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Monitoring Your Covered Call Trades

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Any strategies discussed, including examples using actual securities and price data, are strictly for illustrative and educational purposes and should not be construed as an endorsement, recommendation, or solicitation to buy or sell securities. Past performance is not a guarantee of future results.

Presentation Outline

- Covered Call Position Management
  - Stock Rallies
  - Stock Consolidates
  - Stock Declines
- Variations
- Myths & Misconceptions

Position Management Techniques

Basic Management Concepts

- Getting out – always a consideration
- Accepting assignment / early exercise for dividend
  - Anticipate when little or no time value remaining
- Rolling (up, down and/or out)
  - Close existing contracts & open new ones
  - Pay or receive additional premium
  - Buy or sell more time
- Avoid selling stock and leaving a naked short call
  - Large margin requirements possible

Stock Rallies

- Rolling up (aggressively bullish)
  - Buy to close short call and sell to open higher strike call
  - Always at net debit
  - Raises BEP by debit amount
  - Increases maximum profit potential
- Rolling out
  - Buy to close short call and sell to open a call option with a later expiration date
  - Always a net credit (if same strike)
  - Could consider rolling up and out
- Close the position
  - Call is ITM with little or no time value
- Accept assignment
  - Comfort with selling shares at strike
  - Capital is free for a new position

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Stock Consolidates (unchanged)

- Sell another call
  - Could execute before (roll out) or after expiration
  - Maintains moderately bullish outlook
  - Consider changing strike price
- Close the position
  - Bullish outlook is uncertain
  - Reallocate capital to another trade
- Implement a different strategy
  - Hold shares
  - Protective Put
  - Covered Strangle (sell call and put)

Stock Declines

- Hold position
  - Maintains bullish outlook
  - Unrealized loss could increase
- Get out
  - Be true to your discipline
  - Know your risk tolerance
  - Sometimes the most difficult trade is to close at a loss
- Roll down
  - Buy to close short call and sell to open lower strike call
  - Always at net credit
  - Lowers BEP by credit amount
  - Decreases maximum profit potential

Variations of the Traditional Covered Call

Staggered Strikes (Example)

Sell various quantities at different strike prices:

Example: **Stock trading $110, long 500 shares**

- Sell 1 30-day 112 call at $3.00
- Sell 1 30-day 115 call at $1.80
- Sell 1 30-day 118 call at $1.00
- Sell 2 30-day 120 calls at $0.70

Total Credit of $720

Staggered Strikes

Advantages (A) and Disadvantages (D) of staggering strike prices:

- (A) Gradually scaling out of the stock position at higher levels provides opportunity for greater profits
- (A) Greater chance that a portion of the stock position will not be assigned

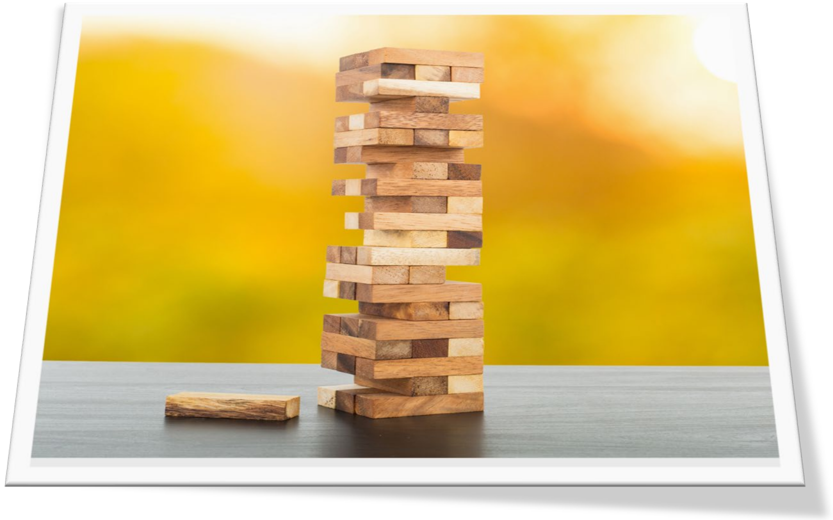
- (D) Less premium received compared with selling entirety of calls at a defined lower strike
- (D) Added layer of execution and position management complexity

Staggered Strikes and Expirations

Sell various quantities at different strike prices and expiration dates:

Example: **Stock trading $110, long 500 shares**

- Sell 1 10-day 112 call at $1.00
- Sell 2 30-day 115 calls at $1.80
- Sell 2 40-day 120 calls at $2.00



Total Credit of $860

Staggered Strikes and Expirations

Advantages (A) and Disadvantages (D) of staggering strike prices and expiration dates:

- (A) Greater flexibility to choose time durations that encompass various rates of time decay
- (A) Ability to choose higher strike prices which provides added room for profitability from share price appreciation

- (D) Longer dated options will have slower time decay
- (D) Longer expirations provide the stock more time to make an adverse move to the downside

Myths & Misconceptions

Myths & Misconceptions

1. The larger the premium, the better.

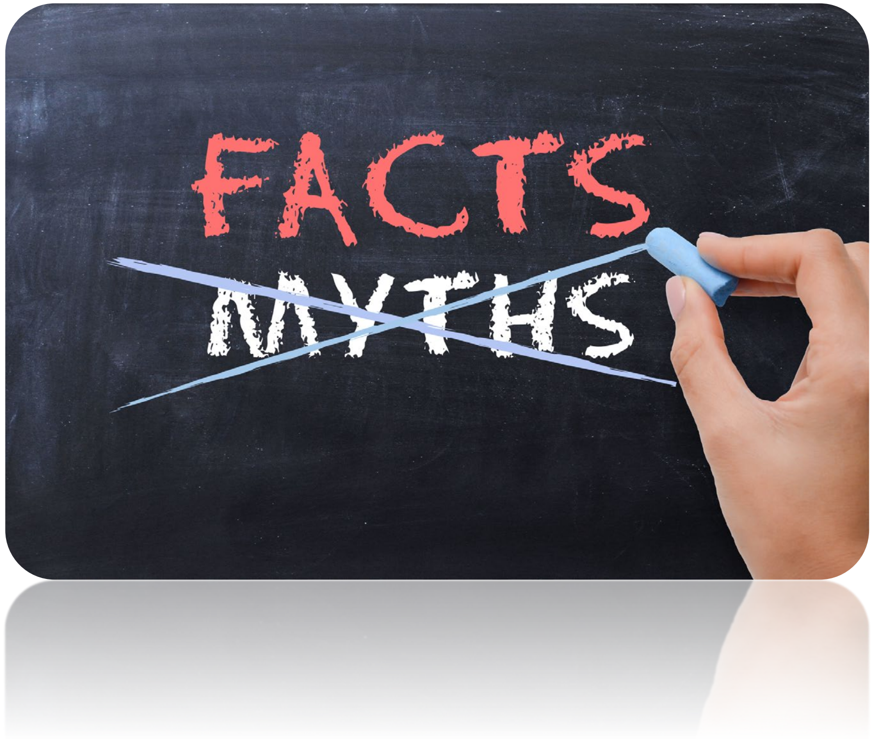
- The reality: The market is efficient. High option premiums means the market is pricing in higher risk.

2. Being assigned is bad.

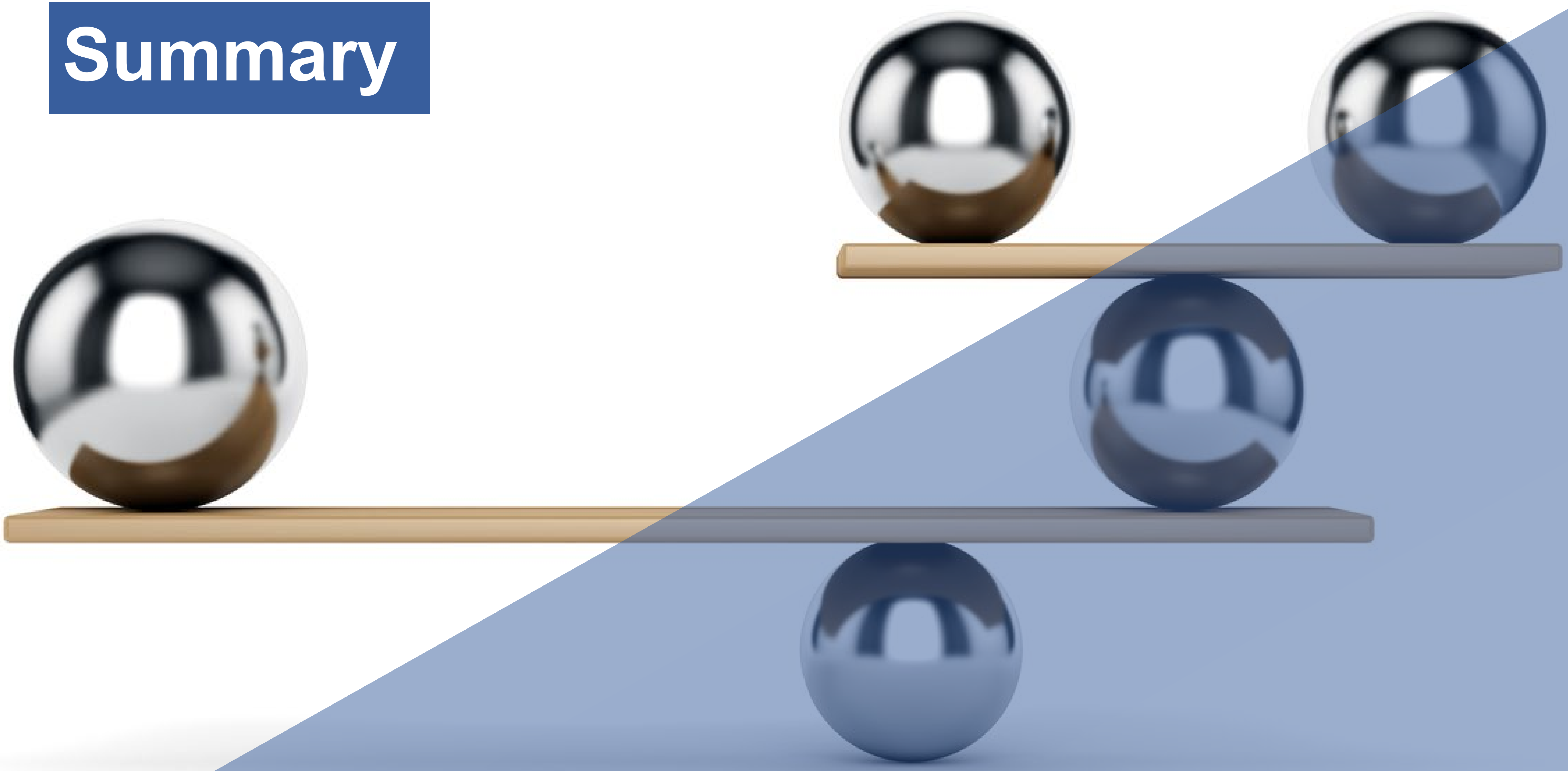
- The reality: Being assigned might be welcome depending on your initial goal.

3. Covered writing forces you to sell winners and keep losers.

- Options strategies often require active position management.



Summary



Covered Call Considerations - Summary

- **Stock Rallies:**
  - Close, roll, or hold
- **Stock Consolidates:**
  - Close option, close position, or sell another call
- **Stock Declines:**
  - Exit for loss, hold position, or roll down (and possibly out)
- **Variations:**
  - Stagger strikes, stagger strikes and expirations
- **Myths:**
  - Larger premium isn't always better, being assigned might be preferred, active position management might be required to keep most desired positions in portfolio

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