WARRINGTON
ASSET MANAGEMENT

April 2007 Market Commentary

The performance for the Warrington Fund for the month of April can be easily summarized using one statistic: from the beginning of the month through options expiration day (April 20th), the S&P futures were up every single day, but one. This run was over the course of 14 trading days and constituted a 4.33% increase over that time span. While this in isolation is noteworthy, it becomes even more astounding when you consider that from the lows seen in the middle of March, the S&P futures had already rallied 4.93% to the end of March. So for the entire move, from mid-March to options expiration on April 20th, the S&P futures rallied 9.46%, performance which would make many money managers happy for an entire year, let alone for the span of a month and a half.

Coming into April on the heels of an already impressive rally, we were positioned for the market to pull back to a certain extent, with ratio put spreads in place and limited synthetic long call exposure against our short call exposure. Those short calls were initiated when the market began its rebound in mid-March, while the VIX (the CBOE Volatility Index) was rather high, making the prices worth the risk that the options represented. As time progressed and the market continued to rally, we began hedging these positions. Then during the week leading up to options expiration, the S&P futures accelerated its upward trend and risk management dictated that we cover the majority of our short calls. This move, although it caused us to incur a loss for the month, proved prescient as the market continued to surge higher through the rest of the week.

The fact that the market surged so much higher after making lows in February and March shows yet again how market participants are discounting possible underlying risks to the stock market in pursuit of returns. For our May positions, initiated in the middle of April, we remained in a defensive posture, with wide ratio put spreads and limited short call exposure. Rallies such as this one have a tendency to go on for longer and go much higher than might seem rational, and therefore, we chose to focus on risk management (especially with our call exposure) and position the portfolio to benefit from market retracement, which is destined to occur at some point.