WARRINGTON
ASSET MANAGEMENT

April 2011 Market Commentary

Historically, a "normal" month for the stock market consisted of a series of up and down days resembling a tug-of-war with multiple back and forth moves. That pattern changed significantly with the Federal Reserve's announcement of the second Quantitative Easing program in late August of 2010 (known as "QE2"). Stock market action became very directional, with consistent steady gains and little to no downside activity. Now that the QE2 program is nearing its stated expiration date of June 2011, markets have been trading in a more normal up and down pattern, leading to significantly better opportunities for the Warrington strategy.

April started off flat, but then markets started to decline as options expiration approached. Sensing this decline, the manager positioned the Warrington portfolio in ratio put spreads. The decline continued, as the S&P 500 futures fell 2.79% in the week preceding options expiration. The manager closed these spreads profitably over the course of options expiration week, accounting for the majority of the profits earned in April.

Ratio Spreads were then rolled to the April month end expiration, which would profit if the S&P continued to drop into the end of the month. Within days of implementing this position, Standard & Poor's (a rating agency) put the US treasury debt on negative watch, essentially telling the US government that it should address its spendthrift ways or the country's debt might lose its triple-A rating, a step that would have severe negative repercussions for the government and its citizens. This "shot across the bow" sent the S&P futures down 2.18% initially, but then the stock market turned and rallied 5.4% to end the month positively. This rally caused the end-of-month ratio put spreads held in Warrington's portfolio to expire worthless. In spite of this, April proved to be a good month for Warrington.