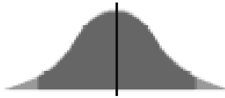

Park Piedmont Advisors LLC

Registered Investment Advisor

VICTOR LEVINSON **NICK LEVINSON, CFP®**

SEPTEMBER 2007 COMMENTS

SEPTEMBER MARKET ACTIVITY

In a major reversal from August's highly volatile stock and bond market activity, presumably fueled in large part by the highly publicized problems in the credit markets, September's market activity, with little fanfare or excitement, produced substantial gains in the stock market and modest gains in the bond market. The apparent catalyst, and highlight of the month, was the Federal Reserve's action to reduce the short term rates it controls for the first time in four years, from 5.25% to 4.75%. This month's Comments will provide additional discussion of various possible consequences of the rate reduction.

OFFER OF PARK PIEDMONT ADV

Each year during September, Park Piedmont publicizes the availability of its ADV for review by clients and others. The ADV is the SEC-mandated disclosure document for Registered Investment Advisors. It is posted on our website, www.parkpiedmont.com, and available to you by mail upon request to Lynette Carmelli, at 212-391-2323.

PARK PIEDMONT ADVISORS (PPA): An Update of Who We Are

PPA now consists of five investment professionals who provide investment advice to our clients. Victor and Nick Levinson, founders of PPA, are two of the five. They are joined by three Certified Public Accountants (CPAs): Richard Backer, in New York City; George Gotthold, in Southern New Jersey; and Stuart Greenberg, in Central New Jersey. Each of the CPAs offers investment advice in addition to his accounting work. Lynette Carmelli heads our administrative and client services staff. PPA is also looking for an additional investment professional to work with Victor's clients in the New York-New Jersey-Connecticut metropolitan area and Florida.

If you know others who you think might benefit from our services, we are always interested in and grateful for your referrals.

CONTENTS

Page 1: Important Notices: What's in This Edition?
Pages 2-4: Index Results for SEPTEMBER 2007, and Year-to-Date 2007; Also Years 1999 – 2006, and Various Other Longer Time Periods
Pages 5-8: Investment Concepts:
5-7: Economic Growth or Inflation, as Fed Lowers Interest Rates
7-8: Recent Hedge Fund Problems

Any recommendation contained in these Comments may not be suitable for all investors. Moreover, although the information contained herein has been obtained from sources believed to be reliable, its accuracy and completeness cannot be guaranteed.

Vic's Home Office Phone: 212-588-0015
Vic's Home Office Fax: 212-588-9032
Nick's Office Phone: 510-601-6662

COMMENTS: INDEX RESULTS for period ending SEPTEMBER 2007

STOCKS	YEAR 1999	YEARS 2000-02	YEARS 2003-05	YEAR 2006	YTD 2007	SEPT 2007
Vanguard Total Stock Market Index Fund (1)	23.8%	(37.2%)	53.1%	15.5%	9.1%	3.8%
Standard & Poor's (S&P) 500 Index (2)	19.6%	(40.1%)	41.9%	13.6%	7.6%	3.6%
Vanguard S&P 500 Growth Index Fund (1)	28.8%	(48.4%)	41.8%	9.0%	12.6%	4.6%
Vanguard S&P 500 Value Index Fund (1)	12.6%	(26.2)%	63.2%	22.1%	6.6%	3.4%
Dow Jones Industrial Average Index (2)	25.2%	(27.5%)	28.5%	16.3%	11.5%	4.3%
NASDAQ Composite Index (2)	85.6%	(67.2%)	65.2%	9.5%	11.8%	4.3%
Vanguard Midcap US Index Fund (1)	25.0%	(18.3%)	83.9%	13.6%	9.8%	3.1%
Vanguard Smallcap US Index Fund (1)	19.6%	(24.2%)	87.5%	15.6%	6.5%	2.2%
Vanguard International Index Fund (EAFE) (1)	25.3%	(45.9%)	95.9%	26.6%	17.0%	7.0%
Vanguard Emerging Markets Index Fund (1)	61.6%	(29.5%)	162.7%	29.4%	34.9%	13.1%
Vanguard Real Estate Investment Trust Fund (1)	(0.4%)	47.5%	98.6%	35.1%	(4.1)%	3.9%
BONDS						
Vanguard Total Bond Market Index (1)	(0.8%)	30.4%	11.1%	4.2%	3.7%	0.7%
Vanguard Intermediate Tax- Exempt Index Fund (1)	(2.9%)	23.7%	10.3%	4.4%	1.9%	1.2%
Vanguard Short-term Bond Index (1)	2.1%	25.8%	6.5%	4.1%	4.5%	0.7%
Vanguard Short Tax- Exempt Index Fund (1)	2.6%	13.8%	4.5%	3.2%	2.8%	0.5%
Vanguard High-Yield Bond Fund (1); starting 2002	NA	1.7%	30.7%	8.2%	3.0%	2.8%
Vanguard Inflation-Protected Bond Fund (1); starting 2001	NA	25.5%	20.0%	0.4%	6.3%	1.4%

NOTE: Three-year results start with a base of 100, and after each year's % change, the result for that year creates a new base. So if at the end of the first year the index is up 10%, then the new base is 110%; and if down 10%, then the new base is 90%. NOTE also that a decline of 50% requires a gain of 100% to get back to the starting value, which explains why NASDAQ, down 67%, would require a gain of 200% to get back to its starting value.

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.

Vic's Home Office Phone: 212-588-0015
Vic's Home Office Fax: 212-588-9032
Nick's Office Phone: 510-601-6662

%	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	3.1	1.6	3.7	(1.9)	5.2	6.6	0.2	5.8	1.6%	
NASDAQ	(8.1)	2.6	4.4	2.5	6.1	(7.6)	3.9	7.1	0.3	7.5	4.0%	
BONDS	(0.5)	3.0	(0.7)	0.6	(0.7)	(0.2)	3.8	1.3	1.4	(0.6)	2.9%	
Interm. Tax.												

SEPTEMBER 2007 COMMENTS

STOCK index prices for US stocks made substantial gains in September, following more modest gains in August, all in spite of the highly publicized credit and housing market problems. Year-to-date (YTD), the broad-based US stock indexes are up in a range of 7.6% to 11.8%. Developed international and Emerging Market international stocks are both significantly outperforming the US indexes, and the REIT sector continues as this year's underperformer, after years of outperformance. See the third paragraph below for discussion of economic factors, and page 2 above for figures for the month, YTD, and since 1999.

BOND returns (price change plus interest) for all parts of the bond market were positive for the month. Prices and longer-term interest rates were essentially unchanged, with the positive returns coming primarily from the interest earned. The benchmark 10-year US Treasury yield closed at 4.58%, an increase of 3bp above August's level of 4.55%. The Federal Reserve, for the first time in four years, lowered the short term rate it controls, a move which, at least initially, was well received by the financial markets. Bond returns for the month, YTD, and since 1999 are set out on page 2 above.

ECONOMIC NEWS for the month indicated a weakening of the economy. The major news was a small decline in employment growth, following many months of gains (WSJ, 9/8-9, front page). Further, "tepid retail sales and manufacturing in August offered more signs that the US economy was softening" (Wall Street Journal [WSJ], 9/15-16, A3). The problems in the housing market continued, with home sales and prices declining (WSJ, 9/28, A3). Inflation figures continued within acceptable ranges (WSJ, 9/20, A4 and 9/29-30, A5).

Vic's Home Office Phone: 212-588-0015
Vic's Home Office Fax: 212-588-9032
Nick's Office Phone: 510-601-6662

From a longer-term standpoint, the current decade has seen a major bear market in stocks (3/00-3/03), followed by a 4 _-year recovery to current price levels. Relative to their 2000 highs, the Dow Industrials are 18% higher, the S&P 500 is at exactly the same level, and the NASDAQ a stunning 46% lower. Thus, the annualized returns for all three indexes since 2000 are far below their long-term average annualized returns. The mutual fund company Vanguard notes that from 1926 through 2005, in only six of 80 years did stock prices fall within 2%, up or down, of the long-term annual average return of plus 10.4%.

However, going back further to the bull market that began in 1995, all three major indexes have remarkably similar average annual returns (ranging from 9.9% to 10.6%), right at the 10.4% average annual return for stocks dating back to 1926. As these returns converge, "regression to the mean," described by Swensen as "one of the most powerful influences in the world of finance" (pg. 154), seems apparent. But Vanguard's observation is also meaningful, since annual returns during the bull market were far higher than the long-term averages, and the returns from 2000-YTD 2007 have been far lower.

The moral: Stock returns are truly unpredictable and volatile in short time frames, and can be over long time periods as well, even with (so far) a fairly stable very-long-term average return. Key Questions: Your relevant time frame and tolerance for risk.

	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)%
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)%
Year End 2005	1,248	(18)%	10,718	(9)%	2,205	(56)%
Year End 2006	1,418	(7)%	12,463	+6%	2,415	(52)%
Year-to-date 2007	1,527	0%	13,896	+18%	2,702	(46)%

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%
SEPTEMBER 2007	1,527	13,896	2,702
Gain	1,068	10,062	1,950
Avg.Ann.%Gain:'95-9/07; 12.75 yrs	9.9%	10.6 %	10.5 %

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

Vic's Home Office Phone: 212-588-0015
Vic's Home Office Fax: 212-588-9032
Nick's Office Phone: 510-601-6662

INVESTMENT CONCEPTS:

Economic Growth or Inflation, as Fed Lowers Interest Rates

The major financial and economic news of September was the Federal Reserve lowering the basic short term ("Fed funds") interest rate it controls by _ of 1% (50 basis points), from 5.25% to 4.75%. The reduction was presumably in response to: (a) evidence of slower growth in the broad US economy, including a negative growth rate in the month's employment report (WSJ, 9/8-9, front page) and a marked slowdown in retail sales figures (WSJ, 9/15-16, A3); and (b) more specific problems created by the severe slowdown in the US housing market, including credit-related issues and declining home prices.

Regardless of the reasons that went into the decision, the first in four years, to lower rates, a number of consequences are likely to flow from the action, and these consequences are likely to have a significant impact on the economy and the markets:

1) Lower short-term interest rates often lead to lower borrowing costs and more borrowing, which tends to stimulate economic activity.

2) Lower short-term interest rates often have a positive impact on corporate earnings, since they tend to stimulate economic activity and corporate sales while reducing borrowing costs.

3) Lower short-term interest rates typically have a negative impact on the value of the US dollar, which in turn tends to make goods and services imported into the US more costly, while making exports from the US more price-competitive. The former impact is thought to be inflationary, while the latter is considered a stimulus for economic activity.

In a WSJ article entitled "Which Way Is Scarier?" (9/24/07, C1), the dilemma is stated as follows: "The Federal Reserve cut interest rates last week in order to address a pressing concern: the risk of recession and of a breakdown in credit markets. By lowering rates before it really wanted to, however, the central back has revived another fear that has been dying down: inflation." (Our note: Te article should read "pressing concerns" in the plural, as there were two important concerns mentioned. This is not just a pedantic point, since the two concerns are both separate and significant on their own). The article states that "until the credit crisis struck, the Fed had signaled no intention of cutting rates so soon. Lower rates typically stimulate the economy by making it easier for companies, consumers and investors to borrow. If the Fed continues cutting rates before inflationary pressures have been stifled, it risks pushing inflation higher….Inflation could come from the still-booming global economy and from the lower rates themselves, which push more money into the economy, making it easier to raise prices….A weakening dollar also adds to inflation….While a weakening dollar helps US exports, boosting earnings for companies that compete with foreign multinationals, it also pushes up import prices, which can make inflation quicken." The article cites a counterargument that there are "no signs of inflation in import prices, because global competition is holding prices down."

Vic's Home Office Phone: 212-588-0015
Vic's Home Office Fax: 212-588-9032
Nick's Office Phone: 510-601-6662

Economist Ben Stein, who writes for the NY Times Sunday Financial section, added to the discussion on inflation and economic growth in a recent article (9/23/07, pg. 8). (It should also be noted that we have quoted extensively from Ben Stein's August articles on the mortgage and credit problems, in which he calmly and persuasively presented the case for stepping back and viewing the so-called crisis from the broader perspective of a huge and mostly well-functioning American economy). His major point is that "we do NOT know what causes inflation." He mentions a variety of theories: "'Cost push', which is a big increase in the cost of certain goods and services;" "'demand pull', which is when aggregate demand surpasses aggregate supply… But then came the stagflation of the 1970s, when we had slow growth, very sluggish additions to aggregate demand, and, still, powerful inflation… Then we had a very rapid rise in aggregate demand through the 1990s and very little inflation… Did loose monetary policy cause inflation?…maybe not, because after the tech sector collapse and the terror of 9/11, we had extraordinary monetary ease, and yet there was mild inflation… Rising productivity was offered as a reason for absorbing all of that monetary ease, but productivity growth was not unusually rapid from 2000 to 2006 and yet prices stayed well under control….The situation became far more mysterious after Hurricane Katrina devastated the gulf coast two years ago. We have had fantastic increases in the price of oil (along with relative monetary ease), yet inflation has not been rampant….To restate, we really don't know what causes inflation."

Stein continues: "We do know that if the Fed starts printing money, Weimar style, we will probably have inflation. Or maybe not. It may be that we can have a great deal of added rate-cutting without creating more inflation. In fact, with a severe falloff in the construction sector, maybe a rate cut will not do much to affect aggregate demand and cause inflation." He poses the following dilemma: "If a rate cut does not stimulate aggregate demand enough to cause inflationary headaches, why will it stimulate the economy enough to make us avoid a recession? If a rate cut does not cause inflationary jitters, is it causing any increase in aggregate demand beyond a placebo effect….The plain truth is we simply do not know how the various parts of the monetary machinery work on the economy. (We don't seem to know much about how the fiscal parts work either. Anyone who would have guessed that we could have run federal budget deficits the size of those since 2001 without major inflation would have failed any basic macroeconomics exam in 1996.")

The article then switches gears and discusses a few impacts of the rate cut, one of which is "that there are very real reasons that the stock market climbs as rates fall. Stocks are worth the net present value of their future earnings (or dividends), which are discounted back to net present value at the prevailing interest rate. If the rate is lower, the net present value will be higher." (Our note: one major counter to this point is that future earnings may well be lower, if the anticipated slower business conditions that were part of the rate-cutting rationale actually come to pass. Additional reasons and some history that questions the relationship between lower interest rates and higher stock prices appear in the next paragraph). The Stein article concludes that "we really have no idea what the inflationary risks are from the rate cut."

Vic's Home Office Phone: 212-588-0015
Vic's Home Office Fax: 212-588-9032
Nick's Office Phone: 510-601-6662

To add to the discussion of how the rate cut might affect the future direction of stock prices, a WSJ article (9/2707, C1) begins with the statement that "the idea that interest rate cuts are good for stocks is viewed as such an absolute truth on Wall Street that it isn't even a matter of debate. But the reality is a bit more complicated." The article proceeds to cite a number of times when rate cutting was not followed by a rising stock market, most recently the period of 2001-02. The article observes that "Fed policy is just one of many factors – including economic data, corporate reports, and political events – that influence financial markets. So it is tough to tell whether it is the Fed that is moving prices or something else…. Further, after investors' initial response there is little in the way of measurable follow through. The change in rates has, after all, been priced into the market. What's more, that initial movement can quickly be overwhelmed by other forces."

As regular readers know, we absolutely concur with the points made in the above paragraph. There are so many factors constantly affecting market prices that to try and single out one as a reason or cause for price movements over any significant period of time does not hold up. To quote Nick Taleb in his latest best seller, "The Black Swan": "Whenever there is a market move, the news media feel obligated to give the 'reason'….It happens all the time: a cause is proposed to make you swallow the news and make matter more concrete" (pg. 74) "You would expect our record of prediction to be horrible: the world is far, far more complicated than we think, which is not a problem, except when most of us don't know it" (pg. 135).

II. Hedge Funds

The past few months have produced negative results for many hedge funds, caught as they were in many unprofitable transactions involving the credit markets. Many hedge funds are marketed to ostensibly sophisticated investors as a way to avoid some of the downside associated with the twists and turns in a variety of markets (e.g., stocks, bonds, currencies, commodities, buyouts, derivatives, and on and on). Hedge fund managers are paid very high fees to accomplish this, so it is interesting when the markets deliver unexpectedly negative results to these managers and their investors.

Hedge funds are one of a number of so-called alternative investments, which refer to their being alternatives to traditional stock and bond investments. There are a number of different methodologies that hedge fund managers use, but rarely are they trying to achieve returns by actually "hedging." (This refers to the relatively conservative technique of buying and selling the same security, hoping to make small gains from some minor pricing inefficiencies but protected from any major moves in either direction since the net ownership position is zero). While hedging may have been the initial technique used by some of these funds, the current managers of hedge funds, needing to justify the very high fees associated with their endeavors, now employ a number of strategies designed to provide high returns, which means they must take on more risk. The recent results of some very high profile funds make this point quite clearly.

Vic's Home Office Phone: 212-588-0015
Vic's Home Office Fax: 212-588-9032
Nick's Office Phone: 510-601-6662

Perhaps the prime example is the Goldman Sachs Global Alpha hedge fund. Often described as Goldman's "flagship fund," during August it had its "worst month in the fund's 12 year history, down 22.7%, and for the year through the end of August, down 33.4%, due to bad bets on everything from the Australian dollar, the Norwegian stock market, and Japanese government bonds….Over the past 12 months, the fund has lost 37% of its value" (WSJ, 9/1407, C2). The article discusses the fund's approach in some detail: "It trades everything from currencies to stocks and bonds and uses a variety of strategies….Its dismal record this year is especially surprising because it is a multi-strategy fund and can engage in an array of strategies. In theory this should give it the flexibility to adapt to volatile and difficult markets and avoid problems arising from any single strategy. But over the past year practically everything went wrong. The problems show how one of the key dangers that have tripped up hedge funds in the current turmoil are strategies touted as unique but which channeled funds into very similar investments. Everyone got hurt when the investments wound up needing to be sold all at once….In a letter to its clients, fund managers blame some of the problems on the massive selling by other funds as credit suddenly dried up in early August."

A second group of poorly performing hedge funds was discussed in a front page WSJ article (9/7/07), describing so-called "quantitative traders," or "quants." "These traders use complex mathematical models to invest in markets around the globe. Their computers track a wide range of data and variables,…and formulas programmed into their computers spit out prices at which stocks or other instruments are to be bought and sold….Large investors such as pension funds have sought out these funds based on the steady returns they have produced….Against this backdrop, quant funds' turmoil in late July and early August was all the more disconcerting." The article then cites a number of well known funds and their losses during the period, and points out that "the summer woes remind some of the near meltdown almost a decade ago of high flying hedge fund Long Term Capital Management, which was steered by brainy academics who made money exploiting out of kilter relationships between different securities….Quants say their bad patch will be forgotten as their strategies continue to churn out steady profits….but even so, the outsized drops could dim the luster of the quant approach, especially since the quants themselves don't know for certain what triggered the carnage. A common theory is that one or more large funds was forced, possibly because of losses on sub-prime mortgages in other parts of its business, to rapidly dump stock to raise cash, and this set off a ripple effect among quant traders….The proliferation of quant funds holding a lot of the same positions may have been a recipe for magnifying the losses."

In our view, if downside protection is one of the attributes advanced by the hedge funds in the first place, and they deliver poor results when the markets are volatile on the downside, then a major justification for paying out high fees is lost. Recall David Swensen, head of Yale's highly successful endowment fund, advising individual investors in his book "Unconventional Success," to avoid hedge funds and invest using a handful of low cost, tax efficient, market mimicking index funds.

Victor Levinson **Nicholas Levinson**