WARRINGTON
ASSET MANAGEMENT

December 2016 Market Commentary

After a brief pause at the beginning of the December, the S&P 500 index resumed the upward trend that has been in place since the U.S. Presidential election concluded. However, after gaining 4.1% from the lows of early December, the S&P's ascent then stalled out and did so in remarkable fashion. The S&P experienced three consecutive "Inside Days," a feat never seen in its history (an Inside Day is when the high for the index is lower than the previous day's high, and the low for that same day is greater than the prior day's low). Two consecutive inside days happens on average once per year, but December's three in a row was the first time it has ever occurred. This lethargic trading behavior indicated to us that the recent rally might moderate or potentially decline.

In the Strategic program, we attempted to capitalize on this anticipated decline by using ratio put spreads. Additionally, we knew that the S&P 500 fell sharply on the first few trading days of January 2016 and as some traders say "market activity doesn't repeat, but it often rhymes." If other market participants anticipated a similar scenario, then selling pressure before such a possible drop could materialize in late December. The market did indeed drop on the last few days of the month, allowing our ratio put spreads to become profitable resulting in a monthly return of approximately 0.62%.

In the Tactical strategy, the drop in trading range volatility benefitted our positions and led the trading program to its best monthly return of the year. The short calls and puts held in the portfolio all expired worthless resulting in a monthly return of approximately 0.92%.

December added to what was a very good year for stocks overall and returns for the broader stock market indices have been consistently good for the past few years, causing some investors to question the need for proper diversification. It may be tempting to chase stocks after such performance but the pages of stock market history are littered with instances where investors have crossed the line from prudent "investing" to simply "gambling" which has often ended in disaster. Maintaining focus and investment discipline during periods of exuberance, whether rational or irrational, is critical during these times and we believe that Warrington's place in a diversified portfolio has served our investors well during both positive and negative periods for the market indices.

We are venturing into a period where U.S. and global leadership is changing radically and we are exposed to economic and geopolitical shocks on a frequency rarely seen in our history. As Americans, and participants in the global financial landscape, we remain optimistic but as investment professionals who have been successfully operating our strategies for over two decades, we also understand the importance of objectively employing our trading methodologies and protecting the long term financial goals of our investors.

As always, we thank you for your continued support of Warrington Asset Management.