WARRINGTON
ASSET MANAGEMENT

February 2012 Market Commentary

February trading proved to be exactly similar to January, in that the S&P futures exhibited almost no volatility and continued the steady grind higher that has punctuated periods of massive central bank action in recent years (in this case, the European "Long Term Refinancing Option II", begun in earnest last December). Not only was the month lacking downside volatility, but upside volatility was non-existent as well. The March S&P 500 futures contract never closed down more than 1 percent and only closed up more than one percent one time (gaining 1.22% after the January Employment number was released). In fact, according to Bloomberg, the decline in equity market volatility this year is as great as it has been since 1934.

Trading activity in January and February has exhibited another relevant statistic, in that the rally this year has already attained the level equal to the consensus year-end price target of the majority of forecasters. Warrington believes it is important to compare this to the same period last year, when the consensus year-end price target forecast was reached in the first three months of the year, but was followed by extremely difficult markets for the balance of the year and proved the forecasts to be significantly inaccurate, as most markets closed poorly for the year. In this environment, Warrington's strategy worked admirably, as our 8.55% net return provided the non-correlated performance we aspire to give our clients.

As was the case in January, Warrington held ratio put spreads in the portfolio in anticipation of a decline that never materialized. The loss on the month was due to the cost of those spreads and from the small expenditures from modifying the position as the market slowly marched higher. At the end of February, the manager held March positions in the portfolio to attempt to capture downside volatility in the S&P futures contract should such a pullback happen. The market's internals (for example: a decreasing amount of stocks making new 52-week highs even as the market achieves new highs, and the decreasing level of total trading volume as the market climbed) have started to deteriorate as the recent rally has become more and more extended, increasing the likelihood for such a decline to occur.