WARRINGTON
ASSET MANAGEMENT

March 2020 Market Commentary

As predicted in our prior commentaries, the potential for the novel coronavirus to severely disrupt the global economy was real and came to fruition much faster than anticipated. The result was one of the worst months in stock market history, as the major U.S. stock indexes recorded the fastest decline from all-time highs to bear market territory ever (defined as a 20% decline). The damage was not limited to equity markets, as extreme volatility buffeted almost every asset class, including many which are normally "safe havens" such as government bonds and gold. The S&P recorded its most volatile month ever, with average daily ranges of 4.8%, while US treasuries dipped into negative yields and crude oil plummeted by 66% during the first quarter.

To combat these massive dislocations, the Federal Reserve cut interest rates aggressively (to effectively zero) and implemented an unlimited Quantitative Easing (QE) program to flood markets with liquidity. Uncharacteristically, equity markets reacted poorly to these initial measures, selling off after each program was announced. Stocks eventually responded positively to the two trillion-dollar fiscal stimulus, dubbed the "Coronavirus Aid, Relief, and Economic Security Act", which was signed into law on March 27th. Even with these aggressive maneuvers, the S&P 500 ended the month down 12.5%, after falling as much as 25% during March and, at the worst point, registering a 36% peak-to-valley decline from the all-time highs reached in February.

The Strategic program was able to opportunistically find profitable trades (a put spread early in the month and a call spread later in the month) to record a gain of 0.13%. More importantly, we successfully avoided the historic volatility brought on by the pandemic as well as the aggressive governmental responses to it. As we stress to investors, risk management is paramount at Warrington, especially in times like these where it is impossible to predict the impact of the global pandemic, and where the damage done to poorly-managed portfolios can take years to repair.

The Tactical program avoided all downside exposure during March, as many of our indicators have been alerting us to extreme danger (some dating back to late January). Instead, we opted to exclusively use call options to capture profits of +0.01%. The extremely high VIX level allowed us to sell calls significantly above the market, with strikes near the previous all-time high S&P levels.

Markets and the global economy are still consumed by the daily negative news, as very little is known about the future economic impacts of the virus and most major US and Europe cities are on lockdown or subject to stay-at-home orders. For every day that such isolation continues, the magnitude of the economic impact and investor uncertainty grow. We feel it is too early to speculate on how severe the contraction will be, but do believe a deep recession or possible depression is almost a certainty. In such an environment volatility will continue to be elevated, even as stock markets digest and try to discount the deluge of news containing conflicting forecasts from economic pundits and medical experts. We believe our decades of experience managing client capital through many global disasters leads us to effectively gauge risk and make the difficult decisions needed to protect investor capital. Our ability to be patient and look carefully for trading opportunities in up, down, or sideways markets will lead to increased trading opportunities, which we believe will result from the current chaos.

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