

The Fed at it Again

Market Summary

September 2007

After a flat first half of the month, stocks resumed their rebound in the last two weeks of September after the Fed surprised the market by cutting the overnight lending rate by 50 bps instead of 25 bps. The cut sparked world markets, leading to ample returns for most major indices.

moderate growth over time.” This aggressive movement by the fed helped to improve conditions in the commercial paper market and improve the sentiment in global equity markets. While it showed that the Fed under Bernanke’s leadership is willing to step in and inject liquidity during periods of stress, it’s unclear how much impact it will have on the economy and what the unintended consequences might be.

	September	YTD	1 Yr	3 Yrs	5 Yrs
Domestic Equities/Fixed					
S&P 500	3.7	9.1	16.4	13.1	15.5
Russell 2000	1.7	3.2	12.4	13.4	18.8
Russell 1000 Growth	4.2	12.7	19.4	12.2	13.8
Russell 1000 Value	3.4	6.0	14.5	15.3	18.1
Dow Jones Wilshire REIT	3.9	(4.6)	3.8	19.6	21.9
Lehman Aggregate Bond	0.8	3.8	5.1	3.9	4.1
International Equities					
MSCI EAFE	5.4	13.2	24.9	23.2	23.6
S&P/Citigroup EMI-EPAC	2.9	11.5	26.1	27.5	29.4
MSCI Emerging Markets	11.0	34.5	58.2	40.8	38.7
Alternative Assets					
GS Natural Resources	8.5	28.5	40.9	29.1	29.7
DJ AIG Commodity	8.0	11.0	17.0	9.5	14.1
HFR Fund of Funds	2.4	8.5	14.3	10.5	9.2

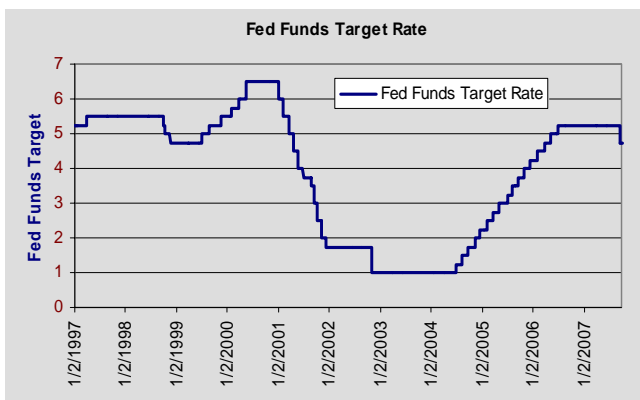
Currently, federal funds futures are predicting that another 25 basis point rate cut is likely by year-end.

Domestic Markets

After the rate cut, domestic markets saw steadily positive returns. U.S. equities ended the month higher, led by large cap stocks. The Russell 1000 Growth, S&P 500, and Russell 1000 Value indices ended September higher by 4.2%, 3.7%, and 3.4%, respectively. Small caps didn’t fare as well, yet still ended the month in positive territory, as the Russell 2000, Russell 2000 Growth and Russell 2000 Value indices returned 1.7%, 2.9%, and 0.5%, respectively. A decline in interest rates during September helped bonds gain 0.8%, as well.

Federal Reserve

On September 18th, the Federal Open Market Committee decided to lower its target for the federal funds rate by 50 basis points to 4.75 percent, representing the first rate cut in more than 4 years.



This cut was in reaction to tightening credit conditions and fear that credit woes will spill over into the economy as a whole. According to the FOMC, the action was “intended to help forestall some of the adverse effects on the broader economy that might otherwise arise from the disruptions in financial markets and to promote

International Markets

Overall, international stocks fared better than their U.S. counterparts, with the MSCI EAFE ending the month up 5.4%. International small cap equities returned 2.9% and emerging market equities rose by 11.0% during September and are the best performing asset class for the year-to-date, and trailing one-, three-, and five-year periods.

Alternative Assets

After a rough August, alternative assets posted outstanding gains in September. The DJ-AIG Commodity Index returned 8.0% in the month, while natural resource equities earned 8.5%. After a turbulent beginning to 2007, REITs posted strong returns for the second consecutive month, gaining 3.9% in September. Coming off their worst month since April 2000, hedge funds posted positive returns, as the HFR Fund of Fund index earned 2.4%.

Volatility

Equity markets saw weak returns in the first 10 days of the month, followed by steady positive performance thereafter. A rally followed the Fed meeting, advancing markets to close the month on a positive note. The Volatility Index (or “VIX”), coming off a four year high in August, dropped roughly 30%, ending the month at 18.

The Falling Dollar

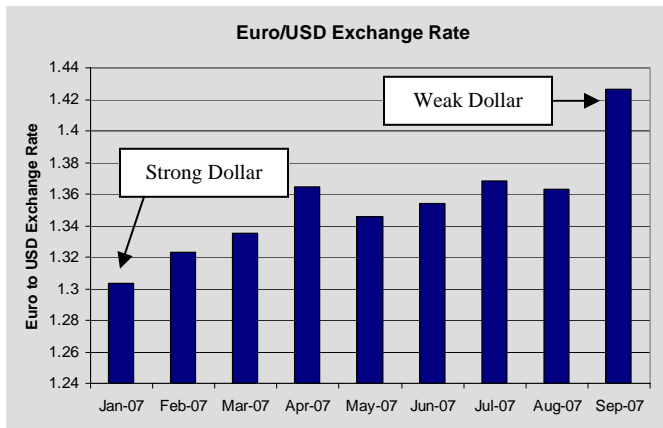
The dollar struggled in September, falling against most major currencies. The euro strengthened by nearly 5% against the dollar, while the yen and pound rose by roughly 1% against the dollar. Some of this decline can be attributed to the Fed’s decision, which caused other currencies to become more attractive on the basis of yield.

appropriately balanced between short-term risk exposure and long-term growth. Adding alternative, diversifying investments like private equity, real assets, and hedge funds will not only provide balanced portfolio volatility, but should prove accretive to long-term portfolio returns.



Scott Zipfel
Associate Consultant
Hammond Associates
101 S. Hanley Rd, 3rd Floor
St. Louis, MO 63105
314-746-1600
www.hammondassociates.com

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While this decline is good for American exports, it is bad news for American consumers, making foreign goods more expensive, leading to an overall decline in purchasing power.

Conclusion

Market and economic changes in September were plentiful. The recent aggressive action by the Fed boosted equity markets, leading to a banner month for most major market indices. Coming off a shaky August, alternative assets posted strong returns, with commodities and natural resources earning the lion’s share. Volatility sharply declined in September following a fickle August. The dollar continued its descent in reaction to falling interest rates and inflation concerns. A myriad of events such as these truly emphasizes the importance of a prudently constructed portfolio. We believe clients should be