Rutherford Investment Management Newsletter: Period Ending 09-30-2004

Rutherford Investment Management, LLC
10300 SW Greenburg Rd. Suite 115
Portland, OR 97223

Phone: (503) 452-1210

www.rutherfordinvestment.com

PERSISTENT HEADWINDS

In my previous letters, I have written of the headwinds facing the markets. Those winds have persisted, and we continue in one of Alan Greenspan's famous "soft patches." The economy is still growing, but at a slower pace. Job creation remains difficult. While incomes in the United States have shrunk for an unprecedented two years in a row, high oil prices, up 17% this quarter, pull nearly 70 Billion dollars out of the economy for the benefit of OPEC. Related energy prices, for natural gas and coal add to the burden. This is an amount sufficient to nullify the benefit of the Bush tax reductions.

The Federal Reserve continues its restrictive policies, raising interest rates three times since June with more increases expected. Money supply figures are restrictive, given the high price of oil.

Inflation continues as a threat even though the Fed feels inflation is well contained. Yet we see the price of basic commodities, such as metals, fibers, food as well as energy increasing. Manufacturers have been unable to pass along the increased costs, so companies are left to make their margins through increased productivity, fewer workers, or settle for lower profits.

Election uncertainty prevails, with the popular vote too close to call, but Bush leading in the all-important electoral vote, as of this writing. With just a month left until the election, voters' opinions will be hardening. Economic indicators are also split. Normally when incumbents are reelected, consumer confidence numbers are above 100 in 8 of 12 months. Confidence numbers have only beaten 100 in two months with one month remaining to the election. The 1.4 million jobs created bode well for Bush, but of course we previously lost 2.5 million jobs. The war in Iraq does not go well and is an additional drain on economic resources. Terrorist threats continue.

The economy usually does better in a presidential election year, but loses some of the stimulus in the year after the election.

In the face of all this uncertainty, we have been holding more cash than is usual for us. Our stock selections are well diversified and defensive while still being growth oriented. Long-term

treasury yields seem to suggest that the markets are not worried about inflation, but the bond market apparently does not see the economy strengthening anytime soon.
The markets, year to date, are nearly flat with the S&P 500 up only 24 basis points and the Dow down 3.57%. I still see the equity markets getting a slight up tick in the fourth quarter of this year, and perhaps the first few month of 2005, but of course the continued high price of oil or terrorist activity could change that. I believe that 2005 will be much like this year, with the economy growing, but the markets soft. Still, our philosophy is to be in the market, making the best selections for your portfolio that we can, and be long term-diversified investors. (Please see the attached charts for the dangers of market timing and the benefit of long term investing.)

Although energy has been our best performing sector, no sector has been a standout, or a big disappointment.

We do not plan any major moves in the portfolio. We intend to be cautious. We may add some basic materials stocks to the portfolio from the cash that we hold, but any additions will have to meet our growth parameters.

William D. Rutherford
Rutherford Investment Management, LLC.