WARRINGTON
ASSET MANAGEMENT

May 2006 Market Commentary

In what turned out to be a very volatile month, May started where April left off: with minimal volatility and no real direction in trading of the S&P 500 futures. Only a few days into the month, the S&P drifted up to new highs for the year. Then on the 10th of May, the Federal Open Market Committee Monetary Policy Statement from Federal Reserve was released, with little fanfare initially. However, the next day, the hawkish tone of the Federal Reserve sparked a dramatic decline in the S&P 500 futures, which would end up being a 6.1% decline over the ensuing two weeks. Given this extreme volatility, we chose to hedge our downside exposure on both May and June positions. This hedging resulted in a small loss on May positions, but our June positions, although only a quarter of the size of a normal trade for us, were deep in-the-money. After May options had expired, we further hedged our June positions and made some trades to protect the portfolio against a sharp contra-trend rally. From the lows on May 24th, the S&P 500 futures did see a strong rally near the end of the month, climbing almost 3% in three days. The wide put spread as well as the positions to protect against a strong rally enabled Warrington to post positive returns despite a very volatile trading environment.