Park Piedmont Advisors LLC

Registered Investment Advisor

VICTOR LEVINSON **NICK LEVINSON**

AUGUST 2005 COMMENTS

IMPORTANT NOTICES:

THOUGHT for the MONTH: From the August 29, 2005 Wall Street Journal (WSJ) article (pg. A2) on Fed Chairman Greenspan's recent speech in Jackson Hole, Wyoming: "Investors have become complacent about risk. They are exhibiting a seeming willingness to project stability and commit over an ever more extended time horizon. This means they have bid up stock and housing prices and accepted unusually low yields on long-term bonds."

SPECIAL SECTION on LIKELY IMPACT of HURRICANE KATRINA on Stock and Bond Market Prices **(see Section II, pages 7-8).**

TAX COST BASIS INFORMATION:

We plan to resume our work that will incorporate in your monthly statements tax cost basis information for all presently owned positions in your taxable accounts. We hope to finish all client accounts by year end. You will be receiving an explanatory letter from us, and a completed cost basis information form that calls for your signature, prior to this information appearing on your statement(s).

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COMMENTS: INDEX RESULTS, period ending AUGUST, 2005

STOCKS	YEAR 1999	YEAR 2000	YEAR 2001	YEAR 2002	YEAR 2003	YEAR 2004	YTD 2005	CURR. MONTH
Vanguard Total Stock Market Index Fund (1)	23.8%	(10.6%)	(11.0%)	(21.0%)	28.4%	12.5%	2.9%	(0.9)%
Standard & Poors 500 Index (2)	19.6%	(10.1%)	(13.0%)	(23.4%)	26.4%	9.0%	0.7%	(1.1)%
Vanguard S&P 500 Growth Index Fund (1)	28.8%	(22.2%)	(13.0%)	(23.7%)	25.9%	7.2%	1.7%	(1.4)%
Vanguard S&P 500 Value Index Fund (1)	12.6%	6.1%	(12.0%)	(20.9%)	32.2%	15.3%	3.9%	(0.4)%
Dow Jones Industrial Average Index (2)	25.2%	(6.2%)	(7.1%)	(16.8%)	25.3%	3.2%	(2.8)%	(1.5)%
NASDAQ Composite Index (2)	85.6%	(39.3%)	(21.0%)	(31.5%)	50.0%	8.6%	(1.1)%	(1.5)%
Vanguard Midcap US Index Fund (1)	25.0%	2.6%	(4.8%)	(16.3%)	34.1%	20.4%	9.1%	(0.4)%
Vanguard Smallcap US Index Fund (1)	19.6%	(4.2%)	1.0%	(21.6%)	45.6%	19.9%	5.4 %	(1.8)%
Vanguard International Index Fund (EAFE) (1)	25.3%	(15.2%)	(22.6%)	(17.5%)	40.3%	20.8%	5.8%	2.9%
Vanguard Real Estate Invest. Trust Fund (1)	(0.4%)	26.4%	12.4%	3.8%	35.7%	30.8%	9.4%	(4.2)%
BONDS								
Vanguard Total Bond Market Index (1)	(0.8%)	11.3%	8.3%	8.2%	4.0%	4.2%	2.9%	1.4%
Vanguard Interm. Tax-Exempt Index Fund (1)	(2.9%)	9.2%	5.0%	7.9%	4.4%	3.2%	2.2%	1.0%
Vanguard Short-term Bond Index (1)	2.1%	8.9%	8.9%	6.1%	3.4%	1.7%	1.3%	0.9%
Vanguard Short Tax-Exempt Index Fund (1)	2.6%	4.9%	4.8%	3.5%	1.6%	1.1%	1.0%	0.2%
Vanguard High-Yield	NA	NA	NA	1.7%	17.2%	8.5%	2.0%	0.3%

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

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%	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
		1999				**2000**				**2001**		
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	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	0.0	(0.5)	0.4	(0.7)	2.4	1.5	3.1	4.3	3.2	0.8	4.3	0.0
Interm. Tax.												
		2002				**2003**				**2004**		
S&P 500	0.0	(13.8)	(14.1)	4.5	(1.8)	12.8	2.2	13.2	1.3	1.3	(2.4)	8.8
NASDAQ	(5.5)	(19.5)	(13.5)	7.0	2.5	19.2	12.1	16.2	(0.5)	2.7	(7.5)	13.9
BONDS	0.0	2.8	3.6	1.8	0.9	2.7	0.2	0.2	2.7	(2.6)	3.1	1.0
Interm. Tax.												
		2005				**2006**				**2007**		
S&P 500	(2.6)	0.9%										
NASDAQ	(8.1)	2.6%										
BONDS	(0.5)	3.0%										
Interm. Tax.												

AUGUST 2005 COMMENTS

STOCK index prices declined in August, although they actually advanced for the week ending Sept 2nd, following Hurricane Katrina. (A detailed discussion of the impact of this natural disaster begins on page 7.) For August, the S&P 500, the Dow Industrials and the NASDAQ Composite declined by (1.1)% to (1.5)%, respectively. The Midcap, Smallcap, and REIT indexes also declined. Only the international index was up for the month. For year to date (YTD), the S&P 500 is still up fractionally, while the Dow Industrials and NASDAQ Composite are down modestly. By contrast, the Midcap, Smallcap, REIT and international indexes are all up more than 5%, substantially outperforming the Largecap indexes. The Total Stock Market index is up 2.9%, benefiting from the Midcap and Smallcap performance. (See page 2 for the monthly and YTD figures).

BOND returns (price change plus interest) advanced during August, reversing their declines of July. The gains accelerated in the week following the hurricane, as there was discussion that the Federal Reserve might slow down its pace of quarter point rate increases. The benchmark 10-year US Treasury yield closed the month at 4.02%, a full quarter point lower than the 4.28% close for July, which in turn was a significant increase over June's close of 3.92%. All YTD figures for bonds are positive. Bond result figures for the month and YTD are reported on page 2.

The stock market rally that began decisively in March 2003 has raised the S&P 500 by 57% from the October 2002 low. While these gains have made investors believe again that stocks do not go down in perpetuity (a widely-held view during the depths of the 2000-02 bear market), the question of whether this recovery will continue is, as always, dependent on unknown future events (of which Hurricane Katrina is an example; see page 7 for discussion). Indeed, this year's Largecap stock indexes, over the first eight months, are essentially break-even. (Note also that after a 50% price decline, it takes a 100% gain to return to the previous level. Since the S&P 500 reached its high of 1,527 in Q1 2000, and then declined by almost half to 777 during Q4 2002, the current level of 1,220 is 57% higher than the low but still another 307 points, or 40%, from the prior high).

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 (also see the figures on page 12). Note that the three indexes have positive average annual returns ranging from 9.6% to 10.3% for the ten-year and eight-month period from the end of 1994 through August 2005, 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 quite applicable.

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

	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)%
Year End 2004	1,212	(21)%	10,783	(8)%	2,175	(57)%
August 31, 2005	1,220	(20)%	10,482	(11)%	2,152	(57)%

Context: Prior Five-Year Gains in Bull Market of 1995 - 1999

	S&P 500 (1)	DOW (1)	NASDAQ (1)
End 1994	459	3,834	752
End 1999	1,470	11,500	4,070
Gain	1,011	7,666	3,318
Avg.Ann.%Gain:'95-'99; 5 years	26.2%	24.6%	40.2%
August 2005	1,220	10,482	2,152
Gain	761	6,648	1,400
Avg.Ann.%Gain:'95-08/05; 10.67 yrs	9.6%	9.9%	10.3%

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

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I. UPDATE OF KEY ECONOMIC INDICATORS

NOTE: This month's update does NOT include any figures related to Hurricane Katrina, which occurred at the end of August. The hurricane's impact will influence future figures.

The strength of the overall US and world economies is one of a number of factors likely to influence the future direction of both stock and bond prices. 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. Further, we believe that even if you could accurately predict any number of actual economic figures, the market's reaction to those figures is essentially unpredictable. In any event, an understanding of the direction of current economic trends may at times be 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 US economy. (GDP figures are inflation-adjusted, annualized growth rates. The NY Times (NYT) article "Economic View," in the 7/31/05 Financial section (pg. 4), lists the following elements of GDP: (a) personal consumption spending for goods and services; (b) government spending and investment; (c) residential and nonresidential investment, and changes in inventories; and (d) net exports). The newly revised estimate for Q2 2005 GDP was a 3.3% increase, slower than the 3.8% growth in Q1 2005. "Consumer spending, business investment and exports rose, while business inventory investment fell" (WSJ, 9/1/05, pg. A2).

(2) Employment for August grew by 169,000, "less than Wall Street forecasters had expected, but the Labor Department also calculated that the nation generated 44,000 more jobs in June and July than it had estimated. Taken together the new data showed that companies expanded their work forces an average of 195,000 jobs a month over the last three months – a pace that suggested that the economy was not slowed much by the sharp increase in gasoline prices earlier this summer" (NYT, 9/3/05, pg. B1).

(3) Interest Rates declined in August. The benchmark 10-year US Treasury interest rate, which is set by buyers and sellers in the bond market, closed at 4.02%, well below July's 4.28% close. These declines occurred even as the Fed raised the short-term rates it controls for the tenth time since June 2004, bringing the short-term rate to 3.5%, up from 1% a year earlier (WSJ, 8/18/05, pg. D1). Interest rates are discussed again in detail in Section III of these Comments, on pages 9 and 10.

(4) Inflation, as measured by the Consumer Price Index (CPI) "core" rate, which excludes the volatile food and energy sectors, increased a modest 0.1% in July, for the third consecutive month, but overall CPI was up a much higher 0.5%, mostly due to a 3.8% rise in energy prices (WSJ, 8/17/05, pg. A2). Through July, the core rate has risen at a 2.2% annual rate (Vanguard Economic Week in Review [VEWR], 8/15-19/05). The Producer Price Index (PPI) core rate increased 0.4% in July, and a much larger 1.0% with food and energy included, again the result of much higher energy prices. This followed no change in June and a decline in May (WSJ, 8/18/05, pg. A2). (Note: the CPI measures prices of goods and services; the PPI, only goods).

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(5) Sector Economic Activity was Mixed in August

(a) Durable goods orders (industrial and consumer) declined by (4.9%) in July, following three months of increases "marring what had been an upbeat picture of third-quarter economic growth" (WSJ, 8/25/05, pg. A2).

(b) Industrial production rose 0.1% in July, "a sharply slower-than-expected pace" (VEWR, 8/15-19/05).

(c) Retail Sales "rose 1.8%, but almost all of that strength came from discounted car sales…excluding autos, retail sales rose 0.3, about half the gain many analysts expected" (WSJ, 8/12/05, pg. A2). (Retail sales are not adjusted for inflation, and include disparate categories such as gasoline sales, auto sales, and non-store retailers such as the Internet.)

(d) Housing sales for existing homes declined (2.6%) in July, after hitting a record in June, but new home sales remained very strong in July, 27% higher than the July 2004 figure (VEWR, 8/22-26/05).

(e) Personal Income rose 0.3% in July, while consumer spending jumped by 1%, the "second consecutive monthly gain of that magnitude. As a result the personal savings rate went into negative territory for the first time since the weeks after the September 11th terrorist attacks. Housing has been a critical source of spending for many Americans, with home-equity loans and cash out mortgage refinancing. When the government calculates the personal-savings rate, it doesn't count the wealth accrued in homes or in the stock market" (WSJ, 9/2/05, pg. A2). (Our note: The rationale for the government's treatment is that one person's gain is the next person's new cost, hence no new income for the overall economy). Despite the short-term negative savings, the increase in home and stock equity does provide the ability to increase spending for a limited time period.

(6) Consumer Confidence, as measured by the Conference Board's Index, jumped in August to its highest level in four years (VEWR, 8/29-9/2/05), although the University of Michigan's report on consumer sentiment showed a "shaper decline than the drop predicted by economists" (WSJ, 8/29/05, pg. A2). In a month of mixed results, these reports provide excellent evidence of yet another mixed result.

(7) Corporate Profits for Q2 2005 "rose a sharp 6.9% from the first quarter, and were up 11.5% after-tax from the second quarter of 2004" (WSJ, 9/1/05, pg A2). While corporate profits are a major driver of stock prices, it is important to note that over extended periods of time the rate of profit growth is closely related to the rate of overall economic growth.

Overall, the economic news for August, pre-Hurricane Katrina, was mixed, and eight months into 2005, the broadly diversified liquid investment markets have produced meager returns. As for the future, prices will, as always, be determined by unpredictable, unknowable future events. This constant conclusion of ours has been made abundantly clear by Katrina, and we now turn to a discussion of the hurricane's likely impacts.

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II. LIKELY IMPACT OF HURRICANE KATRINA

The month of August, 2005 will now be remembered for Hurricane Katrina and its devastating impact on the people who lived in its path in the states of Louisiana, Mississippi, and Alabama. This section of our Comments will be devoted to the likely impacts of the hurricane on the overall economy, and particularly on stock and bond prices. We have already had a number of inquiries from clients, and hope this section answers at least some of your questions. Please feel free, as always, to contact us to discuss any specific concerns.

Our bottom-line advice to clients is to make no changes in your current asset allocations as a result of the Hurricane. This of course assumes your allocations were appropriate to your investment objectives and risk tolerances before this particular catastrophe. The reasons for this advice are as follows:

1) ACTUAL MARKET PRICES: At least initially, the markets have already spoken. The following chart shows the prices of key stock and bond measures, and oil, as of Friday August 26th, while the expected storm was still approaching, and then as of Friday, September 2nd, four days after the storm had hit.

Stock Indexes	Aug. 26	Sept. 2	Change
S&P 500	1,205	1,218	+ 1.07%
Dow Jones Ind.	10,397	10,447	+ 0.48%
NASDAQ Comp.	2,121	2,141	+ 0.96%
Bond Yields (Bond Prices increase when Bond yields decline)			
Ten-Year Treasury	4.21%	4.04%	- (0.17)%
Two-Year Treasury	4.10%	3.75%	- (0.35)%
Oil (as distinguished from gasoline prices)			
Crude Oil, per barrel	$66.57	$67.57	+ 1.5%

Therefore, both stock and bond prices finished HIGHER at the end of the week than they were at the beginning of the week, and even crude oil prices were fairly stable. It is worth emphasizing that these prices are determined, as always, by all sorts of market participants, from traders who react to daily and hourly price changes, to long-term buy-and-hold investors, to chartists who look for future price trends from past price movements, to the growth and value investors who each have a different preference as to the reasons for owning particular securities in a given time frame. Some of these investors are professionals, some amateurs, and some manage mutual funds or hedge funds, both domestic and international. All of these participants, taken together, in their buying and selling activities, are essentially making their own predictions as to the impact that the hurricane is likely to have on market prices in the context of all the other factors that determine market prices. And at the end of this most harrowing week, with media images of great human suffering and loss, the financial markets, on balance, ended with higher prices than the levels at which they started the week. In our view, this is a remarkable result that would have been extremely difficult, if not impossible, to predict in advance.

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2) NEW EVENTS: Regardless of the eventual financial impacts of this hurricane, many of which are of course unknown as of this time and are not likely to be known for some time to come, we believe, as always, that other future events, as yet unknown, are likely to intervene and become more significant to securities markets pricing than even this calamitous event. Whether the next events will be favorable or unfavorable to prices is of course unknown, but the idea that "new news" will occur, and become the new price driver for some period of time, is highly likely. One example: While reporting all the hurricane related problems, the NY Times ran a story (9/1/05, pg. A6) about the possibility of Iraq producing and shipping twice its current daily level of oil, under certain circumstances.

3) HISTORY: History indicates that the US economy and its financial markets recover from these kinds of events. The most recent example would be 9/11. One week after trading resumed in financial markets following this unprecedented attack on US soil, stock prices were down approximately 10% (an expected result). Yet by year end 2001, stock prices had recovered and were higher than their 9/10 closing levels (an unexpected outcome, obviously affected by other, more recent events and perceptions). In the same NY Times article cited extensively in 4) below, the authors observe that "the fast economic recovery from the Sept. 11 attacks showed that traumatic events often have a relatively small economic impact."

4) PROJECTIONS BY ECONOMISTS IN THE MEDIA: Based on what is known currently, with much that can only be estimated, the media has presented its views and those of various economists and other "experts." The WSJ states (9/6/05, pg. A1) that "the US economy's shock absorbers kicked in within days of one of the worst natural disasters in its history, offering hope that the massive jolt to the country's energy and transportation systems won't produce a long-lived, serious economic contraction…. Hurricane Katrina is the biggest test in years of the economy's resilience. But recent history offers encouraging, though by no means definitive, evidence of the US economy's ability to bounce back from shocks... Katrina came at a time when the economy was in solid shape." The article refers to a survey of economists indicating second-half growth projections of 3.5% annualized, down from pre-storm expectations of 4%. Actual first-half growth was 3.6%.

For its part, the NY Times writes (9/4/05, pg. 27) that "the broad American economy has largely withstood the early effects of Hurricane Katrina, even as residents of the Gulf Coast suffer through a regional economic disaster with few equals….The effect of the damage to oil rigs and refineries is the greatest uncertainty. But contrary to early fears, the nation's transportation network has not become overwhelmed so far, and despite spot shortages drivers have generally been able to buy gasoline… Economists said that the storm and its aftermath had raised the risks of a downturn. One major question is whether the damage to oil refineries aggravates what had already been a growing burden caused by soaring energy prices….But the most likely outcome, according to forecasts that Wall Street firms revised after the storm, is a slowdown in growth during the rest of this year and a pickup next year as New Orleans and southern Mississippi are rebuilt." In a somewhat less optimistic article, the NY Times states (9/4/05, Sunday Business section) that "just as the 1973 crisis led to a global shortage of oil that sent prices soaring and pushed the American economy into recession, today's sudden shortfall of gasoline that is rippling through the economy is likely to slow American growth by as much as a full percentage point….For two years, steadily rising oil prices barely weighed on global economic growth….Then came Katrina, which shut down…a quarter of domestic oil production and 10% of the country's refining industry."

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III. OIL PRICES, INTEREST RATES, AND SECURITIES MARKETS PRICES

(This section was written prior to Hurricane Katrina, but we think it continues to be relevant.)

It is no secret that oil prices have been soaring recently; a visit to the gas station provides ample proof. "Over the past 24 months, there has been a near-doubling of oil prices – to $70 per barrel,…although still below the record price in inflation adjusted terms of over $90 reached in April 1980" (WSJ, 8/29/05, pg. A1)

It is also no secret that certain interest rates have been increasing. "Last week, the Federal Reserve raised its target rate for short-term interest rates for the tenth consecutive time (since June 2004), to 3.5%, and showed no signs of letting up. Because rates on most consumer loans are tied to the prime rate – now 6.5%, compared with 4.5% a year ago – average rates have risen alongside the Fed's moves. Home equity lines of credit, for instance, have risen 2% in the last year" (WSJ, 8/18/05, pg. D1). This same WSJ article also makes a point similar to the one made in the oil price article cited above: "Granted, today's consumer loans are nowhere near the levels of the early 1980s when the prime rate was as high as 21.5%, or even throughout the 1990s when the prime rate averaged around 8%."

Given the above two facts it would be reasonable to expect an increase in the rate of inflation, which measures the actual purchasing power of a given amount of money. If the price of oil is rising, and the price of money is rising (that is, interest rates), an overall increase in prices, which reduces the purchasing power of a given amount of money, would be expected. Interestingly, the government's inflation statistics show a mixed picture. As reported in the previous section, consumer prices for July rose 0.5%, with "half the gain from a 3.8% jump in energy prices….But, with rampant vehicle discounting and large-scale declines in apparel prices in the past month, the core inflation index, which excludes food and energy items, rose a moderate 0.1% for a third month in a row; and in the past four months, the core rate has increased at an annual rate of only 1.3%" (WSJ, 8/17/05, pg. A2). Further, the producer price index, which measures the prices of goods but not services, rose a full 1.0% in July, after a flat June…." but economists expressed little concern that the higher prices producers are paying signal broad inflation. Here again, much of the overall monthly increase reflected a 4.4% rise in energy prices. The core index, which excludes food and energy, rose an unexpectedly large 0.4%, because of a sharp rise in auto prices, which appears inconsistent with the aggressive discounting by auto makers over the past few months" (WSJ, 8/18/05, pg. A2). In its report on the producer price index, the NY Times' article (8/18/05, pg. C3) noted that wholesale prices for the last twelve months are up 4.6%, and the core rate up 2.8%, "its fastest pace since 1995." Still, 2.8% is not that high from a historical perspective.

Not only are broad measures of inflation not soaring along with soaring oil prices and rising short-term interest rates, but longer-term interest rates, as reflected by the prices of longer-term bonds in the bond market, have actually been DECLINING during the same time period. This fact, which has been reported on regularly in these Comments and in the daily newspaper financial sections, is unquestionably the most unusual outcome in this time of otherwise higher pricing of oil and short-term interest rates. This is the situation that Fed Chairman Greenspan has described as a "conundrum," and that he made reference to in the Jackson Hole speech cited on page 1 of this month's Comments.

When the Federal Reserve began raising short-term Fed Funds rates from 1% in June of 2004, the yield on the benchmark ten-year US Treasury bond was 4.7%. (Since the new issue of 30-year Treasuries was discontinued a few years ago, the ten-year Treasury has become the benchmark for longer term bond yields). Now, fifteen months later, the short-term Fed Funds rate is 3.5%, and the ten-year bond yield is below 4.2%. So in the same time frame that short rates have increased by 2.5%, the longer-term rate has DECLINED by 0.5%. No wonder Greenspan talks of investors "accepting unusually low yields on long-term bonds."

In a recent article on the state of the bond market (WSJ, 8/29/05, pg. C4), the authors state that "Fed Chairman Greenspan's warning last week about the dangers of asset bubbles left the bond market with one clear message: it is OK to keep flattening the yield curve. Mr Greenspan's message that stable economic conditions during the past decade may have encouraged investors to accept increasingly lower levels of compensation for risk caused little commotion in the broader bond market. But it gave Treasuries further incentive to keep compressing the difference between the two-year and ten-year yields, known as the benchmark yield curve." The article continues by noting that the yield curve based on Friday's close (August 26th) had narrowed to 0.11%, "the lowest it has been since January 2, 2001, and well below the 1.16% spread at the beginning of 2005." The actual yields were 4.18% for the ten-year and 4.07% for the two-year.

This narrowing yield curve means that prices on the ten-year bond have been INCREASING at the same time prices on the two-year bond have been DECLING. The reason is that interest rate yields decline as bond prices rise, and yields rise as bond prices decline. The two-year bond price and yield have clearly reacted in line with the increases in the short-term Fed Funds rate, whereas the longer-term bond price and yield have moved in the opposite direction. While this is not unprecedented, it is an absolutely unexpected result. And, again referring to Greenspan's warning from Jackson Hole, he believes that "some investors mistakenly view lofty valuations in stocks, bonds and housing, that have been persistent for some time now, as something permanent" (WSJ, 8/29/05, pg. C4).

As for stock prices in this high oil price/higher short-term interest rate environment, the S&P 500 index was absolutely even for the year 2005 as of the close Monday, August 29th, and the Total Stock Market, which includes the S&P 500, Midcap, and Smallcap stocks, was up 2.0%. This is obviously not an example of lofty valuations, but Greenspan's comments take into account the returns of 2003 and 2004, which were 26.4% and 9.0%, respectively, for the S&P 500, and an even better 28.4% and 12.5% for the Total Stock Market. For 2005, the stock market advance of the prior two years has ground to a halt, a far more expected result in this time of higher oil prices and higher short term interest rates than the increases in longer term bond prices.

As a final thought on these subjects, there are observers who think that because of higher oil prices and short-term interest rates, there will be a slow down in economic activity, and that this projected slowdown is a rational reason for lower long-term interest rates. Whether this concern or Greenspan's risk warning proves correct remains to be seen.

IV. ANNUITIES, AND A BRIEF UPDATE ON HEDGE FUNDS

In keeping with our recent focus on investment alternatives, which has included a discussion of Commodity funds (March, 2005) and Hedge funds (July, 2005), this month's Comments will begin a discussion on Annuities. Because of the added section on Hurricane Katrina, most of this Annuity discussion will continue in next month's Comments.

Annuities are not an alternative asset class, but rather a specialized kind of account within which investments in stock funds, bond funds, and other fixed income funds, can be made. Annuities are issued by insurance companies in return for investments made by the investor, and promise a flow of money for as long as one (or more) person lives, or some other agreed-upon time period. The idea of a guaranteed flow of money is one key advantage of annuities. A second key advantage is that the investment earnings accumulate income tax free until such time as money is withdrawn. Annuities have several offsetting disadvantages, chief among which are: (a) the high cost, and severe premature withdrawal charges, typically associated with these products, and (b) the fact that when money is withdrawn, the investment earnings component is taxed as ordinary income with no opportunity for favorable capital gain treatment. Also, depending on the way money is withdrawn, the income tax consequence comes before, or coincident with, the tax free invested capital component. Amounts invested are made with after tax dollars, and receive no income tax benefit, which means that investors should generally fund all tax deductible retirement programs before considering funding any annuity investment, since a tax deduction is available for the retirement plan investment, and all other income tax treatment is the same. (Note: Roth IRAs involve different tax treatment.)

The key economic question for investors is whether, given all the above mentioned advantages and disadvantages, it is better to accumulate money inside an annuity or in a regular taxable account. In our next monthly Comments, we will provide a detailed financial analysis relating to this question, along with a discussion of other issues that recent WSJ articles have raised regarding annuities.

HEDGE FUND UPDATE: The financial pages have been filled with stories about Bayou Management, a hedge fund that appears to have lost a substantial amount, if not all, of up to $400 million reported to have been invested in it. From our standpoint, this story provides yet another example of the reasons to be highly cautious with regard to these funds. The stories discuss how many prominent and presumably knowledgeable investors, along with outside consulting firms that analyze hedge funds as to their appropriateness, were investors in the fund. "Several investors say they were attracted to Bayou for the firm's remarkably steady returns, but also were comforted by the firm's unusually frequent reports to investors" (WSJ, 8/30/05, pg. C1). Whatever the eventual outcome of this story, our basic objections to hedge funds are that: (a) they invest in ways unknown to their investors (they are a "black box"), and (b) investors are totally reliant on the skills and credibility of the managers, as made abundantly clear by this situation. Regardless of the high profile names who invest, the reported results, and the sophisticated strategies employed, handing money over to hedge funds is an act of faith, very different from investing in highly transparent and regulated mutual funds, particularly low cost index funds with long track records. Even with the mutual fund scandals of a few years ago, the actual financial losses to investors caused by the illegal acts of the funds were miniscule compared to the kinds of losses for investors (sometimes total) that can occur when a hedge fund fails.

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	S&P 500 (1)		DOW JONES (1)		NASDAQ (1)	

1) Results for S&P 500, Dow Jones, and NASDAQ indexes 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		DOW JONES		NASDAQ	
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)%
End of 2004	1,212	(17.5)%	10,783	(6.2)%	2,175	(46.5)%
August 31, 2005	1,220	(17.0)%	10,482	(8.8)%	2,152	(47.1)%

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

	S&P 500		DOW JONES		NASDAQ	
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.%
End of 2004	1,212		10,783		2,175	
10 Year Gain; Annualized %	753	10.2%	6,949	10.9%	1,423	11.2%
August 31, 2005	1,220		10,482		2,152	
10.67 Yr Gain; Annualized %	761	9.6%	6,648	9.9%	1,400	10.3%

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