WARRINGTON
ASSET MANAGEMENT

March 2013 Market Commentary

Most investors throughout the world consider deposits at their banks to be sacrosanct; the money deposited with the bank for safekeeping and for emergency use will be available when needed. The recent bank closures and levies applied in Cyprus have reminded depositors that this is not always the case. If such a step can be taken in a small European Union country (one with an essentially insolvent banking system), then how much worse do the banks of Greece, Portugal, Spain and Italy need to deteriorate before such a drastic measure is enacted there as well?

News of this depositor levy was first floated over the weekend (March 16th and 17th), and world markets dropped materially when they opened that following Monday. On that day, the S&P 500 futures declined 1.8% overnight and seemed poised for further losses in the day session. However, once trading began markets stabilized and continued the consistent grind higher that has been the hallmark of U.S. equity markets so far this year. The Warrington Fund was holding ratio put spreads in anticipation of a decline, which initially gained value after the Cyprus news. The S&P 500 continued its ascent through the end of the month, causing those ratio put spreads to decrease in price. The manager was able to capture some value from those positions by rolling them into April ratio put spreads, on the anticipation of a pullback in equity prices.

As history often rhymes, the first quarter of 2012 was eerily similar to the first quarter this year: the U.S. stock market displayed very little volatility and had consistent, steady gains. At the onset of the second quarter of 2012, volatility resumed with a vengeance and Warrington was able to capitalize on the choppiness in the equity markets. The manager anticipates similar behavior and is positioning the portfolio for a continued parallel to last year.