

**IN REAL ESTATE AN OPTION CAN
CONVEY THE RIGHT TO BUY
(A CALL OPTION IN THE EQUITY MARKETS)**

**MARKET VALUE TODAY
\$250,000,000**



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CALL OPTION - THE RIGHT TO BUY

**MARKET VALUE TODAY
\$250,000,000**



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THE HOUSE HAS BEEN ON THE MARKET FOR 6 MONTHS AND NO OFFERS YET !

I think the market will rise, and offer you \$10,000,000 for a three-month option to buy at \$250,000,000 – the Strike Price.

You think the market is flat and sell me the option for \$10,000,000 – the Premium.



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If the market rises to \$450,000,000, I can exercise my option. I have the right to buy, and you have the obligation to sell.

**Strike \$250,000,000
Term 3 months
Premium \$10,000,000**

If the market falls and the house is worth \$200,000,000, I can abandon my option and forego the Premium.

You retain the Premium and keep the house.

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TYPES OF OPTION CONTRACTS

CALL OPTION

PUT OPTION

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OPTION BASICS

- Rule #1
 - Always have an exit plan before you enter a trade.
- Rule #2
 - Never ever forget, pooh – pooh, disparage, or in any other manner be disrespectful or cavalier about Rule #1!

Options Basics

- Rule #3
 - Always let the market know what rule #1 is by placing your exit order in the market.
- Why?
 - There have many cases of catastrophe between the time an order is filled and your ability to execute your mental stop.
 - Lost connectivity
 - Heart attack / illness
 - Emergency
 - Death
 - Natural disaster
 - Equipment failure
 - Man made disasters

Options Basics

- What is an option?
- Before we get into what a stock option is let's take a look at the concept of an "option."

AMERICAN AND EUROPEAN STYLE OPTIONS

- An American-style option can be exercised at any time before expiration.
- European-style options can be exercised only at the expiration date.
- It has nothing to do with where the options are traded.

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BUYING A CALL OPTION

- THE CONTRACT GIVES THE BUYER THE RIGHT, BUT NOT THE OBLIGATION (a choice or option)
 - to buy the futures contract (*underlying asset*)
 - at a pre-determined price (*the strike*).
- You purchase a Call option contract
 - for a certain period of time (*time to expiration*)
 - for a price (*premium*).

IT IS IMPORTANT TO KNOW THE RIGHTS OF AN OPTION BUYER!

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BUYING A CALL – PROFIT AND LOSS

- Profit is unlimited.
- Loss is limited to the premium paid.

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SELLING A CALL

- Selling a Call contract imposes the obligation on the seller, if exercised
 - to sell the stock (*underlying asset*)
 - at a pre-determined price (*the strike*).
- You sell a Call option contract
 - for a certain period of time (*time to expiration*)
 - for a price (*premium*).

SELLING AN OPTION IS SOMETIMES CALLED
“WRITING AN OPTION”

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WRITING A CALL – PROFIT AND LOSS

- Profit is limited to the premium received.
- Loss is unlimited.
- Seller/Writer must put up margin or cash.

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SELLING / WRITING A CALL

- Seller has immediate, but unearned, profit.
- The trade is not profitable until you earn back the premium.
- Gives you unlimited loss potential. (If you don't know what you are doing)
- Gives you limited profit — profits are limited to the premium earned.

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SELLING / WRITING A CALL

- Exchanges and brokers will tell you there is no way to protect against unlimited loss.
- *That is not true – if you know how! We teach you how to protect yourself.*
- Exchanges and brokers emphasize that all you can win is the premium paid.
- *Because they want to sell you the options knowing that you will lose your money 75% of the time.*

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SELLING / WRITING A CALL

AS A SELLER:

- You must manage the option to its conclusion so you don't lose the premium.
- You have cash in your hand - don't lose it!

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EXERCISING A CALL OPTION

- The Buyer
 - Will exercise only when it is profitable.
 - Will receive a long stock position at the strike price.
 - Will have to sell the stock to close out and realize a profit.
- The Writer
 - Will receive a short stock position at the strike price.
 - Will have to buy the stock to close out his position.

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EXERCISING A CALL OPTION

- The Buyer
 - Makes more money by selling the option than by exercising it.
 - Exercises it when he can't sell it.
 - Exercising is not often before expiration.
 - Options will not be exercised if they are in the money or close to it (ASK your broker for their rules).
- The Seller
 - Will seldom be exercised.
 - Will be exercised if the option is in the money.
 - Will usually be exercised at or close to expiration. ¹⁸

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EXERCISING A CALL OPTION

- The Seller
 - is assigned a futures position.
 - must offset by taking an opposite futures position — this gets him out of the trade.
 - Note: Selling is not as drastic as it's made out to be, but exchanges and brokers will try to scare you away from being an option seller.
 - Note: American style options can be exercised at any time — European style options are exercisable only at expiration.

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BUYING A PUT

- THE CONTRACT GIVES THE BUYER THE RIGHT, BUT NOT THE OBLIGATION (the choice or option),
 - to sell the futures contract (*underlying asset*)
 - at a pre-determined price (*the strike*).
- You purchase a Put option contract:
 - for a certain period of time (*time to expiration*)
 - for a price (*premium*).

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BUYING A PUT

- **Strike prices are the same for Puts as for Calls.**
- **Most Puts are purchased at strike prices close to the current futures price.**
- **More Calls are traded than Puts because of trader/investor bias towards prices moving up.**

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BUYING A PUT – PROFIT AND LOSS

- **Profit is unlimited (to a futures price of zero).**
- **Loss is limited to the premium paid.**
- **Buyer does not have to put up margin.**

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WRITING / SELLING A PUT

- The contract imposes the obligation on the writer, if exercised
 - to buy the futures contract (*underlying asset*)
 - at a pre-determined price (*the strike*).
- You can write a Put option contract
 - for a certain period of time (*time to expiration*)
 - for a price (*premium*).

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SELLING A PUT – PROFIT AND LOSS

- Profit is limited to the premium received.
- Loss is unlimited (to a futures price of zero).
- Writer/Seller has to put up margin.

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SELLING / WRITING A PUT

- You have immediate unearned profit.
- Is not profitable until you earn back the premium.
- Gives you unlimited loss potential.
- Gives you limited profit — profits are limited to the premium earned.
- Requires managing the trade so you keep the premium.

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EXERCISING A PUT OPTION

- The Buyer
 - Will exercise only when it is profitable.
 - Will receive a short futures position at the strike price.
 - Will have to buy futures to close out and realize a profit.
- The Seller
 - Will receive a long futures position at the strike price.
 - Will have to sell to close out his position.

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EXERCISING A PUT OPTION

- The Buyer
 - Makes more money by selling the option than by exercising it.
 - Exercises it when he can't sell it.
 - Exercising is not often done.
 - Options will not be exercised unless they are in the money.
- The Seller
 - Will seldom be exercised.
 - Will sometimes be exercised if the option is deep in the money.
 - Will usually be exercised at or close to expiration.

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TERMINOLOGY

- **Buyer or Owner** - person who buys an option.
- **Writer/Seller** - person who sells an option.
- **Strike** - price at which you will be given a futures position if you exercise your option.
- **Premium** - amount the option costs.
- **Note: do not confuse Strike with Premium.**
- **Expiration date** - the option becomes worthless.
- **Declaration date** - date option is exercised.

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BASIC DEFINITIONS

- **LONG CALL** owner can **BUY** futures.
- **LONG PUT** owner can **SELL** futures.

- **SHORT CALL** Seller must **SELL** futures if assigned.
- **SHORT PUT** Seller must **BUY** futures if assigned.

- **Note:** long and short are not market directional — long = buy, short = sell.

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THE LONG AND THE SHORT OF IT.....

- THE **BUYER** OF A CALL IS **L O N G** THE CALL.
- THE **BUYER** OF A PUT IS **L O N G** THE PUT.

- THE **SELLER** OF A CALL IS **S H O R T** THE CALL.
- THE **SELLER** OF A PUT IS **S H O R T** THE PUT.

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OPTION SYMBOLS

- One stock can have hundreds of options
 - Let's use Apple Computer (AAPL) as our example
 - A stock can have 4 or more expiration months
 - Depending on the stock's price there can be more than 25 strike prices
 - Puts and Calls have the same strike prices

OPTION SYMBOLS

- Apple currently has 6 months in which it has options. These months can change:
 - Call strike quantity = 25
 - Put strike quantity = 25
 - Total strike quantity = 50
 - Total expirations months = x 6
 - Total options choices for AAPL = 300
- Knowing which option to choose can determine your profit. Option-Trading-Educators will teach how to select the correct option.

AN OPTION CHAIN LISTS ALL THE AVAILABLE OPTIONS FOR A GIVEN MONTH

- Calls and puts
- Month and year of expiration
- Bid and ask price
- Strike price
- All Options expire on the 3rd Friday of the expiration month

Calls				Puts							
Last	Bid	Ask	Strike	Last	Bid	Ask					
May 10 Calls (50 days to expiration)				AAPL @ 235.97				May 10 Puts			
0	94.35	96.25	140.00	0.01	0	0	0.02				
80.30	99.40	99.25	145.00	0.04	0.01	0.02	0.02				
79.75	84.40	86.25	150.00	0.03	0.02	0.04	0.04				
81.25	80.90	81.25	155.00	0.03	0.04	0.05	0.05				
77.10	75.95	76.30	160.00	0.06	0.06	0.08	0.08				
89.65	71.00	71.30	165.00	0.08	0.10	0.11	0.11				
83.70	66.05	66.40	170.00	0.12	0.15	0.16	0.16				
82.90	61.15	61.45	175.00	0.23	0.22	0.24	0.24				
57.40	56.25	56.55	180.00	0.34	0.33	0.34	0.34				
50.25	51.35	51.70	185.00	0.50	0.46	0.48	0.48				
44.75	46.05	46.30	190.00	0.67	0.67	0.69	0.69				
36.63	41.05	41.15	195.00	0.96	0.96	0.98	0.98				
37.25	37.30	37.55	200.00	1.37	1.34	1.37	1.37				
28.60	28.60	28.75	210.00	2.63	2.50	2.62	2.62				
20.75	20.75	20.90	220.00	4.79	4.70	4.80	4.80				
14.20	14.20	14.30	230.00	8.19	8.10	8.20	8.20				
9.15	9.10	9.20	240.00	13.13	13.00	13.15	13.15				
5.50	5.45	5.55	250.00	19.45	19.40	19.50	19.50				
3.15	3.15	3.20	260.00	27.89	27.00	27.20	27.20				
1.70	1.71	1.75	270.00	34.56	35.60	35.80	35.80				
0.94	0.91	0.95	280.00	46.00	44.80	45.05	45.05				
0.46	0.48	0.50	290.00	63.70	64.35	64.60	64.60				
0.25	0.24	0.25	300.00	86.40	84.10	85.70	85.70				
0.12	0.12	0.13	310.00	0	74.00	75.65	75.65				
0.08	0.08	0.08	320.00	0	83.95	85.55	85.55				
0.05	0.03	0.05	330.00	0	93.90	95.70	95.70				
0.04	0	0.03	340.00	0	103.90	105.65	105.65				

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IN THE MONEY (ITM) AND OUT OF THE MONEY (OTM)

- An **ITM** Call has a strike price less than the price of the stock
 - Example the AAPL May 2010 230 call is less than the stock price of 235.97. Therefore it is ITM
- An **OTM** Call has a strike price greater than the price of the stock
 - Example; the AAPL May 2010 240 call is greater than the stock price of 235.97. Therefore it is OTM
- A Put is the opposite of a Call

Calls				Puts							
Last	Bid	Ask	Strike	Last	Bid	Ask					
May 10 Calls (50 days to expiration)				AAPL @ 235.97				May 10 Puts			
0	94.35	96.25	140.00	0.01	0	0	0.02				
80.30	99.40	99.25	145.00	0.04	0.01	0.02	0.02				
79.75	84.40	86.25	150.00	0.03	0.02	0.04	0.04				
81.25	80.90	81.25	155.00	0.03	0.04	0.05	0.05				
77.10	75.95	76.30	160.00	0.06	0.06	0.08	0.08				
89.65	71.00	71.30	165.00	0.08	0.10	0.11	0.11				
83.70	66.05	66.40	170.00	0.12	0.15	0.16	0.16				
82.90	61.15	61.45	175.00	0.23	0.22	0.24	0.24				
57.40	56.25	56.55	180.00	0.34	0.33	0.34	0.34				
50.25	51.35	51.70	185.00	0.50	0.46	0.48	0.48				
44.75	46.05	46.30	190.00	0.67	0.67	0.69	0.69				
36.63	41.05	41.15	195.00	0.96	0.96	0.98	0.98				
37.25	37.30	37.55	200.00	1.37	1.34	1.37	1.37				
28.60	28.60	28.75	210.00	2.63	2.50	2.62	2.62				
20.75	20.75	20.90	220.00	4.79	4.70	4.80	4.80				
14.20	14.20	14.30	230.00	8.19	8.10	8.20	8.20				
9.15	9.10	9.20	240.00	13.13	13.00	13.15	13.15				
5.50	5.45	5.55	250.00	19.45	19.40	19.50	19.50				
3.15	3.15	3.20	260.00	27.89	27.00	27.20	27.20				
1.70	1.71	1.75	270.00	34.56	35.60	35.80	35.80				
0.94	0.91	0.95	280.00	46.00	44.80	45.05	45.05				
0.46	0.48	0.50	290.00	63.70	64.35	64.60	64.60				
0.25	0.24	0.25	300.00	86.40	84.10	85.70	85.70				
0.12	0.12	0.13	310.00	0	74.00	75.65	75.65				
0.08	0.08	0.08	320.00	0	83.95	85.55	85.55				
0.05	0.03	0.05	330.00	0	93.90	95.70	95.70				
0.04	0	0.03	340.00	0	103.90	105.65	105.65				

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IN THE MONEY (ITM) AND OUT OF THE MONEY (OTM)

• An **OTM Put** has a strike price less than the price of the stock

• Example the AAPL May 2010 230 Put is less than the stock price of 235.97. Therefore it is OTM

• An **ITM Put** has a strike price greater than the price of the stock

• Example; the AAPL May 2010 240 Put is greater than the stock price of 235.97. Therefore it is ITM

Calls				Puts			
Last	Bid	Ask	Volume	Last	Bid	Ask	Volume
May 10 Calls (50 days to expiration)							
0	94.35	94.35	0	0.01	0	0.02	0
80.30	89.40	89.50	145.00	0.04	0.01	0.02	0.02
79.75	84.40	84.50	150.00	0.03	0.02	0.04	0.04
79.25	80.90	81.00	155.00	0.03	0.04	0.05	0.05
77.60	75.95	76.00	160.00	0.06	0.06	0.08	0.08
69.65	70.95	71.00	165.00	0.08	0.10	0.11	0.11
63.70	66.00	66.10	170.00	0.12	0.15	0.16	0.16
62.90	61.15	61.20	175.00	0.23	0.22	0.24	0.24
57.40	56.25	56.30	180.00	0.34	0.33	0.34	0.34
50.25	51.35	51.40	185.00	0.50	0.46	0.48	0.48
44.75	46.05	46.10	190.00	0.67	0.67	0.69	0.69
36.63	41.05	41.10	195.00	0.96	0.96	0.98	0.98
37.25	37.30	37.35	200.00	1.37	1.34	1.37	1.37
28.60	28.60	28.70	210.00	2.63	2.50	2.62	2.62
20.75	20.75	20.80	220.00	4.79	4.70	4.80	4.80
14.20	14.20	14.30	230.00	8.19	8.10	8.20	8.20
9.15	9.10	9.20	240.00	13.13	13.00	13.15	13.15
5.00	5.45	5.55	250.00	19.45	19.40	19.50	19.50
3.15	3.15	3.20	260.00	27.89	27.00	27.20	27.20
1.70	1.70	1.75	270.00	34.56	35.60	35.80	35.80
0.94	0.91	0.95	280.00	46.00	44.80	45.05	45.05
0.46	0.48	0.50	290.00	63.70	64.35	64.80	64.80
0.25	0.24	0.25	300.00	86.40	84.10	85.70	85.70
0.12	0.12	0.13	310.00	0	74.00	75.65	75.65
0.08	0.08	0.09	320.00	0	83.95	85.55	85.55
0.05	0.03	0.05	330.00	0	93.90	95.70	95.70
0.04	0	0.03	340.00	0	103.90	105.65	105.65

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BASICS

Options Trading Newsletter

Sign up for Jim Augustine's FREE weekly Stock Options Trading Newsletter, "Options Scan," to learn:

- How to apply the Law of Charts to a current trading opportunity.
- Which Option he picks or if he trades just the stock.
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OPTIONS TRADING SEMINAR for STOCKS with Jim Augustine in Dallas/Ft. Worth, Texas

August 28-29, 2010



- This options trading seminar will teach you how to become a winning trader if you are willing to take action on the simple techniques presented in the seminar.
- The information you will receive will help you succeed beyond your expectations. We share with you the greatest achievement; the ability to trade any market, in any time frame: day trade, position trade, swing trade, or long-term trade in any market, any time, anywhere in the world. All you need is a data source and the ability to place an order.

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