

TRANSCRIPT

Option strategies for ETPs

Presenters: Brett Yoder & Robert Kwon

Brett Yoder: Always a pleasure to be here with you in these big events. The Strategy

Desk is a very unique group. Fidelity, we're much smaller. The whole idea with us is we want to teach you mechanically how to take advantage of your analysis. So that includes everything from trading strategies, which is a very broad topic, but to the specifics of how to analyze with technical analysis, with fundamental analysis, and then ultimately how to pick which medium to take advantage of the outlook with, which is really where we come from today.

We're talking about exchange-traded funds and some of the unique opportunities they give us, but then also options strategies and that whole world of options trading, how we can take advantage of those ETFs and those unique setups that we can find.

With that, pretty easy agenda for you here today. We'll talk about why these ETFs, talk about those unique opportunities. We'll jump right in to the common options strategies that can be used to take advantage of the analysis that you have, and then finally finish it with ETF screening and a bit of live demo, walking through both the ETF screener on Fidelity.com, as well as mocking up some trades here in our Active Trader Pro on the profit and loss

calculator. So it should be a pretty dense hour for you, excited to jump right in, and just talk about why ETFs.

ETFs probably aren't new to you at this point. ETFs launched way back in '93. And with that, the very first ETF was just set up to follow an index in a passive manner. The S&P 500 is what the first one was launched on. And with that, the ETF market has continued to grow. The exposures of the ability of taking a fund money, you know, that is going to be invested into one specific objective, where we can then trade intraday, is a novel idea, right? We have, the very first one on the S&P 500. Well why not the DOW industrial average, we have ETFs for that, as well as Nasdaq, the Russell, and it has continued to grow, over the years that as of the last figure I saw, was over \$7.7 trillion were invested now in ETFs, and that was as of 2020. So certainly have grown, and I'd imagine to say if I asked you in attendance today, you know, why don't you tell me an ETF; what is a ticker symbol of an ETF that you know, you'd probably be able to produce at least one, maybe two, or a handful of them. But it's in that exposure that this growing market of ETFs, we can start to really take advantage of some of the macroeconomic analysis you might be aware of, some of the big, broad headlines maybe you're reading about in media, and say okay, well is there a way that I could truly profit from whatever the current news story of the day, or the week, or the month is? Key in point, right

now we've been talking about this idea of information technology, the driver of the market. Well how would we actually take advantage of this sector holistically? What about inflation; do we have inflationary concerns? Is there a way that we could truly build a trade, either based off of the dollar, or currency, or maybe some sort of metal, that would be able to have that influence in price because of inflation? CPI's numbers coming out today, even higher than expected.

And so, with that the exposure that ETFs give us allow us then to go in and take advantage of those big, broad-scale opportunities that are around us. Many asset classes are available, so a large amount of index-based objectives, meaning okay, you want something that's going to follow the dollar? Okay, here's an exchange-traded fund, and its investment objective is truly the dollar versus the world currencies. Right, and other examples of that. And in the more recent years, we're seeing an emergence of hybrid and active objectives. Okay, we want to take advantage of this one specific area in the market that is a little changing, it's a bit fluid so we need an active manager now behind the exchange-traded fund, and that is starting to emerge. Many more of these active funds are there. You might even hear them as this hybrid of smart beta, some of the different terminology that gets thrown around, and the only real difference that we're seeing in that small aspect of the market is a

management company will go out and build a proprietary index for their exchange-traded fund to follow in a passive manner. So again there's this hybrid in between just following an index, and being fully active, we have this hybrid area that ETFs are working into. So it's an exciting space now, because again, we can take advantage of these big ideas that maybe we didn't know necessarily how to take advantage of before. And also, I mean of course we're in an exchange-traded fund. Let's talk diversification just for a moment, right? We can help diminish a little bit of the individual stock risks we have, if I invest in a stock, I have to deal with maybe larger volatility, overnight gaps, maybe the influence of earnings announcements, corporate announcements, product launches, all these different one-off situations that were very specific to my one company, right? If I'm in an exchange-traded fund that's invested, we'll go back to the S&P 500, 500 different companies, the influence of one company's overnight move may not be nearly as devastating or as beneficial as if we just had that one company in and of itself. There's a lot of benefits to talk about with diversification because of that lower volatility that you may be able to find based off of one given name, and then we are hitting today this idea of hedging your portfolio. We know that in a basic hedge, and if hedging is new to you, we want some sort of failsafe, some sort of way that we can get out of our investment if it starts going against us, or at least offset the losses that we might be occurring, if the asset we invested in went down, there's a

way to use a broad-scale ETF with options to actually hedge your portfolio. So great topics here today, but this is why ETFs, let's take advantage of these macro-conditions that we're seeing. Let's diversify away from maybe some of the individual name risk that we have, and as we move over to this next slide, I just wanted to show, almost briefly here, the amount of different places we can get all of these different opportunities, and we're seeing exposures, right? We're looking at the idea of the currencies, those were mentioned. We were talking about fixed income, bonds, a hybrid, in-between, multi assets, you know, fixed income and equities, real estate volatility and so forth, and we can even get as specific as individual sectors, individual industries. We can continue to dial down and get more narrowly-based with these ETFs just because there's so many of them out there. But in any sense, because we have so many choices, there should be an opportunity based off of our analysis, we can take advantage of it.

One of the ways that we want to talk about today, obviously as self-named, is the idea of using options. Right, options are still going to entail specific option risk, but now we can speculate on those more broad ideas that we truly have. And Robert, with that, I'll put it right over to you, why would we use options?

Robert Kwon: Thanks, Brett, and welcome everybody. So why trade options? As you can see from this slide, there's many different reasons why a trader or investor would look to the options market, and a very common use is risk management. So options can reduce risk for an individual security, like a stock or an exchange-traded product. But you do want to remember that options are not available for all securities, so you would want to check, you know, just put the symbol in the option chain and see if something comes up. And then just as important, even if a security itself does have options, and does have active participation and liquidity, so maybe you check for volume, a tight bid-ask spread, in the exchange-traded product itself, the liquidity of the options can vary dramatically, even on two different competing products tracking the same benchmark, and is something to certainly be aware of, we'll look at an example when we go to the demo.

Now I would say, one of the dominant reasons a trader/investor may look to options that might otherwise not have is for some type of protection, and rather than going through and individually protecting specific situations or positions, more from a broader portfolio perspective. So imagine you've created a diverse portfolio, maybe there's 10, maybe there's 15, 20, 30, maybe more. And imagine how time-consuming in the analysis that involved to try to go through and make a decision on each one specifically. But if you think

there's just some broader risk to say the market, or you know, the sectors that you're concentrated in, you might use an exchange-traded product that tracks a benchmark like an index or a sector, and use that as the underlying for the options for hedging purposes, and again, we'll dive into this later.

Now part of managing risk is simply looking at the amount of capital that you put at risk for, of course, make potential profit; that's the whole purpose of putting yourself at risk, right, is you're trying to make money here. So with options, there can potentially be less out-of-pocket capital to gain that type of exposure.

Now let's briefly talk about yield enhancement, as this is a very popular reason, right, especially newer traders are drawn, as options can be bought or sold, and many traders actually look to selling a strategy to kind of generate income and potentially improve returns on a trade, especially for kind of more neutral type of outlooks. And again, we'll cover a few examples. And finally, right, that word you hear everywhere, "leverage," right? Options can be used for leverage. Again, it's potentially less money out of pocket to gain exposure. Right, so especially from the perspective of an options buyer to gain exposure, a lot of times that leverage kind of perspective comes into play.

But in addition, options give us more tradable outlooks in general, right, by either buying or selling single-leg options, utilizing multi-leg strategies, or combining options with stock or ETPs. And what I'm referring to is this: imagine your outlook is neutral. There would literally be no reason to enter a stock or ETF trade, because if you're correct, there would be no benefit. So excluding dividends, if the security doesn't move, it would neither benefit you or hurt you. It would just tie up your capital. So options can potentially give us ways to take advantage of neutral or range-bound expected price movement. And it also gives us a way to take advantage of expected volatile movement without actually picking a direction. So imagine you thought a security was either going to be volatile up, or volatile down, but you couldn't decide which way. Again, if you were someone who just made decisions about stock or an ETF, there would be no justification to enter a trade where you couldn't decide what you think was more likely to happen. But the options market does have tools in the "toolbox" to potentially take advantage of this type of outlook.

So now we're going to start taking a look at a few of those different positions/takes. Brett, let's start by looking at long calls. So if your exchange-traded product has options, one long call, or buying the call, will give you the right to purchase 100 shares at the strike price any time through and including the expiration date. Now the ability for the option-buyer to exercise early is

called American-style, and you want to be aware, right, there are certain other products out there, especially index options, that are what we call European-style, that do not allow for that. But anything that has an underlying in the United States would typically trade with American-style, so you want to be, when Brett gets to the selling of it, right, if the option buyer has that right, the option sellers have that obligation, a very important thing to consider.

So your breakeven point at expiration is going to be the premium you paid added to the strike price. So since this benefits from rising prices, your outlook should obviously be bullish. Now the maximum profit is potentially unlimited, which is similar to the profit and potential of simply owning the exchange-traded fund. There is no ceiling. However, the maximum loss, or risk, is going to be the premium that we paid. So how bullish you are, and how long you think it will take to rise are going to be factors that determine which strike and expiration date that you pick.

But you do also have to factor in what we call "implied volatility," and also implied volatility skew. So if you're not familiar with implied volatility, if you look at an option premium, and you kind of take a snapshot, the market's open right now, we'll take a look in the demo, the marketplace determines what that bid and ask is at any time. Now part of it's going to be based off the strike price,

and where the stock or the ETF is in relation to that strike, the money-ness, right? Part of it's going to be due to how much time is remaining. But imagine, for whatever reason, that option was trading for a larger premium than what you're looking at, but everything else was the same.

Mathematically, an option pricing model would say it has a higher implied volatility. If the premium were lower, or smaller, all else being equal, it would translate to a lower level of implied volatility. So in a way, it's simply the mathematical translation of demand for an option, given everything else is the same.

Now volatility skew refers to simple differences in implied volatility, or demand across things like different expiration dates, and also different strike prices, which is very important to understand, if you plan on trading out of your option before expiration, you need to factor in how you think implied volatility will change in addition to what you think the underlying price of the exchange-traded product will do. And again, we'll take a little bit closer look during the demo. So the example here shows the profit-loss diagram of a 100-strike long call, trading at a \$3.30 premium. Now we start below the horizontal axis, because we need a rise in price to get to our at-expiration breakeven point, in this case \$103.30. The line extends upward to the right, and that represents the potential profits from further increases in the share price. But if the share

price declines, the most we can lose is that \$3.30, and at expiration, the maximum losing scenario will occur at the strike price or anywhere lower, whether or not you still have that option at expiration is something to consider. Now the red-dashed curved line represents extrinsic or time value prior to expiration.

So Brett, let's flip over to take a look at the put side. So one long put, or buying the put by itself, will give you the right to sell 100 shares at the strike price of the option, again any time through, and including the expiration date. Your breakeven point at expiration is the premium you paid subtracted this time from the strike price. And since this benefits from declining prices, your outlook should be bearish. Again, we're thinking about just a long put as a trade by itself; it's a bearish trade.

So the maximum profit is actually defined, and it's the strike price minus the premium, because exchange-traded products, just like stocks, have a floor at zero, whereas on the upside for the calls, there is no ceiling. But so much of the calls, the maximum risk is the premium paid. So again, how bearish you are and how long you think it will take to fall may determine which strike and expiration date you pick, and to emphasize, think about what we all went through the past year or so. If you plan on trading out of your option before

expiration, you need to factor in a level of implied volatility and how you think that will change, because it can become a significant part of the premium in real-time.

So in this example, we have a 100-strike long put trading at \$3.15. Yet again, we're going to start below this horizontal axis on the profit-loss diagram. But this time, we need a decline in price to get to our expiration breakeven of \$96.85, and the line extends upward to the left, representing potential profits on further declines in the share price until we reach that vertical axis "wall" which represents zero. Right, so if the share price rises, the most we can lose is, in this case, \$3.15, and once again at expiration, the maximum losing scenario, if you still have it, will occur at the strike price or higher.

So why don't we take a look at some selling strategies now, Brett?

Brett Yoder: Absolutely, Rob. And then thanks so much for that. One of the things I really want you to take away from this, especially if you already have a little bit of background in options, is options are still options, right? Options unique to ETFs, the ETF might be giving us unique exposure, but the option we've got to still be thinking about the same way.

And to reiterate what Rob was saying around this idea of implied volatility, how it's a representation of the expense of the option, another way to talk about that expense or premium is the speculation. You might think your broad-based idea is going to move a certain amount. In our coaching sessions, we certainly talk about coming up with an analysis that would provide an expectation of the value in the future. Right, if you are bullish, you're bullish to which point, and beyond that point, are you still bullish? There's a threshold to how bullish you could be, or how bearish you should be. You should define that as part of that option plan that Rob will talk to us about here in a few moments. But with that, with that premium, if it's going to be the risk I take when I buy an option, it is going to be the gain I can make if I sell an option. And our first stop here on selling options, or selling that speculative amount, selling the premium, thinking that that is well within the realm of your analysis as far as the effective price would be, right, then we can talk about covered calls.

My next slide will talk about selling puts. Covered calls is a multi-leg strategy. We're going to incorporate both long shares as well as selling a call. Our benefit here is the obligation when we sell to open a call is I simply have to sell shares. If I already have a hundred shares to deliver, or meet that obligation, it's almost like I'm just placing a sell order on the underlying, whatever the

underlying ETF is. In our example, we have 100 shares, we bought them for \$98. We sold a 100-call strike at \$3.50. So essentially this means if the underlying trades up to \$100, most likely more than that, we will be assigned and have to deliver our shares in \$100. Immediately, we'd profit by \$2, the difference of 98 and 100. But keep in mind, we sold the premium. We took on the obligation at the beginning of the trade, and we pocketed \$3.50 at the get-go when we put on the covered call. We have to account for that premium also.

Now we can account for it as an effective sales price. To do that, we'd look at the strike price 100, we'd add the premium, \$3.50. And then I would think about my overall prospect here is spending \$98 to sell at \$103.50. We could also account for the premium within the shares themselves. I spent \$98 but I had an inflow of cash of \$3.50, my difference there of course being \$94.50. Now this is my new basis, or my adjusted basis for the shares. So if it trades below \$94.50, at this point I'd be a capital loss, right? And we talk about this over here in the construction. We talk about buying the stocks, selling the call, the max gain we're going to incorporate, the strike price, and the premium received will take away the cost of our long shares. That's going to be the most amount of money that we can make. The max loss, whatever we spent on our shares offset by the premium of \$3.50. That also giving us that lower

breakeven price, stock price minus premium received. So where I would be more apt to think about covered calls, is if I looked at the premium on these different strike prices in my underlying. I said, you know what, there's a lot of premium here. The speculation, whatever the analysis was that I was looking at, and I thought the price was going to go up on this underlying, you know, the general investing public is thinking yeah, it's going to go up that amount, and even more than what my personal analysis says.

And when that's the case, okay, well why don't we just get paid for selling it at whatever the profit analysis was, or price analysis was that we had going into the strategy. That's one of many different cases. Again, we could use some relative analysis and decide if the premium is simply going to go down because of our IV, the implied volatility, its normal trend, is there some sort of even that's coming up that you want to take advantage of that, and by definition, we just showed an out-of-the-money covered call, we could definitely sell an in-the-money or an at-the-money covered call, and be able to profit in some different ways. So there's many variations to that, just like there's many variations to selling puts. But essentially, on the most easiest terms, this is still a strategy I'd be thinking about, when that price, that put premium, how much people think they believe that the stock will fall from

whatever strike price we're choosing, it's just so much, we feel that it's not within reason with our analysis.

So here we have a short put, and just to point out, our profit and loss diagrams look eerily similar, don't they? I can make money up to a certain point.

Beyond that point, I don't make any additional money. This is a short put with a strike price of \$100. Above \$100, my put is out-of-the-money, I won't be assigned, I'm able to pocket my max gain, which is that premium that I sold the put for. My risk is if the price falls down, and if the price continues to go down. In fact, if I take my 100 strike put and subtract my \$3.15, and you'll notice from Rob's example, this is just the exact opposite, this is selling that put instead of buying it, my breakeven is still \$96.85. Anything below that, I'm going to start to see loss at expiration. So we have our max gain, our max loss, our breakeven of course is just that \$96.85 that was described. Both of these strategies, and that bullish-to-neutral category, I've talked about more choices with options, this would be it. Maybe we've done our inflation analysis and we think there's going to be movement in the dollar, but we're not certain when. But we certainly think that we're either bullish or neutral, given the pair that we're looking at, the ETFs, the ETPs, I'm alluding to. So this give us the ability that if it does go sideways, if the change in the influence of the dollar doesn't happen right away, I'd still be able to profit, because if this 100 put stays out of

the money, it doesn't go down, I get to pocket the \$3.15. So again, there's more layers here; we start to deal with selling, we start to deal with selling and stock, the multi-leg the covered call, the selling of the put, simply different considerations that's precipitated on the idea of how much premium there is on those strike prices.

And then lastly here, we have the hedging. We talked about that. Rob, go into hedging for us.

Robert Kwon: Yeah, thanks, Brett. So, before, we looked at long puts as tools for bearish outlooks. However, if we own the actual underlying ETF or ETP, or we own a portfolio we feel closely correlates to that exchange-traded product or its benchmark, and then buy a put, it creates a hedged risk-reward profile synthetically similar to simply buying a long call at the same strike as the put we buy. Now Brett touched upon looking at covered calls and selling puts, and notice how similar those diagrams looked. Those are synthetic equivalents at the same strike. Now notice how similar this profit/loss diagram looks to the long call example from earlier. So, if the underlying exchange-traded product or portfolio rises or keeps rising, we still have the unlimited profit potential. What does that put do? That put benefits if the price declines, but our shares or our portfolio is expected to lose in that scenario.

So those kind of offset each other on the downside. However, we must overcome the cost of the put with the rising prices or portfolio value by expiration to get to our breakeven point. Same thing as if we just bought a call. Therefore, you hedge because your outlook is still bullish -- this is very important -- if you're concerned by an adverse down move and want to control what losses look like in that scenario. If you are in fact outright bearish, the first thing you want to do is consider whether holding your current position or positions still makes sense given that expectation, at least in terms of their current position size or allocation. Because if you hedge your long portfolio or exchange-traded product, and you end up needing that hedge, because it went down, you're not making money; you're simply defining what losing looks like. That's what the hedge accomplishes.

So now, if you own the actual exchange-traded product, hedging with a put synthetically replicates the long call, and there's no fancy math involved, just like if you were hedging a stock position, for every 100 shares, it would be one standard contract. So in this example, we own 100 shares of the exchange-traded product. And to make the math simple, we made the basis \$100 a share. And imagine we purchase an exactly at-the-money 100 strike put for \$3.25. Our breakeven is upward at \$103.25, and that's the premium added to our cost basis of the shares. Our maximum loss is defined partially by the

strike price of the put that we pick. In this specific example, we're using an at-the-money strike that's identical to our cost basis, so our maximum loss in this specific example is \$3.25. However, if we picked a lower strike put typically used to save some expense, and also a lot of traders out there, like hey, if it goes down a little bit, that's not really what I'm concerned with. I only care if it's really in jeopardy, right? So sometimes we might pick a lower strike put, but keep in mind at expiration, that means the protective aspect of owning the put is not going to kick in right away.

So there's a very specific thing you want to pay attention to if you're hedging. The breakeven of the put by itself, so remember when we covered just buying the put as a bearish trade. That's actually where the protection actually did something in hindsight versus not hedging from a financial mathematical perspective. Now that doesn't cover the cost of being able to sleep at night. But mathematically, it's the breakeven of the put by itself, when used as a hedge, is where it actually did something, versus just holding on to your portfolio. And we'll demonstrate what this looks like in the demo.

Now, for those of you who might try to hedge a portfolio, the correlation of the portfolio to the exchange-traded product is going to determine how effective the hedge is. Notice the little asterisk on the slide. And your breakeven and

maximum loss scenario could vary depending on that correlation. So there's always the risk that correlation does not behave as expected, so you want to be aware of that.

Now when using an exchange-traded product to protect a portfolio, there's more math involved here, because it's not just 100 shares. So what you would do is you would take the current value of the exchange-traded product per share, to literally look at what it's trading for, and then factor in the multiplier of a standard contract, which is typically 100, and multiply it out. So once you get that total, you would then take your portfolio value that you are trying to protect and then divide to get the number of contracts. And that will give you the basis, right, that number to use, and then of course you dive into your strike and expiration selection. So Brett, a common kind of mistake people make, is they look to the strike price to do the calculation. Say you wanted to protect against a 10% decline, say in the market, right? You don't do the math based off the strike price 10% lower. You base it off the current value, and then if you want, and accept a certain amount of decline before the protection kicks in, then you use that for your strike selection. And we'll cover this in the demo in just a moment. But that's probably the number one mistake where kind of misapplied logic comes into play when you're getting started, always do the math right at the money.

So Brett, let's kind of talk about things holistically here, right? Make a plan. It's very important when dealing with options to have a specific outlook and objective, and the reason why and it's why it's so much different than just investing or trading in stock, is because options have finite lives. They have fixed expiration dates, and fixed strike prices. So, the moneyness of the strike, so in-the-money, at-the-money, out-of-the-money, it's gonna change as the underlying price changes. And as far as I'm aware, Brett, time only goes in one direction, so the expiration date is always getting closer, since time only goes forward. So what makes this different is your option is always changing, unlike shares of stock, or shares of the exchange-traded product. Like those things don't have some type of time component. They can go away, or a company can go bankrupt; they don't expire.

So when you're evaluating your approach, there's the initial decision to select this tool out of a toolbox. But as time goes on and things have changed, ask yourself, has my outlook changed? Does the option I have still make sense given what's happened, and my updated expectations, not what the option started out as, but what it has become, and I think another great question to ask yourself, Brett, when you're trying to make these types of decisions of what to do next is, look at your current option. Would I open this option for what it

currently is, if I didn't already have it? If the answer is yes, then consider keeping it. If the answer is, not at all, or not really; I might do something similar, but it'd be different than this, that's how you can justify making an adjustment. Consider closing it, move on to the next trade completely, or deploying a different version you think closer fits your new expectations from here.

So imagine the example of a hedge. You buy an at-the-money put, your fears come to play, something right, spooks the market, or spooks your sector, and the stock right, declines, or the ETF declines, the market declines. Well your at-the-money put is no longer at the money; it's in the money. What do you do next? Look at it for what it's become, not what it started out as. Hopefully that gives you a good sense, even if you're brand new, is that with options trading, your initial decision, right, is for that moment. And then it's on to the next potential decision, depending on which version of the future presents itself.

So why don't we jump over to the demo, we've hinted at this, and I think a lot of times seeing things in practice can help conceptualize some of the things we've been talking about from a narrative perspective.

Brett Yoder: Absolutely, Robert. I couldn't agree more. We're about to journey over to Fidelity.com, see the cookie crumbs there at the top. I'm going to be going to News and Research, ETFs, and then finally the screener, so I'm switching over right now, you'll see Fidelity.com, I'm already logged in to our test account here. Up at the top, we'll first navigate to News and Research, down to ETFs. As our ETFs Flash page loads, we'll notice we'll be able to dive directly into a screener if we want to, but I'm actually going to click at the Launch Screener button down here at the corner, bottom left of this bricklet. So we see the ETF screener. And again, if we wanted to jump right into some sort of market cap. Right, we hear this rotation from value to growth, we hear rotation from the small caps, the mid-caps, to the large caps. And that's where we would want to go, and there's a very quick way to get into the screener. Same thing, we already have pre-built for you a sector screener. We want to take advantage of the rotation of sectors of the equity market, you can certainly jump right in here to find some ETFs to do that or take advantage of that strategy on as well as fixed income.

And then, some of these active equity ETFs. Like I said, I want to show the ETF screener, just want to showcase a couple of different metrics that you might want to choose, and especially how the ETF screener works. So we have the body, or the results of our screening criteria will be in the center here, and you

can actually see without any criteria, so no criteria here on the left side, I'm just given that same bricklet that I had on the previous page. But we can certainly add our criteria. And we're talking about options with ETFs. So the very first thing I want to do is add optionable, make sense, right? So here on the left side, there's three different ways that we're going to add our criteria. We have this more accordion-style menu, where we can click the plus sign, we'll have everything for basic ETF, ETP facts dropdown. If we click one of these metrics that we want, one of these criteria that we want, we notice that now, we have criteria, two were already added for us, and here's optionable, and the way that we know that the filter, which now we have results, is giving us what the criteria truly is, it's the amount of information, or these different metrics above the search bar.

So we Add Criteria below, and we have the search bar. Everything below we're not looking for. Everything above, we are. By default, we're looking at exchange-traded funds, not exchange-traded notes, completely different product. We're not considering leveraged or inverse ETFs. These are our funds that use derivatives to try to achieve some sort of variance of return on their indexes. We're not considering those; we're just on optionable, and I want to click "yes," and we'll notice out of the 2,430 exchange-traded products, we are now down to 654 given our different criteria. That's the way

that we're going to filter, how, whatever criteria we have, we'll continue to narrow our results.

So that was, here on the left side, like I said, using the accordion menu. Give you one more example of that. Let's say we wanted to look at overall objective. So we click on "Objectives." Now we have this accordion expand. We can go to "Equity" and add the style box, one more click. Style box, you'll notice, refers to your analysis tab of your homepage. I don't know if any of you have had the chance to look at that, but we talk about these different factors of equities. We talk about whether they are more growth-oriented. Haven't really proven themselves yet, company's trying to gain market share, whether they're value-oriented. Companies that are fully-established now are just looking for maybe variance in market price to what we believe fair price is, of the stock or blend, blended companies, or a mix of both, kind of found their foot, but might expand a little bit more here in the growth section. And we also have the factors of market capitalization, large cap, mid cap, or small cap. And from here, we can see how many different ones we have. Like if we wanted to remain with a large blend, we can go to, put a little checkmark here, now we're filtered down to 133.

And as, if you want, just to point out, if you ever have a question about any one of these criteria, here in the upper-left corner, click "Definition." You're going to have our glossary pull up, and then you'll be able to read through exactly what those metrics mean. So again, Definition, take you directly to that. That's the accordion style of adding your criteria. You can also search for specific criteria. So if I look at specific criteria, maybe I want to know some things like what is the, how about volume, how much does this ETF actually trade? I can simply type in, in this case, volume. I can look relative intraday volume, that's in the analytic metric. I can look at just hard volume for today, today divided by the 10-day average. I'm going to look at the 90-day average. Here's a quarter worth of trading. With that, what is the overall average of volume the ETF has? As Rob pointed out, just because we have volume in the ETF does not mean we have volume in the options. We're still going to want to do some more analysis, and more research, if you will, on those options, seeing what the true opportunity is there. But, with this, now we've added volume.

The third method, scroll back down, we can look at the "View All" button.

View All button, I just want to showcase this for a second. This shows all of that accordion-style menu, but we can click what we're looking for. Right, so in this case, what if I did want to take a look at the different sectors? And we

had talked about these different ways, or different exposure we can get, let's go to "Asset Class." Okay, another metric to maybe separate different funds from each other, because you'll find funds that have the same objective. Let's talk about the tracking error. For a passive fund, this is how well, and in the way that it's expressed is how poorly, it tracks the underlying index. You know, a low number's what we're looking for. We want something that tracks very well. We don't want a high tracking error; that implies that it tracks it poorly.

So we've put these checkmarks in, and you can see all of these different trading characteristics, shares outstanding, the median bid-ask spread. What's the slippage between how much you're spending, and how much you'd receive on any one trade? Some of these ETFs might move a very small amount. Once we're done picking the different metrics, and again, I encourage you to go in and read through and find the metrics you're looking for, we click "Apply Criteria," without any suspense here, everything that we've checked is now available to us here on the left side above, let me just shrink down the sector exposure, above our search criteria bar.

So then to decide what we actually want to look at, and one, we could find a general idea of metrics that we're looking for, and I just want to point out that

we can save it to our own personal screens. You can have your own personal screener, for maybe different asset classes, scrolling down, clicking on "Asset Class," it's going to expand, now here's the different asset classes that we can look at, right? And with removing our style box, all I have to do is click the "X," now I'm not just looking at large blended companies, now all my asset classes are showing for us. I can choose commodities, currencies, equities, fixed income, these multi-assets, et cetera, right? And by clicking them, of course those are the results I'm going to get. Case in point, here I have equities. Now the 494 displayed. Here in my center, drop that off. I just wanted to look at the currencies. I can certainly do that, as you would expect, of course, I have currencies. And so on and so forth, right?

But anyway, set up the scan that you're looking for. Asset class is going to get you into maybe these hard-to-reach areas, like the commodities, right, currencies, fixed-income, if you don't want the actual bond or bond exposure right? Going into the sector exposure. Of course, we can drill into this too, I just want to look at discretionary ETFs, et cetera. Set up your screen, save them individually, because again, the idea is using ETFs to take advantage of that more broad macro idea that you kind of have. And for that, Rob, I want to switch over to you. Why don't we use something, maybe more commonplace, the S&P 500, as an example, and let's use Active Trader Pro, which is going to

be our charting and our options analytic tool, and look and see what some of these option opportunities would be.

Robert Kwon: Yeah, and Brett, before I switch over to my screen, one thing that's very important, the category is called Exchange-Traded Product, and exchange-traded fund is a very specific type of exchange-traded product. And the other common one is exchange-traded note, so you make sure, I know we kind of mention this from time-to-time, but whatever you find when it's new to you, make sure you're familiar with what specific type this is, what it actually is, and I know it can seem kind of boring from time-to-time, but make sure you're reading the prospectus if it's the first time you're researching something, you've got to do your own due diligence, so again, in general, they both have shares that are traded, right? But underneath, they could mechanically be different, and you want to be aware of what those differences are, that's just not the primary focus of today's webinar. So just something I wanted to point out, make sure like anything else you do in a self-directed decision, you do your due diligence and you understand the product that you selected.

But now as Brett touched upon, one thing we're going to look at is we're going to look at two competing products that track the S&P, and depending on whether you're an investor or trader in these shares, or an options trader,

there's different things that you might prioritize. Let me switch to my screen really quick.

And what I have, okay, so I've done the switch, Brett, can you just give me the okay? Hopefully that's showing up for everybody here.

Brett Yoder: Yes, you're good to go.

Robert Kwon: Perfect. So what I have here is just two quote tools open on Active Trader Pro, and then I have an option chain down below. And I've selected the next monthly expiration coming up for June 18th. Now what I have at the top-left is SPY, it's the original ETF. And as you can see here, right now, the market is up about half a percent. SPY is up about half a percent. Then I have a competing product that also tracks the S&P, that's also up about half a percent. Now if you look at the quote for the actual shares, SPY has a penny-wide spread. If I look at the quote for this competing product, IVV, it has a penny-wide spread. So if you were just trading the underlying, right, you might look at things, like do I already own some of this, and I want to add or build my position or close out of something. You might look at the shares, again, SPY is almost 26 million, IVV's closer to 2 million, but as far as the tightness of the bid-ask, you're trading a hundred, couple hundred shares, you

might look at things like expense ratio, tracking error, or there's many things that track the S&P. Maybe it's a competing product elsewhere or something like that.

But let's look at the options now. So if you look at SPY, it's option chain for June 18th. And I have 20 strikes selected, meaning some in-the-money, some out-of-the-money, surrounding right where SPY is trading. And what are we seeing here? Tens of thousands of contracts traded on a lot of these options. Some even have tens of thousands, or hundreds of thousands of open interest. It's not universal, mind you. Right, some have more than others. But there's a lot of participation in this monthly contract that expires in eight days.

Notice at the top, there's an expiration for June 11th, June 14th, June 16th, June 21st, June 23rd. So SPY actually has Monday/Wednesday/Friday options. They have month-end options, quarter-end options, long-dated options. It has single-point strike differential, 423, 424, 425, 420, 419.

Now let's go over to IVV. Same expiration. So right off the bat, notice that there's weekly options, just like SPY for Fridays, but there's none of those Monday or Wednesday options. What do we notice here? We still have the single-point strikes, just like SPY for this June 18th. But look at the difference in

the amount of volume and open interest. There's a good chunk of these, this is the contract coming up in eight days, mind you, the monthly contract, that have no volume today. Look at the pricing. So here's a 425 call option, 220 by 255. Let me go back to SPY really quick. And again, there is a nominal difference in the share price, so I'll pick this 424.

So you might be noticing a couple different things here. Number one, the one on the left looks like a dynamic video, right, with constantly adjusting price, quantities, whereas the one on the right looks like a wall of bids at the left, and a wall of asks at the right. Notice the option on SPY is one, two cents wide, and the spread on the IVV is 35 cents. And notice the trade just went off on that actual SPY contract. So this is a visual demonstration of dramatically different liquidity situations. It doesn't mean you can't trade the one on the right, especially if you own the stock, and are considering doing a covered call, right, this is what you would literally need to look at to trade. But just be aware that even if as an ETF investor or trader, you might find these two comparable from an options perspective liquidity-wise, they are quite different in terms of their participation. Something to keep in mind, because if you enter into a lower-liquidity situation, you can protect yourself using things like limit orders. When are you most likely going to try to close your trade in a hurry? Either to

secure a profit, or to prevent a bigger loss. And if there's no liquidity, or poor liquidity going in, it's not just going to magically appear.

Think of it like going to a dance party, right? There's two people at the dance party and you, and they don't want to dance with you, then nobody's having a good time, right? If there's hundreds of people there, you might eventually find somebody to dance with, right? So there's more people dancing at the SPY party in terms of options than IVV. Just something to keep in mind, even if they both have options, even if both from a share trading standpoint, comparable, right, you want to factor this in when you make your decisions, especially when you're using something as a proxy, like a portfolio hedge.

Okay, so now let's take a look at an incredibly useful tool, and that is going to be the profit/loss calculator. So, the way you would get this is click on "Options" at the top, Profit/Loss Calculator, it's going to be blank initially, you put the ticker you're interested in at the top-left. Your account's down below, if you have multiple accounts, select the account you want. Now if you already have a position, whether a stock or an option that will be here, but you've seen in this test account, I've added a bunch of simulated positions, if you want to test things out and consider, compare. And you do that by click "Add Simulated Position." And again, don't be afraid of this; this is not a trade

ticket, but it looks like one. So you could fill this out, hey, what if I wanted to buy a put for protection? You just fill this out. That evaluation price is kind of like the price you would try to enter, and you'd click "Apply."

Now I've already done this, and what I've done here is let's go through. The top one, I went to August 20th, 423 strike long call, with an evaluation, or basically a basis if it was a real trade of 9.88. We see what we saw on the slides. Rising price, look at the grid here. Rising price, that's how we can make money, and it's not capped. If it starts going down, that's where the red numbers on the grid come from. Now what these dates look like, it's three dates, and the first date initially looks like it's duplicated. See the dark blue 610, the orange 610, and then light-blue 820. So the last line is the at expiration perspective where there's no theory anymore. Your option is either intrinsically worth something, or it's worthless. And you can see this 9.88 number below 923, it doesn't get any worse. Whereas if we owned 100 shares of stock, that red number can keep getting bigger and bigger, the lower you go and move to the left. Notice our breakeven point is just 9.88 added to the 423, and the tool does it for you up here, at 422.88. Here's a 423 put version for August 20th. Now the reason why the price is slightly different here, SPY has coming dividend, right, and dividends are taken out of the share price, so known dividends are factored into option pricing. And you can see here, it's

very similar, below 423, that's where the green numbers are, right? But we're paying 10.76 for this example, so at expiration, if this is not below 412.24, right, we're not making any money at expiration. And if it goes up, you can see what our maximum loss is.

Now let's look at the selling strategies Brett took a look at. So this is the opposite side of that put. This is selling the put. So if the person who bought this can only lose 10.76 if it rises, no matter how high it rises, that means that's the most we can make if we sell this put. So what's the risk? Well if the person that bought this put is benefiting, that means that must be what's hurting us. But notice the breakeven point is exactly the same. So Brett mentioned covered calls are kind of used as substitutes for selling stock. Sometimes people use selling puts as ways to, hey, if it goes sideways or up, I'll just keep the premium. But if it goes down and I'm forced to buy the stock, in this case an effective price of 412.24, well I would have bought the stock anyway. So they can use it as a way to potentially acquire stock at less than the current market price if it goes down and you in fact get assigned, and notice the synthetic symmetry when I click on this "Buy Right," which is the fancy nickname for a covered call at the same strike, notice how the profile looks shockingly similar.

Now what I want to demonstrate here is let me click on the stock. So let's first go to the long call, and look at the shape of this graph. Now I'm going to click on the stock by itself, I'm going to hold Control, and click on the long put. And what have I done? I've cut off the downside risk with the put, but I paid a premium for it, synthetically creating the long call profile. Now obviously, there's real-world difference, like if SPY is paying a dividend, I don't own SPY, I don't get the dividend. So there are real-world mechanical differences, but from a risk-reward profile, you're creating the same situation, right?

Now the last thing I wanted to cover is this. So, this is the implied volatility, and I'm just going to take us down memory lane here. So I've done, this is SPY, looking back through the pandemic crash. And this at the bottom is roughly one- and two-month implied volatility of options. Look at the mountain of volatility when SPY was collapsing, and look how it reverted when SPY recovered. So you can see how important this can be to the value of your option depending on what happens to the demand for option. So we didn't focus on that today, but if you're new to options trading, you must factor this in, or you can be completely blindsided. Anybody who sold puts here, if you did not manage risk, not only did the decline in SPY hurt you, but the explosion in demand, or the value of options rose with it, and anybody who hedged up here, it would have been an incredibly effective hedge. How does

that translate? Well if implied volatility is relatively low and you think the market's in jeopardy of declining, if you end up needing that hedge in hindsight, lower implied volatility means maybe you might not need this, but if you do, it's relatively less expensive than it might be when everybody else thinks like they need to protect themselves as well.

END OF AUDIO FILE

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