What are my Options for 2020

Options Institute at Cboe Global Markets

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January 21, 2020



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Stock Replacement Strategy

- Typically performed by purchasing LEAPs* call options
- Similar long term investment as stock purchase with less capital outlay
- Allows time for investor to benefit from potential rise in stock

- Example:
  - Investor Bob is bullish on stock ABC which is currently trading at $150 per share.
  - Bob thinks the company has great fundamentals, and it is currently in the process of bringing several new products to market.
  - Bob thinks the stock price could potentially go to $200 per share or even higher if the company is successful with the launch of its new products.
  - Bob's understanding is that the products may take anywhere from 9-15 months to bring to market.

*Long-Term Equity Anticipation Securities

Stock Replacement Strategy

P/L CALCULATOR

Add Option Contract(s) | Find Symbol

Price/Volatility | Interest | Dividends/Size

Evaluation Price: 175.00

Days to Expiration: 0

Expiration: 01/14/21

Volatility Change: 0.00 % Absolute

-100% 100%

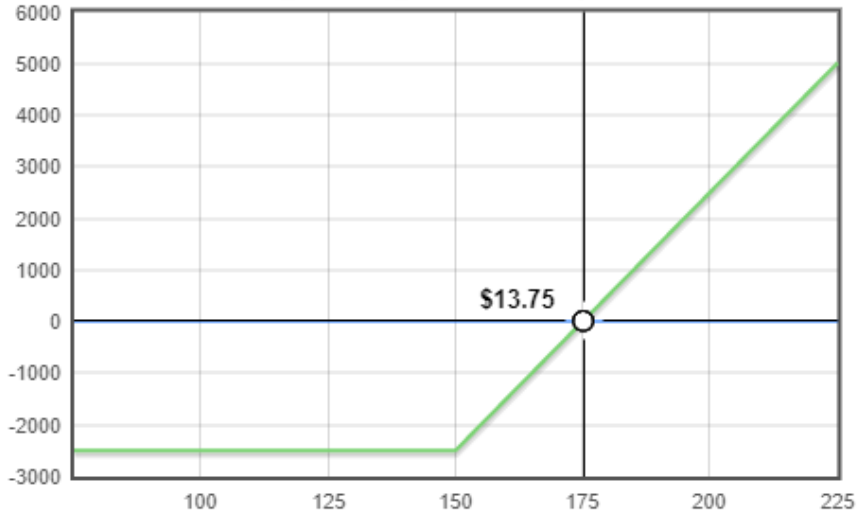
Restore Defaults | Apply

Last: 150.29 | **Change:** 0.28

Price Points	P/L
90.00	-$2,500.00
150.00	-$2,489.62
165.00	-$1,000.00
175.00	$0.00
180.00	$500.00
195.00	$2,000.00
210.00	$3,500.00
225.00	$5,000.00
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Refresh | How to Use the P/L Calculator (PDF) | View Demo

Graph Display: Price | Mid-Price | Invert Position



Total Strategy

Bid	Mid	Ask	Delta	Gamma	Theta	Vega
26.40	26.62	26.85	100.00	0.00	0.00	0.00

Buy/Sell	Quantity	Expiration/Strike	Bid	Ask	Theoretical Price	Evaluation Price	IV	Delta	Gamma	Theta	Vega	Action
Buy Sell	1	Jan 15 2021 150 Call	26.40	26.85	25.00	25.00	32.29	100.00	0.00	0.00	0.00	Trade

For illustrative purposes only.

Stock Replacement Strategy

150 Call strike for XYZ Stock trading $150

- 150 strike Call expiring in 7 days
- Price $2.95
- Implied Volatility: 26.95
- Delta: 0.56
- **Gamma: 0.060**
- **Theta: -0.160**
- Vega: 0.090

- **150 strike Call expiring in 575 days**
- **Price $25.00**
- **Implied Volatility: 31.72**
- **Delta: 0.61**
- Gamma: 0.010
- Theta: -0.020
- **Vega: 0.750**

For illustrative purposes only.

Stock Replacement Strategy

- Benefits
  - Investment is less capital intensive than trading underlying
  - Arguably better use of capital and potential higher ROI
  - Very low time-decay (Theta)
  - Longer time for predicted stock move to play out
  - Behave more closely to underlying stock

- Limitations
  - Option bid-ask spread can be wider than near-term options
  - More expensive than near-term options
  - Do not receive dividends
  - Not readily available in every optionable stock
  - Long time frame ties up investment dollars



Income Generation: Covered Call



Income Generation: Covered Call

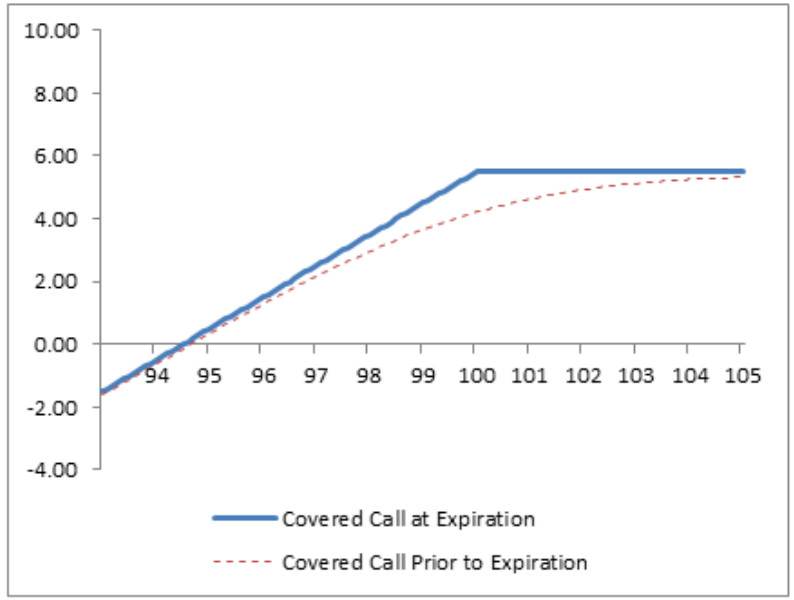
- Long shares of stock combined with a short call option position
  - Trader sells (writes) one or more equity call contracts
  - Trader buys equivalent # of underlying shares
  - 1 short call for each 100 long shares

- Neutral strategy; Expecting a minor increase/decrease in underlying stock

- Short call option (potentially) results in obligation to SELL underlying stock
  - At strike price; If assigned
  - For this obligation, the seller receives a premium

Income Generation: Covered Call

- Reasons to Use:
  - Collect cash income
  - Sell a stock holding above current price
  - Provide limited downside protection
    - Lowers long stock break-even point



- When to Use:
  - When there is a neutral to moderately bullish outlook
  - Create a possible preset price to exit the underlying stock

- Be Aware……
  - Early assignment (related to dividend) could result in calls being assigned prior to expiration

Income Generation: Covered Call

- Upside profit potential is limited
  - Strike price + call premium received – stock price paid
  - If assigned stock sold at strike price
- Break-even point
  - Stock price paid – call premium received
- Downside loss potential is substantial
  - Downside risk is with stock
  - Short call option offers limited protection
  - Entire stock cost less call premium received is risk

Hedging Strategies



Hedging Strategies

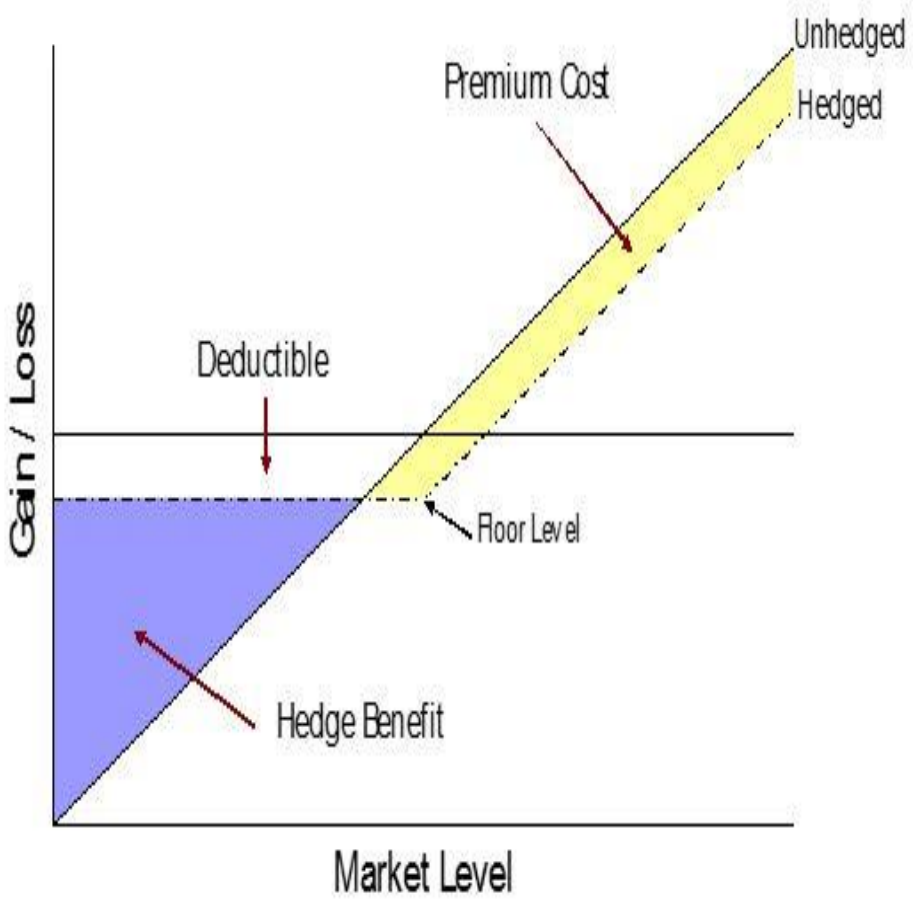
Protective Put – Options as a “stop-loss”

Pro:

- **Insulates holder against losses below a specific point over a defined time frame.**
- **Simple, clear cut.**
- **Defined risk.**

Con:

- **Protection comes at a premium – cost.**
- **Higher BEP than unhedged position**



Hedging Strategies

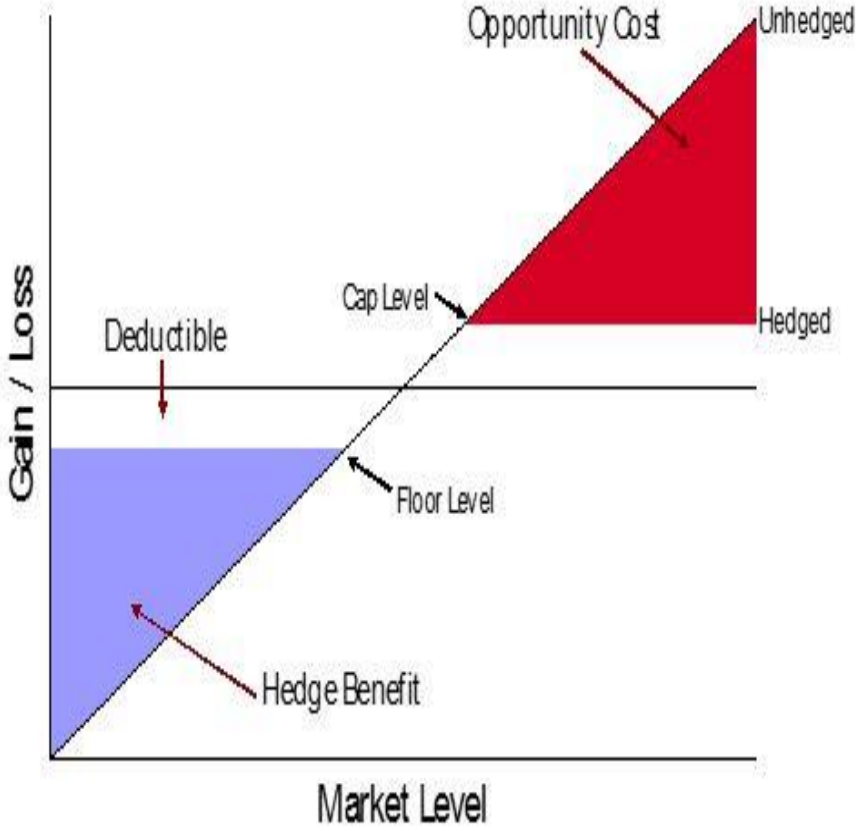
Collar – Financing your Protective Put

Pro:

- **Insulates holder against losses below a specific point over a defined time frame.**
- **Defined risk.**
- **Low or No Premium/Cost**

Con:

- **Waive some potential upside in stock to finance insurance**



Hedge Example w/SPY trading $320:

Investor could:

- **+5 Mar 310 puts @ 5.40 each - total hedge outlay = $2,700**
- **-5 Mar 325 calls @ 4.90 v. +5 Mar 305 puts @ 4.40 – total hedge collects $250**

Each alternative protects, to varying degrees the long position in the underlying market.

Premiums are different depending on the type of coverage.

Rights versus Obligations

XSP℠: What is it?

- SPX – Flagship Cboe product ($300k notional/contract)
  - ADV in 2019 ~1.45 million ($435 BN Daily Notional)
- XSP is the ticker for Cboe's Mini S&P 500® Index Options
  - Notionally equivalent to SPY options with meaningful potential benefits
- SPY options ADV ~ 2.9 million ($87 BN Daily Notional)
  - Clear Institutional & Retail demand for Index optionality on Mini S&P 500 product
- XSP affords end users the same exposure with benefits NOT typically associated with ETF options
  - 1256 Contract*: XSP (Yes); SPY (Generally, NO)
  - European Style (Eliminates early assignment risk)
  - Cash Settled (No portfolio disruption)

*Section 1256 of United States Tax Code. Investors should consult with their tax advisors to determine how the profit and loss on any particular option strategy will be taxed. Tax laws and regulations change from time to time and may be subject to varying interpretations.

In Summary

- **Stock Replacement**
  - Typically performed by purchasing LEAP call options
  - Similar long term investment as stock purchase with less capital outlay
  - Allows time for investor to benefit from potential rise in stock
- **Covered Call**
  - Long shares of stock combined with a short call option position
  - Neutral strategy; Expecting a minor increase/decrease in underlying stock
  - Short call option (potentially) results in obligation to SELL underlying stock
- **Hedging - Protective Put**
  - Purchasing put option against long holding or portfolio or holdings
  - Gives right to sell underlying at specific price and expiration date
- **Hedging – Collar**
  - Combination of Covered Call and Protective Put
  - Important to understand Rights (long put) vs. Obligations (short call)

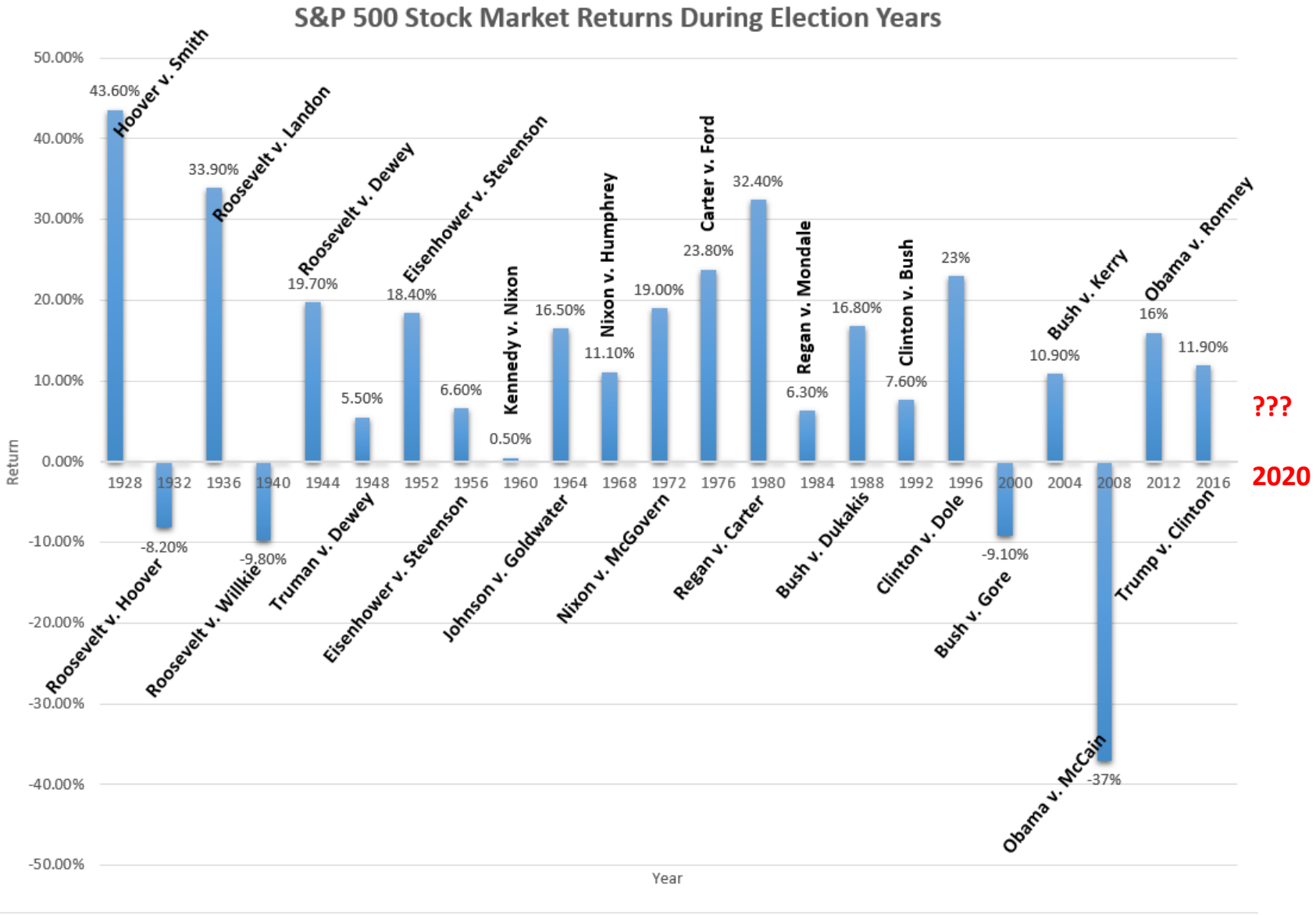


Four Part VIX Course…..



https://www.fidelity.com/learning-center/events/volatility-classroom

Teaser: Four-Week Course on VIX and Volatility



Teaser: Four-Week Course on VIX and Volatility

- What is Volatility?
- Cboe Volatility Index® (VIX)
- VIX Futures, VIX Options & VIX Term Structure

