WARRINGTON
ASSET MANAGEMENT

July 2018 Market Commentary

The S&P 500 Index ("Index") marched higher for most of July, encountering resistance only in the last few days of the month. The upward move in July was surprisingly non-volatile, as markets seemed to ignore many of the concerns that have previously impacted them, including trade wars, retaliatory tariffs, and the Putin/Trump summit in Helsinki. Positive news regarding trade concessions from the EU buoyed the markets late in the month, only to have Facebook then suffer the largest one-day market value decline in U.S. history, dragging indices lower. The subsequent losses in FAANG stocks, which represent 12% of the Index's market capitalization, have driven much of the growth in the S&P 500 this year. The massive declines and widely held nature of these stocks could cause investor fears to spill over into the broader stock markets, as similar losses in tech stocks did in the early 2000s.

The Strategic program delivered a positive return of 0.27% in July. As the Index climbed throughout the month, the program used ratio put spreads attempting to profit from mean reversion in the Index. These early spread positions accrued small losses from the debit costs of the spreads. However, as the market pulled back towards the end of July, additional ratio put spreads were employed to capitalize on our market analysis, leading to a profitable month.

The Tactical program had a solid month and delivered a positive return of 1.16%. The program was able to profitably employ both puts and calls to deliver these returns, despite some debit costs from risk management hedging trades. Even though headline volatility was not high, the implied volatility in some option prices has remained elevated, most likely due to the consistent geopolitical issues which continue to resurface. This volatility discrepancy provided ongoing profit opportunities in July.

While July seemed to break from our standing view that markets are returning to a period of higher volatility, we were able to take advantage of the volatility that did appear at the end of the month and deliver positive returns to our investors. We remain focused on the long-term implications of a changing market environment, which is transitioning from one based upon artificial support of the markets by the Fed to one that is based on true market fundamentals. We believe that the current period of positive employment and GDP growth figures will encounter increased headwinds and will naturally give way to a period of more normalized volatility.

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