



The Space Between the Notes

While rummaging through my office bureau, I discovered an old *Wall Street Journal* stashed away for posterity. The front page contained the following headline: “The S&P 500 fell 2.7% putting it more than 49% off its record and making this the worst bear market since the 1930s. Stocks were hurt in part by a downgrade of J. P. Morgan’s credit and worsening corporate earnings...”

It sounded familiar. I reached for *The Wall Street Journal* I had finished reading earlier that morning. The front page had the following headline: “J.P. Morgan Chase, now the biggest money-center bank by market value, is to report fourth-quarter results on Thursday, six days ahead of schedule. In mid-November it warned analysts it could add \$2.4 billion to its reserves for bad loans and that quarterly losses on its \$95 billion home-equity portfolio could be as much as \$850 million.”

The first article appeared on October 10, 2002, and the second on January 10, 2009. Of course, you can find a myriad of negative reports in the financial press that date back to the 1800s. It does not matter if the event occurred seven years ago or seventy. There have been stories of companies reporting quarterly losses as well as examples of financial fraud perpetrated on investors, including scandals, corporate malfeasance, and stock manipulation. When it comes to increasing their advertising revenues, you can rest assured that the media will always be available to refresh our memories as to how uncertain the economy, the markets, and the world are.

Why is it easier for the media to find things that can go wrong, especially in a recession? When the economy is doing well, potential problems for companies and investors are not so obvious. It is when they are faced with a recession and other financial challenges that problems are highlighted. There is a saying on Wall Street that “You can’t see who is swimming naked until the tide goes out!” In their wonderful book Manias, Panics and Crashes, Charles P. Kindleberger and Robert Aliber aver, “Soon after a recession appears likely, the loans to firms that were fueling their growth with credit declines as the lenders become more cautious about the indebtedness of individual borrowers and total credit exposure. In the absence of more credit, the fraud sprouts from the woodwork like mushrooms in a soggy forest” (165).

So it is that Wall Street is littered with a plethora of disaster stories during economic slumps. If you recall, in the 1980s when junk bonds reigned supreme, the government-sponsored Resolution Trust Corp bailed out hundreds of saving and loans. This was followed by the sudden demise of the corporate bond giant Drexel, Burnham, Lambert, who sold these bonds. A decade later we witnessed the collapse of Long-Term Capital Management, one of the largest hedge funds in the world. These were significant financial catastrophes that rocked the markets and economy at the time. Amidst all this fear and uncertainty, investors somehow managed to survive, and eventually the market climbed to new highs.

REGISTERED INVESTMENT ADVISOR

Paragon Capital Management 10 Edgewood Avenue Smithtown, New York 11787
PHONE (631) 863-2700 FAX (631) 863-2706 www.pcmwm.com

Our task is to increase our awareness and realize that history repeats itself. Recessions and financial crises typically are followed by times of growth and prosperity. It's all a cycle. Instead of becoming fearful, maybe this could be an opportunity to look at things in a new and different way. New age thinker Wayne Dyer says it so well: "When you change the way you look at things, the things you look at change." Though the financial news seems grim and we are encountering adversities, we have, as Dyer noted, an opportunity to see things differently.

Perhaps that ability to see things differently for me is the direct result of my college music teacher. As many of you know, in addition to receiving a Masters Degree from Columbia University, I am also a serious student of classical piano. When I was in college, my teacher, whom I studied with privately, was a very well known concert pianist. Not only was she knowledgeable about the history and the structure of music, but also she possessed a keen insight into the meaning the composer was trying to convey. Whenever I studied a musical work, my teacher would challenge me to look beyond any preconceived ideas of how the piece should be performed. I recall a particular lesson, a lesson where I expressed my frustration with the interpretation. She turned to me and said, "Have you tried to listen to the space between the notes?" I realized she was asking me to hear the piece differently. She was suggesting there was an alternative way to hear the music and mentioned that some of the greatest musicians in the world, including Artur Schnabel and Issac Stern, heard the space between the notes. Or as composer Gustav Mahler said, "It is not the notes being played, but it is the silence between the notes being played that contains what is best about the music."

This metaphor can be useful in the current economic environment, especially when news comes out that appears particularly upsetting. It may be possible to view it in a different context and see opportunity where others have fear and see only collapse.

The following are questions from clients, especially those retired and living on a fixed income, who are deeply concerned about the future.

Frequently Asked Questions

Question: "What is the possibility of another Great Depression similar to the one in the 1930s?"

Answer: We believe this is unlikely. The Great Depression of the 1930s was dramatically different from the recession we are currently experiencing. From 1929 to 1933, Gross Domestic Product in the United States declined significantly. Unemployment reached almost 25%! The situation is totally different today. Certain regions may experience higher or lower rates of unemployment. Some of these reports can be skewed as well because they don't take into consideration the fact that some workers losing their jobs can, among other things, be taking an early retirement or just be in the process of changing jobs. I feel strongly that the economy may contract a little in 2009 but nothing in comparison to the magnitude of the Great Depression.

Question: "The stock market was down today. Will it ever go up again?"

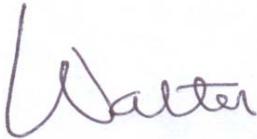
Answer: Well, if we compare the stock market in the fall to the present, we will notice market volatility—as measured by the VIX index—has decreased significantly. The volume of selling has also decreased. These are very positive developments, possibly signaling an end to the current downtrend.

Question: "The debt markets are struggling. Why aren't banks lending?"

Answer: Based on information we have received it appears that banks are lending to creditworthy customers. The yields on overnight loans to businesses have declined significantly since the credit crisis in

While some of you may be listening to the news of the *Wall Street Journal* or other news sources exclusively, I am encouraging you—as I did with my college music professor—to listen differently. When we do this and become more proactive in our thinking, we will become more effective at finding solutions. If we trust in each other to accomplish what needs to be done, I believe we can overcome the current challenges. If you trust in me to guide you during this financial crisis, we can accomplish much more together rather than on our own. I look forward to meeting with you face-to-face in the weeks and months ahead.

Note: In office news, we are installing video monitors in the conference room and reception area. The ones in our conference room will make client data more accessible in our meetings. Furthermore, Rita Barrera has decided to follow a path focused on divorce financial planning. We wish her well. In the meantime, we are in the process of interviewing candidates for a financial planning position from a pool of very bright and talented individuals.



Walter Wisniewski, President
CERTIFIED FINANCIAL PLANNER™ practitioner
Paragon Capital Management

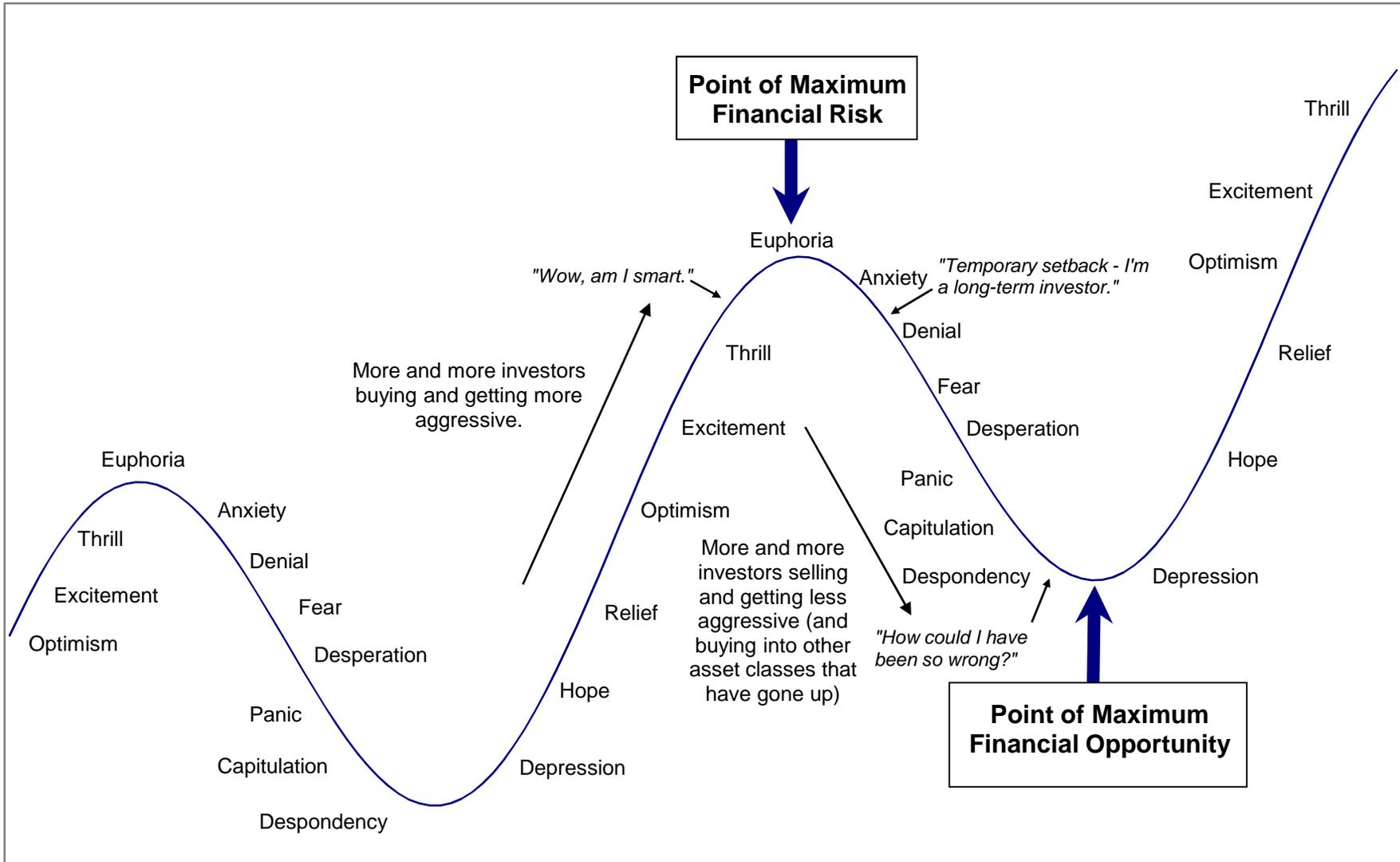


REGISTERED INVESTMENT ADVISOR

Paragon Capital Management 10 Edgewood Avenue Smithtown, New York 11787
PHONE (631) 863-2700 FAX (631) 863-2706 www.pcmwm.com

The Cycle of Market Emotions

Where are you in the cycle?



This presentation is intended to demonstrate certain emotions that may be experienced by investors implementing a long-term investment strategy during rising and declining market cycles and is not intended to represent a comprehensive list of emotions each investor may experience based on their individual risk tolerances and investment objectives. Source: Janus and Paragon Capital.