VICTOR LEVINSON **NICK LEVINSON**

JANUARY 2004 COMMENTS

We are pleased to report that our new Registered Investment Advisory firm, PARK PIEDMONT ADVISORS LLC ("PPA"), is up and running. We want to thank all our clients for their continued support, and their time and patience in the changeover. We have every expectation of continuing and improving our advisory services as we move forward with our new Broker Dealer, LaSalle Street Securities, and our new Clearing Firm, National Financial Services, a 100% owned subsidiary of Fidelity Investments. All pertinent contact information is listed at the bottom of this page.

About Our Name: Park Piedmont refers to where we live and work: Vic on Park Avenue in New York City, and Nick in Piedmont, a suburb of Oakland, California.

About Our Logo: We have chosen the bell shaped curve as our logo. This choice reflects our view that the stock and bond markets are very much influenced by long-term trends that produce investment returns in a "normal" distribution. In other words, most returns, both positive and negative, fall within a well-defined range (illustrated by the sloping center portion of the "bell"), with few extremely positive or negative returns (illustrated, respectively, by the right and left side "tails" of the bell). This explains in part why we are such strong proponents of implementing clients' asset allocations with indexed investments, which attempt to match market returns, rather than using actively-managed investments, which seek the often-elusive outperformance represented by the right side of the bell curve.

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COMMENTS: INDEX RESULTS, period ending January 31, 2004

STOCKS	YEAR 1999	YEAR 2000	YEAR 2001	YEAR 2002	YEAR 2003	YTD 2004	CURRENT MONTH
Vanguard Total Stock Market Index Fund (1)	23.8%	(10.6)%	(11.0)%	(21.0)%	28.4%	2.2%	2.2%
S&P 500 Index (2)	19.6%	(10.1)%	(13.0)%	(23.4)%	26.4%	1.7%	1.7%
Vanguard S&P 500 Growth Index Fund (1)	28.8%	(22.2)%	(13.0)%	(23.7)%	25.9%	2.2%	2.2%
Vanguard S&P 500 Value Index Fund (1)	12.6%	6.1%	(12.0)%	(20.9)%	32.2%	1.6%	1.6%
Dow Jones Industrial Average Index (2)	25.2%	(6.2)%	(7.1)%	(16.8)%	25.3%	0.3%	0.3%
NASDAQ Composite Index (2)	85.6%	(39.3)%	(21.0)%	(31.5)%	50.0%	3.1%	3.1%
Vanguard Mid Cap US Index Fund (1)	25.0%	2.6%	(4.8)%	(16.3)%	34.1%	2.1%	2.1%
Vanguard Small Cap US Index Fund (1)	19.6%	(4.2)%	1.0%	(21.6)%	45.6%	4.3%	4.3%
Vanguard International (EAFE) Index Fund (1)	25.3%	(15.2)%	(22.6)%	(17.5)%	40.3%	1.6%	1.6%
BONDS:							
Vanguard Total Bond Market Index (1)	(0.8)%	11.3%	8.3%	8.2%	4.0%	0.9%	0.9%
Vanguard Interm. Tax-Exempt Bond Index (1)	(2.9)%	9.2%	5.0%	7.9%	4.4%	0.3%	0.3%
Vanguard High Yield Taxable Bond Fund (1)	NA	NA	NA	1.7%	17.2%	0.9%	0.9%

	1999				2000				2001			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
S&P 500	4.1	7.6	(7.7)	15.6	2.0	(3.0)	(1.3)	(7.8)	(12.1)	4.8	(13.8)	8.1
NASDAQ COMP	14.6	10.0	0.0	61.0	12.4	(14.8)	(7.2)	(29.6)	(25.5)	12.9	(26.7)	18.3
BONDS Interm. Taxable	0.0	(0.5)	0.4	(0.7)	2.4	1.5	3.1	4.3	3.2	0.8	4.3	0.0

	2002				2003				2004			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
S&P 500	0.0	(13.8)	(14.1)	4.5	(1.8)%	12.8%	2.2%	13.2%				
NASDAQ COMP	(5.5)	(19.5)	(13.5)	7.0	2.5%	19.2%	12.1%	16.2%				
BONDS Interm. Taxable	0.0	2.8	3.6	1.8	0.9%	2.7%	0.2%	0.2%				

1) Results for Vanguard funds are net of dividends and fund expenses but do not reflect PPA's advisory fee.
2) Results for S&P 500, Dow Jones, and NASDAQ indexes but do not reflect dividends or PPA's advisory fee.

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JANUARY 2004 COMMENTS

During the month of January, 2004, **STOCK PRICES** continued to advance. For the month, the S&P 500 was up 1.7%, the Dow Industrials gained 0.3%, and the NASDAQ Composite gained 3.1%. These continuing favorable stock market results occurred against a backdrop of decidedly mixed influences. On the one hand, there was positive economic news regarding the U.S. economy, corporate profits, interest rates and inflation (see pages 5 and 6 for details). On the other hand, a number of factors typically viewed as negatives for stock prices also continued, including weakness in the U.S. dollar, high oil and gold prices, soaring projected U.S. budget deficits, problems with mutual funds, and the geopolitical issues of terrorism and Iraq. The continuing gains in the stock market highlight our view, expressed frequently in prior Monthly Comments, that attributing causes to stock price movements is a complex matter, and that many seemingly relevant news events have already been factored into stock prices by the combined activity of all market participants.

BOND RETURNS (price change plus interest) were positive for January, even as the Federal Reserve changed its language regarding the timing of potential future interest rate increases (see Interest Rate discussion on page 5). For the month, high quality intermediate-term taxable and tax-exempt bonds had returns of +0.9% and +0.3% respectively. High Yield Junk bonds continued to provide better returns than high quality intermediate-term bonds. Some of the same factors mentioned in the above paragraph as influencing stock prices are typically attributed to moving bond prices as well. Here again, causation is a complex matter; in January, the end result was favorable.

While the 2003 – early 2004 percentage increases for Stocks have been considerable, it should be remembered that after a decline of a certain percentage, the percentage increase required to return to the starting point is a much higher number, as indicated below:

	High (3/00)	Low (10/02)	% Decline	% Gain Needed
S&P 500 (1)	1,527	777	(49%)	97%
NASDAQ Comp. (1)	5,048	1,114	(78%)	353%

History suggests these indexes are likely at some point in time to reach and surpass their prior highs. The more relevant question is in what time frame such a recovery takes place. For instance, if the S&P 500 increases from its current 1,131 back to 1,527 over the next five years, the annualized investment return would be 6.2%, well within reasonable long-term return expectations for the stock market. But if it takes 10 years, the annualized return would be only 3.0%, which is more closely associated with bond returns. The NASDAQ recovery would be far more dramatic; to regain prior highs in five years from the current 2,066, the annualized return would have to be 19.5%; over ten years, 9.3%.

1) Results for S&P 500 and NASDAQ indexes but do not reflect dividends or PPA's advisory fee.

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Stock and bond investment results for the January 2004 period and for the five full years 1999–2003 are set out on page 2. The stock market rally of 2003, which began in March, has now raised the S&P 500 45% from the 2002 lows. While this is an impressive figure, and has certainly made investors believe that the stock market is not likely to go down in perpetuity (a view that was widely held during the depths of the bear market), the question of whether this recovery turns into a new, sustained bull market continues to be dependent on future events, as of now unknown.

In order to keep the current recovery in perspective, we continue to show the chart below, which sets out the extent of the declines measured from the highs of Q1 2000. The chart also puts these declines in the context of results since the end of 1994 (see also the figures on page 9). Note that the three indexes have positive average annual returns ranging from 10.4% to 11.7% for the more than nine year period from the end of 1994 through January 2004, very much in line with long term stock returns going back to 1926. Further, as these returns converge more and more, the idea of "regression to the mean" seems applicable.

<u>The long-term investor therefore has a very different view of the stock market's returns than those measuring returns from the highest levels.</u>

	S&P 500 (1)		**DOW (1)**		**NASDAQ (1)**	
1st Qtr 2000 High	1,527		11,723		5,048	
Year End 2000	1,320	(13)%	10,785	(8)%	2,470	(51)%
April 10, 2001 Low	1,103	(28)%	9,390	(20)%	1,684	(67)%
September 21, 2001 Low	965	(37)%	8,235	(30)%	1,425	(72)%
Year End 2001	1,148	(25)%	10,020	(17)%	1,950	(61)%
October 9, 2002 Low	777	(49)%	7,286	(38)%	1,114	(78)%
Year End 2002	880	(42)%	8,342	(29)%	1,336	(73)%
Year End 2003	1,112	(27)%	10,454	(11)%	2,003	(60)%
January 31, 2004	1,131	(26)%	10,488	(11)%	2,066	(59)%

<u>Context: Prior Five-Year Gains in Bull Market of 1995 - 1999</u>:

	S&P 500 (1)	**DOW (1)**	**NASDAQ (1)**
End 1994	459	3,834	752
End 1999	<u>1,470</u>	<u>11,500</u>	<u>4,070</u>
Gain	1,011	7,666	3,318
Avg. Ann. % Gain, '95-'99; 5 years	26.2%	24.6%	40.2%
Jan 2004	<u>1,131</u>	<u>10,488</u>	<u>2,066</u>
Gain	672	6,654	1,314
Avg. Ann. % Gain, '95-1/04; 9.1 yrs	10.4%	11.7%	11.7%

1) Results for S&P 500, Dow Jones, and NASDAQ indexes but do not reflect dividends or PPA's advisory fee.

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I. Update of Key Economic Indicators

The strength of the overall U.S. and world economies is one of a number of factors likely to influence the future direction of both stock and bond prices. (Note: We, along with many market observers and academics who write about the markets, believe stock and bond prices already reflect consensus expectations of economic growth). In any event, an understanding of the direction of current economic trends is useful as a context to help understand market conditions. This section of the Comments provides an update of key economic indicators.

(1) Gross Domestic Product (GDP) is the broadest measure of goods and services produced in the U.S. economy. The first estimate of GDP for the quarter ended December 2003 showed a 4.0% inflation-adjusted annualized growth rate. This rate is "much slower than the torrid pace of last summer though still rapid by historical standards" (NY Times, front page, Jan. 31, 2004). According to the same article, "after scrutinizing the latest data, many analysts predicted that the most important indicators of future growth still pointed to a strong year."

(2) Employment levels for December showed a gain of 1,000 new jobs, a figure that was highly disappointing in light of consensus expectations for job growth of 150,000 (Vanguard Economic Week in Review ("VEWR"), 1/5-9/04, pg. 1). The "jobless recovery" appears to be continuing. As with many economic factors, however, employment levels cut in various ways. On the one hand, jobs provide income that allows people to buy goods and services; on the other hand, employment represents a cost to business, and producing more with the same or less labor improves profits. It should also be noted, as has been mentioned in other Comments, that other measures of employment have been reporting more favorable figures. A January 21st, 2004 NY Times article on the job market, for example, quotes "many economists" as thinking that "for all of the payroll survey's strengths, it often underestimates job growth at economic turning points because it misses numerous start-up businesses" (pg. C1).

(3) Interest Rates declined modestly during January, even after the Federal Reserve, while leaving the short term rates it controls unchanged at a 45-year low of 1%, surprised the markets by changing the language it has been using to describe how long it might take until the Fed sees fit to begin raising interest rates. A front page Wall Street Journal article describing the Fed's action observed that "the announcement doesn't seem to suggest an interest-rate increase is imminent. Rather, it appears the central bank wants the freedom to raise rates if the economy continues to improve, without worrying about violating a perceived commitment to keep them down" (WSJ, 1/29/04, pg. 1). The benchmark 10-Year US Treasury bond now yields 4.14%, about midway in a range of recent yields as low as 3.93% at the end of September, and as high as 4.45% at the end of August. While these rates are low by historical standards, they are approximately one full percentage point (or 100 basis points) higher than the low point reached in early June 2003. It is also worth noting that weak employment figures provide the Fed with another reason to keep rates low.

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(4) Inflation remains low. The "core" inflation rate, as measured by the Consumer Price Index ("CPI") and excluding volatile food and energy prices, increased 0.1% in December. The most recent twelve-month CPI increase of 1.1% was the slowest pace since 1965 (VEWR, 1/12-16/04, pg. 1). The most recent twelve-month gain in the "core" Producer Price Index was just 1.0%, including a 0.1% decline for December (VEWR, 1/12-16, pg. 1). Low inflation rates also provide the Fed a reason to keep interest rates low.

(5) Sector Economic Activity was Mostly Higher

(a) Durable goods orders were flat in December (WSJ, 1/29/04, pg.2).
(b) Manufacturing activity was higher in December, registering its biggest monthly gain since 1983 (VEWR, 12/29-1/2/04, pg. 1). Manufacturing production was modestly higher, although capacity utilization "remained well below its historical average." (VEWR, 1/12-16/04, pg.2). Non-manufacturing business activity also rose in December (VEWR, 1/5-9/04, pg.1). Below average capacity utilization is yet another reason for the Fed to keep rates low.
(c) Retail Sales rose in December, mostly due to strong auto sales (VEWR, 1/12-16/04, pg. 1), continuing their upward trend for all of 2003.
(d) Housing sales for new homes declined in December, but sales figures for the two prior months were revised upward (WSJ, 1/29/04, pg. 2).
(e) Personal Income rose 0.5% in November, while personal spending, which accounts for two-thirds of U.S. economic activity, grew 0.4% (VEWR, 12/22-26, pg. 1; figures for December 2003 are not available at this time).

(6) Consumer Confidence, as measured by the Conference Board's Index of Consumer Confidence, rose over 5% in January after a modest decline in December, which in turn followed a November level that was as high as it had been since September 2002. Both the "present situation index," a measure of consumers' assessment of current economic conditions, and the "index of consumer expectations" for the state of economic activity over the next six months, increased (WSJ, 1/28/04, pg. 2).

(7) Corporate Profits for the fourth quarter are still being reported, but indications from the many companies that have already reported are for very strong performance. A January 20, 2004 Wall Street Journal article cites analyst expectations of 39% profit growth for small company stocks, and 47% profit growth for the 1,000 largest companies in the U.S. stock market, comparison with earnings for the fourth quarter of 2002 (pg. C3). High productivity, as reflected in the modest gains in employment levels and low interest rates, are two important contributing factors to these exceptionally high reported profit figures.

Even with all the good news, there is the ever-present question of whether this news has already been incorporated into current stock and bond price levels. A February 2, 2004 Wall Street Journal article indicates that the price earnings, or "P/E", ratio of U.S. stocks was 24 times the past 12 months' earnings, a figure higher than the historical average of 15 times but lower than the 36 times prevalent in 1999 (pgs. C1-4). The same article noted a P/E of 19 times forecast earnings for 2004.

II. Alternative Responses to Significant Market Price Moves

In response to the significant increases in stock prices since the October 2002 lows, including, most recently, the nine month period from April through December 2003, investors have three likely investment alternatives:

1) Retain current positions, making no changes. Since stocks have significantly outperformed bonds since October 2002, stock allocations by definition have increased relative to bonds. A 50-50 allocation at the end of 2002 would have changed to 55% stocks, 45% bonds by the end of 2003. Why? In a hypothetical $1 million portfolio, the 26.4% rise in stocks (measured by the S&P 500 index) would have increased the $500,000 stock allocation to $630,000, while the 4% rise in bonds (measured by Vanguard's Intermediate Term Total Bond Fund) would have increased the $500,000 bond allocation to $520,000. Although the overall 15% increase from $1 million to $1.15 million is clearly a desirable result, investors must assess whether the additional exposure to the stock market inherent in the new 55% allocation to stocks and 45% allocation to bonds is appropriate for their particular goals and circumstances. A significant part of our job as investment advisors is to assist in this decision process.

2) Add to stock allocations, hoping prices continue to rise. This decision would essentially be an attempt to "time" the market, actively disregarding the~~ir~~ earlier allocation in hopes that the current trend of price increases continues. It is the same thinking that causes people to want to sell when prices are declining. This approach often leads to a buy-high, sell-low result, not at all the desired outcome. While we do not advocate this approach, we note that it can prove profitable if market prices continue in the current upward trend. To the extent that "regression to the mean", or the tendency of prices to return to their long-term historical averages, operates in the liquid markets, however, this market timing approach is unlikely to provide favorable results over extended time periods.

3) Reduce stock positions to previous allocation levels in a process referred to as REBALANCING. Assuming no change in personal circumstances or investment goals, we favor this third alternative. Rebalancing suggests that investors sell the higher priced asset class, and invest the proceeds in the lower priced asset class, at predetermined percentage allocation intervals. Using the example of the 50-50 allocation changing to 55-45 after last year's stock price outperformance, if the 5% change up and down is viewed as sufficient to rebalance, then enough stocks would be sold and bonds purchased to bring the allocation back to 50-50. If the 5% change is viewed as too narrow a range to justify the changes involved in rebalancing, a 10% change (that is, to a 60-40 or 40-60 stock-bond allocation) might be sufficient to warrant rebalancing. Furthermore, rebalancing can also be accomplished without buying and selling if the investor has new funds to invest in the asset class with the reduced allocation.

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It is important to note that in the recent 2000-2002 bear market, this approach would have suggested BUYING stocks as they were declining, and selling bonds during a period of outperformance. Although it would have been difficult to adhere to as stock prices continued to decline in 2002, the increases of 2003 would have justified the decision to rebalance. Specifically, a 50-50 allocation of $1 million at the end of 2001 would have declined by 7.5% to $925,000 overall at the end of 2002, with a revised allocation of 41%, or $385.000, to stocks (based on an S&P decline of 23.4%) and 59%, or $540,000, to bonds (based on an intermediate bond increase of 8.2%). Rebalancing to 50-50 at that time would have shifted approximately $80,000 from bonds to stocks, resulting in a stock portfolio of $465,000 and a bond-portfolio of $460,000. This rebalanced allocation would then have produced a portfolio result of $587,000 in stocks and $478,000 in bonds, or a total of $1,065,000, at the end of 2003, taking into account last year's 26.4% increase in S&P 500 stocks and 4% increase in intermediate bonds. Without the rebalancing at the end of 2002, the portfolio would have totaled $1,049,000 at the end of 2003 (with $487,000 in stocks and $562,000 in bonds), or $16,000 less overall than in the rebalanced portfolio.

III. Rising Interest Rates and Investment Choices

For the better part of the past two years, as interest rates have remained at historically low levels, both stock and bond prices have had intermittent periods of declines, presumably caused in part by the fear that the Federal Reserve would raise interest rates. To date, these fears have not come to pass. Even as the general economy has strengthened, employment and capacity utilization levels have not increased to the point of creating upward price pressures in the economy. But there is a clear consensus that at some point the Fed is likely to raise rates, and this discussion assumes such an increase.

Bond investors fear rising interest rates, because higher rates lower the value of existing bonds. That said, investors in liquid markets have ONLY three broad categories in which to invest their money, namely CASH EQUIVALENTS (money markets and short term CDs, which currently have very low yields to offset the fact they do not decline in price); BONDS, which, depending on maturity and quality, do decline in price by varying amounts when rates rise; and STOCKS, which obviously can rise and fall dramatically based on a multitude of factors, including changes in interest rates.

What is the appropriate action for investors with allocations to all three categories in an environment in which rate increases are likely? Here again, there are a limited number of choices available, assuming the portfolio remains invested in a mix of liquid investments. Investors can increase cash equivalents, accepting the current low yields but preserving 100% of capital in anticipation of higher yields on these short-term investments; shorten bond maturities or select inflation-adjusted bonds, both of which offer lower yields in the hopes of limiting capital declines; or adjust stock positions (either up or down) depending on one's view of the impact of the severity of the interest rate changes that may be coming. This last point is extremely important, since the extent and pace of the rate increases are major factors in the degree to which prices change, both up and down. Modest, gradual rate increases would likely result in moderate changes in stock and bond prices, whereas frequent rate increases in substantial amounts would likely prove harmful for both stock and bond prices.

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A look at history should prove helpful. A January 28, 2004 NY Times article displayed the Federal Reserve's benchmark short term interest rate (discount rate) from 1969 to the present (Financial section, pg. 1). (The year-to-year figures for the Discount Rate, and the stock and bond returns mentioned in the following discussion, are available on request.) When rates spiked up from just above 4% in 1973 to almost 8% in 1976, stock prices declined substantially but bond returns remained positive in all four years. Interest rates fell below 6% during 1976-77 and the stock markets recovered, only to be confronted with historically large rate increases that peaked during 1980-82 at almost 14%. During these years, the stock market had only one modest down year (1981, at minus 4.9%), while bond returns were positive each year, as high interest rates overcame the price declines. (Note: In the bond market, as rates rise and old bonds mature, they are replaced by new bonds with higher interest rates, thereby softening some or all of the impact of price declines caused by these same higher rates.) Starting with 1982, rates declined and stock and bond prices soared until the stock market crash of 1987. Following a few years of rates at 8%, another period of declining rates in the early 1990s helped stock and bond prices to rise. In 1994, the Fed raised rates often and in substantial amounts, causing the worst year on record for bonds (negative 5% for intermediate term bonds). This result occurred because interest rates were relatively low to begin with and the price declines exceeded even the new higher yields. Rates rose as high as 8% in 1998, but the stock market kept advancing. In this latest interest rate cycle of sharply declining rates, the years 2000-2002 were excellent for bonds and terrible for stocks. With rates remaining low and the economy recovering, 2003 was excellent for stocks and modest for bonds. Because rates are still quite low, a sharp increase in rates might cause an overall decline in bond returns similar to what occurred in 1994.

What does all this history tell us? It is not at all simple to conclude what the impact of rising rates will be on bond returns, let alone on the far more complex interrelationships that determine stock prices.

The advice we advocate was put into print by the head of Alliance Bernstein's Private-Client Investment Policy Group (December 2003, page 4), as follows: "While no one can say whether or when yields will rise, in our view bonds should remain a central component of most private investors' portfolios. They offer a reliable income stream and in most years an important element of portfolio stability; none of that is going to change if rates rise." The author then continues by advocating high credit quality bonds and intermediate-maturity portfolios that, he writes, "offer the best risk/reward trade-off over time and are appropriate for most clients." Our approach is somewhat more varied, mixing shorter-term, inflation-protected, and high-yielding junk bonds with high credit quality intermediate maturity bonds (both taxable and tax exempt).

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1) Results for S&P 500, Dow Jones, and NASDAQ indexes but do not reflect dividends or PPA's advisory fee.

I. Figures From Period Starting 2000 (% Figures Are Cumulative Declines From 1/01/00)

	S&P 500 (1)		**DOW (1)**		**NASDAQ (1)**	
Start of 2000	1,470		11,500		4,070	
End of 2000	1,320	(10.1)%	10,785	(6.2)%	2,470	(39.3)%
Sept. 21, 2001 Low	965	(34.3)%	8,235	(28.4)%	1,425	(65.0)%
End of 2001	1,148	(21.9)%	10,020	(12.9)%	1,950	(52.0)%
Oct. 9, 2002 Low	777	(47.1)%	7,286	(36.6)%	1,114	(72.6)%
End of 2002	880	(40.1)%	8,342	(27.5)%	1,336	(67.2)%
End of 2003	1,112	(24.3)%	10,454	(9.1)%	2,003	(50.8)%
January 2004	1,131	(23.1)%	10,488	(8.8)%	2,066	(49.2)%

II. Figures From Period Starting 1995 (% Figures Are Gains From 1/01/95)

Start of 1995	459		3,834		752	
End of 1999	1,470		11,500		4,070	
5 Year Gain; Annualized %	1,011	26.1%	7,666	24.6%	3,318	40.2%
End of 2001	1,148		10,020		1,950	
7 Year Gain; Annualized %	689	14.0%	6,186	14.7%	1,198	14.6%
End of 2002	880		8,342		1,336	
8 Year Gain; Annualized %	421	8.5%	4,508	10.2%	584	7.5%
End of 2003	1,112		10,454		2,003	
9 Year Gain; Annualized %	653	10.3%	6,620	11.8%	1,251	11.5.%
January 2004	1,131		10,488		2,066	
	672	10.4%	6,654	11.7%	1,314	11.7%

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