraged shoppers. However, home builders and other housing related stocks reported strong earnings gains. The Financial stocks were adversely affected by rising short-term rates, which flattened the yield curve and put pressure on companies that borrow short and lend long. A summary of second quarter earnings is provided in Exhibit 2.

Exhibit 2
Comparison of Second Quarter Earnings of Standard & Poor's 500 Sectors

Sector	Percent Change 2005 vs. 2004 2Q
Consumer Discretion	-4%
Consumer Staples	+8%
Energy	+41%
Financials	+2%
Health Care	+10%
Industrials	+21%
Information Technology	+18%
Materials	+21%
Telecommunications	+28%
Utilities	+6%
S&P 500 Average	+13%

Source: Baseline

Earnings from most of the companies in the portfolios of Bridges' clients had similarly strong results in the second quarter. In addition to the Energy companies, especially strong second quarter earnings gains were reported by Best Buy, Amgen, EBay, Symantec, Target, O'Reilly Automotive, UnitedHealth Group, Zimmer Holdings, Capital One, Allergen, Fiserv and Intel. A summary of the earnings of selected companies is presented in Exhibit 3.

Earnings Outlook

Analysts are forecasting growth in corporate earnings to decelerate in the second half of 2005 and throughout 2006. Earnings per share for the Standard & Poor's 500 Average are estimated to increase 15% in the third quarter year-over-year and then slow to a 6% rate of increase in the fourth quarter and have similar single-digit increases throughout 2006. Most of the earnings deceleration is expected to occur from companies in the Energy, Materials and Industrials sectors due to lower expected increases in energy and commodity prices and lower economic growth. However, analysts expect earnings growth to accelerate in the Consumer Discretion, Consumer Staples, Health Care and Information Technology sectors. Consensus earnings estimates are presented in Exhibit 4.

Exhibit 3
Second Quarter Earnings per Share of Selected Companies

COMPANY NAME	2Q2005 Actual EPS	2Q2005 Estimated EPS	2Q2004 Actual EPS	% CHG 05 vs. 04
ABBOTT LABORATORIES	0.58	0.57	0.54	7%
ALCOA	0.46	0.46	0.46	0%
ALLERGAN	0.78	0.74	0.64	22%
ALTRIA GROUP	1.40	1.34	1.20	17%
AMER INT'L GROUP	1.27	1.20	1.14	11%
AMGEN	0.88	0.72	0.62	42%
ANADARKO PETROLEUM	2.12	2.04	1.59	33%
APACHE	1.76	1.74	1.21	45%
BANK OF AMERICA	1.08	1.01	0.95	14%
BEST BUY	.51	0.30	0.34	50%
CAPITAL ONE FIN'L	2.03	1.75	1.65	23%
CARNIVAL	0.49	0.45	0.41	20%
CHESAPEAKE ENERGY	0.50	0.45	0.33	52%
CHEVRON	1.76	1.67	1.53	15%
CISCO SYSTEMS	0.25	0.25	0.21	19%
CITIGROUP	0.91	1.02	1.02	-11%
CONAGRA FOODS	0.26	0.26	0.41	-37%
DOMINION RESOURCES	0.99	0.81	0.81	22%
EBAY	0.21	0.18	0.15	40%
FAIR ISAAC	0.53	0.44	0.45	18%
FIRST DATA	0.56	0.57	0.53	6%
FISERV	0.59	0.54	0.48	23%
FPL GROUP	0.66	0.69	0.70	-6%
GANNETT	1.37	1.37	1.30	5%
GENERAL ELECTRIC	0.44	0.44	0.38	16%
HARRAH'S ENTMT	0.90	0.93	0.79	14%
HOME DEPOT	0.83	0.79	0.70	19%
INTEL	0.33	0.32	0.27	22%
JOHNSON & JOHNSON	0.93	0.91	0.82	13%
LOWE'S COMPANIES	1.05	1.02	0.89	18%
MCGRAW-HILL	0.51	0.47	0.43	19%
MICROSOFT	0.32	0.31	0.28	14%
OMNICARE	0.60	0.60	0.58	3%
OMNICOM GROUP	1.24	1.24	1.10	13%
O'REILLY AUTOMOTIVE	0.39	0.36	0.30	30%
PEPSICO	0.70	0.67	0.61	15%
PFIZER	0.46	0.44	0.47	-2%
PROCTER & GAMBLE	0.56	0.55	0.50	12%
QUALCOMM	0.33	0.25	0.29	14%
STATE STREET	0.66	0.68	0.68	-3%
STRYKER	0.45	0.44	0.37	22%
SYMANTEC	0.27	0.25	0.18	50%
SYSCO	0.44	0.44	0.43	2%
TARGET	0.61	0.58	0.44	39%
TEVA PHARM ADR	0.36	0.36	0.35	3%
TOYOTA MOTOR ADR	1.47	1.66	1.58	-7%
TYCO INT'L	0.50	0.49	0.45	11%
U.S. BANCORP	0.60	0.59	0.54	11%
UNITED TECHNOLOGIES	0.86	0.85	0.83	4%
UNITEDHEALTH GROUP	0.61	0.60	0.47	30%
WAL-MART STORES	0.67	0.65	0.62	8%
WELLPOINT	1.00	0.97	0.83	20%
WELLS FARGO	1.12	1.13	1.00	12%
WEST	0.53	0.47	0.39	36%
ZIMMER HLDGS	0.80	0.75	0.58	38%
AVERAGE				17%

Source: Baseline

Exhibit 4

Percentage Change in Estimated Earnings per Share

Sector	3Q05 vs. 3Q2004	2005 vs. 2004	2006 vs. 2005
Consumer Discretion	+3%	0%	+22%
Consumer Staples	+6%	+7%	+9%
Energy	+43%	+31%	+4%
Financials	+18%	+10%	+8%
Health Care	+5%	+8%	+10%
Industrials	+22%	+21%	+14%
Information Technology	+13%	+12%	+16%
Materials	+8%	+23%	+6%
Telecommunications	+15%	+19%	+4%
Utilities	+13%	+13%	+10%
S&P 500 Average	+15%	+10%	+6%

Source: Baseline

Stock Valuations

One positive outcome of this year's near zero returns has been the improvement in the valuations of stocks. The better-than-expected first half earnings of many companies have caused analysts to increase their estimates of 2005 and 2006 earnings, which when coupled with flat stock prices, have resulted in lower price/earnings ratios. Comparisons of price/earnings ratios and growth rates for the companies in the Standard & Poor' sectors are presented in Exhibit 5.

As you can see, the current average price/earnings ratios based on 2005 and 2006 earnings estimates are near or below the average low price/earnings ratio of the past five years in every sector except Utilities. The Standard & Poor's 500 Average is currently selling in line with its long-term average of about 16 times earnings, which suggests that it currently is priced at an average value. However, there has historically been an inverse correlation between price/earnings ratios and interest rates (i.e., price/earnings ratios have tended to be higher when interest rates were lower and vice versa). As a result, we believe that stocks are currently under-valued compared to cash and fixed-income alternatives.

Exhibit 5

Comparison of Sector Price/Earnings Ratios
And Estimated Earnings Growth Rates

S&P Sector	Price/ '05 EPS	Price/ '06 EPS	Price/Earnings 5 Year Average High – Low	Estimated Earnings Growth
Consumer Discretion	20.3	16.7	27.3-17.7	14%
Consumer Staples	18.3	16.8	23.8-18.2	11%
Energy	11.7	11.3	20.4-13.1	10%
Financials	11.8	10.9	17.1-10.9	11%
Health Care	18.3	16.7	27.7-20.4	12%
Industrials	17.1	15.1	25.6-18.5	12%
Information Tech	22.1	19.1	52.6-26.9	15%
Materials	13.9	13.1	30.1-17.5	10%
Telecommunications	15.4	14.8	24.9-15.5	7%
Utilities	16.8	15.2	16.6-11.5	5%
S&P 500 Average	16.4	15.5	23.6-17.8	6%

Source: Baseline

Investment Strategy

We continue to be constructive on the outlook for stock prices over the next several years, and we believe they offer better value than fixed-income alternatives at current prices. We acknowledge that there is a risk that rising short-term interest rates could adversely impact consumer spending and housing starts. However, we think that there is a high probability that the Federal Reserve will be successful in slowing the economy without triggering a recession. While it is true that the Fed has often overstayed its tightening policy in the past, causing a recession in the process, we believe they are less likely to do so in the current low inflation environment. In most other economic expansions since 1975, the Fed has faced accelerating inflation, which required them to aggressively tighten credit in large interest rate increments. However, outside of energy prices, inflation has been largely absent during this recovery, and this has enabled the Fed to gradually slow economic growth through modest quarter point increases in the Federal Funds rate over the past year. In addition, in most prior economic recoveries, long-term interest rates have followed short-term rates higher, eventually resulting in a choking point for most borrowers. However, long-term interest rates have not increased in this recovery, which should enable many borrowers to find other financing alternatives.

We also acknowledge that there is probably a housing bubble in certain parts of the country. However, in our opinion, a bubble in housing does not carry the same economic risks as a bubble in the financial markets because most houses are primary residences, and their prices are not quoted in an auction market every business day. If the perceived market value of one's house declines, they are not happy about it, but it doesn't cause most consumers to sell in a panic at a distressed price out of fear that prices might go lower. If a seller doesn't get a buyer at his or her asking price, the seller (if he can) often takes the house off the market and waits to sell another day. Thus, housing bubbles tend to burst via a levelling off of home prices rather than through a dramatic rapid decline such as we saw in stock prices in 2000. The recent bursting of housing bubbles in Australia and the UK are good examples of this experience. Nonetheless, even a levelling of home prices will remove a significant stimulus from the economy through a slower build-up of home equity that can be tapped for cash-out financing and slower growth in perceived individual net worth. Some economists have estimated this impact at a potential 0.5% -1.0% reduction in annual real GDP growth.

Rising energy prices could also reduce consumer spending, particularly among lower income consumers. Over the next several years we believe that many consumers will adapt to higher gasoline prices by trading in their large gas guzzling SUV's and buying more fuel efficient vehicles. Despite the large increase in the price of gasoline in the past year, current gasoline prices in the U.S. are still only half the price of gasoline in most European countries. An analysis of past spikes in energy prices by a Merrill Lynch strategist indicated that recessions occurred each time oil prices rose more than 150% over a two-year period. A 150% increase over the current two-year low price would equal $75/barrel, compared to the current price of $67/barrel.

We believe that most of these uncertainties are already largely discounted in the current prices of stocks. However, we have been reviewing our clients' portfolios to make sure they are invested appropriately for the best opportunities that we see over the next several years. We believe energy prices will trend higher on an irregular path for the foreseeable future due to strong demand from developing countries and the industry's limited ability to increase supply. As a result, we recommend a strong weighting in energy stocks in most client portfolios. Where portfolios are under-weighted we plan to add to the energy holdings during any temporary price corrections in the energy stocks. Companies that we favor in this sector include Apache Corp. (APA, $XX), Anadarko Petroleum (APC, $90), ChevronTexaco (CVX, $61), ConocoPhilips (COP, $65) and Chesapeake Energy (CHK, $31).

We also recommend a heavy weighting in Health Care stocks, which should benefit from growth in the number of senior citizens in most industrial countries and new markets in developing countries. While some of the pharmaceutical companies have been adversely affected by maturing new drug pipelines, drug recalls and litigation, there are many opportunities in medical equipment, medical supplies and health benefit services. Companies that we favor in this sector include Johnson & Johnson (JNJ, $63), Omnicare (OCR, $52), Wellpoint (WLP, $74), UnitedHealth Group (UNH, $51), Amgen (AMGN, $79), Medtronic (MDT, $57), Stryker Corp. (SYK, $54) and Zimmer Holdings (ZMH, $82).

Another Sector that we have emphasized has been Consumer Discretion stocks because of the high growth rates many of these stocks have had and we believe will continue to have in the future. While this sector could face some temporary headwinds if consumer spending slows, we have tried to mitigate this by investing in niche companies that are leaders in their market segment. Companies the we favor in this sector include, Home Depot (HD, $40), Lowes (LOW, $64), and Toyota Motor (TM, $81).

Finally, we are recommending a heavy weighting in Financial stocks, which have very cheap valuations, reasonable growth prospects, competitive dividend yields, consolidation opportunities and some insulation from international competition. Many of these stocks have lagged the market in the past year due to the flattening of the yield curve. However, we believe that this temporary negative is well reflected in the stock prices, and the Federal Reserve is probably closer to the end of this round of rate increases than the beginning. Our favored stocks in this sector include Capital One (COF, $82), American International Group (AIG, $59), Bank of America (BAC, $43), Citigroup (C, $43), U.S. Bancorp (USB, $29) and Wells Fargo (WFC, $59).

We have been underweighted in Industrials, Materials and Information Technology stocks due to our expectations of slower economic growth and decelerating earnings growth. Some of these companies are also challenged with volatile commodity prices, rapidly changing technology and foreign competition. However, we may increase our investments in select Information Technology stocks due to their attractive long-term growth rates and relatively attractive current stock valuations. We have also been underweighted in Consumer Staples, Telecommunications and Utilities stocks due to their sub-par expected future earnings growth and, in many cases, high stock valuations.

Of course, not all clients have the same investment objectives, and these general recommendations have to be modified to each client's specific situation. For example, if a client requires a high level of current income from his or her portfolio, we may increase the weighting in Utilities and Consumer Staples stocks in order to increase the dividend yield on the portfolio. If you have any questions regarding the investment strategy in your account, we invite you to contact your portfolio manager.

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