July 2020 Market Commentary

The stock market continued to climb in July, with all major U.S. indices posting gains. However, the economic reality underpinning these markets reflected a very different reality, with Q2 GDP registering the worst decline since the Great Depression, corporate earnings dropping -34% (according to *The Wall Street Journal*) and daily records for Covid-19 positive cases spreading all across the country. Hopes for continued stimulus, further Federal Reserve ("Fed") easing and talks of a vaccine helped buoy equities, while advances in large-cap technology stocks proved to be a driving force, as the Nasdaq advanced almost 7%. As the month concluded, many fiscal stimulus programs were set to expire with congress yet to extend those benefits. Market expectations are for those unemployment payments and eviction and foreclosure moratoriums to be extended, but as seen in prior crises, politics often can stymie such negotiations.

The Strategic Program took advantage of the relentless grind higher by realizing profits on call spreads. While expected volatility has remained elevated above historical averages, the actual market trading ranges have been more compressed. This dislocation creates additional trading opportunities, with wide option call and put spreads that offer the potential for outsized profits, which may not be realized if the market does not move into those ranges. Due to the debit cost of positions outweighing the profits from call spreads, the net return for July was -0.07%.

The Tactical Program also benefitted from the higher expected volatility, as we welcomed the opportunity to profit from volatility anomalies while maintaining our risk management protocols. We realized gains from all of our call and put strangles, even while maintaining our cautious approach. At the end of July, the Tactical Program achieved a net return of +0.38%.

The growing disconnect between economic reality and the strength of the U.S. equity market recovery can be attributed to the anticipation of continued stimulus from the Fed controlling interest rates and more direct government stimulus to relieve the stresses brought on by continued virus-related demand destruction. A key question is whether the economy, regardless of the timing of a vaccine, can regain its pre-pandemic footing before stimulus efforts are curtailed. With an election looming, it is likely that the political will to maintain the stimulus is there, but at some point the long-term costs of such actions may force a degree fiscal restraint. A day of reckoning will materialize and we will continue to be sensitive to the market pricing and those other indicators that will highlight its arrival.

We will continue to focus on profit opportunities in every market environment and, as always, we thank you for you continued support of Warrington Asset Management.