

Options Trading For Income Crash Course – Day 1



• Just a quick introduction...





Founded over 23 Years Ago. We've been working with over 100,000 people just like you for over two decades. Bull markets, Bear Markets, Sideways Go Nowhere Markets. People like you using our systems in over 110 Countries Worldwide!



Just Who is the NetPicks Team?

These are the people who will be with you every step of the way



Mark Soberman, Founder 1996







Will Feibel, Senior Programmer Mike Rykse, Senior Options Analyst & Educator



TJ Noonan, Active System Developer & Trading Coach



Brian Short, Partner

Shane Daly, Trading Educator Adnan Younes, Forex Analyst



Cheryl Nofziger, Customer Support Manager





Just Who Is This Mike Rykse 😀

Mike has been working with NetPicks for over 13 years and has developed our entire line-up of highly successful options trading systems and curriculum. This includes our Options Fast Track. Options Mastery. Options Blueprint and more.

Mike has been trading options for nearly two decades and actually walks the walk. Options trading has been a primary source of income for Mike. Would you rather learn and trade the same setups of someone doing it live in the market daily or just hypothetically?

Mike never stops working to improve his personal trading and results and sharing those breakthroughs with all of you. Today? We have his most important breakthrough to date to share.





Agenda

- Day 1
 - How much capital do I need to trade with?
 - Broker Selection and Account Setup
 - Options 101 Review
 - Long Calls and Long Puts
 - Debit Spreads
- Day 2
 - Credit Spreads
 - Which options strategy should I use?
 - Setting Alerts, Daily Routine, Trade Journal
 - Risk Management
 - Watch List Creation



Why Options Trading is Superior

- Amazing Leverage You can control \$100,000+ of ETFs for pennies on the dollar. Just a few hundred dollars but still enjoy the upside.
- **Controlled Risk** Unlike most highly leveraged markets such as Forex or Futures, Options can be traded with a maximum fixed risk
- Trade the Well Known Markets, Sectors & Locations - Whether it's the S&P 500, Nasdaq 100, or Emerging Markets, Biotech, Technology, Silver, China, Financials or more...
- Win 5 Different Ways Name another trading strategy that you can win with 5 different outcomes, normally it's just one
- **Scaling** There's huge volumes, especially on the markets we trade so your account grows and so does your position sizing and therefore income without any additional work. Liquidity galore in options





- We recommend starting with a \$3500 account
- While you can start with less it becomes more difficult to control the risk if you do.
- You want an account size where you can keep the risk at 2-5% of your account per trade



- 2 Main types of options accounts:
- Margin Account
 - Subject to the pattern day trading rules
 - Will be able to use any options strategy you want. This will help you control the risk much easier.
- Cash Account
 - Is not subject to the pattern day trading rules
 - Ideal if you are looking to day trade options
 - Limited to trading long calls and puts



Broker Options

- 1. TastyWorks <u>http://www.tastyworks.com</u>
- 2. TD Ameritrade <u>http://www.tdameritrade.com</u>
- 3. Tradestation <u>http://www.tradestation.com</u>
- 4. Interactive Brokers <u>http://www.interactivebrokers.com</u>

tastyworks.

A brokerage from the brains behind tastytrade









Options 101 Review: What is an option?

- Call option
 - A contract between a buyer and a seller for a specific period of time
 - Buyer has the <u>right</u>, but not the obligation, to purchase 100 (or 10 with a mini contract) shares of stock at a specific price by a specific date. This has the effect of locking in the purchase price for a period of time.
 - The buyer has rights
 - The buyer is considered long the option.
 - The buyer is considered long the position
 - Seller has the <u>obligation</u> to sell 100 (or 10 with a mini contract) shares of stock at a specific price, when requested, up until a specific date.
 - The seller has obligations
 - The seller is considered short the option.
 - The seller is considered short the option.



- Put option
 - A contract between a buyer and a seller for a specific period of time
 - Buyer has the <u>right</u>, but not the obligation, to sell 100 (or 10 with a mini contract) shares of stock at a specific price by a specific date.
 This has the effect of locking in the sales price for a period of time.
 - The buyer has rights
 - The buyer is considered long the option.
 - The buyer is considered short the position.
 - Seller has the <u>obligation</u> to buy 100 (or 10 with a mini contract) shares of stock at a specific price, when requested, up until a specific date.
 - The seller has obligations
 - The seller is considered short the put option.
 - The seller is considered long the position.



Options 101 Review: Option Specs

- Standard option contract:
 - 100 shares of a stock

 Number of Contracts 	Number of shares of stock
1	100
2	200
5	500
20	2000

- Option price quote is per share
- Commission quoted per contract
- Cost of an option trade:

Total cost = (number of contacts) x (\$ per contract) x 100 + commissions Example: 10 contracts quoted at \$1.25 with \$1.50 commission $(10 \times $1.25 \times 100) + (10 \times $1.50) = 1,250 + 15.00 = $1,265.00$ equivalent to 1000 shares of stock



Options 101 Review: Expiration

- Monthly options
 - expire on 3rd Friday of the month
 - Front month
 - Next month
 - plus about 6 out months
 - LEAPS©: Long-term Equity AnticiPation Securities, longer term options expiring a year to up to 2 years and 8 months out
- Weekly options, also called Weeklys, short-term or short-dated options
 - Recent product first released for major indexes
 - First released for stocks in June 25, 2010: AAPL, BAC, BP, C
 - Listed on Thursday 8 days before expiration
 - More released each month
 - Available products: http://www.cboe.com/micro/weeklys/ availableweeklys.aspx



Implied Volatility – IV Percentile







1. Delta

- The delta of an option is a measurement that estimates how much an option premium will increase or decrease with every \$1 move in the underlying stock or index. Also known as the % change.
- Calls will have a positive delta ranging from 0 to 1
- Puts will have a negative delta ranging from 0 to -1
- The delta of a call increases in value as a stock moves up and decreases as the stock moves down.
- The delta of a put decreases as a stock moves up and increases as the stock moves down.
- ATM options will have a delta close to +/- .50
- ITM options will have a higher delta which means they react faster to the movement in the stock
- Delta will also increase and decrease faster as you get closer to expiration.



Greeks – Delta cont.

- 1. Calls:
 - Positive delta
 - ITM delta >.50
 - ATM delta=.50
 - OTM delta <.50
- 2. Puts:
 - Negative delta
 - ITM delta > -.50
 - ATM delta = -.50
 - OTM delta < -.50



Greeks - Gamma

• 2. Gamma

- An option's gamma is a measurement that estimates the rate of change in an option's delta for each dollar move in the underlying stock.
- The delta of the delta
- Buy an option = long gamma
- Sell an option = short gamma
- Gamma will reflect the volatility of the stock
- Higher volatility = lower gamma
 - This reflects the fact that a larger move on a volatile stock isn't as significant as a larger move on a slower one.



Greeks - Gamma

• Example:

- XYZ \$30
- 30 strike call option \$1.50
- Stock moves to \$31
- Call option moves from \$1.50 to \$2.00 (delta of the option was .50)
- Stock moves to \$32
- Call option moves from \$2.00 to \$2.75
- Delta of the option during the move from \$31 to \$32 was .75
- This means the gamma of the 30 option was .25 (taking the difference between the deltas of both \$1 moves)



Greeks - Gamma

Gamma cont.

- Gamma highest for the ATM options
- Gamma highest in the front month options
- Higher gamma is good for the option buyer as long as the stock moves fast enough
- The further ITM or OTM an option moves the more stable gamma becomes.



Greeks - Theta

3. Theta

- A measure of time decay on an option with a one-day change in time.
- Options have 2 values
 - Intrinsic value does not decay
 - Extrinsic value value over and above intrinsic value.
- Not the same for each option
- Not the same each day
 - Decay at a non-linear fashion

Time Decay







Greeks – Theta Cont.

• Theta cont.

- Highest with the ATM option
 - Decreases the further ITM or OTM you go
- Highest in the front month options
 - Decreases the further out in time that you go



Long Call & Long Put



Long Call

- Outlook: Bullish
- Typical Duration: 2 days 3 weeks
- Max Profit: Unlimited
- Max Loss: The amount paid for the call
- P/L Graph Listed Below





- 1. Wait for your system to produce a valid setup that fits your trade plan.
- 2. Make sure the options on your stock have an open interest of at least 30 times the number of contracts that you are looking to trade.
- 3. Make sure you have target points and exit points before entering the position.
- 4. You need to form an opinion on how long you feel the move in the stock is going to take.
 - Back test
 - Get to know the stocks that you are trading



Long Call Strategy Criteria

5. Time Left to Expiration

- NetPicks Trades: 20-60 days
 - If VIX is above 15 then you can also look at the shorter-term weekly options with 7-20 days left
- 6. Length of trade:
 - 1 week or less: delta of .50 (ATM) or .60-.65(1 strike ITM)
 - 1-3 weeks: delta of .60-.65 (1 strike ITM) or 1-2 strikes in the money. If one option clearly has more volume and open interest us that one.
 - More than a month: delta of .70-.75 (2 strikes ITM)
- 7. Manage the trade according to your trade plan.



Long Put

- Outlook: Bearish
- Typical Duration: 2 days 3 weeks
- Max Profit: Unlimited
- Max Loss: The amount paid for the put
- P/L Graph Listed Below





- 1. Wait for your system to produce a valid setup that fits your trade plan.
- 2. Make sure the options on your stock have an open interest of at least 30 times the number of contracts that you are looking to trade.
- 3. Make sure you have target points and exit points before entering the position.
- 4. You need to form an opinion on how long you feel the move in the stock is going to take.
 - Back test
 - Get to know the stocks that you are trading



Long Put Strategy Criteria

5. Time Left to Expiration

- NetPicks Trades: 20-60 days
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- 6. Length of trade:
 - 1 week or less: delta of .50 (ATM) or .60-.65(1 strike ITM)
 - 1-3 weeks: delta of .60-.65 (1 strike ITM) or 1-2 strikes in the money. If one option clearly has more volume and open interest us that one.
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Vertical Spreads



- The vertical spread is put on by purchasing one call (or put) within a given month and selling a different strike call (or put) with the same expiration.
 - Benefits:
 - Lower cost
 - Define Risk (collect premium)
- Example:
 - Buy 1 AAPL September 270 call
 - Sell 1 AAPL September 275 call





Long Vertical Call Spread

- 1. What does it look like?
 - ➤ XYZ Stock \$40
 - ➢ Buy 1 40 call for \$3
 - ➢ Sell 1 45 call \$1
 - ➤ Total Cost is \$2.00
 - ➤ We have the right to buy 100 shares at \$40
 - ➤ We are obligated to sell 100 shares at \$45
- 2. Max Profit:
 - □ Limited to the difference between long strike and short strike minus the debit paid.
 - Short strike (45) Long Strike (40) = 5
 - ➤ 5 \$2 debit = \$3.00



Long Vertical Call Spread

- 4. Max Loss: Limited to the debit paid
 ▶ \$2.00
- 5. Break Even: Long Strike plus debit paid
 - ▶ 40 + \$2.00 = 42.00
- 6. When do we use it?
 - When you are bullish and want to lower cost
 - Defined Risk position
 - > When you feel volatility is low (below the 50th percentile is ideal)
- 7. Where do we want stock/ETF to finish at expiration?
 - > You want the stock to be right at or above the short strike at expiration.

8. Volatility: You want volatility to rise or at least not go lower while in the trade. Once you hit the short strike then you want volatility to go down.



Long Vertical Call Spread – P/L Graph





Long Vertical Put Spread

- 1. What does it look like?
 - ➤ XYZ Stock \$40
 - ➢ Buy 1 40 put for \$3
 - ➢ Sell 1 35 put \$1
 - ➤ Total Cost is \$2.00
 - ➤ We have the right to sell 100 shares at \$40
 - ➤ We are obligated to buy 100 shares at \$35
- 2. Max Profit:
 - Limited to the difference between the short strike and the long strike minus the debit paid.
 - Long strike (40) Short Strike (35) = 5
 - ➤ 5 \$2 debit = \$3.00



Long Vertical Put Spread

4. Max Loss: Limited to the debit paid

▶ \$2.00

- 5. Break Even: Long Strike minus debit paid
 - ▶ 40 \$2.00 = 38.00
- 6. When do we use it?
 - > When you are bearish and want to lower cost. Keep in mind you will limit your profit potential.
 - Defined Risk position
- 7. Where do we want stock/ETF to finish at expiration?
 - > You want the stock to be right at or below the short strike at expiration.

8. Volatility: You want volatility to rise or at least not go lower while in the trade. Once you hit the short strike then you want volatility to go down.

- 9. Tips
 - When Implied volatility is high consider buying a put spread instead of just buying a put. The spread includes selling a put which will somewhat offset the effect of a decrease in implied volatility.



Long Vertical Put Spread – P/L Graph





- Ideally, we want to see implied volatility lower than the 50th percentile (using TOS)
- 2. Use the front month if there is at least 20 days left to expiration. If not, then go to the next month out.
- 3. We will buy the option one strike ITM. This will allow us to get in by paying as little extrinsic value as possible. We will then look to sell the the next strike OTM. We can also play around with the strikes to make the spread wider or tighter if we can pay 50% or less of the width of the strikes.
- 4. We are targeting 80-100% returns on this trade. We will also look to exit the trade no later than Wednesday of expiration week if we are still in the trade.



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