

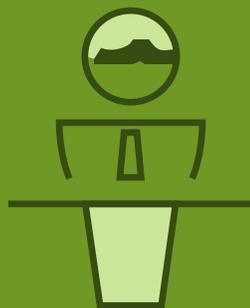


A Fidelity Investments Webinar

Buying an option? 5 things to know before you place the trade

BROKERAGE: **OPTIONS**





Agenda

How do I know which strategy to use?

What are strike and expiration dates and how can I choose?

What is exercise and why is it important?

Do liquidity and options pricing factor into my decision making?

How do I place an option trade?



How do I know which strategy to use?

Buying Options



Buying Calls – Bullish outlook

- Right to buy
- Long market exposure with risk limited to premium paid for options plus commissions



Buying Puts – Bearish outlook

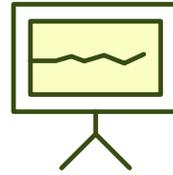
- Right to sell
- Short market exposure with risk limited to premium paid for options plus commissions
- Can potentially be used to help protect a single position or an entire portfolio

Buy a Call



Situation

XYZ is trading at \$42 a share



Market Forecast

Bullish on the stock, but want limited downside risk



Action

Buy one XYZ APR 42.50 call for \$2.10 (pay \$210)

Buy a Call: Profit and Loss Table

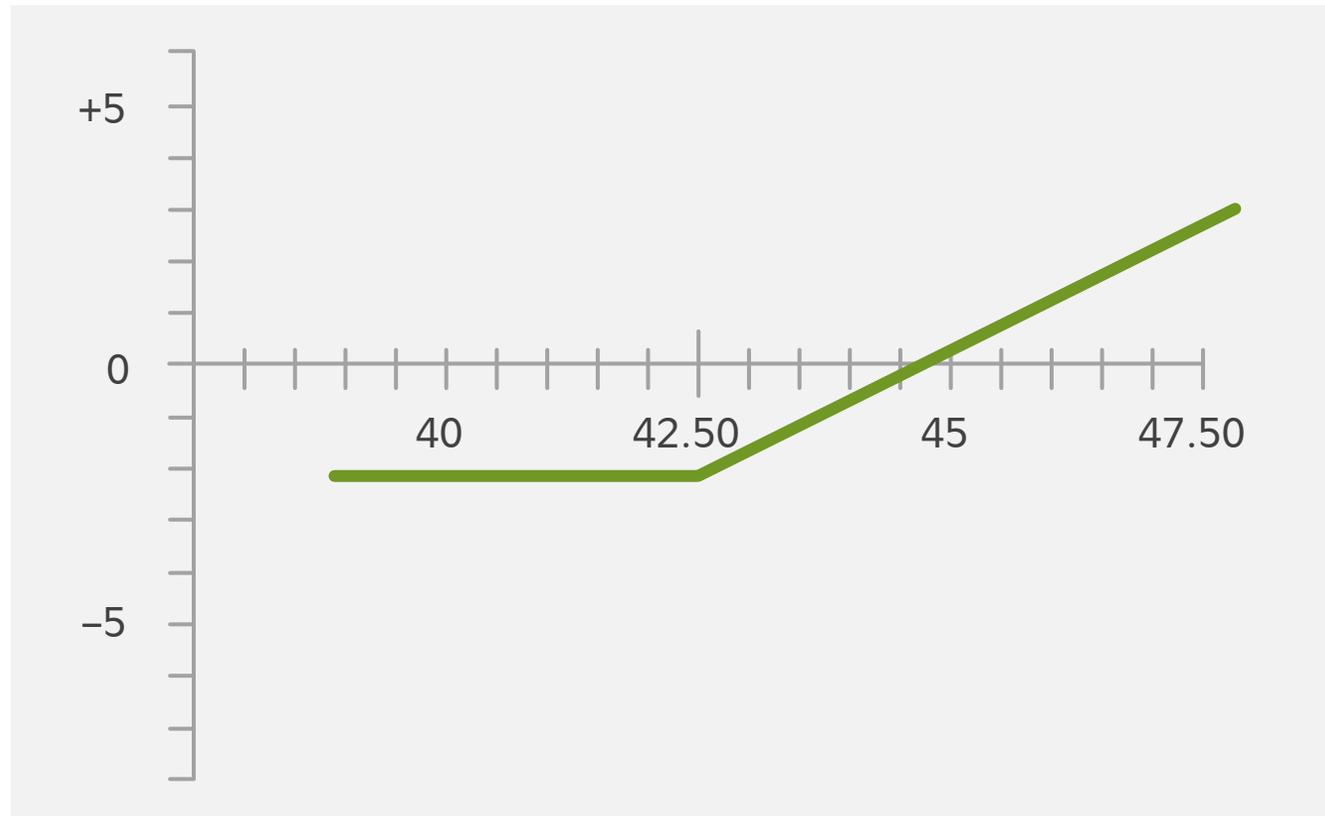

 Buy One XYZ APR 42.50 Call @ 2.10

PRICE AT EXP	OPTION COST	VALUE AT EXP	PROFIT/(LOSS)
50	2.10	7.50	5.40
45	2.10	2.50	0.40
44.60	2.10	2.10	0 (Breakeven)
42.50	2.10	0	(2.10)
40	2.10	0	(2.10)
37.50	2.10	0	(2.10)

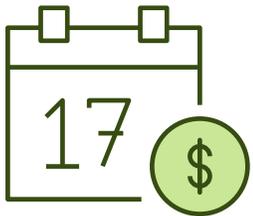
Buy a Call: Profit and Loss Diagram



Buy One XYZ
APR 42.50
Call @ 2.10

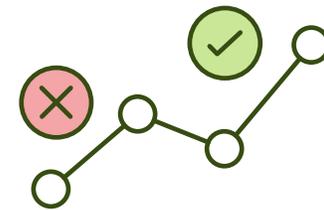


The Put Buyer



The Put Buyer

- Has the right to sell the underlying stock at an agreed-upon price (the strike) until the expiration date
- For this right, the put buyer pays a premium



Risk/Reward Profile

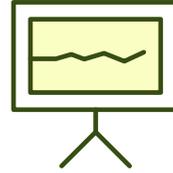
- Risk limited to option premium paid plus commission
- Maximum profit potential reached with the underlying at zero.

Buy a Put



Situation

XYZ is trading at \$42.50 a share



Market Forecast

Bearish on the stock, but want limited risk



Action

Buy one XYZ APR 42.50 put for \$2.30 (pay \$230)

Buy a Put: Profit and Loss Table

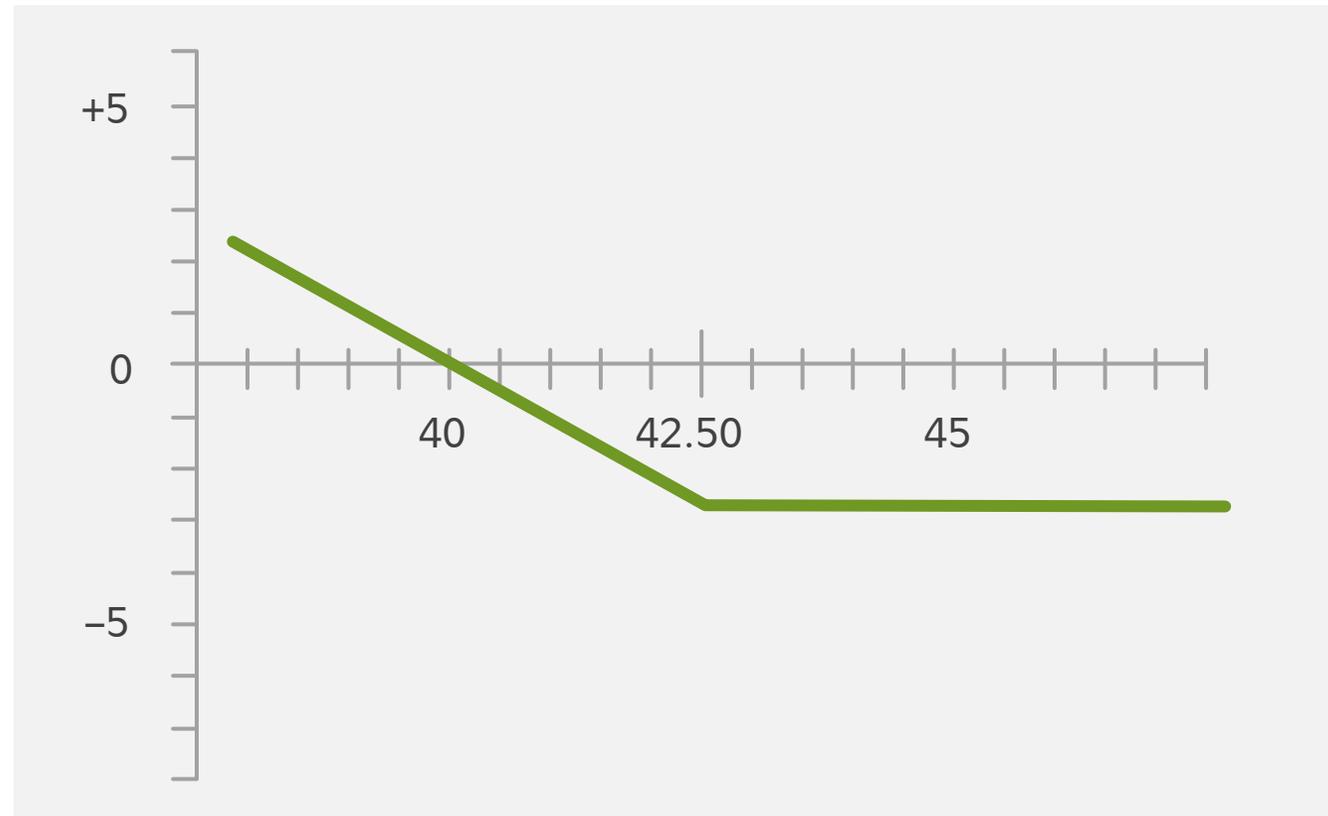

 Buy One XYZ APR 42.50 Put @ 2.30

PRICE AT EXP	OPTION COST	VALUE AT EXP	PROFIT/(LOSS)
50	2.30	0	(2.30)
45	2.30	0	(2.30)
42.50	2.30	0	(2.30)
40.20	2.30	2.30	0 (Breakeven)
40	2.30	2.50	0.20
37.50	2.30	5	2.70

Buy a Put: Profit and Loss Diagram



Buy One XYZ
APR 42.50
Put @ 2.30





What are strike and expiration dates and how can I choose?

What are strike prices and expiration dates?

Strike price

The strike is the price per share for which the underlying security may be purchased (in the case of a call) or sold (in the case of a put) by the option holder upon exercise of the option contract.

Expiration date

The last date that you can exercise your stock options; after this date, your options have no value.

Strike selection

Moneyness considerations

1 In the money

Pay a higher premium

Makes sense when:

Looking for option price moves that are more closely aligned to that of the underlying.

2 At the money

Most time value

Makes sense when:

Looking for balanced exposure but typically has most exposure to time decay.

3 Out of the money

Lower premium paid

Makes sense when:

Looking to risk less capital and expecting large move in underlying

Expiration selection

Reason for trade will impact the selected time frame

1 Shorter term

Pay a lower premium

High price acceleration,
but more time decay

2 Longer term

Pay a higher premium

Less time decay, but less
price acceleration

Typically, option buyers use further out expirations

Time works against long option positions

Further-dated expirations reduce the effects of time decay

More time for outlook to play out



What is exercise and why is it important?

What is exercise?

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 no intrinsic value at exercise, it will expire worthless.

Remember

Long options are exercised, while short options are assigned.

Only allow an option to be auto-exercised if it is commensurate with the number of shares you would want to own/sell.

What is exercise?

Early Exercise

Makes Sense When:

You cannot sell the option in the open market for at least intrinsic (exercise) value.

- Typically, the option is either very deep in the money, close to expiration, or both

Example

You are long (own) one ABC Call expiring this Friday with a strike of 100. ABC is at 105.

Your ABC contract is currently trading at 4.50 x 5.50 and you wish to close the position.

If you sold your contract to the bid, you would only receive \$4.50. But, if you exercise your option to buy ABC at \$100 and then sell the stock on the open market for \$105, you'd receive the \$5.00 difference.



Do liquidity and options pricing factor into my decision making?

Understanding options liquidity

What is bid?

The highest price a prospective buyer is willing to pay for a unit of a security. This is the current price in which you can **sell** an option.

What is ask?

The lowest price a dealer or market maker will accept for a security. This is the current price in which you can **buy** an option.

The spread and why it matters

Wider spreads can result in paying more for or receiving less than the theoretical value of that contract.

▼	Bid	Ask	Strike ▼		Bid	Ask
▼	CALLS		Mar 02 (W) (29 days)		PUTS	
	2.75	3.49	26		3.95	4.78
	3.30	3.76	25		3.23	4.03
	3.30	4.07	24		2.55	3.33
	3.60	4.43	23		2.25	2.67
	4.00	4.85	22		1.34	2.06

▼	Bid	Ask	Strike ▼		Bid	Ask
▼	CALLS		Mar 04 (W) (31 days)		PUTS	
	2.23	2.28	21.5		3.15	3.25
	2.36	2.41	21		2.83	2.89
	2.50	2.55	20.5		2.47	2.52
	2.66	2.71	20		2.13	2.18
	2.82	2.89	19.5		1.81	1.85

Options Premium Components

$$\text{Premium} = \text{Intrinsic Value} + \text{Extrinsic Value}$$

An options contract that has intrinsic value is
"in the money"

An options contract that has no intrinsic value is
"out of the money"

Factors That Affect Price



Stock Price



Time to Expiration



Volatility

Option Valuations

What factors affect the supply and demand for options?

Stock owners
get nervous

Buy options for potential
protection or speculation

Buying pressure
raises IV levels

Higher expected
move in the security

Higher demand for
option contracts

Higher IV levels

Implied Volatility:

Implied Volatility (IV) can be used as a measure of an option's relative value. Supply and demand for option contracts affects IV.

Result: More expensive premiums

Consider Time Decay



Time decay typically accelerates as expiration comes closer, meaning shorter-term options have the highest time decay.

Strike	Last	Bid	Ask	Theta
Nov 22 CALLS				
85	13.40	13.45	13.65	-0.0198
87.5	11.25	11.10	11.30	-0.0258
90	9.00	8.90	9.05	-0.0336
92.5	6.95	6.85	7.00	-0.0413
95	5.10	5.05	5.20	-0.0473
97.5	3.55	3.55	3.60	-0.0491
100	2.35	2.35	2.38	-0.0468
105	0.85	0.84	0.86	-0.0317
110	0.30	0.29	0.30	-0.0176
115	0.12	0.12	0.13	-0.0099
Apr 17 CALLS				
95.71	8.50	8.45	8.60	-0.0204
96.43	8.15	8.05	8.20	-0.0204
97.14	7.95	7.70	7.85	-0.0205
97.5	7.63	7.50	7.65	-0.0204
97.86	7.45	7.35	7.50	-0.0205
98.57	7.10	7.00	7.15	-0.0205
99.29	6.66	6.65	6.80	-0.0204
100	6.45	6.35	6.45	-0.0204
100.71	6.10	6.05	6.20	-0.0204
101.43	5.70	5.75	5.90	-0.0203

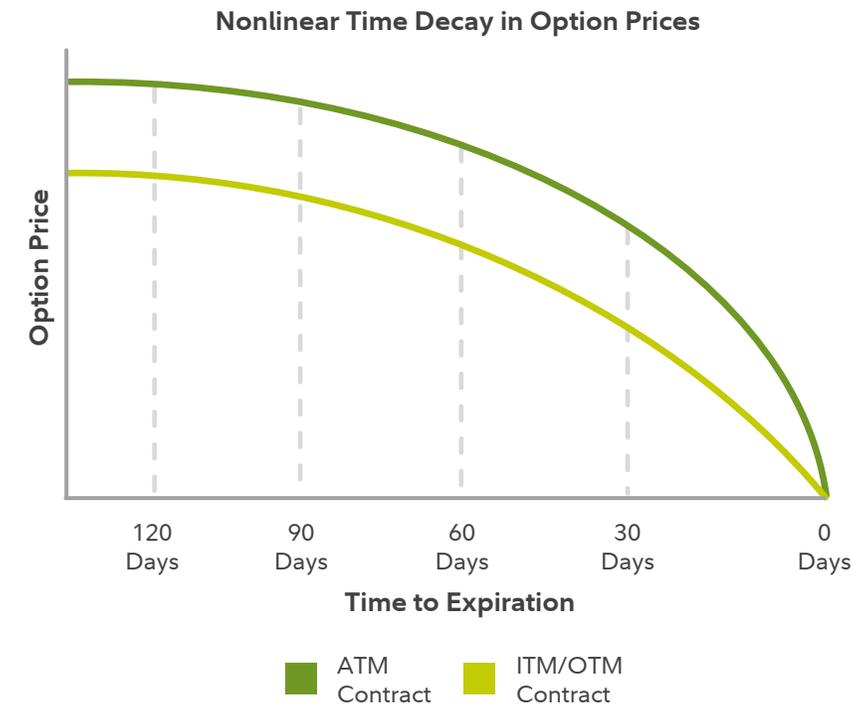
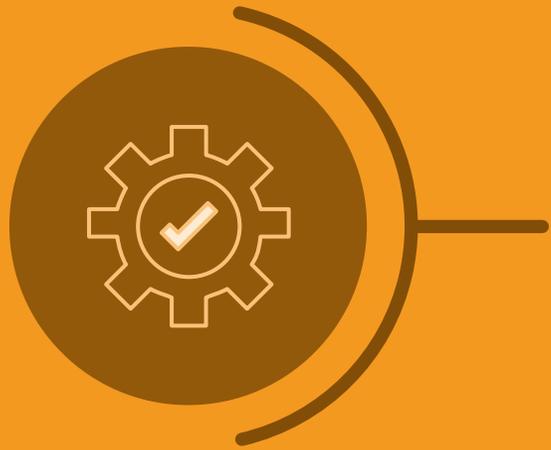


Image is for illustrative purposes only.



How do I place an
option trade?

Before You Place a Trade, Consider...

1

Buying one call is the equivalent of buying 100 shares of stock

2

Consider how much risk you are comfortable taking on

3

Be aware of position size to manage your risk

Placing an option trade

How do you **open a trade**?

To initiate a new long position, you would select "***buy to open.***"

How do you **close a trade**?

Long option holders simply "***sell to close.***" This sells your right to exercise the option.

Market or limit order?

A limit order sets the maximum price at which you're willing to buy or the minimum price at which you're willing to sell. Limit orders target price, but do not guarantee execution.

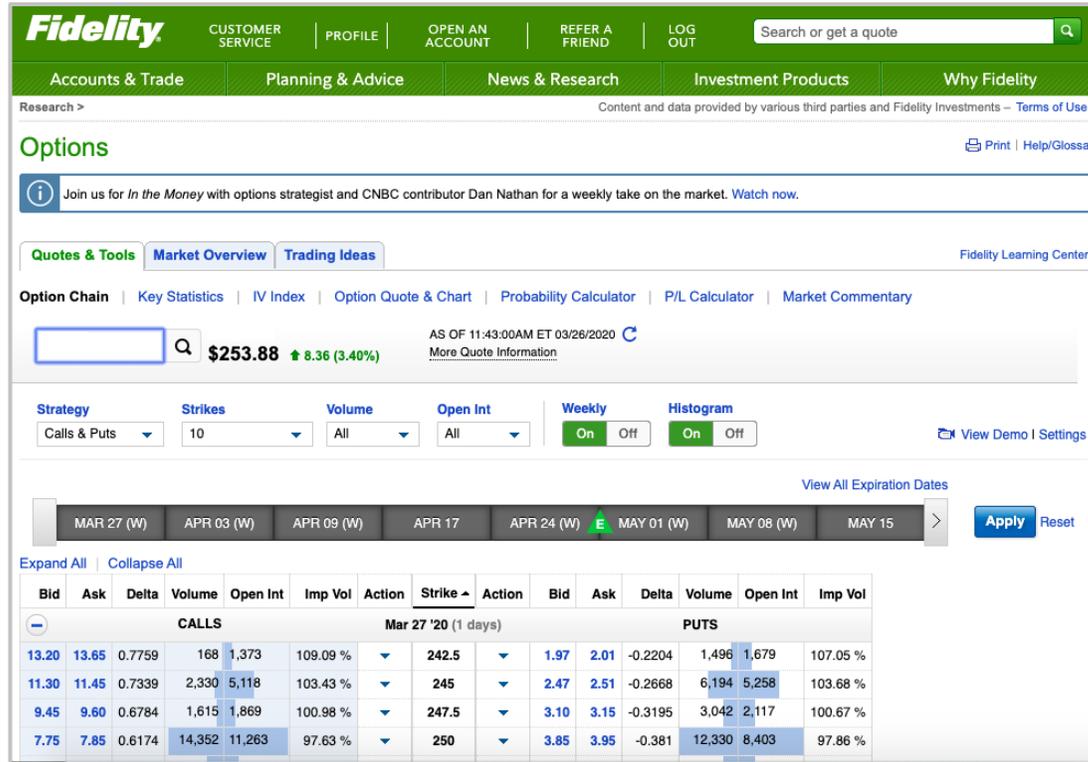
A market order indicates you are willing to either buy or sell at the next available market price. Market orders target execution, but do not guarantee price.

Place a Trade on Fidelity.com

News & Research > Options > Option Chain

Start a trade from the Option Chain

- Easily see all the available options
- Fully customizable to meet your needs



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AS OF 11:43:00AM ET 03/26/2020 [More Quote Information](#)

Strategy: Calls & Puts | Strikes: 10 | Volume: All | Open Int: All | Weekly: On | Histogram: On

View All Expiration Dates

MAR 27 (W) | APR 03 (W) | APR 09 (W) | APR 17 | APR 24 (W) | **E** MAY 01 (W) | MAY 08 (W) | MAY 15 | [Apply](#) [Reset](#)

Bid	Ask	Delta	Volume	Open Int	Imp Vol	Action	Strike	Action	Bid	Ask	Delta	Volume	Open Int	Imp Vol	
CALLS															
Mar 27 '20 (1 days)															
13.20	13.65	0.7759	168	1,373	109.09 %	▼	242.5	▼	1.97	2.01	-0.2204	1,496	1,679	107.05 %	
11.30	11.45	0.7339	2,330	5,118	103.43 %	▼	245	▼	2.47	2.51	-0.2668	6,194	5,258	103.68 %	
9.45	9.60	0.6784	1,615	1,869	100.98 %	▼	247.5	▼	3.10	3.15	-0.3195	3,042	2,117	100.67 %	
7.75	7.85	0.6174	14,352	11,263	97.63 %	▼	250	▼	3.85	3.95	-0.381	12,330	8,403	97.86 %	
PUTS															

Place a Trade on Fidelity.com

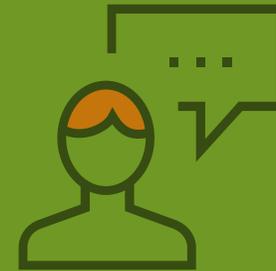


News & Research > Options > Option Chain

- Easy access to your balances and positions
- Quickly adjust to contract specifications

The screenshot displays the Fidelity Options trading interface. At the top, there is a navigation bar with links for 'Accounts & Trade', 'Planning & Advice', 'News & Research', 'Investment Products', and 'Why Fidelity'. Below this, a 'Trade' section includes a search bar and a 'New to options trading? Register for free options coaching' link. The main area shows account information: 'TRADE Options', 'ACCOUNT', 'Margin Buying Power \$17,529.82', 'Non-Margin Buying Power \$8,764.91', and 'Options Level 5'. A 'Symbol' search bar is present. Below the search bar, there are links for 'Option Chain', 'Option Summary', and 'View Orders'. The 'Option Chain' section is active, showing 'Calls & Puts', 'Spread', and 'More Strategies'. The 'ACTION' dropdown is set to 'Buy To Open', and the 'Call' button is selected. The 'Expiration' and 'Strike' dropdowns are also visible. At the bottom, there are fields for 'ORDER TYPE' (Limit), 'Limit Price \$', 'TIME IN FORCE' (Day), 'TRADE TYPE' (Margin), and 'ROUTE' (Auto). The 'Estimated Order Value' is shown as '--'. At the very bottom, there are links for 'Probability Calculator' and 'Profit & Loss Calculator'.

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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.

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