August 18, 2004

**STOCK PRICE CORRECTIONS ARE UNDERWAY
AFTER A LONG ADVANCE**

Executive Summary

Second Quarter Earnings Surpass Expectations – Over 70% of companies in the Standard & Poor's 500 average exceeded analysts' earnings estimates for the June quarter, with an average increase over the 2003 quarter of 25%. Earnings growth is expected to decelerate as the economic cycle matures to a 15% annual rate in the September quarter and to 7% in 2005.

The Economy Slows – Real GDP grew at an estimated 3.0% annual rate in the second quarter, which was well below economists' forecasts and the first quarter's 4.5% annual rate. Consumer spending slowed significantly during the summer due to high gasoline prices, cool weather, sluggish growth in wages and the absence of mortgage refinancings and tax cuts. The jury is still out on whether this weakness was an aberration or if it will continue in the second half. Energy prices may be the wild card. Overall, our Firm holds a constructive view of the future prospects for the U.S. economy.

An Opportunity in Healthcare – Many healthcare companies have under-performed the stock market in recent quarters due to concerns about potential political/regulatory constraints, maturing patents on several blockbuster drugs, potential legal liabilities, and alleged accounting irregularities. However, we think the concerns over political constraints and decelerating growth have been amply discounted in the stock prices and offer an opportunity for long-term investors. Our top choices are Amgen (AMGN, $54); Stryker (SYK, $44); Zimmer (ZMH, $70); and Pfizer (PFE, $31).

Waiting for Resolution - The uncertainties about terrorism, Iraq, the November elections, rising interest rates, and a decelerating economy have put a cap on the trading range of most stocks. Our valuation studies continue to tell us that at current prices, stocks represent a better investment for the next several years than bonds. We believe the stock market could decline another 5%-10% between now and the November elections. However, we believe the U.S. and most foreign economies are on an expansion pathway and should provide a base for positive earnings and equity returns over the next several years.

Second Quarter Earnings Surpass Expectations

Most corporations reported strong increases in earnings for the quarter ended June 30, 2004, and over 70% exceeded analysts' estimates. Based on earnings reported through August 10, operating earnings per share of the companies in the Standard & Poor's 500 Index (S&P) increased an average 25% over the same quarter last year. The largest earnings increases came from companies in the materials, information technology, and energy sectors as shown in Exhibit 1.

Exhibit 1
Earnings Per Share for the Quarter Ended June 30, 2004
Standard & Poor's 500 Average

Sector	Percent Change from Quarter Ended June 30, 2003
Consumer Discretion	41%
Consumer Staples	10%
Energy	59%
Financials	13%
Health Care	17%
Industrials	25%
Information Technology	61%
Materials	79%
Telecommunications	-14%
Utilities	5%
Standard & Poor's 500	25%

Source: Baseline

The earnings from the companies that Bridges Investment Counsel, Inc. follows reported similar gains. Of the companies that had reported June quarter earnings through August 4, 77% had met or exceeded estimates. A sample of these results is presented in Exhibit 2.

Exhibit 2
Earnings Per Share of Selected Companies
Followed by Bridges Investment Counsel, Inc.

Company Name	Q2 2004 Actual EPS	EPS Est.	Q2 EPS 2003	% Chg. 04 Vs 03
Alcoa	0.46	0.47	0.27	70%
Altria	1.20	1.27	1.26	-5%
Amgen	0.62	0.59	0.49	27%
Anadarko Petroleum	1.59	1.59	1.23	29%
Apache	1.21	1.08	0.88	38%
Bank of America	1.90	1.74	1.80	6%
Best Buy	0.34	0.33	0.21	62%
Capital One Financial	1.65	1.50	1.23	34%
Citigroup	1.02	0.97	0.83	23%
Colgate Palmolive	0.66	0.67	0.62	6%
Exxon Mobil	0.88	0.82	0.62	42%
Fair Isaac	0.45	0.34	0.40	13%
First Data	0.53	0.53	0.46	15%
Fiserv	0.48	0.47	0.40	20%
General Electric	0.38	0.37	0.38	0%
Johnson & Johnson	0.82	0.79	0.70	17%
Microsoft	0.28	0.29	0.23	22%
PepsiCo	0.61	0.61	0.54	13%
Pfizer	0.47	0.47	0.30	57%
Procter & Gamble	0.50	0.49	0.44	14%
Qualcomm	0.58	0.53	0.33	76%
State Street	0.68	0.68	0.52	31%
Stryker	0.37	0.34	0.27	37%
Tyco Intl.	0.45	0.41	0.32	41%
U.S. Bancorp	0.54	0.53	0.47	15%
Wells Fargo	1.00	1.04	0.90	11%
Zimmer	0.58	0.58	0.45	29%

Source: Baseline

Company managements and Wall Street research analysts are expecting earnings growth rates in future quarters to materially decelerate starting with the calendar third quarter results. The average earnings per share estimate on the Standard & Poor's 500 Index for the third quarter represents a 15% increase over the same quarter in 2003, down from the 25% average earnings increase in the second quarter. This change is due to tougher comparisons with the strong results in the second half of 2003 and due to expectations for slower growth in the Gross Domestic Product (GDP) toward normal progress for this phase of the economic expansion. Typical earnings growth is expected to slow further in 2005 with an average estimated increase of 7% compared to the expected earnings growth of 17% in 2004. This pattern is usual for most economic cycles. Early in the economic recovery, companies are operating below normal capacity and can realize rapid earnings growth as revenues begin to improve. As companies operate closer to full capacity and profit margins reach their peaks, earnings growth must necessarily slow to growth rates more similar to that of revenues.

The Economy Slows

The Department of Commerce recently reported that real GDP increased at an estimated 3.0% annual rate in the second quarter, which was significantly lower than the first quarter rate of 4.5%. This drop surprised many economists who were forecasting growth of 3.5% to 4.0% for the quarter. The biggest drag during the quarter was consumer spending, which increased at only a 1.0% annual rate, compared to a 4.1% rate in the first quarter. However, real residential fixed investment (home purchases) increased at a 15.4% annual rate compared to 5.0% in the first quarter. Business spending also was strong, with investment in equipment and software increasing at a 10.0% annual rate (versus 8.0% in the first quarter) and investment in structures increasing at a 5.2% annual rate (versus -7.6%).

The most recent monthly economic reports also indicated weaker consumer spending. Retail sales declined 1.1% in June, which was the steepest monthly decline in 16 months. The June pullback was led by a sharp 4.3% decline in sales at auto dealerships. Excluding automobiles, retail sales fell only 0.2%. Retailers said that cooler-than-normal weather in much of the country and high gasoline prices adversely impacted sales. Economists also noted that retail sales grew at an 11.9% annual rate in the first quarter, the highest rate of growth in 20 years! This rate of advance was not sustainable, and thus, some slowdown was inevitable. However, there is evidence that middle and lower income families are struggling to make ends meet. Inflation-adjusted earnings for production and non-supervisory workers declined 0.8% in June and are down 1.4% compared to June of 2003. The index of leading indicators declined for the first time in over a year, falling 0.2% in June. The number of people employed increased at a meager pace of 78,000 in June and 32,000 in July compared to expectations of over 200,000 each month. However, there were some bright spots on the outlook for consumer spending. The number of persons filing initial claims for unemployment insurance continued to decline, and the unemployment rate actually improved slightly in July to 5.5% from 5.6%. Indications are that retail sales rebounded modestly in July, and auto sales were higher due to new incentives offered by the auto companies. In addition, the Conference Board's consumer confidence index increased for the fourth straight month in July, reaching its highest level in two years.

Economists are divided on their opinions regarding consumer spending in the second half of 2004. The pessimists are concerned that high energy prices, sluggish wage growth, the absence of mortgage refinancings, and the lack of new tax cuts could pinch consumers' pocketbooks. The optimists hope that rising consumer confidence and expanding employment will enable the consumer to continue to spend. The wild card in the forecast is the trend for energy prices. If energy prices remain high or increase further, the price penalty will probably adversely affect consumer spending for middle and lower income families. However, on an inflation-adjusted basis, oil and gas prices are still well below the peak price of over $70 per barrel (in 2004 dollars) reached in 1981. In addition, gasoline prices in the U.S. are still well below the prices paid in most other areas of the world. The average price of gasoline in Europe is near $5 per gallon.

In the second quarter of 2004, spending by businesses picked up the slack from slower consumer spending. While there was some concern that industrial production declined 0.3% in June after strong increases of 0.9% in May and 0.8% in April, most economists blamed a sharp, weather-related drop in output by utilities and a decline in auto production for the June decline. Some economists said a slowdown in industrial production was to be expected after such strong gains during the first five months of the year. Industrial production was still up a strong 5.6% versus June 2003. Economists were encouraged that new orders for durable goods increased 0.7% in June after revised declines of 0.9% in May and 2.7% in April. Excluding the volatile aircraft and defense categories, durable goods orders increased 1.2% in June. The Institute for Supply Management's July manufacturing index rose to 62.0 from 61.1 in June with 18 out of 20 industries reporting growth. The Institute noted that its manufacturing index has been above 60 for nine consecutive months, the longest stretch since the period between July 1972 and June 1973. On average, manufacturers reported higher levels of new orders and production in July. Economists expect that tax incentives for business investment that expire at year-end will give capital spending a boost during the second half of the year.

Economists also cheered the latest reports on inflation. Consumer prices increased 0.3% in June compared to 0.6% in May. The core index, which excludes food and energy prices, increased only 0.1%, the smallest monthly increase this year. Compared to June of 2003, consumer prices were up 3.2%, and the core index was up 1.9%. Producer prices declined 0.3% in June, its first decline in seven months. Excluding energy and food prices, the producer index increased 0.2% in June.

An Opportunity in Healthcare

The last few quarters have been very difficult for a number of healthcare companies. Despite the tail wind of an aging population, investors have been cautious on some of theses stocks due to concerns about potential political/regulatory constraints (John Kerry is perceived as less supportive of healthcare companies), maturing patents on several blockbuster drugs, potential legal liabilities, and alleged accounting irregularities. It all started in October 2002 when hospital operator, Tenet Healthcare (THC, $10) was accused by Medicare and private managed care providers of overcharging for health insurance claims, causing the stock to drop precipitously from over $50 per share to less than $20. After appreciating over 40% from April through June in 2003, Wyeth (WYE, $35) has since given all of that back due to concerns over its Fen-phen drug litigation. Pfizer (PFE, $31) has declined about 20% from its 52-week high reached in early February due to concerns over a deceleration in revenues and earnings in the next few quarters. More recently, Cardinal Health (CAH, $44) reported that it expects earnings to be modestly weaker than expected in its last fiscal (June) quarter, and it reduced its outlook for fiscal 2005. In addition, Cardinal reported that it is being investigated by the Securities and Exchange Commission (SEC) for possible accounting irregularities. Cardinal's stock is down over 35% since June 30. Surgical implant leaders, Stryker (SYK, $44) and Zimmer (ZMH, $70), have each backed off over 20% from their respective all-time highs due to concerns about the valuation of their stock prices. Biotechnology leader, Amgen (AMGN, $54), has also declined over 20% from its 52-week high.

As a result of these price declines, a number of these stocks now appear to be undervalued, in our opinion. Statistical information on selected healthcare stocks is presented in Exhibit 3. We think the concerns over political constraints and decelerating growth have been amply discounted in the stock prices. These stocks traded down on similar political concerns when Bill Clinton launched his radical healthcare plan in the early 90's. However, President Clinton was unable to convince Congress to approve his plan. We believe Kerry, if he wins, will find a similar skeptical response from Congress. While it is true that the growth rates on some of the healthcare companies are expected to decelerate, they will, for the most part, still represent much faster rates of growth than the average company in the Standard & Poor's 500. In addition, we believe that the healthcare companies' superior relative long-term growth rates will become more attractive to investors as growth rates of most of the companies in the more cyclical sectors reach their peak in 2004. Our top choices are Amgen, Stryker, Zimmer, and Pfizer.

Exhibit 3

Selected Health Care Companies

Company Name	Price Per Sh. 08/06/04	52 Week Hi	52 Week Lo	P/E 2004	P/E 2005	P/E Five Year Hi	P/E Five Year Lo	P/E 2004 Rel to SPX	P/E 2005 Rel to SPX	P/E 5 Yr. to SPX Hi	P/E 5 Yr. to SPX Lo	Erns Chg 04 Vs. 03	Erns % Chg 05 Vs. 04	Erns LT Ftr Gr Rt
Abbott Labs	38.69	44	35	17.0	15.4	32	14	1.0	1.0	1.4	0.6	3	11	12
Amgen	53.80	70	52	22.3	18.9	78	23	1.4	1.2	3.4	1.0	27	18	20
Cardinal Health	44.01	76	42	12.5	11.3	46	12	0.8	0.7	1.8	0.6	11	10	15
Johnson & Johnson	54.60	58	48	18.0	16.5	40	17	1.1	1.1	1.7	0.8	14	9	13
Medtronic	49.01	52	42	30.1	25.9	70	26	1.8	1.7	2.8	1.2	16	16	16
Pfizer	31.18	38	29	14.7	13.2	95	15	0.9	0.9	3.4	0.8	21	12	12
Stryker	44.24	57	36	30.9	25.9	57	28	1.9	1.7	2.5	1.0	28	20	20
Teva Pharm ADR	28.33	34	26	20.5	17.7	64	21	1.3	1.2	2.5	0.8	29	16	21
Wyeth	34.91	48	33	13.1	12.2	42	11	0.8	0.8	1.6	0.5	9	8	10
Zimmer Hldgs	69.79	89	47	30.5	25.1	46	24	1.9	1.6	2.4	1.1	27	21	20
Universe Aver (EQ WT)				21.0	18.2			1.3	1.2			18	14	16
S&P 500	1063.97	1163	974	16.4	15.2	31	16	1.0	1.0	1.0	1.0	17	8	7

Source: Baseline

Waiting for Resolution

After reaching their peaks in the first quarter, the popular stock indices appear to be treading water. The uncertainties about terrorism, Iraq, the November elections, rising interest rates and a decelerating economy have put a cap on the trading range of most stocks. However, we believe that the underlying economic fundamentals are still favorable. Economic growth is expected to continue at a 3%+ annual rate, which is near the long-term historical average. Inflation has increased, but it appears that the core indicators should be contained to a 2%-3% range, provided energy prices can level off. Short-term interest rates are expected to slowly rise in quarter point increments but still remain well below the historical average for the foreseeable future. The rate of growth in corporate earnings is decelerating, but it should stabilize in the mid-to-high single digit range. The price/earnings ratio of the Standard & Poor's 500 Index is 15 times the 2005 earnings estimates, which is in line with the long-term historical average. However, compared to price/earnings ratios in other periods of low interest rates, stocks currently appear to be modestly undervalued. There appear to be few excesses, except possibly the historically high level of consumer debt and the sizable federal budget deficits. In summary, the economy and the financial markets appear to be on solid footing for a period of sustained but modest growth, barring a continuing rise in energy prices.

Investors hate uncertainty, and the current geopolitical environment is full of unresolved problems both domestically and internationally. However, the U.S. political picture will be clearer by no later than November, and we believe eventually investors will see an improving trend in Iraq as Iraqi's take greater control of their country (and the U.S. presence is reduced). Terrorism may take a longer time to resolve, but is it any greater threat than the Cold War was? Two of the best bull markets in recent history, during the 1960's and during the 1980's, occurred while Americans contemplated the threat of a nuclear holocaust.

We continue to believe that high quality, consistent growth companies such as those in the healthcare sector will be preferred by investors as the more cyclical companies such as in the information technology, energy, and materials sectors reach peaks in their growth rates. Presented below in Exhibit 4 are the forecast growth rates in earnings per share for each of the S&P sectors.

Exhibit 4
Earnings per Share Growth Rates
By Standard & Poor's 500 Sector

Sector	2003	2004	2005	2006
Consumer Discretion	2%	28%	14%	15%
Consumer Staples	7%	10%	11%	10%
Energy	63%	28%	-15%	-11%
Financials	18%	14%	10%	12%
Health Care	10%	14%	12%	11%
Industrials	-3%	20%	17%	14%
Information Technology	44%	48%	19%	8%
Materials	17%	75%	22%	2%
Telecommunications	-5%	-13%	0%	14%
Utilities	-8%	2%	8%	6%
Standard & Poor's 500	15%	17%	7%	7%

Source: Baseline

Our valuation studies continue to tell us that at current prices, stocks represent a better investment for the next several years than bonds. For 2004, the S&P has had a total return of -3.2% through August 9, and it has declined 7.9% from its March 5, 2004, high. We believe the stock market could decline another 5%-10% between now and the November elections. However, we believe the U.S. and most foreign economies are on solid footing and should provide a base for positive equity returns over the next several years.

Recent positive earnings reports and an expected continuation of the present expansion for the U.S. economy are encouraging factors to long-term investors in common stocks, but short-term traders have other concerns that are reducing equity prices. Improved stock purchase opportunities are coming into focus now and in the months ahead.

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