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TRANSITIONING TO A SUSTAINABLE GROWTH RATE

Executive Summary

First Quarter Results – The majority of publicly traded common stocks experienced single-digit negative returns in the First Quarter of 2005, due to rising energy prices and interest rates. The S&P 500 Composite Index had a -2.15% total return. Energy stocks fared the best with an 18% return, while telecommunications stocks performed the worst with a -8% return for the Quarter.

Corporate Earnings Growth is Slowing – While corporate earnings are expected to increase in 2005, the rate of earnings growth compared to results in 2004 is expected to decelerate. First Quarter 2005 S&P 500 earnings are estimated to increase only 9% over the prior year's First Quarter record compared to a 20% rate of increase for the Fourth Quarter of 2004. Earnings for the full 2005 year are estimated to rise only 4% over 2004 levels.

Economic Update – Recently reported economic statistics are indicating that economic growth is decelerating from 2004's rapid rate, and inflation is picking up from the historical low rates of the past few years. However, GDP growth should be strong enough to support employment advances and some increases in corporate earnings. We believe energy prices will remain stubbornly high, and interest rates may rise further above present levels, but we do not expect these expanded costs to derail the economy.

Bridges Fixed Income Strategy – Recently, the 10-year yield broke through the upside of its three-year long 3.5%-4.5% trading range, pushing from 4.0% on February 9 to 4.6% on March 19. Bonds, in our view, will become modestly attractive as real rates increase to 2% (if inflation stays around 3% that would occur as the 10-year yield rises to 5%, a likely event in 2005, in our view). Our strategy will be to gradually extend bond portfolio maturities to realize higher available nominal and real yields if and as interest rates move from current levels toward our intermediate 10-year yield objective of 5.0%.

Bridges Equity Strategy -- We continue to believe that equities are more likely to outperform fixed income investments over the next several years. We believe investors will favor larger capitalization and higher quality stocks that can consistently grow earnings. Many of the best values for purchase and holding are companies in the health care, financial services and industrial sectors.

First Quarter Results

The stock market started out 2005 with negative returns in the First Quarter as increases in oil prices and interest rates took their toll on investor confidence. There was only modest variance in the returns from either investing style (growth or value) or market capitalization (large, mid or small). Total returns for selected market indices in the three month and 12 month periods ended March 31, 2005 are presented in Exhibit 1.

Exhibit 1

Index	Total Returns for Periods Ended March 31, 2005 3 Months	 12 Months
Standard & Poors 500	-2.15%	6.69%
Dow Jones Industrials	-2.06%	3.80%
NASDAQ Composite	-8.10%	0.25%
Russell 1000 Growth	-4.09%	1.16%
Russell 1000 Value	0.09%	13.17%
S&P MidCap 400	-0.40%	10.41%
S&P SmallCap 600	-2.07%	13.06%

Source: Bloomberg

However, there was considerable variance in returns among economic sectors in the First Quarter, which are presented in Exhibit 2.

Exhibit 2

S&P Economic Sector	Total Returns for Periods ended March 31, 2005 3 Months	 12 Months
Consumer Discretion	-5.2%	6.5%
Consumer Staples	0.8%	3.9%
Energy	17.8%	46.9%
Financials	-6.4%	-1.1%
Health Care	-0.6%	2.1%
Industrials	-1.6%	17.5%
Information Technology	-7.3%	-2.8%
Materials	1.8%	17.0%
Telecommunications	-7.7%	4.6%
Utilities	5.4%	22.8%
S&P 500	-2.2%	6.7%

Source: Thomson Baseline

As you can see, four of the 10 economic sectors had positive returns during the First Quarter of 2005 led by Energy, which had a strong 17.8% total return. Energy stocks benefited from the surge in oil prices to a new all-time high near $57 per barrel. During the First Quarter, oil prices increased 27%, wholesale unleaded gasoline increased 41% and natural gas increased 16%. As a result, research analysts increased their energy price assumptions and energy company earnings estimates for the remainder of 2005. The Materials sector also benefited from stronger than expected commodity prices. Chemical and lumber prices rose, and Aluminium reached a nine-year high price of $0.92 per pound. The CRB Index of commodity prices increased 10% during the First Quarter.

The other two sectors showing positive returns for the quarter were Consumer Staples and Utilities, both of which contain defensive stocks. These are companies that have historically had consistent earnings regardless of economic conditions. Rising energy prices, higher interest rates and decelerating earnings growth may have convinced some investors to emphasize such defensive stocks and to take profits in the stocks that are more sensitive to slowing economic growth. This also could explain the weakness in all of the other sectors. The weakest sectors were Telecommunications and Information Technology. The companies in these sectors are dominant in the NASDAQ Composite, which largely explains the weak relative performance of that index.

Corporate Earnings Growth is Slowing

While corporate earnings are expected to increase in 2005, the rate of earnings growth is expected to decelerate as presented in Exhibit 3.

Exhibit 3

	Percent Change in Earnings Per Share			
S&P Economic Sector	4th Quarter 2004	1st Quarter 2005E	Year 2004	Year 2005E
Consumer Discretion	9%	-13%	30%	6%
Consumer Staples	8%	3%	10%	9%
Energy	92%	39%	52%	10%
Financials	9%	1%	12%	10%
Health Care	10%	5%	12%	7%
Industrials	16%	13%	20%	17%
Information Technology	21%	11%	50%	15%
Materials	80%	50%	84%	25%
Telecommunications	-4%	0%	-7%	3%
Utilities	12%	4%	1%	10%
S&P 500	20%	9%	21%	4%

Source: Thomson Baseline

Deceleration in the rate of gain for earnings per share is typical for this stage of the economic cycle. In the initial stage of the cycle, the economy has excess production capacity and deferred demand, which enables businesses to rapidly increase sales and improve profit margins. As deferred demand is satisfied and capacity utilization reaches higher levels, sales growth slows to a more normal long-term average rate and profit margins reach their maximum levels. In the early stage, after recently witnessing a recession, research analysts tend to be conservative and underestimate earnings growth. As actual earnings exceed the analysts' estimates, investors tend to bid stock prices higher. However, as the economic expansion off the initial recovery becomes more mature, research analysts tend to overestimate earnings growth. If actual earnings fail to meet analysts' estimates, investors tend to temporarily temper their enthusiasm for stocks until earnings estimates are revised to meet the new expectations. The First Quarter 2005 earnings reports should be a good test of whether analysts are currently too optimistic regarding their earnings estimates.

Economic Update

Recently reported economic statistics are indicating that economic growth is decelerating from 2004's rapid rate, and inflation is picking up from the historical low rates of the past few years. Orders for durable goods increased 0.3% in February from the prior month and were up 10% over the prior year. However, excluding the volatile transportation sector, durable goods orders declined 0.2% in February over the prior month. The Leading Economic Indicators increased 0.1% in February, but this statistic has been close to zero for the past several months, suggesting slower growth for the first half of 2005. Housing has remained strong with new home sales up 9.4% in February. However, auto sales were down 0.4% in the first quarter. The employment statistics are also suggesting slowing economic growth. The initial claims for unemployment insurance rose during March and reached the highest level since January of 2005. The March unemployment report showed a decline in the unemployment rate to 5.2% from 5.4%, but only 110,000 new jobs were created compared to 243,000 in February. This was the lowest number of new jobs created in the last eight months. The Conference Board's Consumer Confidence Index also declined in March to 102.4 from 104.4 in February. It appears that rising energy prices, slowing job growth and a weak stock market may be weighing on the consumers' outlook. However, while growth in real Gross Domestic Product (GDP) is expected to slow from 2004's rapid rate of 4.4%, most economists still expect GDP growth of 3.0%-3.5% in 2005, which is near the average growth rate for the past 25 years.

Inflation appears to be inching higher, primarily due to higher energy and commodity prices. In February, the Consumer Price Index increased 0.4% and was up 0.3%, excluding food and energy items. The February Consumer Price Index was up 3.0% year-over-year and up 2.4%, excluding food and energy. The Producer Index was also up 0.4% in February, but showed a more modest 0.1% increase if food and energy were excluded. However, economists were quick to point out that if autos were also excluded, producer prices increased 0.4% for the month and were up 2.8% year-over-year. An inflation rate of 2.5%-3.0% is not yet alarming by historical standards, but it represents a noticeable increase over the 1.0%-2.0% rates enjoyed in the U.S. over the past several years. This increase in inflation was noted in the Federal Reserve Board's rate adjustment announcement on March 22 when it reported, "While long-term inflation expectations remain well contained, pressures on inflation have picked up in recent months, and pricing power is more evident."

The value of the U.S. dollar strengthened modestly during the most recent quarter despite continuing record trade and federal budget deficits. The dollar appreciated 6% against the Euro and 4% against the Yen during the First Quarter. Economists said the rise in interest rates and the anticipation of possible budget deficit reducing legislation probably accounted for the dollar's recent strength.

While the rate of economic growth appears to be slowing, we still expect it to be strong enough to support some normal employment advances and increases in corporate earnings. Higher energy prices could adversely affect consumer spending, but thus far the consumer has been amazingly resilient to higher energy prices. A significant increase in interest rates could also reduce economic strength through declines in housing starts and sales of big ticket consumer products such as automobiles. However, as discussed below in the next section, we do not expect interest rates to increase significantly to unusually high levels during 2005.

Bridges Fixed-Income Strategy

The Firm has taken a cautious approach to bonds since the first half of 2002, when the yield on the 10-year U.S. Treasury Note (the yield that we use as a benchmark for valuing the attractiveness of both bonds and stocks) hit a record low of 3.11% on June 13, 2003, a precipitous drop from the interim 10-year yield high on 6.51% in May of 2002 and the longer term high yield of 8% reached in late 1994.

Since interest rates bottomed in mid-2002, real bond yields, the difference between the nominal yield and the current rate of inflation, have been unattractive relative to historic levels. We would like to acquire real bond yields of at least 2%. Since mid-2003, the 10-year yield has bounced between 4.0-4.5%, while inflation has increased from around 1% to 3%, causing real rates to fall to around 1%, in our view a relatively unattractive bond valuation level. Real bond yields have historically ranged between 1.0-4.0%, with most valuations centering on 2.0-3.0%.

Recently, the 10-year yield broke through the upside of its three-year long 3.5%-4.5% trading range, pushing from 4.0% on February 9 to 4.6% on March 19, marking the first time the yield on the 10-year had been above 4.5% since 2002, except for a short period in May of 2004.

The recent increase in interest rates is being driven by increasing inflation concerns stemming largely from the material rise in energy prices over the past 18 months, as well as continuing economic strength and a concomitant rise in demand for credit.

While inflation has risen from 1% to 3% since 2002, real interest rates have expanded from 1% to 1.5% as nominal rates have increased, in a sense moving bonds from very unattractive valuations to modestly unattractive valuation territory. Bonds, in our view, will become modestly attractive as real rates increase to 2% (if inflation stays around 3% that would occur as the 10-year yield rises to 5%, a likely event in 2005 in our view).

As noted in our comments regarding the economic outlook, we expect the economy to slow in 2005 but remain solid, while inflation continues to expand at a moderate pace that is somewhat restrained by intense competition.

Given our macro-economic expectations and current bond market valuations, we expect to become increasingly more comfortable with bond purchases over the course of 2005 and as nominal, and more importantly, real yields rise. If our outlook in fact materializes, we expect to increase the average lives of bond portfolios to capture higher available yields for longer periods of time. At present, most of the Firm's bond portfolios are at the short end of their typical average life ranges (postured relatively defensively), given that we have been in a low interest rate environment for several years and our expectation that rates will eventually move back to somewhat higher levels than prevail at present.

The average yield for the 10-year over the past decade is 5.5%; we believe it is reasonable to assume that rates will approach that level during the current cycle. Our strategy will be to gradually extend bond portfolio maturities to realize higher available nominal and real yields if and as interest rates move from current levels toward our intermediate 10-year yield objective of 5.0%.

Bridges Equity Strategy

We continue to believe that equities are more likely to outperform fixed-income investments over the next several years. Based on historical comparisons and dividend discount models, we believe equities currently are modestly undervalued relative to interest rates. While we expect interest rates to rise, we do not expect the increase to be significant enough to materially dampen economic growth or equity valuations. We expect equity prices to resume a positive trend, rising commensurately with increases in earnings over the next several years. Due to the slowing rate of economic growth and a compression of price/earnings ratios on high quality companies compared to low quality companies, we believe investors will favor larger capitalization and higher quality stocks that can consistently grow earnings. Many of the best values are companies in the health care, financial services and industrial sectors.

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