

WARRINGTON

A S S E T M A N A G E M E N T

May 2019 Market Commentary

The S&P futures contract trades almost 24 hours a day during the week, from Sunday evening through Friday afternoon. During “normal” market periods the price of the S&P will move moderately when the underlying equity markets are closed. During “volatile” times, where global events are at the forefront of investor concerns, the reduced liquidity in the overnight sessions can amplify moves and cause abnormally large gaps (the change in price at the open versus the prior day’s close). In May, the S&P futures dropped -8.9% cumulatively during the overnight trading sessions but the net change on the month was less severe, at approximately -6.7%. As Chinese tariff issues resurfaced and with a new threat of tariffs against Mexico, overnight markets seemed to dictate the tone for the full days’ trading, leading to increased volatility in equity markets.

The renewed volatility in May provided increased opportunities for the Strategic program, resulting in a solid monthly return of +1.12%. Unlike other recent reversals in the S&P, the market declined steadily throughout the month, yielding consistent profits in all five contract expirations traded. As we have discussed in our recent commentaries, we believed the potential depth of the reversal could be significant so we utilized positions with strikes farther away from the market, adding an additional margin of safety to protect against increased volatility. Though the price action in the S&P was elevated, the volatility (as measured by the VIX) peaked at 23.4, significantly lower than December’s high of over 36.

The Tactical program was flat in May, posting a return of -0.02%. With much of the price movement in the S&P occurring overnight, the excessive price gaps triggered our risk management protocols, causing us to close a few trades during the month for small losses to protect investor capital. As volatility did not significantly expand, the opportunity set for potential trades remained limited and left few risk-appropriate opportunities.

This type of environment, dominated by sporadic announcements and rumors concerning trade and tariffs, is often labeled “Headline Roulette.” These periods are filled with unknown risks, where we have systematically opted to err on the side of conservatism and select only those trades that meet our risk/reward parameters. May’s returns reflect the implementation of a strategy developed over decades dedicated to prudent selection of profit opportunities in any environment. One thing that is evident is the base level of volatility has increased in recent months. We believe this pattern will continue and present additional trading opportunities for Warrington’s programs and our clients.

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