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A Fidelity Investments Webinar

Introduction to Options

BROKERAGE: OPTIONS

Options Trading Webinar Series

Introduction to Options

Get to know the basics of options investing; learn key terms and concepts essential for any new options trader.

Buying Options

Understand what to expect when buying options; learn the difference between calls and puts.

Selling Options

Understand what to expect when selling options; learn how to navigate the risks associated with selling.

Options Trade Management

Now that you've placed a trade, learn strategies to manage before, during, and after its expiration.

Options Pricing

Understand how options are priced and learn how to you can get the best returns.

What are Options?

Strategies for Trading Options

Anatomy of an Options Symbol

Exercise and Assignment

Agenda

What are Options?

What are Options?

An option is a contract that gives buyers rights and sellers obligations.

Buyer Rights:

Can choose to buy or sell 100 shares (typically) of the underlying security up and until the:
Expiration date

At the:
Strike price

For this right, the buyer:
Pays a Premium/Price

Seller Obligations:

Obligated to sell or buy 100 shares (typically) of the underlying security **when called upon** up and until the:
Expiration date

At the:
Strike price

For assuming the obligation, the seller:
Receives a Premium/Price

Two Exercise Styles:
American (Anytime before expiration) vs. European (Only at expiration)

Why Trade Options?

Risk Management

- Individual security and potential portfolio protection
- Less money out of pocket

Yield Enhancement

- Helps improve returns on individual securities
- Helps improve overall portfolio returns

Leverage

- Less money out of pocket
- More choices

Stock vs. Options

Stock

- Substantial risk of capital (stock could go to zero)
- Lower break-even
- Voting rights
- Potential dividends
- Limited strategies (Buy stock, sell short stock)

VS

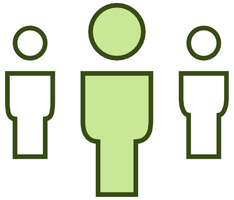
Options

- Leverage with risk limited to premium paid
- Higher or lower break-even
- Limited life, decaying asset
- No voting rights or dividends
- Many strategies (Options give you options)

NOTE: Call buyers do not receive cash dividends and do not have voting rights.

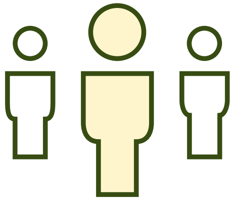
Option Buyer or Option Seller

With options, you can be either a buyer or seller



Option Buyer

- Pay a premium/price
- Has the right to Exercise and buy or sell 100 shares of the underlying security
- **Also called a call or put holder (long the option)**



Option Seller

- Receive a premium/price
- Has an obligation to buy or sell 100 shares of the underlying security at Assignment
- **Also called a call writer or put writer (short the option)**

NOTE: Call buyers do not receive cash dividends and do not have voting rights.

Types of Options

Long Call

Allows the option **holder** (buyer) to **buy** 100 shares (typically) at the strike price up to the defined expiration date.

Said to be **LONG** the call.

Bullish

Long Put

Allows the option **holder** to **sell** 100 shares (typically) at the strike price up to the defined expiration date.

Said to be **LONG** the put.

Bearish

Short Call

Obligate the **option writer** (seller) to **sell** 100 shares (typically) of the underlying at the strike price when exercised.

Said to be **SHORT** the call.

Bearish

Short Put

Obligate the **option writer** (seller) to **buy** 100 shares (typically) of the underlying at the strike price when exercised.

Said to be **SHORT** the put.

Bullish

What Happens When a Stock Splits?

Options can be adjusted in a number of ways to account for corporate events. These are called **adjusted options**.

Other adjustments may occur from corporate actions. Terms can be found in the option chain, or check with the Options Clearing Corp to find out the new terms of an adjusted option.

Example

You own one contract for XYZ stock with a strike price of $75, the company announces a 3 for 2 stock split.

How is the option contract adjusted?

Old option contract: 100 x $75 = $7,500

Share conversion: 100 x 2 * 3 = 150

Price conversion: $75 x 2 ÷ 3 = $50

New option contract: 150 x $50 = $7,500

The number of shares and the strike price are adjusted to maintain the notional value of the contract post-split, **keeping the notional value the same**.

Risk of Buying Options

What's the trade-off?

Time

Options have a finite expiration date. They will either expire worthless or be turned into long or short shares of the underlying security.

Leverage

Leverage goes both ways; it can hurt as much as it can help.

NOTE: Call buyers do not receive cash dividends and do not have voting rights.

Anatomy of an Options Symbol

Example: Anatomy of an Options Symbol

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Plain English Symbol: SPY Jan 21, 2022 Call 208

SPY	22	01	21	C	208
The symbol of the underlying	Year of the expiration	Month of the expiration	Day of the expiration	C for a Call, or P for a Put	The Strike Price

Holder (buyer) of this call has the right to BUY 100 shares of SPY at $208 per share at any time until January 21, 2022.

Premium Components

Premium = Intrinsic Value + Extrinsic Value

An option contract that has intrinsic value is "in the money."

An option contract that has negative intrinsic value is "out of the money."

Exercise and Assignment

Exercise and Assignment

What is **Exercise**?

Exercising a call is when the option holder opts to buy the underlying security at the strike price.

Exercising a put is when the option holder opts to sell the underlying security at the strike price.

If the option has intrinsic value of at least $0.01 at expiration, it will be automatically exercised.

If the option has negative intrinsic value at exercise, it will expire worthless.

Remember

Long options are exercised, while short options are assigned.

Exercise and Assignment

What is **Assignment?**

Assignment of a call is the option writer fulfilling their obligation to sell the shares at the strike price.

Assignment of a put is the option writer fulfilling their obligation to buy the shares at the strike price.

An option seller does not choose if/when assignment will occur. The option buyer controls the action; assignment occurs when they choose to exercise their option.

Remember

A short (sold) option can be assigned at any time! Even if it has no intrinsic value.

Exercise of a Long Call

American Style: Example 1

An option holder who exercised a long XYZ call at 146 would purchase 100 shares of XYZ at $146 per share, or 100 x $146 = $14,600.

If 10 of those contracts were exercised, the cost for 1,000 shares would be 10 x 100 x $146 = $146,000.

If the option has intrinsic value of at least $0.01 at expiration, it will be automatically assigned.

Remember

American Style can be exercised at any time.

Exercise and Assignment

American Style: Example 2

Using the same example, what would Assignment look like?

The seller, assigned on one call, would be required to deliver 100 shares of XYZ, and would receive $146 per share, or 100 x $146 = $14,600.

Remember

American Style can be exercised at any time.

Exercise and Assignment

American Style: Example 3

But what if the seller didn’t already own the shares?

The seller would have to buy them at whatever price they were trading post-assignment, which could be higher than $146 per share.

What if XYZ was now trading at $155? It would now be 100 x $155= $15,500

Remember

American Style can be exercised at any time.

Exercise and Assignment

American Style: Example 4

This time, substitute an XYZ 146 put for the call. Now what would Exercise of the put look like?

A holder who exercised a long XYZ put would sell 100 shares of XYZ for $146 per share, and would receive proceeds of 100 x $146 = $14,600.

Remember

American Style can be exercised at any time.

Exercise and Assignment

American Style: Example 5

Using the same example, what would Assignment look like?

A writer assigned on the one put would be required to buy 100 shares of XYZ at $146 per share, or 100 x $146 = $14,600.

Once again, remember leverage: A writer assigned 10 puts would be required to buy 1,000 shares of XYZ stock at $146, or 10 x 100 x $146 = $146,000.

Remember

American Style can be exercised at any time.

Exercise and Assignment

European Style: Example

You are Long (Own) 1 SPX call with a strike of 2440.
If your one SPX call were exercised because SPX closed at 2441 on expiration, you would receive
$100 CASH in your account.

Your option has $1 of intrinsic value times the multiplier for SPX which is $1 x 100 = $100.

*The multiplier for index options is “usually $100.”

Remember

European can only be exercised at expiration.

They’re based on an index (which cannot be delivered) and they are settled in cash.

Strategies for Trading Options

Review: Strategies for Trading Options

Long Call	Long Put
Short Call	Short Put

Which strategies are bullish and which are bearish?

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Visit the Fidelity Learning Center

Learn more about options

Read: Access the Options Strategy Guide

Watch: Check out videos that cover options basics

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Glossary

Option

Like stocks, options are financial securities that you can buy or sell. Options give buyers rights, and sellers an obligation to buy or sell the underlying stocks and other underlying investments. There are two kinds of options: calls and puts.

Call

The buyer of call options has the right, but not the obligation, to buy an underlying security at a specified strike price. Essentially, that means if you were to buy call options on a stock, you would have the right to buy that stock at an agreed-upon price up, and until a specific date. Conversely, the seller of a call option has the obligation to sell the underlying security at the specified strike price.

Puts

The buyer of put options has the right, but not the obligation, to sell an underlying security at a specified strike price. Essentially, that means if you were to buy put options on a stock, you would have the right to sell that stock at an agreed-upon price, up and until a specific date. Conversely, the seller of a put option has the obligation to buy the underlying security at the specified strike price.

Glossary

Premium

The current market price of an option contract. The option buyer pays the premium and the option seller receives the premium.

European Style

An option that can only be exercised/assigned at expiration.

American Style

An option that can only be exercised/assigned at any time before the option expires.

Thank You

Please join us for our upcoming webinars

For more information, please visit
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Questions? Contact a Fidelity representative at
877-907-4429

Important Information

Options trading entails significant risk and is not appropriate for all investors. Certain complex options strategies carry additional risk. Before trading options, please read Characteristics and Risks of Standardized Options, and call 800-544- 5115 to be approved for options trading. Supporting documentation for any claims, if applicable, will be furnished upon request.

There are additional costs associated with option strategies that call for multiple purchases and sales of options, such as spreads, straddles, and collars, as compared with a single option trade. Examples in this presentation do not include transaction costs (commissions, margin interest, fees) or tax implications, but they should be considered prior to entering into any transactions.

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