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Fed Quarter Cut Disappoints Markets

by [Paula Schaap, Reporter](#) , December 11, 2007

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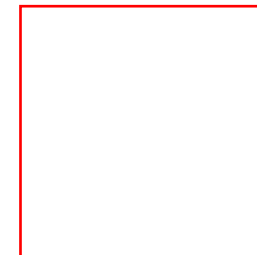
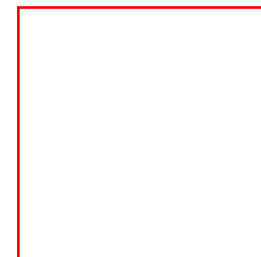
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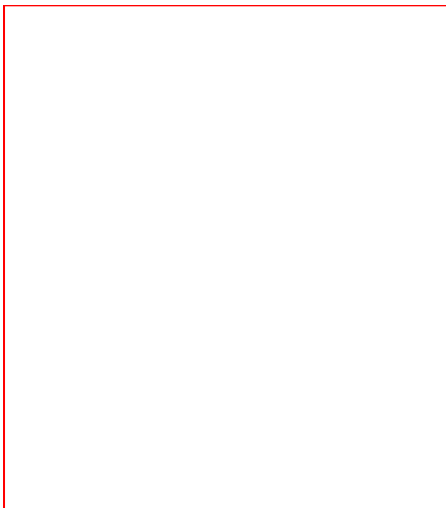
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Hedge fund firms waiting for news of a rate cut from the U.S. Federal Reserve got some of what they wanted when the central bank lowered the federal funds rate 25 points to 4.25%.

The big question was whether it would be enough to rescue those funds that had a hard month in November when equities markets dropped in the face of increasing strains from subprime mortgage defaults and the consequent credit crunch.

“Incoming information suggests that economic growth is slowing, reflecting the intensification of the housing correction and some softening in business and consumer spending,” the Fed said in a statement.

November was a tough month for hedge fund firms, the second worst since August. The Hedge Fund Aggregate Average was down .89%, as compared to August’s drop of 1.56%.

The worst off were those firms whose strategies were tied into the November drop in the markets.

Some analysts had speculated that the Fed would go down a full 50 basis points in the face of severe financial turmoil.

Indeed, investors seemed to say that 50 would have the preferred antidote to their woes, as the market took a sharp dip after the 2:15 p.m. announcement. Right before the Fed announcement, the Dow Jones Industrial Average was up 40 points; within the half hour, it had fallen more than 200 points. The S&P 500 dipped about 25 points while the NASDAQ Composite dropped to 45 points.

Steven Sheldon, director of Houston-based SMS Capital Management, said that he expected a post-Fed cut selloff.

“I don’t think it will be severe,” Sheldon said, “but I think there will be some interest in taking some money off the table.”

J. Scott Sykora, president of LJM Partners agreed with that assessment.

“I’m not expecting anything dramatic; no more than a slight selloff or a slight rally.”

The Fed held out hope that another rate cut could be in store if this one did not restore market stability.

In a related action, the Fed also approved a 25 basis point cut for the discount rate, or the rate banks use to loan money to each other, to 4.75%. The move was seen as the Fed’s way of loosening up credit for investment banks that have been forced to write-off tens of billions of dollars for securities linked to subprime mortgage assets.

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