Ri$k Doctor Forums

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		Managing a beast	Qoff	7	208	December 20, 2010, 08:54:04 AM by Ri$k Doctor	
		Options Metamorphosis I -- II-3 Conversion	csrote	4	381	February 19, 2010, 10:45:40 AM by csrote	
		Options Metamorphosis I-II-4 SHORT PUT rolled to different strike using spreads	csrote	5	279	February 18, 2010, 08:48:31 AM by csrote	
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	Author

Qoff
Members
Newbie
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Posts: 40

Managing a beast
« **on:** November 23, 2010, 08:07:43 AM »

Hi, Charles, et. al,

I would like input as to whether I am looking at this possible position correctly from a risk/reward standpoint.

I am long the Feb11 9 calls, with a 2.18 debit.
I am looking to morph this into a bear spread by selling a lower strike call. Here are my choices (mark prices per as I type):

max risk: difference in strikes - net credit
max reward: net credit
breakeven: lower strike + net credit

Strike	debit	credit	net credit/max reward	max risk	risk:reward ratio
6	2.18	4.35	2.17	3.83	1:0.57
7	2.18	3.38	1.20	0.80	1:1.50
8	2.18	2.50	0.32	0.68	1:0.47

So, if I'm understanding this correctly, my best risk:reward scenario would be to sell the 7 calls, since I would be risking $1 to make $1.50. Is this correct?

Thanks for your input.
Regina

$eaTrader
Members
Jr. Member
⭐⭐
Posts: 79

Re: Managing a beast
« **Reply #1 on:** November 23, 2010, 11:51:37 AM »

Hey Regina,

    I'm a little confused by your table. Is it safe to assume what you are calling your credit column is the price you can sell the options for?
And if that is the case, what you are calling your debit column is the option asking price, which is all set to $2.18.

But to your original question about looking at the trade correctly, and I know Charles will chime in and let us know his thoughts, you must be bearish on this underlying to be morphing into a bear spread. The likely questions I have is where do you think this underlying will go? How much lower from the current price?

Lastly my first consideration would be to consider the likely hood of having the underlying move below the strike I'm looking to sell. Next I would then look at things like making sure the strike I'm selling is worth selling by being a least 0.25% of the option I'm long. If you'd want to consider the Risk:Reward it may be a good idea to look at the at/out of the money put spread over the call credit spread to get a better assessment of Risk:Reward value because synthetically call bear spreads are the same as put bear spreads.

Just my thoughts

Ronnie

Re: Managing a beast

Qoff
Members
Newbie
⭐
Posts: 40

Hi, Ronnie,

Thanks for taking the time to reply. The forum timed out and erased my first attempt at a reply before I could post it, so I'll try to remember everything I wrote the first time around. Sorry if it sounds choppy.

The credit column is the mark price between the bid/ask, as of when I was writing. That is usually where I place my sell limit order.

The debit column is not the option asking price. It's the debit that I paid for the calls that I am already long. That's why it's fixed for all the scenarios.

Yes, I'm bearish on the underlying. Honestly, I don't have a price target. I'm learning about P&F charts, which I really like. The chart has an established downtrend, but that's as far as I've gotten – which is why I'm no longer happy being long the calls. (In a different forum, I asked about using P&F charts with Diamonetrics, which Charles offered to examine.)

So my point in considering a bear spread is because I thought I'd try to profit as the underlying fell, as well as recouping some of my loss by receiving a credit for the sale of the calls.

Does it matter, though, if the underlying falls below the strike? . . . Because with the bearish spread, my profit and loss are limited. Or are you asking with something else in mind?

You said, "… making sure the strike I'm selling is worth selling by being at least 0.25% of the option I'm long". Do you mean 25% (i.e., 0.25) or do you really mean 0.25% (which is, I think, 0.0025 – a quarter of one percent)? And whichever amount you mean, do you mean being that amount of the current value of the option I'm long?

You also thought I should look at the put bear spread, as it is synthetically the same as a bear call spread. I get the idea of C=U+P mathematically, but I have a hard time translating that theoretical knowledge to real-life calls and puts. Do you have another way of explaining that to me? Also, since I'm already long the calls, and to enter into a bear spread I need to sell a lower strike call, are you saying that I may also want to consider selling the underlying and selling the put?

Thanks for your help.
Regina

Re: Managing a beast

$eaTrader
Members
Jr. Member
⭐⭐
Posts: 79

Hey Regina,

   I believe all elements of your table is clear to me now. So let me address your questions:

Does it matter, though, if the underlying falls below the strike? . . . Because with the bearish spread, my profit and loss are limited. Or are you asking with something else in mind?

   In this case the underlying would need to move to (within a penny)/ below the short strike to avoid being assigned on the short call: To keep your credit of selling say the 8 strike call; you would want the short call to expire worthless by expiration.

You said, "… making sure the strike I'm selling is worth selling by being at least 0.25% of the option I'm long". Do you mean 25% (i.e., 0.25) or do you really mean 0.25% (which is, I think, 0.0025 – a quarter of one percent)? And whichever amount you mean, do you mean being that amount of the current value of the option I'm long?

Sorry about 0.25% I really meant to say 25% and I believe Charles would say 33% or (1/3) of the long strike price or [(1/3)*$2.18= $0.72]. For all strikes in your table, all is well in this regards.

You also thought I should look at the put bear spread, as it is synthetically the same as a bear call spread. I get the idea of C=U+P mathematically, but I have a hard time translating that theoretical knowledge to real-life calls and puts. Do you have another way of explaining that to me? Also, since I'm already long the calls, and to enter into a bear spread I need to sell a lower strike call, are you saying that I may also want to consider selling the underlying and selling the put?
   For this case I was thinking the Box relationship between the call & put spreads.If you think the underlying will keep moving south the put spread may be better from a Risk:Reward stand point than the call credit spread, here I mean move to the short strike and beyond.If you sell a lower strike call and it is assigned on expiration, you will have short underlying, which reflect your bearish stance.But you will have to buy back that short stock to close the trade out.
will be limited; meaning the underlying moves to say $6.00, you could consider turning your long call into a Iron butterfly to lock in the $2.17 rebate and improve your RR relationship by trading a out of the money put credit spread.Finally, and I know this is hard sometimes, never hesitate to sell out that call for any remaining value especially if your opinion on the underlying has changed and it not worth morphing due to pricing.It may just be more cost effective to sell the call and buy a put spread.

      Hope this helps

      Ronnie

Ronnie
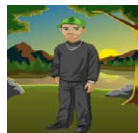
Qoff
Members
Newbie
⭐
Posts: 40

Re: Managing a beast
« **Reply #4 on:** November 24, 2010, 06:22:14 AM »

Hi, Ronnie,

In this case the underlying would need to move to (within a penny)/ below the short strike to avoid being assigned on the short call: To keep your credit of selling say the 8 strike call; you would want the short call to expire worthless by expiration.

So the highest probability (and therefore least risky) of my short call expiring worthless by expiration would be the 8 calls, right?

I still have to mull over what you wrote about the box relationship. I might get back to you on more questions.

Thanks, and Happy Thanksgiving ~
Regina

$eaTrader
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Jr. Member
⭐⭐
Posts: 79

Re: Managing a beast
« **Reply #5 on:** November 24, 2010, 08:36:04 PM »
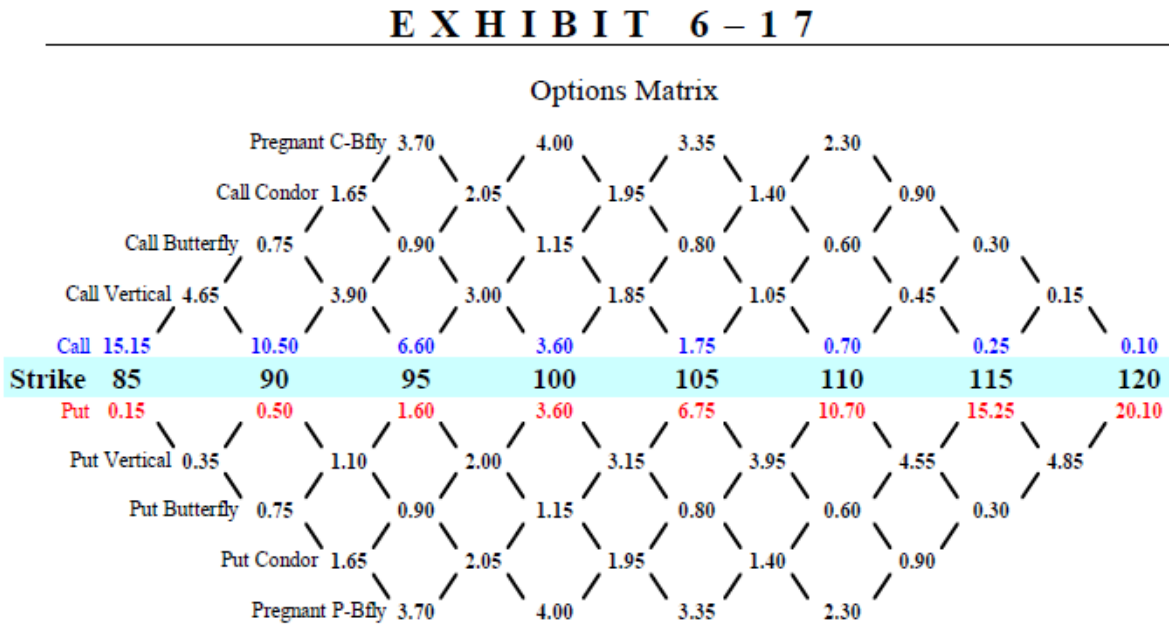
Hey Regina,

   Yes, I'd add that if the volatility of the underlying is 'sufficiently high' the probability of the 9/8 call spread expiring worthless would probably be higher than the 9/7 & 9/6 call spreads.

   To help you lock in that vital understanding of the BOX relationship, with vertical spreads, I have compiled a list of resources:

From the Books:
- **Starting on Page 6 of this pdf is an exerpt from chapter 2**
- OTTHR Hard Cover:Pg 166 Exhibit 6-17 and PDF:pg 185: Options Matrix:

EXHIBIT 6-17

Options Matrix

```
Pregnant C-Bfly 3.70      4.00      3.35      2.30
Call Condor   1.65    2.05     1.95     1.40     0.90
Call Butterfly 0.75   0.90    1.15    0.80    0.60    0.30
Call Vertical 4.65  3.90    3.00    1.85    1.05    0.45    0.15
```

Call	15.15	10.50	6.60	3.60	1.75	0.70	0.25	0.10
Strike	**85**	**90**	**95**	**100**	**105**	**110**	**115**	**120**
Put	0.15	0.50	1.60	3.60	6.75	10.70	15.25	20.10

```
Put Vertical 0.35   1.10    2.00    3.15    3.95    4.55    4.85
Put Butterfly 0.75   0.90    1.15    0.80    0.60    0.30
Put Condor   1.65    2.05     1.95     1.40     0.90
Pregnant P-Bfly 3.70      4.00      3.35      2.30
```

From the Videos:

- RD1 Video1: Time Segment starting @ 19:00, Charles talk about the Options Matrix and give a very good question to help in understanding the Option Matrix

Within the RD Forum:
- **"The Box" from the "RD1 Options Basics Beyond the Basics" Forum**
- **SHv1OTTHR-ManagingTheBeast.pdf**

I'm glad to be of help because helping other RD students also helps me solidify my understanding of options & the RD way of looking at options.

Thanks & Happy Thanksgiving you and everyone else who reads this post
Ronnie

Re: Managing a beast
« **Reply #6 on:** November 29, 2010, 07:04:48 AM »

Thanks for this list of resources, Ronnie. This is very helpful. I'll work through them.

Hope Thanksgiving was great for you.
Regina

Re: Managing a beast
« **Reply #7 on:** December 20, 2010, 08:54:04 AM »

Thanks Ronnie, for responding and helping out.
BTW: Regina:
Quote

Strike	debit	credit	net credit/max reward	max risk	risk:reward ratio
6	2.18	4.35	2.17	3.83	1:0.57

Should be:

Strike	debit	credit	net credit/max reward	max risk	risk:reward ratio
6	2.18	4.35	2.17	0.83	1:2.61

Risk Reward does not explain the whole picture. We don't have enough information here either. Although one might be able to guess the approximate underlying price and my guess would be about 8.25? The time left can be offset by IV but it is another critical decision to consider what happens if the underlying sits still. Assuming 8.25 that make the call spreads value and P/L at expiry;

	Value	P/L	
6/9 Spread:	2.25	(.08)	Time against you (even though best risk:reward ratio)
7/9 Spread:	1.25	(.05)	Time against you
8/9 Spread:	.25	.07	Time working for you

Depending on time to go and prices it may be best to sell the 9 Calls and consider buying the 10s or 11s. It is best to take a screenshot and email it to me for upload. If you can include the Greeks and/or a chart, that would be even better. The more exact info that we have to work with will eliminate chance for typos and a lot of ambiguity so that everyone can quickly get on the same page and motivate them to chime in for a more fluid discussion.

C H A P T E R

2 (Excerpt)

MANAGING THE BEAST

With so many alternatives *(options)* available, it may be prudent to change the "nature of the beast" (i.e., adjust the position) instead of exiting the initial trade due to a new market opinion or pricing considerations. We saw how Gil Bates made his trades but let's examine closer just what we can do with a simple 10 lot of calls. The following example illustrates when it makes sense to adjust the initial position.

Suppose that a trader has a bullish call position, for example, long the 10 Oct 50 calls at $2.00, that was initiated when the underlying market was at $49.00. The market then rallies to $54.00. The call value has now appreciated by 3.00 to 5.00. Looking at the grid of prices on the next page, the trader can choose from an infinite number of alternative strategies in an attempt to take profits while remaining in the market with a new strategy. Scenarios A to I, which follow, demonstrate some possible strategies. Note: the actual cost[1] and the "fair cost[2]" (prices presently available in the market) will be discussed in the next section. Stock and Options Prices with the Underlying at $54.00

Stock $54.00

Call $	Strike	Put $
9.25	**45**	.25
5.00	**50**	1.00
2.00	**55**	3.00

Long 10 Oct 50 calls @ $2.00

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[1] **Actual Cost**

Actual or synthetic cost based upon the put call parity equation, assuming cost of carry until expiration equals the dividend: $k + c = s + p + i - d$, or stri**K**e + **C**all price = **S**tock price + **P**ut price + **I**nterest − **D**ividend.

[2] **Fair Cost**

This is what it would cost to put the position on at present market prices. This term is only used when the trader decides to make an options trade as an adjustment to an existing position. Since the position being adjusted has been executed in the past, one would make a biased evaluation (in the present) if they used prices particular to those transactions made in the past.

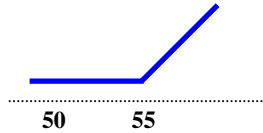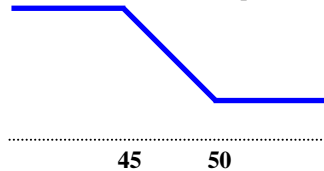A.   Sell 10 Oct 55 calls at 2.00. The result is **10*50/55 bull call verticals,** each for even money (fair cost = 3.00 debit). The trader is still long, but not as aggressively so, and has limited the possible gain.

50
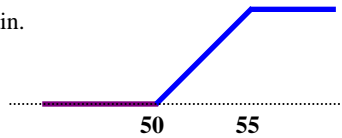
50   55

B.   Sell 10 Oct 50 calls and buy 10 Oct 55 calls for a 3.00 credit (sell 50/55 call vertical i.e., bear spread). The result is **long 10 Oct 55 calls**, each for a 1.00 credit (fair cost = 2.00 debit). The trader is still long, but for a price that is cheaper than free, and has limited risk.

50   55

C.   Sell 10 Oct 45 calls at 9.25. The result is **10*45/50 bear spreads,** each for a 7.25 credit (fair cost = 4.25 credit). The trader anticipates a downward move.

45   50

D.   Sell 20 Oct 55 calls at 2.00. The result is a **50/55 call ratio spread** (+10 by −20), each (+1 by −2) for a 2.00 credit (fair cost = 1.00 debit). The trader would now like the market to stay around 55.

45   50   55   60
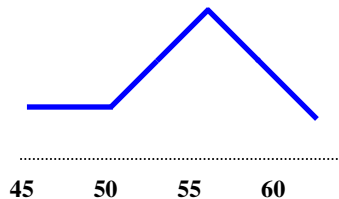
E.   Sell 5 Oct 45 calls at 9.25. The result is a **45/50 call back spread** (+10 by −5), each (−1 by +2) for a 5.25 credit (fair cost = .75 debit). The trader now hopes for a large move in either direction, preferably upward.

45   50
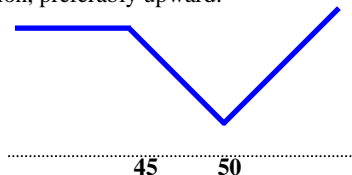
F.   Buy 10 Oct 55 puts at 3.00. The result is **long 10 Oct 50c / 55p "guts" strangle**, each for a 5.00 debit (the minimum possible value for this gut strangle is 5.00) (fair cost = 2.00 debit). This will win if there is a large move in either direction.

50   55

RiskDoctor@RiskDoctor.com
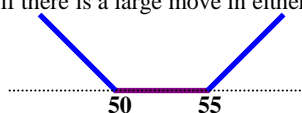
G.   Buy 10[3] Oct 50 puts at 1.00. The result is **long 10 Oct 50 straddle**, each for a 3.00 debit (fair cost = 6.00 debit). This will win if there is a big move in either direction. Since the underlying is already at 54.00, a continued move upward will generate a profit. A break from here would most likely be a loss until the underlying goes below 47.

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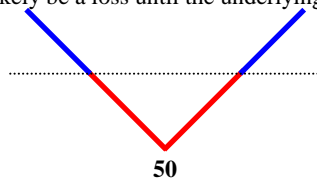
H.   Sell 10oo shares at 54.00 (10 calls x 1oo shares each).   The result is synthetically **long 10 Oct 50 puts** for a 2.00 credit[4] (fair cost = 1.00 debit). The trader anticipates a downward move.

50

I.   Selling only 8oo shares at 54.00, assuming a hedge ratio of .80 for the Oct 50 calls, results in **long a synthetic** ratioed straddle [5] **at the 50 strike** $(+2*50c/+8*50p)$. Each of the $2*(+1c$ by $+4p)$ spreads, for a 6.00 credit [6] (fair cost = 9.00 debit[7]). The trader would profit from a large move in either direction, but eventually more so from a downward move.

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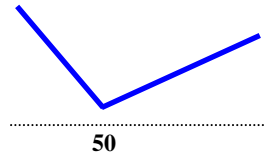
[3] 10

At this point, it might warrant purchasing more than 10 to achieve market neutrality. This would be called a ratioed strangle.

[4] 2.00 Credit

Selling the 1oo stock at 54.00 is the same as selling 1 combo, which is selling the call and buying a put for a 4.00 credit. Since the original call cost 2.00 debit and we now receive 4.00 credit, the puts are synthetically owned for a net 2.00 credit. (For a cost of 2.00 better than free.)
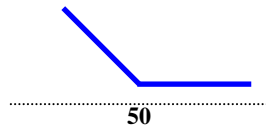
[5] Ratioed Straddle

A ratioed straddle is not 1 : 1, meaning one call for every one put.

[6] 6.00 Credit

Selling the 8oo stock (.80*10oo) at 54.00 is the same as selling 8 combos for 4.00 credit (5.00 credit for the calls and a 1.00 debit for the put). That's a total credit of 32.00 versus the original purchase of 10 calls for a 2.00 debit (20.00) leaves a running credit of 12.00. Since the result is $2*(+1c$ by $+4p)$ spreads, each is for a net credit of 6.00.

[7] 9.00 Debit

Selling the 8oo stock (.80*10oo) at 54.00 is the same as selling 8 combos for 4.00 credit (5.00 credit for the calls and a 1.00 debit for the put). That's a total credit of 32.00 versus the present purchase price of 10 calls for a 5.00 debit (50.00) leaves a running debit of 18.00. Since the result is $2*(+1c$ by $+4p)$ spreads, each is for a net debit of 9.00.

This could go on and on, but by now one should have the idea. Once the trader has any of these aggregate spreads on, the strategy could evolve into many alternative configurations or risk profiles. Unlike a stock trader, who generally uses stop orders or mental stops to limit his or her risk, an options trader often adjusts rather than exits a position, providing that the position does already contain built in stops, as it were, by virtue of its design. This way he or she may be able to recoup some or all of the loss (where applicable) and even go on to profit. The adjustment turns the original strategy into a more appropriate one given current price levels, even though the trader's position is (perhaps temporarily) running at a loss.

When the nature of the beast is changed, it is essential that traders realize that any adjustment is identical to the liquidation of their old strategy and the initiation of a new strategy without all of the trades. One new trade changes the nature of the strategy and a new position exists at that point.

To decide whether an adjustment is really something that traders want to do, it is important to realize that they must like the current price (alternative cost) of the adjusted spread. In other words, they should look at the spread that they will end up with synthetically, and then assess its value and their reason for putting it on. This is the point where understanding the concept of synthetics separates the women from the girls. It is better to think about the most basic risk profile in the most simple[8] terms (i.e., synthetic terms) as opposed to the actual price terms.

At every stage in the analysis of the alternatives and adjustments to a position, traders should ask whether they would put this spread on having had no position whatsoever. They must make the decision based upon the "fair cost" disregarding all the previous prices paid or received (actual cost) on the aggregate spread. If the answer is that they "would not put on the trade", then this particular adjustment is not right for them. Their thinking should be consistent whether the position has just been initiated or has already been on for some time. The trader should get out of the position if the risk / reward profile is not attractive from this point forward. Some of the most important revelations for traders occur when they understand at what point they are contradicting themselves. This is when the "lights go on" and they really learn from their misperceptions.

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[8] Simple Terms

Example: A "fenced" position (+u / + lower strike put and short higher strike call) is best viewed in its simplest terms, namely, a bull spread. Manage the bull spread by watching either the long call spread or the short put spread, whichever is more liquid.

ADJUSTMENT COSTING

The following tables examine trades A to I from the perspective of actual and fair cost.

Actual Costs
First Trade and Second Trade = Total for each spread
A. 10 @ 2.00 debit and 10 @ 2.00 credit = 10 @ 0 or even
B. 10 @ 2.00 debit and 10 @ 3.00 credit = 10 @ 1.00 credit
C. 10 @ 2.00 debit and 10 @ 9.25 credit = 10 @ 7.25 credit
D. 10 @ 2.00 debit and 20 @ 2.00 credit = 10 @ 2.00 credit
E. 10 @ 2.00 debit and 5 @ 9.25 credit = 5 @ 5.25 credit
F. 10 @ 2.00 debit and 10 @ 3.00 debit = 10 @ 5.00 debit
G. 10 @ 2.00 debit and 10 @ 1.00 debit = 10 @ 3.00 debit
H. 10 @ 2.00 debit and 10oo @ 54.00 credit = 10 @ 2.00 credit
I. 10 @ 2.00 debit and 8oo @ 54.00 credit = 2 @ 6.00 credit

Fair Cost (3.00 more times 10) [9]
Present Value of First Trade and Second Trade = Total
A. 10 @ 5.00 debit and 10 @ 2.00 credit = 10 @ 3.00 debit
B. 10 @ 5.00 debit and 10 @ 3.00 credit = 10 @ 2.00 debit
C. 10 @ 5.00 debit and 5 @ 9.25 credit = 5 @ 4.25 credit
D. 10 @ 5.00 debit and 20 @ 2.00 credit = 10 @ 1.00 debit
E. 10 @ 5.00 debit and 5 @ 9.25 credit = 5 @ .75 debit
F. 10 @ 5.00 debit and 10 @ 3.00 debit = 10 @ 8.00 debit
G. 10 @ 5.00 debit and 10 @ 1.00 debit = 10 @ 6.00 debit
H. 10 @ 5.00 debit and 10oo @ 54.00 credit = 10 @ 1.00 debit
I. 10 @ 5.00 debit and 8oo @ 54.00 credit = 2 @ 9.00 debit

Obviously all the current costs look less attractive than the actual costs because it costs 30.00 (10 contracts times 3.00) more. The important point here is that it may not make sense for some players to make any adjustment. Take scenario A for example. If there was a poll taken from the viewers of CNBC which asked whether or not they would ever buy a 5 point vertical for $3.00 (current cost) the results would probably be a resounding 100% saying "***NO WAY!***" Even if a professional group were polled, probably 70% would concur. Therefore, scenario A is rolling into a situation where one would have 3.00 on the table and it can go up to 5.00 or down to zero. That is risking 3.00 to

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[9] **3.00 more times 10**

Had there been no prior position, the calls would have otherwise cost 5.00 instead of 2.00 meaning 3.00 more for 10 calls each turning into 10 spreads, 6.00 more for 10 calls turning into 5 spreads, and 15.00 more for 10 calls turning into 2 spreads.

make 2.00. A discussion in Chapter 6 discusses what on earth the other 30% might be thinking when compelled to risk 3.00 to make 2.00. Scenario B, on the other hand involves a strategy with unlimited upside potential. It is therefore difficult to say definitively how much the premium is worth. Its value would be calculated using the usual variables such as time to go, proximity to the money and volatility.

RULE THE BEAST

1. Predetermine strategy based on market opinion.
2. Predetermine point of entry based on an attractive price level.
3. Predetermine profit-and-loss objective based on pain threshold.
4. Enter the market.
5. Ongoing "live" reassessment of the position at current price levels.

Would the trader execute the same trade now if he or she were not already in the market? If the answer is yes, then the traders should do nothing and stay in the position. If the trader would never execute the trade at this point, this is where he or she should either exit the trade or change the nature of the beast. When looking to adjust the prevailing prices must represent a good value as if it were a fresh new initiation price. If not, one should exit. Failure to do so is a contradiction of desires. In example A, again, the trader would have to like the idea of having a long call vertical at the current price of $3.00 which can only go to $5.00. If he or she had no position and prefers not to buy that spread for $3.00, then it is pointless to stay in the trade. It would be inappropriate to stay in the trade just because it was legged[10] into for free. Long-term consistent winnings in the market have much to do with taking profits. If that spread goes from $3.00 to worthless, the trader will wish that he or she had taken the profits. There is no justification for adjusting into positions that the trader normally would not put on at current prices. If there is an adjustment to the position it should be managed like it is new without past consideration to accumulated profits or loss on the prior setup.

Rule the Beast (continued)

6. Redetermine strategy based on new market opinion.
7. Predetermine point of entry for adjustment (changing the beast).
8. Predetermine a profit-and-loss objective.
9. Exit or adjust the position.
10. Ongoing "live" reassessment of the basic position profile in simplest terms at current price levels.

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[10] Leg, Legging, Legged

Legging is trading into a spread on separate orders. When the quoted spread price is too wide or not a desirable price, traders will do what is referred to as legging into the position by executing one side first and then at a later time entering an order to transact the second leg (the other side). There is transaction risk in getting 'caught between legs'. As an example, the market moves a large amount adverse to the first leg of the position resulting in the price of the overall spread to be executed being at undesirable levels. It can be dangerous to leg spreads but sometimes that is the only way in or out of a spread position.

When thinking about speculating with any options strategy (e.g. purchasing calls, puts, straddles or verticals) remember that the trader should not only think in terms of the maximum cost of that strategy. For example, the trader decides to buy a straddle (put and a call at the same strike price) because he or she believes that the market will make a large move in one direction or the other (but does not know which). The trader is willing to risk $10,000. The straddle is going for $1,000, which means that the trader can afford ten spreads and ride them through to expiration. An alternative would be to buy the straddle 6 or 7 times, leaving $3,000 or $4,000 to have in reserves for adjustment purposes.

Actual Position

	Premium$	Liq Val $	Net C/P		U Units	K	40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	K	Net C/P	
																		Mid K											U Price	
U Price																		54.00												
Trade 1	($2,000)		10 ActC														10											ActC 10		Trade 1
			ActP																									ActP		
Trade 2			ActC																									ActC		Trade 2
			ActP																									ActP		
Trade 3			ActC																									ActC		Trade 3
			ActP																									ActP		
Trade 4			ActC																									ActC		Trade 4
			ActP																									ActP		
Trade 5			ActC																									ActC		Trade 5
			ActP																									ActP		
Trade 6			ActC																									ActC		Trade 6
			ActP																									ActP		
Trade 7			ActC																									ActC		Trade 7
			ActP																									ActP		
Trade 8			ActC																									ActC		Trade 8
			ActP																									ActP		
Trade 9			ActC																									ActC		Trade 9
			ActP																									ActP		
Trade 10			ActC																									ActC		Trade 10
			ActP																									ActP		
Actual Position	($2,000)	$5,002	10 ActC														10											ActC 10		Actual
			ActP																									ActP		

CurrentPNL		$3,002		U Units

Option Chain

U Price		54.00	U Price

Option Prices

K	40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	K
Calls $	14.04	13.05	12.07	11.09	10.13	9.19	8.28	7.40	6.55	5.75	5.00	4.31	3.68	3.10	2.59	2.15	1.76	1.43	1.14	0.91	0.72	Calls $
Puts $	0.01	0.02	0.04	0.06	0.10	0.16	0.25	0.36	0.52	0.72	0.97	1.27	1.64	2.07	2.56	3.11	3.72	4.38	5.10	5.87	6.67	Puts $
IV %	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	31.4%	IV %

OS | OC Summary | OC Summary

Key Data	
U	xyz
Expiry	18-Dec-09
U Price	54.00
ATM IV%	31.40%
Today	26-Oct-09
Actual DTE	53
Aged DTE	1

IV | IV% Analysis | IV% Analysis

Pay-Off Graph – Actual Position

Pay-Off Graph – Actual Position v Adjustment A

Pay-Off Graph - v Adjustment B

Pay-Off Graph - v Adjustment C

| Trade Analysis | | Index | Close Groups | | | | | | | | | | | | | | | | | | | | | | | | Trade Analysis |

Data Input — Inc Adj: Y | PivotK 1: 50 (ok 50)

U Price: 54.00

	Premium$	Liq Val $	Net C/P		U Units	K 40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	Net C/P	
Actual Position	($2,000)	$5,002	10 ActC / ActP													10											10 ActC / ActP	Actual
Adjustment	$9,194	($9,194)	(10) AdjC / AdjP	n/a							(10)																(10) AdjC / AdjP	Adjustment
Adjusted Position (Net)	$2,194	$805	NetC / NetP	n/a							(10)				10												NetC / NetP	Adjusted (Net)

U Price: 54.00

Key Data

Today	26-Oct-09	CurrentPNL	
U	xyz	Actual DTE	53
Expiry	18-Dec-09	Aged DTE	1
U Price	54.00	DTE - ADTE	52
ATM IV%	31.40%	Adj premium	$9,194

CurrentPNL: $3,002

	Premium$	Liq Val $	Net C/P	
Actual Position	($2,000)	$5,002	10 ActC / 10 ActP	
Adjustment	$9,194	($9,194)	(10) AdjC / AdjP	
Adjusted Position (Net)	$2,194	$805	NetC / NetP	

Greeks	Actual	Adjustments	Adjusted
Delta			
Gamma			
Vega			
Theta			
Rho			

Legend: PNL Actual, PNL Adjusted (Net)

Right side panel:
xyz	U
54.00	U Price
$3,002	PNL
18-Dec	Expiry
53	DTE

Net C/P — Trade Analysis: Actual 10 / 10; Adjustment (10); Adjusted (Net)

U Price: 54.00

PNL Analysis

	AP Premium$	($2,000)		
	AP Liq Val $	$5,002		
	AP Current PNL	$3,002 ok		

K	40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	K
% diff K	-25.9%	-24.1%	-22.2%	-20.4%	-18.5%	-16.7%	-14.8%	-13.0%	-11.1%	-9.3%	-7.4%	-5.6%	-3.7%	-1.9%		1.9%	3.7%	5.6%	7.4%	9.3%	11.1%	% diff K
PNL Act	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($1,000)		$1,000	$2,000	$3,000	$4,000	$5,000	$6,000	$7,000	$8,000	PNL Act
PNL Adj	$7,194	$7,194	$7,194	$7,194	$7,194	$7,194	$6,194	$5,194	$4,194	$3,194	$2,194	$2,194	$2,194	$2,194	$2,194	$2,194	$2,194	$2,194	$2,194	$2,194	$2,194	PNL Adj

PNL Actual — Expiry 18-Dec-09, DTE 53
PNL Adjusted — Expiry 18-Dec-09, DTE 53

Pay-Off Graph - v Adjustment D

Pay-Off Graph - v Adjustment E

Pay-Off Graph - v Adjustment F
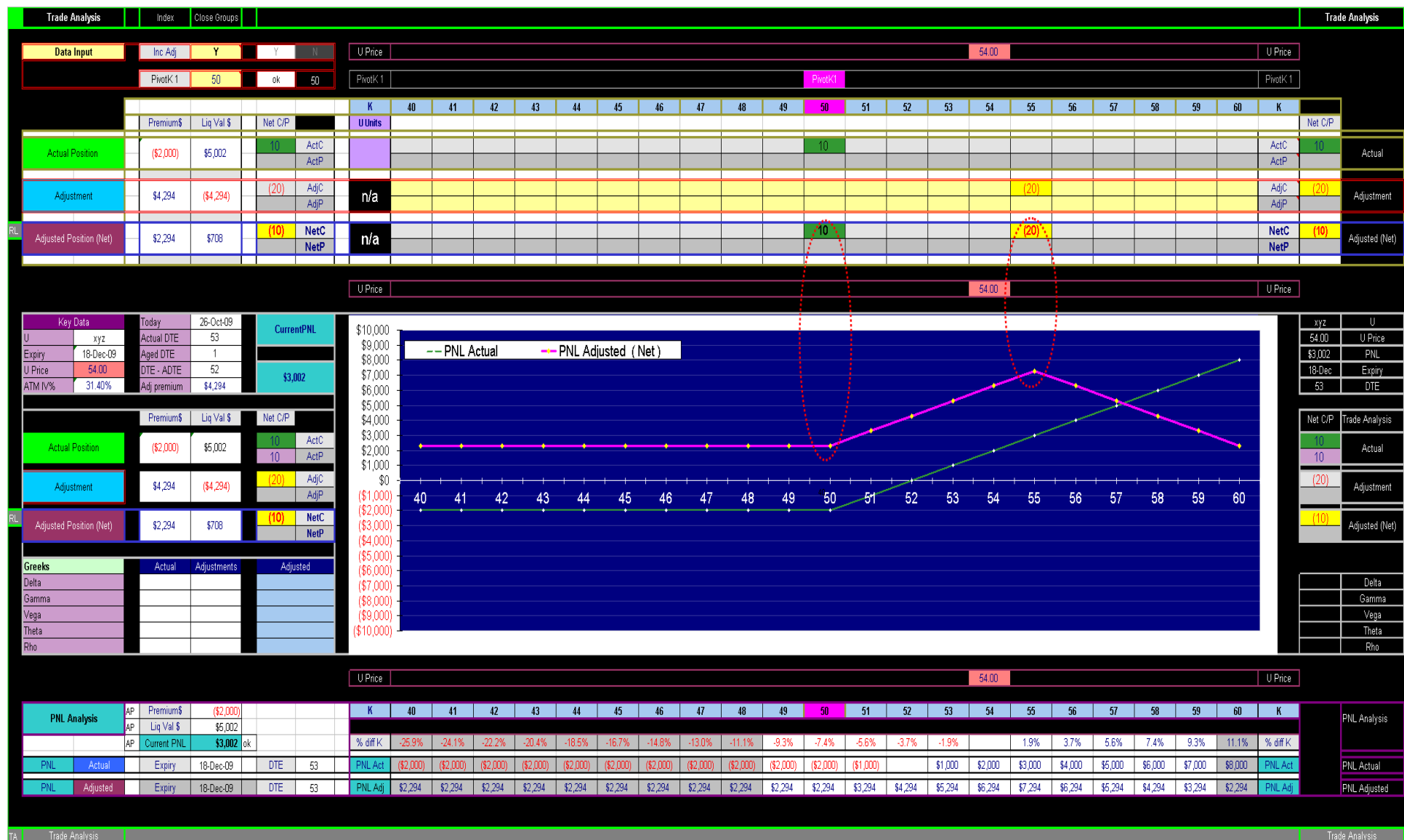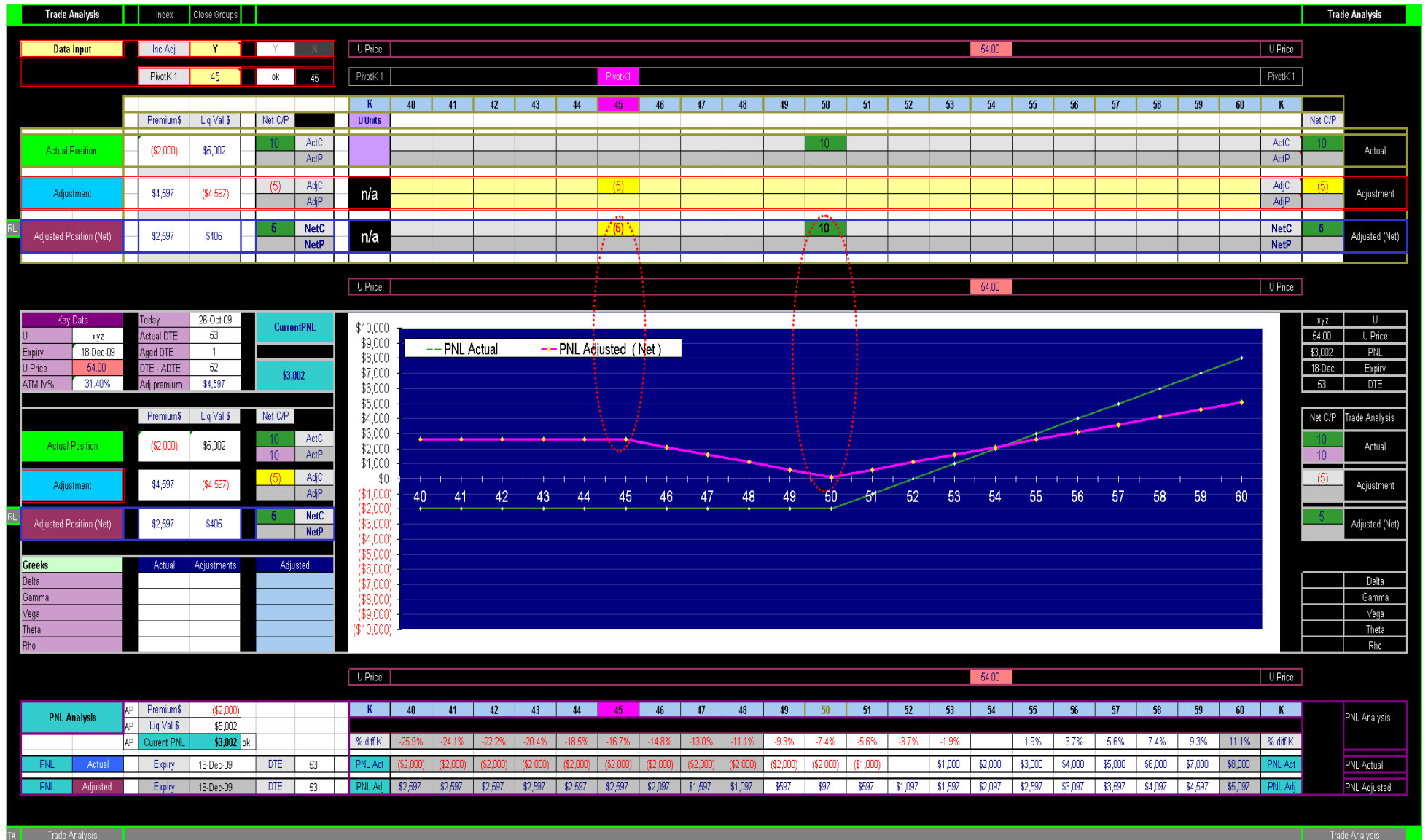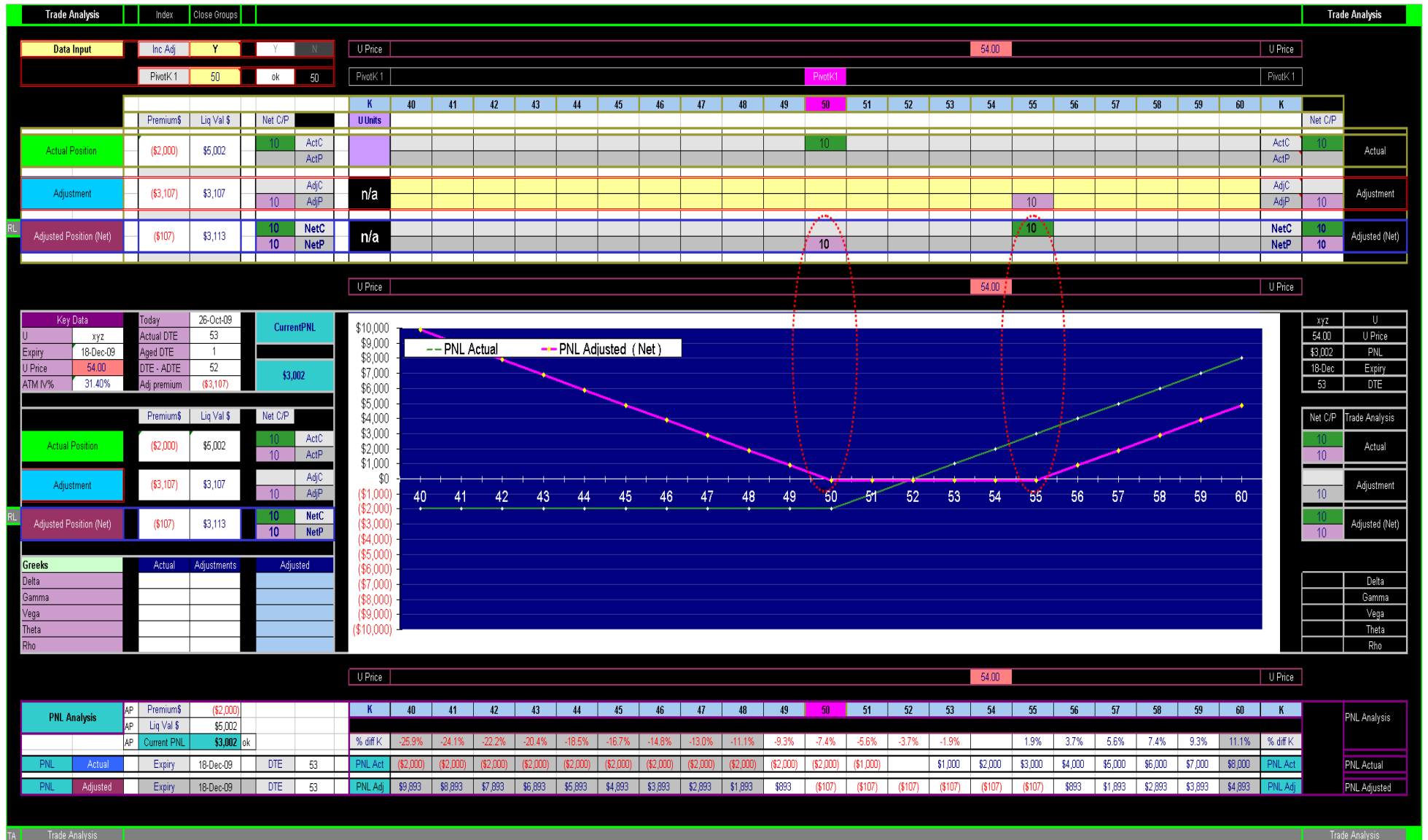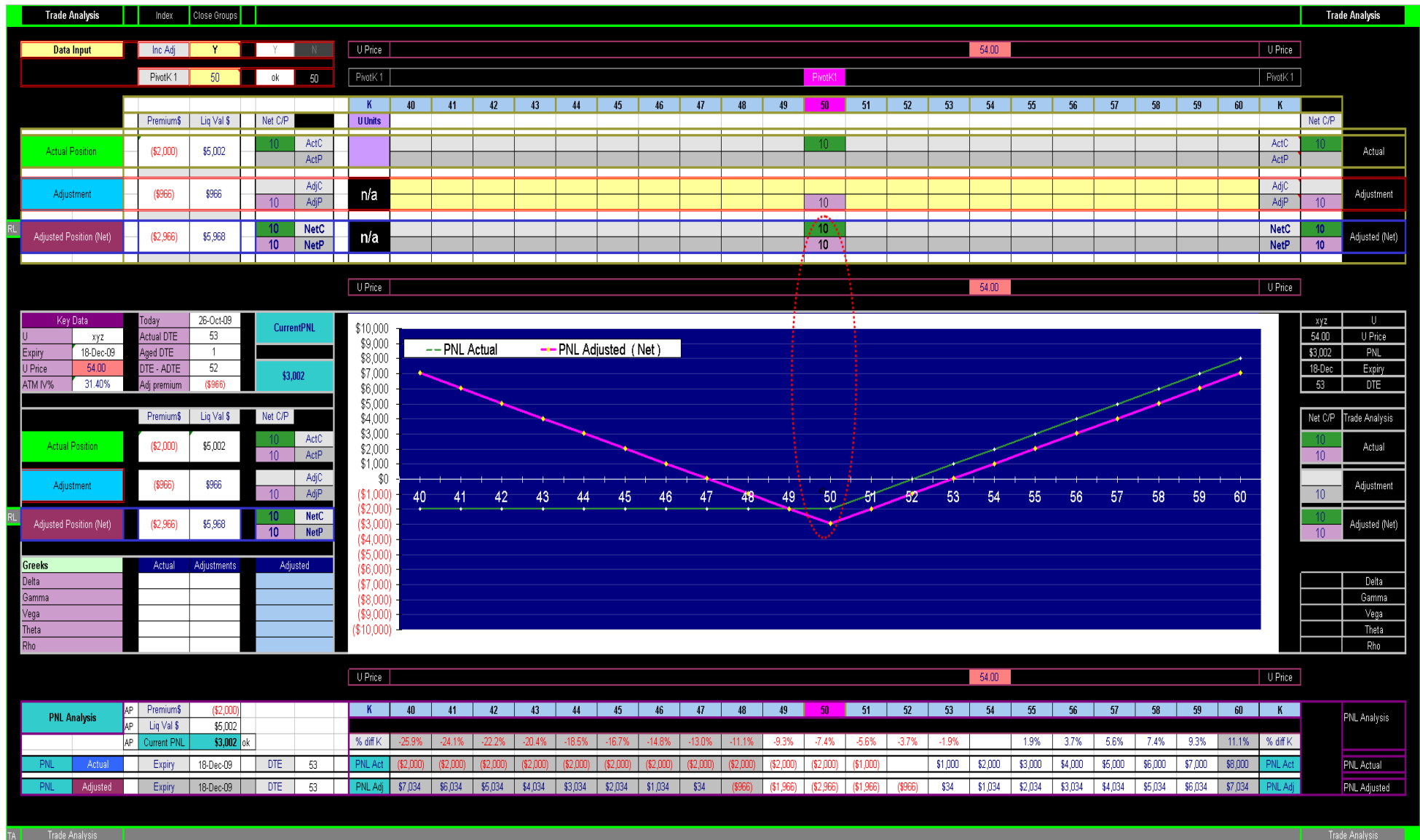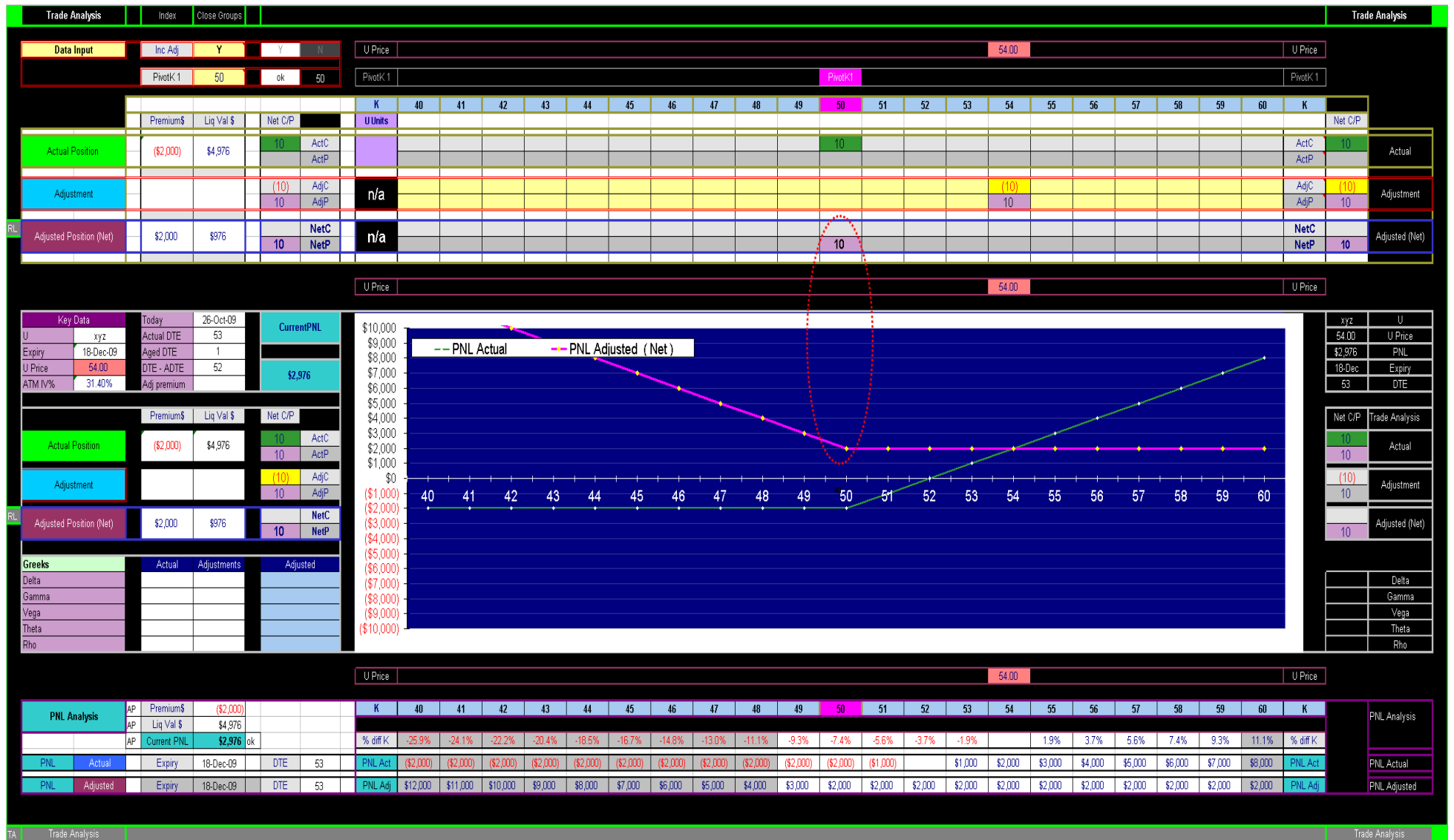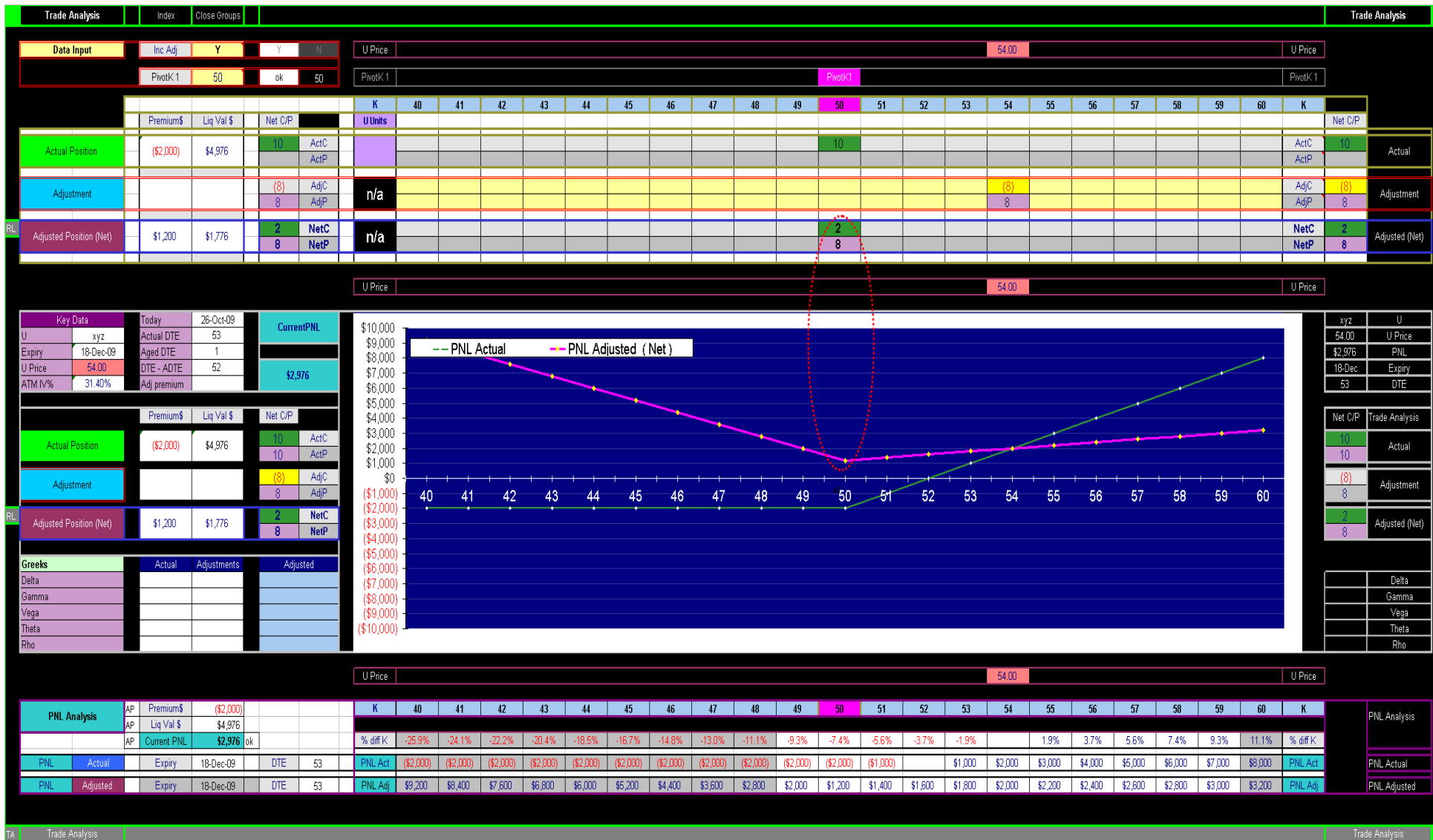
Pay-Off Graph - v Adjustment G

Pay-Off Graph - v Adjustment H

Data Input

	Inc Adj	Y		Y	N
	PivotK 1	50	ok	50	

K	40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	K

U Price: 54.00 — PivotK1 at 50

	Premium$	Liq Val $	Net C/P			Net C/P
Actual Position	($2,000)	$4,976	10 ActC / ActP	10 (at 54)	ActC 10 / ActP	Actual
Adjustment			(10) AdjC / 10 AdjP	n/a	(10) / 10 (at 54)	AdjC (10) / AdjP 10	Adjustment
Adjusted Position (Net)	$2,000	$976	NetC / 10 NetP	n/a	10 (at 54)	NetC / NetP 10	Adjusted (Net)

U Price: 54.00

Key Data

Today	26-Oct-09		CurrentPNL
U	xyz	Actual DTE	53
Expiry	18-Dec-09	Aged DTE	1
U Price	54.00	DTE - ADTE	52
ATM IV%	31.40%	Adj premium	$2,976

xyz	U
54.00	U Price
$2,976	PNL
18-Dec	Expiry
53	DTE

	Premium$	Liq Val $	Net C/P	
Actual Position	($2,000)	$4,976	10 ActC / 10 ActP	Actual 10 / 10
Adjustment			(10) AdjC / 10 AdjP	Adjustment (10) / 10
Adjusted Position (Net)	$2,000	$976	NetC / 10 NetP	Adjusted (Net) 10

Greeks

Greeks	Actual	Adjustments	Adjusted
Delta			
Gamma			
Vega			
Theta			
Rho			

Pay-Off graph (y-axis $10,000 to ($10,000), x-axis 40 to 60):
Legend: PNL Actual (green dashed), PNL Adjusted (Net) (magenta)

PNL Analysis

	AP	Premium$	($2,000)
	AP	Liq Val $	$4,976
	AP	Current PNL	$2,976 ok

K	40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	K
% diff K	-25.9%	-24.1%	-22.2%	-20.4%	-18.5%	-16.7%	-14.8%	-13.0%	-11.1%	-9.3%	-7.4%	-5.6%	-3.7%	-1.9%		1.9%	3.7%	5.6%	7.4%	9.3%	11.1%	% diff K
PNL Act	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($2,000)	($1,000)		$1,000	$2,000	$3,000	$4,000	$5,000	$6,000	$7,000	$8,000	PNL Act
PNL Adj	$12,000	$11,000	$10,000	$9,000	$8,000	$7,000	$6,000	$5,000	$4,000	$3,000	$2,000	$2,000	$2,000	$2,000	$2,000	$2,000	$2,000	$2,000	$2,000	$2,000	$2,000	PNL Adj

PNL	Actual	Expiry	18-Dec-09	DTE	53
PNL	Adjusted	Expiry	18-Dec-09	DTE	53

Pay-Off Graph - v Adjustment I

Data Input	Inc Adj	Y		Y	N
	PivotK 1	50	ok	50	

	Premium$	Liq Val $	Net C/P	U Units		Net C/P

K	40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	K

Actual Position: ($2,000) | $4,976 | 10 ActC / ActP — U Price 54.00 — ActC 10 / ActP — Actual

Adjustment: (8) AdjC / 8 AdjP | n/a — AdjC (8) / AdjP 8 — Adjustment

Adjusted Position (Net): $1,200 | $1,776 | 2 NetC / 8 NetP | n/a — NetC 2 / NetP 8 — Adjusted (Net)

U Price 54.00

Key Data

Key Data				xyz	U
U	xyz	Today	26-Oct-09	54.00	U Price
Expiry	18-Dec-09	Actual DTE	53	$2,976	PNL
U Price	54.00	Aged DTE	1	18-Dec	Expiry
ATM IV%	31.40%	DTE - ADTE	52	53	DTE
		Adj premium			

CurrentPNL: $2,976

	Premium$	Liq Val $	Net C/P	Net C/P	Trade Analysis
Actual Position	($2,000)	$4,976	10 ActC / 10 ActP	10 / 10	Actual
Adjustment			(8) AdjC / 8 AdjP	(8) / 8	Adjustment
Adjusted Position (Net)	$1,200	$1,776	2 NetC / 8 NetP	2 / 8	Adjusted (Net)

Greeks	Actual	Adjustments	Adjusted		
Delta					Delta
Gamma					Gamma
Vega					Vega
Theta					Theta
Rho					Rho

Graph: PNL Actual (green dashed) and PNL Adjusted (Net) (magenta), Y-axis from ($10,000) to $10,000, X-axis from 40 to 60.

U Price 54.00

PNL Analysis

			K	40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	K

AP	Premium$	($2,000)																							PNL Analysis
AP	Liq Val $	$4,976																							
AP	Current PNL	$2,976	ok																						

	% diff K	-25.9%	-24.1%	-22.2%	-20.4%	-18.5%	-16.7%	-14.8%	-13.0%	-11.1%	-9.3%	-7.4%	-5.6%	-3.7%	-1.9%		1.9%	3.7%	5.6%	7.4%	9.3%	11.1%	% diff K

| PNL | Actual | Expiry | 18-Dec-09 | DTE | 53 | PNL Act | ($2,000) | ($2,000) | ($2,000) | ($2,000) | ($2,000) | ($2,000) | ($2,000) | ($2,000) | ($2,000) | ($2,000) | ($2,000) | ($1,000) | | $1,000 | $2,000 | $3,000 | $4,000 | $5,000 | $6,000 | $7,000 | $8,000 | PNL Act | PNL Actual |

| PNL | Adjusted | Expiry | 18-Dec-09 | DTE | 53 | PNL Adj | $9,200 | $8,400 | $7,600 | $6,800 | $6,000 | $5,200 | $4,400 | $3,600 | $2,800 | $2,000 | $1,200 | $1,400 | $1,600 | $1,800 | $2,000 | $2,200 | $2,400 | $2,600 | $2,800 | $3,000 | $3,200 | PNL Adj | PNL Adjusted |

	Author

edsyl
Newbie
☆
Posts: 26

The Box
« on: April 18, 2009, 09:09:18 AM »

After reading the section over and over I fail to see how adding a four position 'box' is not affecting the original position or distorting it.
The SynTool makes sense as all components of the addition are zero sum.
This is NOT the case however with the box tool.
From what I can see there will always be a bias equal to the value of the spread of the box, so in my mind it is an approximation.

Can someone clarify this or tell what I am missing from all this?
Regards
Ed

Ri$k Doctor
Administrator
Hero Member
★★★★★
Posts: 3247

The Box
« Reply #1 on: April 24, 2009, 11:42:07 AM »

I am not sure what you are asking but the box value holds pretty much like the SynTool shows about Reversals and Conversions. The Box only differs from the SynTool in that it is 2 Sets of SynTools at 2 different strikes (one long and one short) where the 2 Syntools showing long and short Underlying offset each other.

The point of a box is that it uncovers the nature of your risk in a simpler fashion, like in the following example from Chapter 5. The actual position is in Blue, the Box Dissection in Red, uncovering the exposure of a long cheap Put in Green:

EXHIBIT 5–11

BoxTool Applied to Three-Legged Box Reveals Synthetic Missing Corner
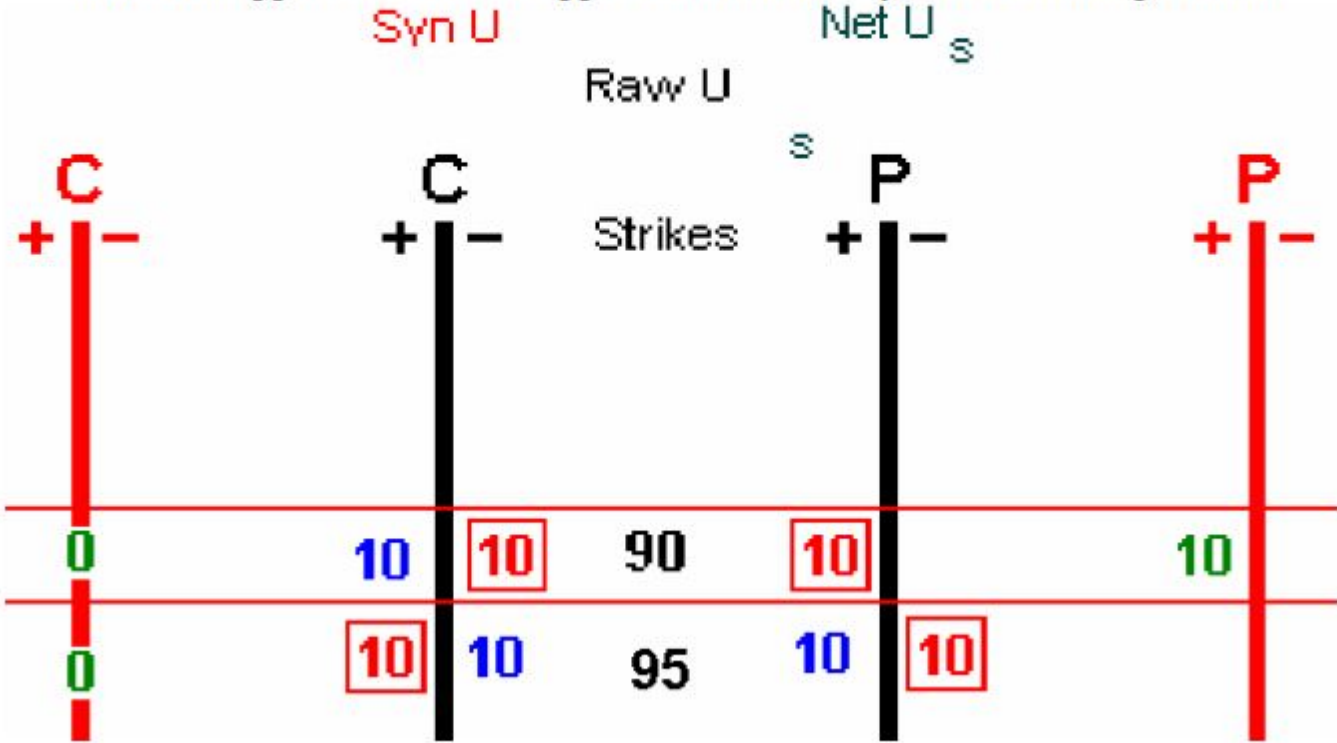
The Box
« **Reply #2 on:** April 25, 2009, 02:43:26 AM »

(edsyl @ Apr. 18 2009,1:09)
QUOTE
After reading the section over and over I fail to see how adding a four position 'box' is not affecting the original position or distorting it.
The SynTool makes sense as all components of the addition are zero sum.
This is NOT the case however with the box tool.
From what I can see there will always be a bias equal to the value of the spread of the box, so in my mind it is an approximation.

Can someone clarify this or tell what I am missing from all this?
Regards
Ed

Boxes are a bit like riding a bike …. difficult to explain how …… but relatively easy when you have practiced a bit …..

I will have a go at explaining a simplified approach to boxes …. and address some of your questions ..

- a box consists of 2 different elements that nett out at expiry to zero

- for example …. 2 + (+z -z) = 2

- a Long Box consists of

* a Long Call Vertical Spread (+z)
* a Long Put Vertical Spread (-z)

- for example ….

* a Long 10 point box at strikes 750 - 760 =
* [Long 750 - 760 Call Vertical] + [Long 750 - 760 Put Vertical]
* will cost approx 10 point debit
* will be worth 10 point credit on expiry
* total impact on position = 0

- however, as Charles says, using boxes to dissect a position can reveal useful insights ….

- for example lets say you have sold a Guts strangle [-750call / - 760put] for 13 points credit

- in order to dissect you have to

* -750call / -760put = +13 points

----
* +750call / -760call = Call Vertical }
* -750put / +760put = Put Vertical } - 10 points

= -750put / -760call = + 3 points

- The ITM Guts strangle for 13 points dissects into an OTM strangle for 3 points

- The 13 points received for the guts strangle is 'illusory' as on expiry the embedded box will result in a debit of 10 points.

Does this help any?

Cheers
James

The Box
« **Reply #3 on:** April 25, 2009, 06:45:10 AM »

Thanks for the reply,
I have one question about this statement:

- The 13 points received for the guts strangle is 'illusory' as on expiry the embedded box will result in a debit of 10 points.

How could the box be 'embedded' when it was only inserted to dissect the original position? I mean it was never really there until we inserted it?

Confusing.
Regards
Ed

The Box
« **Reply #4 on:** April 25, 2009, 06:57:24 AM »

(Ri$k Doctor @ Apr. 24 2009,3:42)
QUOTE
I am not sure what you are asking but the box value holds pretty much like the SynTool shows about Reversals and Conversions. The Box only differs from the SynTool in that it is 2 Sets of SynTools at 2 different strikes (one long and one short) where the 2 Syntools showing long and short Underlying offset each other.

The point of a box is that it uncovers the nature of your risk in a simpler fashion, like in the following example from Chapter 5. The actual position is in Blue, the Box Dissection in Red, uncovering the exposure of a long cheap Put in Green:

EXHIBIT 5-11

BoxTool Applied to Three-Legged Box Reveals Synthetic Missing Corner
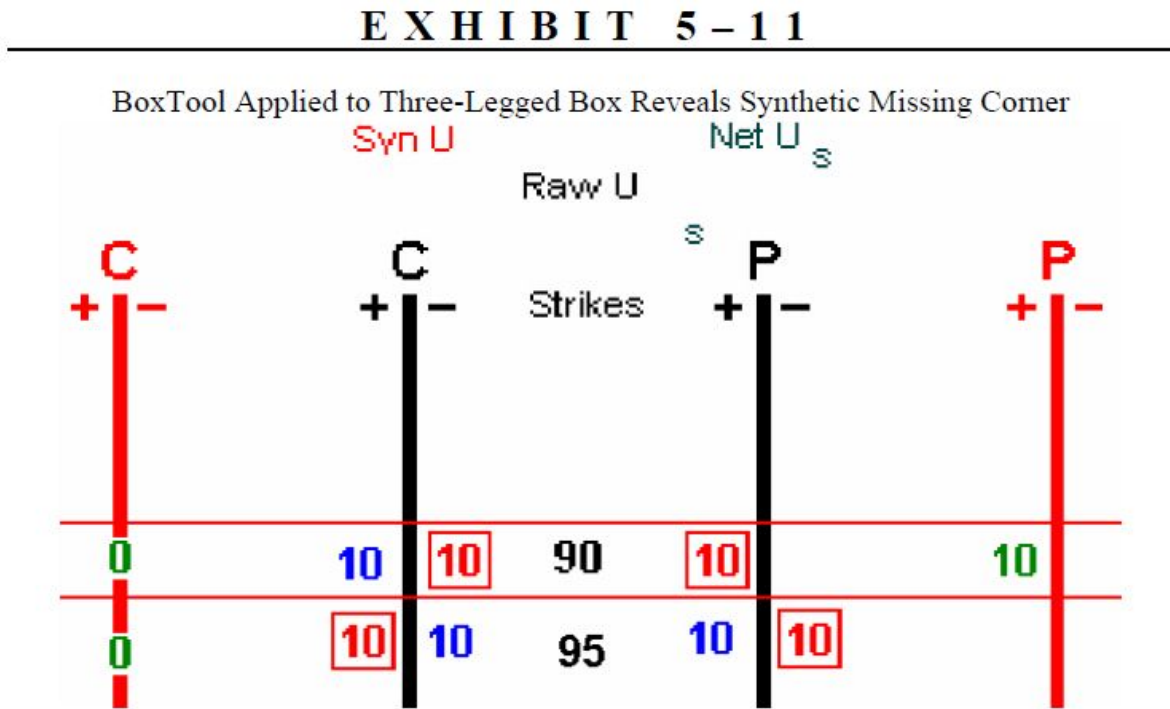
BoxTool: Using the BoxTool is basically taking out a conversion at one strike and a reversal at the other, without the underlying positions that would offset each other. Once one of these locked positions is removed from the position, we can then see a new position. The C/R and box positions are referred to as zero-sum spreads, meaning they are basically flat.

 The Box only differs from the SynTool in that it is 2 Sets of SynTools at 2 different strikes (one long and one short) where the 2 Syntools showing long and short Underlying offset each other.

I think that the above in italics would have been a much better choice of wording than what I quoted from the book IMHO. It made alot more sense when looked at in this way.

I still do not quite understand these 'embedded' boxes as we are the one that put them in there to dissect, it is not as if they were there to begin with. Perhaps you can explain a bit more?

Regards,
Ed

The Box
« **Reply #5 on:** April 25, 2009, 07:03:48 AM »

(James Parker @ Apr. 25 2009,6:43)
QUOTE
- for example ....

* a Long 10 point box at strikes 750 - 760 =
* [Long 750 - 760 Call Vertical] + [Long 750 - 760 Put Vertical]
* will cost approx 10 point debit
* will be worth 10 point credit on expiry
* total impact on position = 0
What I see here is that the box will maintain at least 10 in value regardless of the underlying movement.
You are assuming the price of entry is roughly equal, but that would not always be the case, would it?

So it is an approximation then?
As to my first comment, I agree that the position is flat but it does add a DC bias to the AC (electronic analogy) position if you will.

That was my original point

regards

ed

The Box
« **Reply #6 on:** April 25, 2009, 01:20:22 PM »

Question on dissection 2:
QUOTE
If Gil chooses to view his position as in dissection 2 (Exhibit 2??7), and feels like taking a bit of money off the table, he may want to sell 10 of the 50 straddle to be left with a steeper 50/55 put ratio spread (+30 by ??50) each (+1 by ??1.6) for a 1.80 debit (5.00 minus [1.6*2.00]).
What was the reason to select 50 straddles to sell?

I sort of see the logic from this box discussion. Is this an 'embedded box' that we are removing because it is money wasted on a 'flat' position?

Thanks in advance,
I have a couple more to follow.

Regards
Ed

edsyl
Newbie
⭐
Posts: 26

◈ **The Box**
« **Reply #7 on:** April 25, 2009, 01:22:20 PM »

Question on dissection 3:

If Gil chooses to view his position as in dissection 3 (Exhibit 2??😎, he may want to buy 10*55p leaving the 30*(??1 by +1.33) call back spread. This would only be prudent if the trader thought it likely that the underlying would spike up with an extended move, without, or in spite of, a collapse in implied volatility. Breaking down hard would also allow the 1.67 credit to be kept, if both calls go out worthless. A slow move upward to 55 would be the worst case for this position.

So the idea here was to 'simplify' the net position so that you could clearly see that the call back spread is an example of how the position can be changed after dissection?

---

edsyl
Newbie
⭐
Posts: 26

◈ **The Box**
« **Reply #8 on:** April 25, 2009, 01:25:17 PM »

Question on dissection 5:

This creates 10*(??1 by +2) call back spread at 1.00 credit (2 x 1.00 debit versus a 3.00 credit) and 10* (+1 by ??2) put ratios spread for a 1.00 debit (2 x 2.00 credit, versus a 5.00 debit). By viewing the position that results from dissection 5 (Exhibit 2-10), it is evident that buying 10*45p would turn the put side into a long butterfly, which would limit the exposure to an amount equaling the cost of the 45 put. This purchase could easily be financed by capturing excess premium from the sale of up to 10*55 calls. If the trader likes the
value of the butterfly and/or it meets with his or her market opinion, the above dissection leads to a rather simple adjustment.

I don't understand the thinking behind the selling of the calls. If I sell an additional 10 55 calls, the I would be net 0 calls, is that what you are trying to imply?

Thanks
Ed

The Box
« **Reply #9 on:** April 27, 2009, 01:38:04 PM »

I will get to your other questions but for now:
QUOTE
The Box only differs from the SynTool in that it is 2 Sets of SynTools at 2 different strikes (one long and one short) where the 2 Syntools showing long and short Underlying offset each other.
I think that the above in italics would have been a much better choice of wording than what I quoted from the book IMHO. It made alot more sense when looked at in this way.
A Bull Spread vs. a Bear Spread is shown in Exhibit 1-9:

EXHIBIT 1-9

Conventional Hockey-Stick Risk Profile of a Box Spread
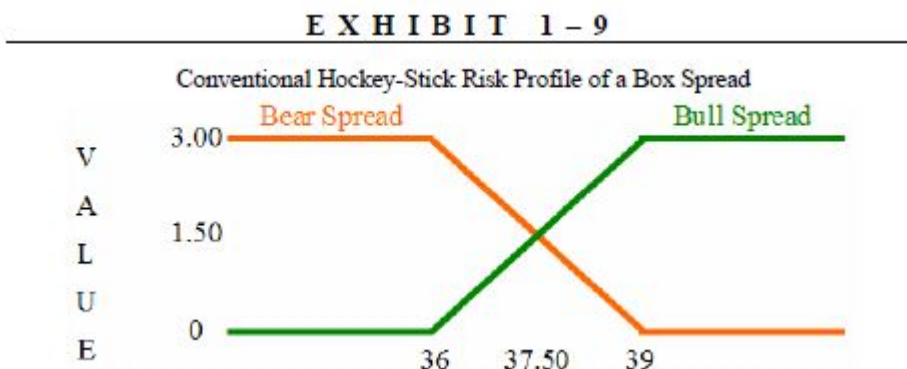
Sorry, I guess I should not have relied on a picture painting a thousand words (not the right words) in this case.

The Box
« **Reply #10 on:** April 27, 2009, 04:39:49 PM »

Charles:
I am only trying to give feedback as to what might help to make it better.
I am sure if I am having issues, others will as well.

I think one of the problems is all the different visual terms: hockey stick, the box spread, and basically flat.
What would have been more effective and drive the point home would have been applying two syntools to a position and then showing how that morphs to your box tool.
The next thing is that the concept of synthetics is very useful, but we make the jump to use a dissection to change a position by synthetics (very complex ones VERY quickly, I might add). Without the understanding of the nuances of ratio spreads and the like a lot of this discussion goes flying overhead really quickly.

What is also lost in here is the idea of things being 'embedded' in a position.
Just what do you mean by that exactly? Why is it important?
The issue being if you don't clearly grasp it in this chapter, you will never get it in the later chapters.
More words and examples, a slower pace, and ease up on the complexity of the examples in the first chapters would go a long way.
Less is more in this case.
I really think that a lot of people get turned off by frustration pretty quickly. But I'm stubborn I guess.

Just my two cents worth as I slog through the very content packed material in the text.
Regards
Ed

James Parker
RDCC
Full Member
⭐

The Box
« **Reply #11 on:** April 29, 2009, 12:22:21 AM »

(edsyl @ Apr. 25 2009,10:45)
QUOTE
Thanks for the reply,
I have one question about this statement:

- The 13 points received for the guts strangle is 'illusory' as on expiry the embedded box will result in a debit of 10 points.

How could the box be 'embedded' when it was only inserted to dissect the original position? I mean it was never really there until we inserted it?

Confusing.
Regards
Ed

Ed

Hi, agreed, it can be incredibly confusing and frustrating to try and understand boxes from first principles as just doesn't seem to make sense ..... embedded positions, imaginary trades, etc ...... however, please persevere as it will revolutionise your perception of option positions.

In respect of your question ..... see if this makes sense ...

ITM GUTS Strangle = OTM Strangle + Box
13 points = 3 points + 10 points

Re-arrange ...

ITM Strangle - Box = OTM strangle
13 points - 10 points = 3 points

I know it looks like we are re-arranging the deck chairs on the titanic, but in reallity we are trying to see the position in its simplest form.

Cheers
James

The Box
« **Reply #12 on:** April 29, 2009, 05:10:36 AM »

edsyl
Newbie
⭐
Posts: 26

Thanks James, much appreciated.
It looks to me like all these tolls are used to try to look at a given position in ways that allow adjustments in many ways depending upon the lay of the land at that given market moment.

I have added questions previously about certain conclusions about the box dissection.
Have a look and maybe you can give me your two cents(debit or credit, you decide...lol)
Regards
Ed

The Box
« **Reply #13 on:** April 29, 2009, 06:47:32 AM »

(edsyl @ Apr. 29 2009,9:10)
QUOTE
Thanks James, much appreciated.
It looks to me like all these tolls are used to try to look at a given position in ways that allow adjustments in many ways depending upon the lay of the land at that given market moment.

I have added questions previously about certain conclusions about the box dissection.
Have a look and maybe you can give me your two cents(debit or credit, you decide...lol)
Regards
Ed

Ed

The ability to dissect a position has numerous advantages ...

- Evaluating a position in its most simple form .... for example ..... it is easier to understand an OTM strangle for 3 points credit has a maximum profit on expiry of 3 points between the strikes .... than an ITM strangle for 13 points credit, that has a maximum profit of 3 points between the strikes

- Adjustments ..... if you wanted to close the ITM strangle prior to expiry .... you have 2 choices .....

Adjustment 1 ..... Buy back the ITM strangle for say 11 points ..... nett profit of 2 points [13 - 11] ..... position closed

Adjustment 2 ..... Buy an OTM strangle for 1 point ...... nett credit is 12 points [13 -1] ..... nett profit of 2 points [13 - 1 - 10 box] ...... the position you are left with is a short box ....

- Long Put / Short Call at the lower strike
- Short Put / Long Call at the higher strike

Wherever the underlying expires, the short box position you are left with is closed for a debit of 10 points.

The reason you would adjust/close using the OTM strangle is that the OTM options are often more liquid and have narrower bid-ask spreads.

Cheers
James

The Box
« **Reply #14 on:** May 05, 2009, 03:29:24 PM »

Risk Doctor:
Still waiting fro replies to questions above!
Ed

Regards

RI$K DOCTOR

csrote
RDCC
Newbie
⭐
Posts: 44

Options Metamorphosis I -- II-3 Conversion
« **on:** February 11, 2010, 06:30:03 PM »

Hello Charles,

I will show you my notes, then pose my question.

Notes-
Conversion: [S = P – C]   [S+C = P] This is why we can watch P as our risk mgmt technique, because P = S+C.
SPY currently at 82.53.
75 call sold a month ago when we went long SPY @ 69. Call was OTM. Now, with SPY at 82.53, call is ITM.
Should be watching the 75 put since our position is making/losing money just like the 75 put. [because this is a Conversion.]
Our risk mgmt technique is to watch the 75 put.
At some point we will buy it back OR liquidate the actual call + stock OR roll call to new month OR take the hedge off....

Question-
In what sense is the Put just like our position of S-C? The Put is worth .15 or .16. How can our position be worth this little?
Thinking out loud:
Intrinsic value of C = 7.53. 82.53 - 7.53 = 75. How is 75 equal to .15 = Extrinsic value of P?

Thnx,
//Cliff

James Parker
RDCC
Full Member
⭐
Posts: 207

Re: Options Metamorphosis I -- II-3 Conversion
« **Reply #1 on:** February 12, 2010, 12:29:52 AM »

Cliff

Let's say you originally bought SPY at 69.00 and sold the 75 call for 1.00.
When you sold the 75c; the 75p would have been 7.00 [75.00-69.00+1.00]

Current Price of SPY is 82.53
Current price of 75c is 7.68.
Current price of 75p is 0.15

```
-----------------------     Buy SPY at 69.00
                            Sell 75c at   1.00
                            Max profit is 7.00 [75.00-69.00+1.00]
Scenario 1                  Current profit:
                            SPY        13.53 [82.53-69.00]
                            Call       (6.68) [1.00 - 7.68]
                                       -------
                            Profit     6.85    being Max profit 7.00 less 0.15 'extrinsic value' of 75c

                            ----------------------

                            Scenario 2

                            Sell 75p at   7.00
                            Max profit is 7.00
                            Current profit:
                                       -------
                            Profit     6.85    being Max profit 7.00 less 0.15 'extrinsic value' of 75p

                            ----------------------

                            All held together will p-c parity
                            Cheers
                            James
```

Re: Options Metamorphosis I -- II-3 Conversion
« **Reply #2 on:** February 12, 2010, 05:16:08 AM »

Thank you, James.

A little Put-Call Parity before breakfast!

This reminds me of Ohm's Law* for electronics.
The "Law" is rather simple, but learning HOW to use it in actual electronic circuits takes some doing...which I am doing!

Will let you know if I don't get it after further cogitation and tea...

Cheerio,
//Cliff

* Ohm's Law (named after German physicist Georg Ohm, who published it in 1826), defines the relationships between (P) power, (E) voltage, (I) current, and (R) resistance. One ohm is the resistance value through which one volt will maintain a current of one ampere.
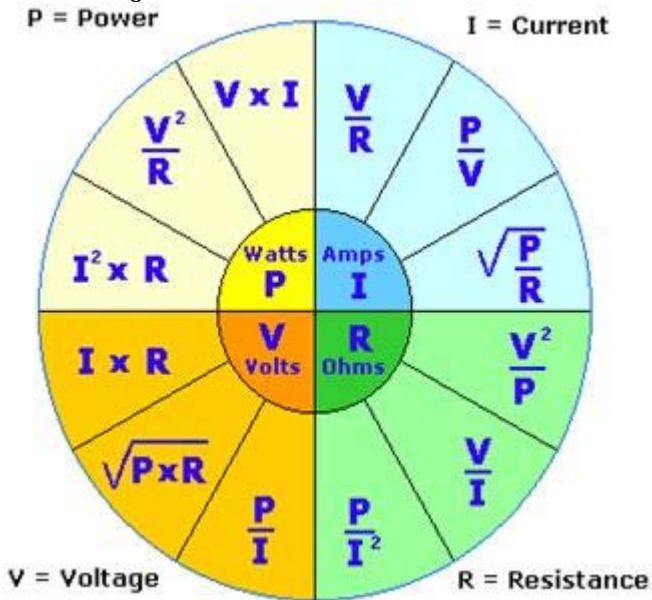
Re: Options Metamorphosis I -- II-3 Conversion

« **Reply #3 on:** February 15, 2010, 12:13:28 PM »

Quote
> Conversion: [S = P – C]   [S+C = P] .....

Wrong. Conversion: [Long S, Long P and Short C].
+S-C is synthetic to -P.
Therefore S will behave = to a long C and a Short P.

Quote
> Intrinsic value of C = 7.53. 82.53 - 7.53 = 75. How is 75 equal to .15 = Extrinsic value of P?

As far as using the equation goes to reconcile the prices, you need the strike (K).
The Call would be 7.68* because:
 K + C = S + P*
75 + 7.68 = 82.53 + .15

*Actially it is K+C = S+P +I - D (Interest and Dividends in Equities)

Re: Options Metamorphosis I -- II-3 Conversion
« **Reply #4 on:** February 19, 2010, 10:45:40 AM »

Charles, thanks for the correction. Got it!

	Author

csrote
RDCC
Newbie
⭐
Posts: 44

Options Metamorphosis I-II-4 SHORT PUT rolled to different strike using spreads
« **on:** February 13, 2010, 12:55:57 PM »

The example in the video shows that this may be accomplished using either put or call spreads.
Are there ever any reasons to prefer one over the other **in this particular situation**?

From the video, it was mentioned that if using a put spread to roll the synthetic short put down, may be faced with pin risk later. This would be a reason to use a call spread, instead. --Yes?

I have seen calendar traders start with a single calendar-
-- If market moves up, they add a second call calendar.
-- If market moves down, they add a second put calendar.

What are legitimate reasons to prefer calls vs puts and puts vs calls for spread trading **in general**?

James Parker
RDCC
Full Member
⭐
Posts: 207

Re: Options Metamorphosis I-II-4 SHORT PUT rolled to different strike using spreads
« **Reply #1 on:** February 14, 2010, 09:29:37 AM »

Cost .....

Administrator
Hero Member
⭐⭐⭐⭐
Posts: 3247

Re: Options Metamorphosis I-II-4 SHORT PUT rolled to different strike using spreads
« **Reply #2 on:** February 14, 2010, 08:32:26 PM »

OTM Vertical for tighter bid/ask or to avoid Pin Risk.

James Parker
RDCC
Full Member
⭐
Posts: 207

Re: Options Metamorphosis I-II-4 SHORT PUT rolled to different strike using spreads
« **Reply #3 on:** February 15, 2010, 01:34:48 AM »

Tighter bid-ask would take priority over pin risk [or if you trade cash settled european style options like the FTSE, there is no pin risk 🙂]

Ri$k Doctor
Administrator
Hero Member
⭐⭐⭐⭐
Posts: 3247

Re: Options Metamorphosis I-II-4 SHORT PUT rolled to different strike using spreads
« **Reply #4 on:** February 15, 2010, 10:35:29 AM »

Agree.

csrote
RDCC
Newbie
⭐
Posts: 44

Re: Options Metamorphosis I-II-4 SHORT PUT rolled to different strike using spreads
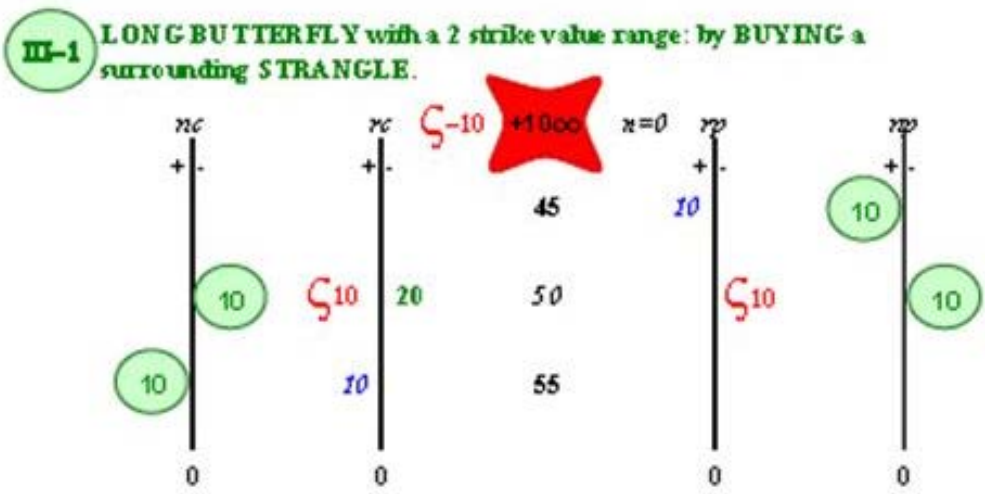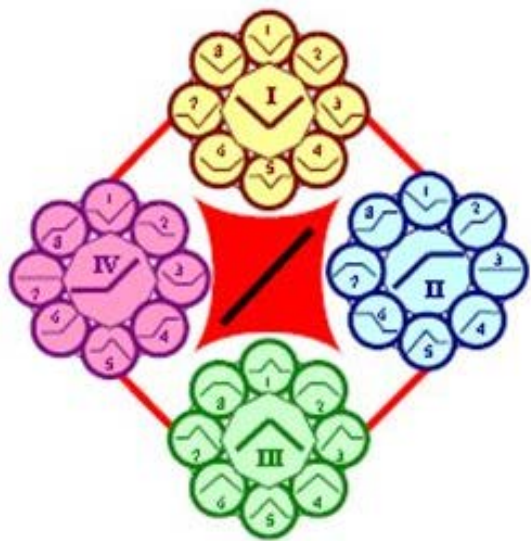« **Reply #5 on:** February 18, 2010, 08:48:31 AM »

Got it.
Thank you!

RI$K DOCTOR

Ri$k Doctor
Administrator
Hero Member
★★★★★
Posts: 3247

◈ **Why take this course?**
« **on:** February 01, 2010, 07:17:33 AM »

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