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Short Term Trading With WeeklysSM Options

April 16, 2014
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Short Term Trading with Weeklys

Outline

- Introduction / Review of Weeklys Options
- Time Decay
- Short Term Diagonal Spreads
- Credit Spreads
- Summary / Q&A

Weeklys Options

Overview

- **Short dated or weeklys options were introduced on stocks and ETFs about four years ago**
- **Weeklys options based on the S&P 500® (SPXsm) have actually been around since 2005, however volume did not really catch on until 2010**
- **Now short dated options represent close to one third of daily option volume**

Weeklys Options

Time Decay

- **A big factor that has contributed to the popularity of short dated options is time decay**
- **For at the money options, time decay accelerates as expiration approaches**
- **Depending on how deep in the money a contract is, an in the money options may have very little time value remaining**

Weekly Options

Time Decay

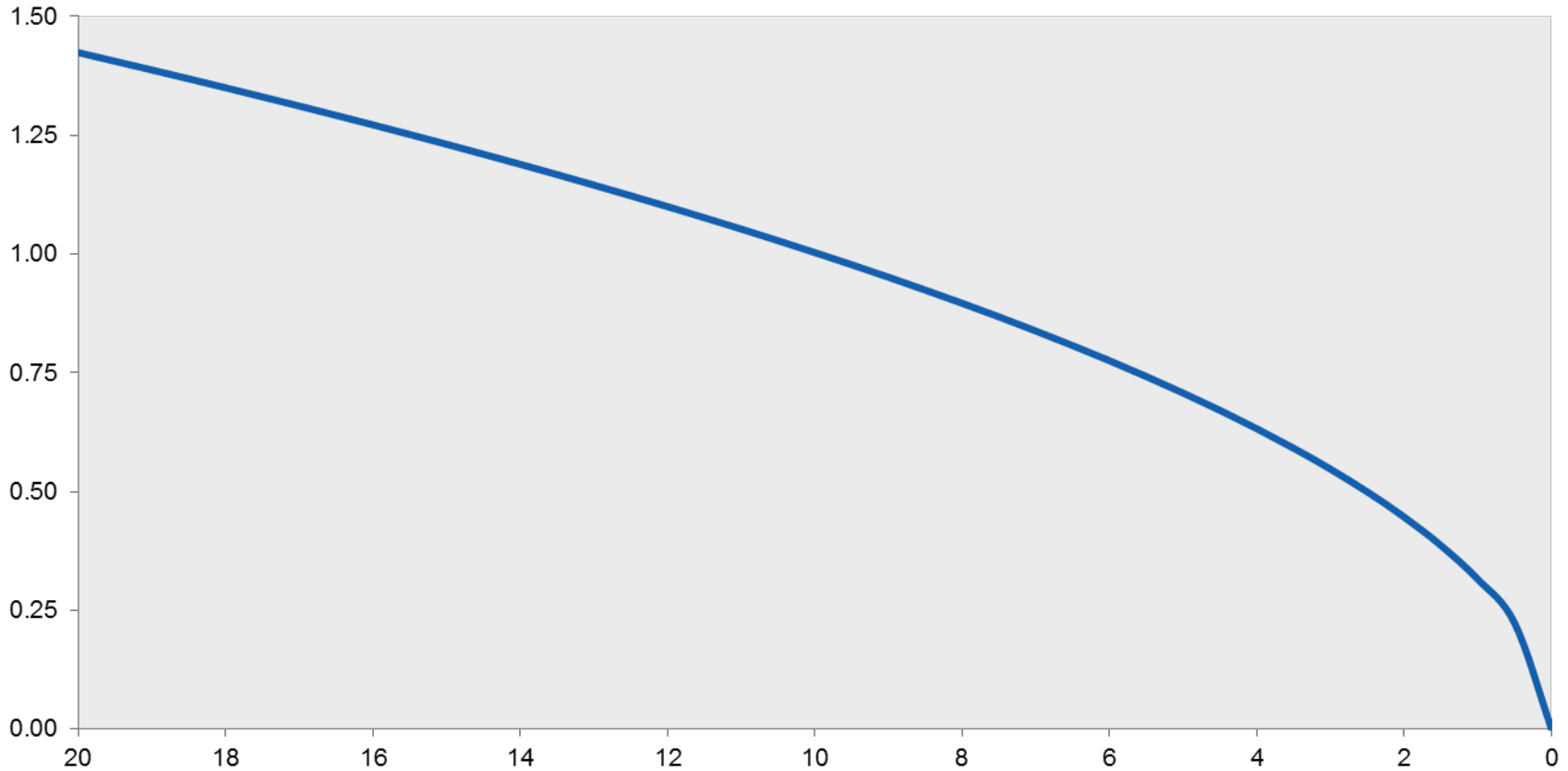
AAPL @ 542.00 – Wednesday Morning

		Time Value		Time Value
	3 Day		8 Day	
AAPL 530.00 Call	12.55	0.55	13.80	1.80
AAPL 542.50 Call	2.65	2.65	5.05	5.05

Weeklys Options

Time Decay

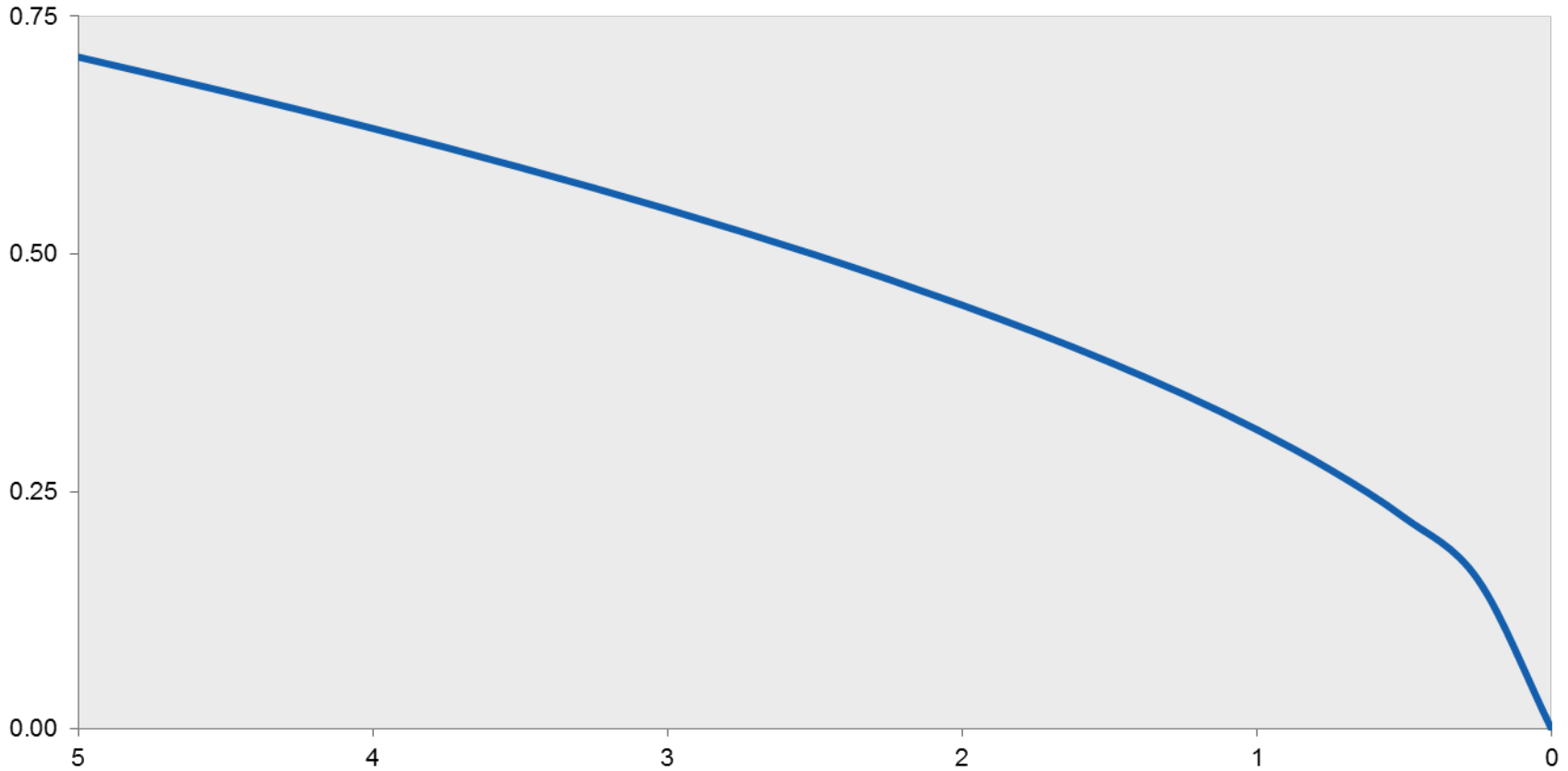
20 Trading Days of ATM Time Decay –



Weeklys Options

Time Decay

5 Trading Days of ATM Time Decay –



Short Term SPX Trading

Time Decay

Friday March 28, 2014 – SPX @ 1857.60 – ATM Time Decay

Weeks	SPX 1855 Put	1 Week Theta*	SPX 1860 Call	1 Week Theta*
1	12.35	12.35	11.70	11.70
2	17.35	5.00	16.00	4.30
3	20.55	3.20	18.55	2.55
4	24.05	3.50	22.40	3.85
5	28.10	4.05	26.10	3.70
6	31.50	3.40	27.95	1.85
7	35.10	3.60	29.80	1.85
8	38.10	3.00	32.90	3.10

Short Term SPX Trading

Time Decay

Friday March 28, 2014 – SPX @ 1857.60 – ITM Time Decay

Weeks	SPX 1875 Put	1 Week Theta*	SPX 1840 Call	1 Week Theta*
1	22.70	5.30	25.15	7.55
2	27.20	4.50	29.00	3.85
3	29.75	2.55	31.60	2.60
4	33.30	3.55	35.30	3.70
5	37.30	4.00	39.05	3.75
6	40.90	3.60	40.80	1.75
7	43.90	3.00	42.10	1.30
8	46.90	3.00	45.10	3.00

Short Term SPX Trading

Diagonal Spread

- Thursday March 27, 2014 – S&P 500 at 1850
- Trader with a bullish outlook for the S&P 500 initiates the following trade

Buy 1 SPX Apr 11th 1845 Call @ 20.90

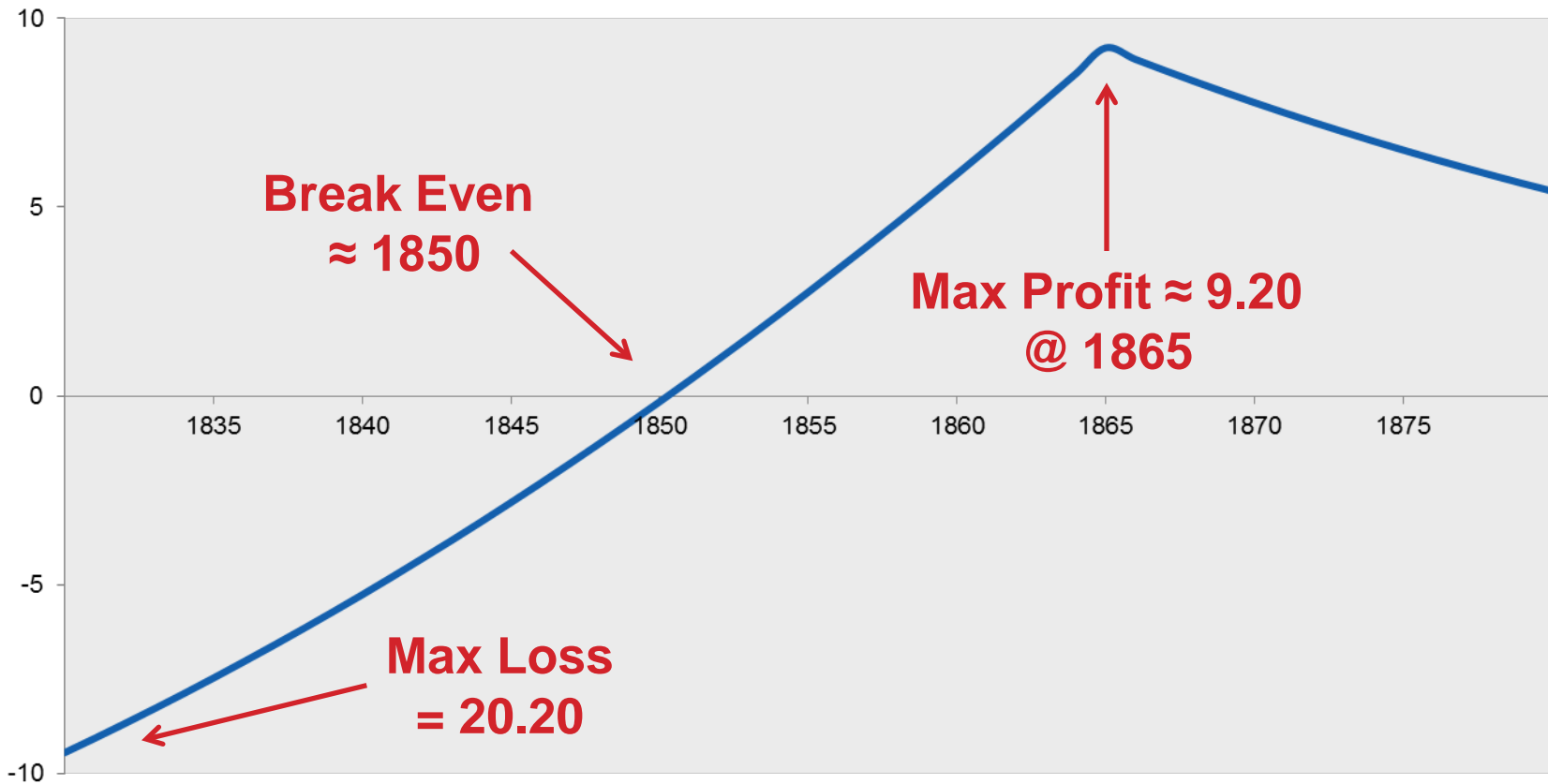
Sell 1 SPX Mar 28th 1865 Call @ 0.70

Net Cost = 20.20

Short Term SPX Trading

Diagonal Spread Payoff

On March 28th Expiration –



Short Term SPX Trading

Diagonal Spread

- **April 11th option has 11 trading days while the Mar 28th option has 1 trading day remaining until expiration**
- **On March 28 the S&P 500 closed at 1857.62 so the March 28th Call expired with no value and the April 11th Call was bid at 24.70 on the close – unrealized profit of 4.50**
- **Trader may choose to sell another short dated call option, leave the position on, or close out the position**

Let's take a look at the April 4th Calls...

Short Term SPX Trading

Diagonal Spread

March 28, 2014 – SPX @ 1857.62

	Bid	Ask
SPX Apr 4 th 1860 Call	11.20	12.20
SPX Apr 4 th 1865 Call	8.60	9.50
SPX Apr 4 th 1870 Call	6.40	7.10
SPX Apr 4 th 1875 Call	4.60	5.20

Sell 1 SPX Apr 4th 1865 Call @ 8.60

Short Term SPX Trading

Diagonal Spread

Current Position –

Long 1 Apr 11th 1845 Call @ 24.70

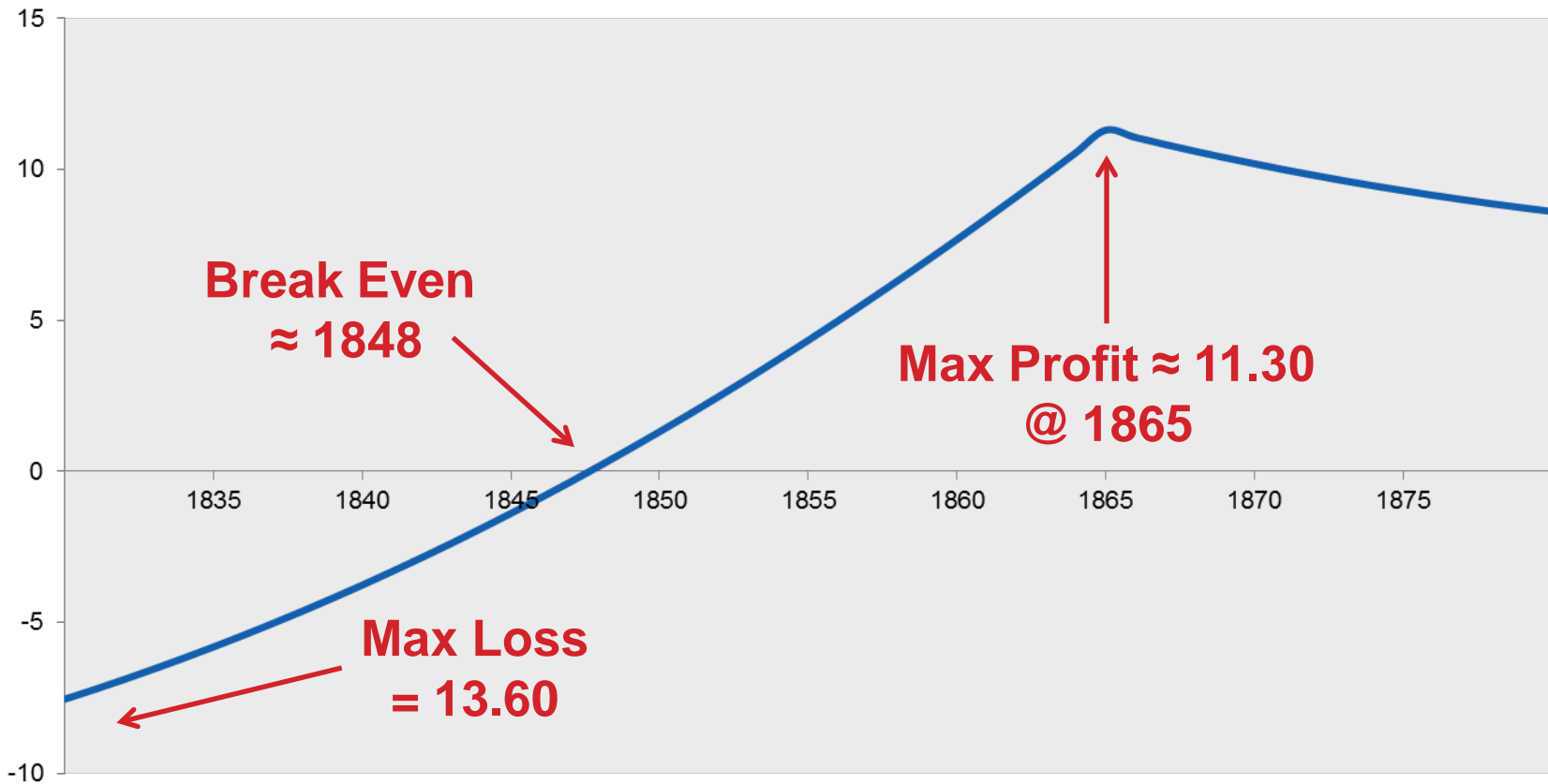
Short 1 Apr 4th 1865 Call @ 8.60

Net Running Cost = 13.60

Short Term SPX Trading

Diagonal Spread Payoff

On April 4th Expiration –



Short Term SPX Trading

Diagonal Spread

- S&P 500 closed at 1865.09 – Short SPX 1865 Call was in the money
- The result was a debit of \$9 ($0.09 \times \100) based on short call position
- Trader still long a SPX Apr 11th 1845 Call at 24.90
- They can choose to sell that option, just hold it, or sell another call option

Let's take a look at the April 11th Calls...

Short Term SPX Trading

Diagonal Spread

April 4, 2014 – SPX @ 1865.09

	Bid	Ask
SPX Apr 11 th 1865 Call	15.20	16.70
SPX Apr 11 th 1870 Call	9.40	10.70
SPX Apr 11 th 1875 Call	7.30	8.00
SPX Apr 11 th 1880 Call	5.30	5.80

Sell 1 SPX Apr 11th 1865 Call @ 15.20

Short Term SPX Trading

Diagonal Spread

Current Position –

Long 1 Apr 11th 1845 Call @ 24.90

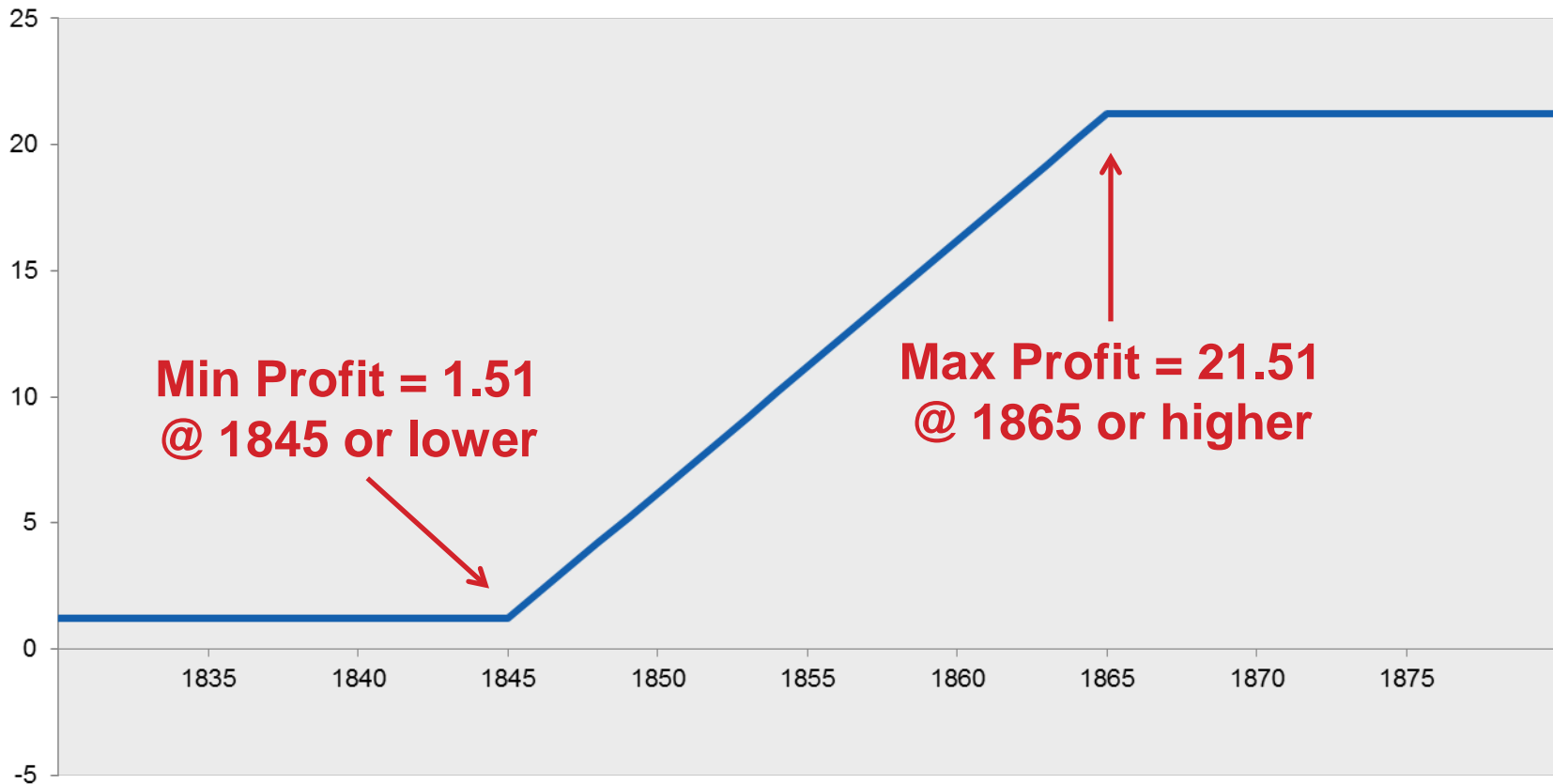
Short 1 Apr 11th 1865 Call @ 15.20

Net Running Income = 1.60

Short Term SPX Trading

Diagonal Spread Payoff

On April 11th Expiration –



Short Term SPX Trading

Diagonal Spread

- Rolling trade consisted of long in the money call combined with at or out of the money calls
- Net result was four trades that resulted in a credit of 1.60
- One of the short calls was slightly in the money and resulted in a cash settlement debit for the trader

Credit Spreads

Overview

- **Credit spreads are a good method for traders to take advantage of option time decay**
- **Often the maximum potential gain from a credit spread is not realized until right at expiration**
- **This makes short dated options excellent candidates for credit spreads**

Credit Spreads

Vertical Spread

- The S&P 500 is at 1857 and we have a neutral to bearish outlook over the next few weeks
- Based on this outlook we check out selling a 20-Day SPX 1860 Call and buying a 1870 Call

Sell 1 20 Day SPX 1860 Call @ 21.90

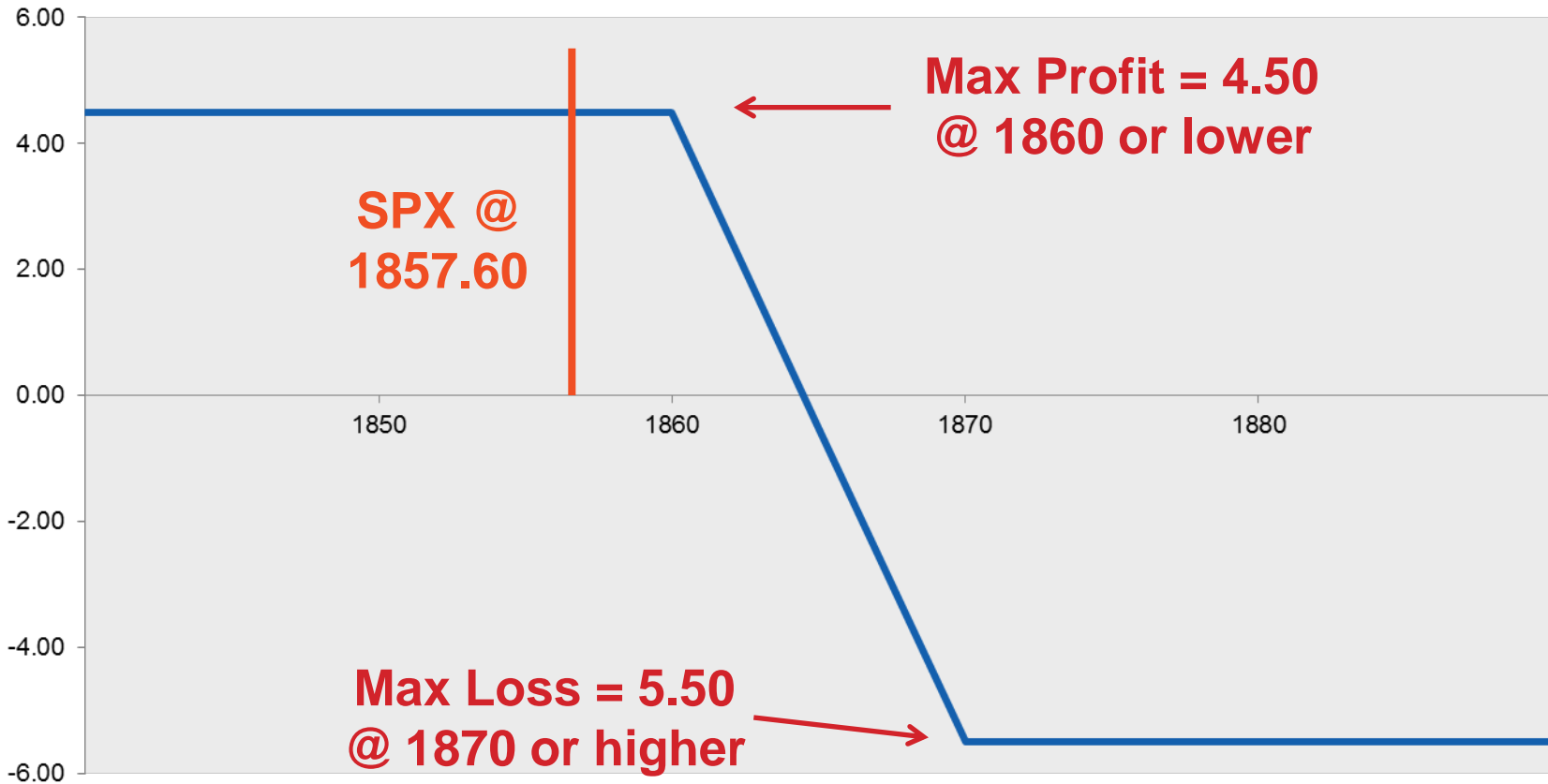
Buy 1 20 Day SPX 1870 Call @ 17.40

Net Credit = 4.50

Credit Spreads

Vertical Spread

Payoff Diagram –



Credit Spreads

Vertical Spread

Weekly Expiration Comparison –

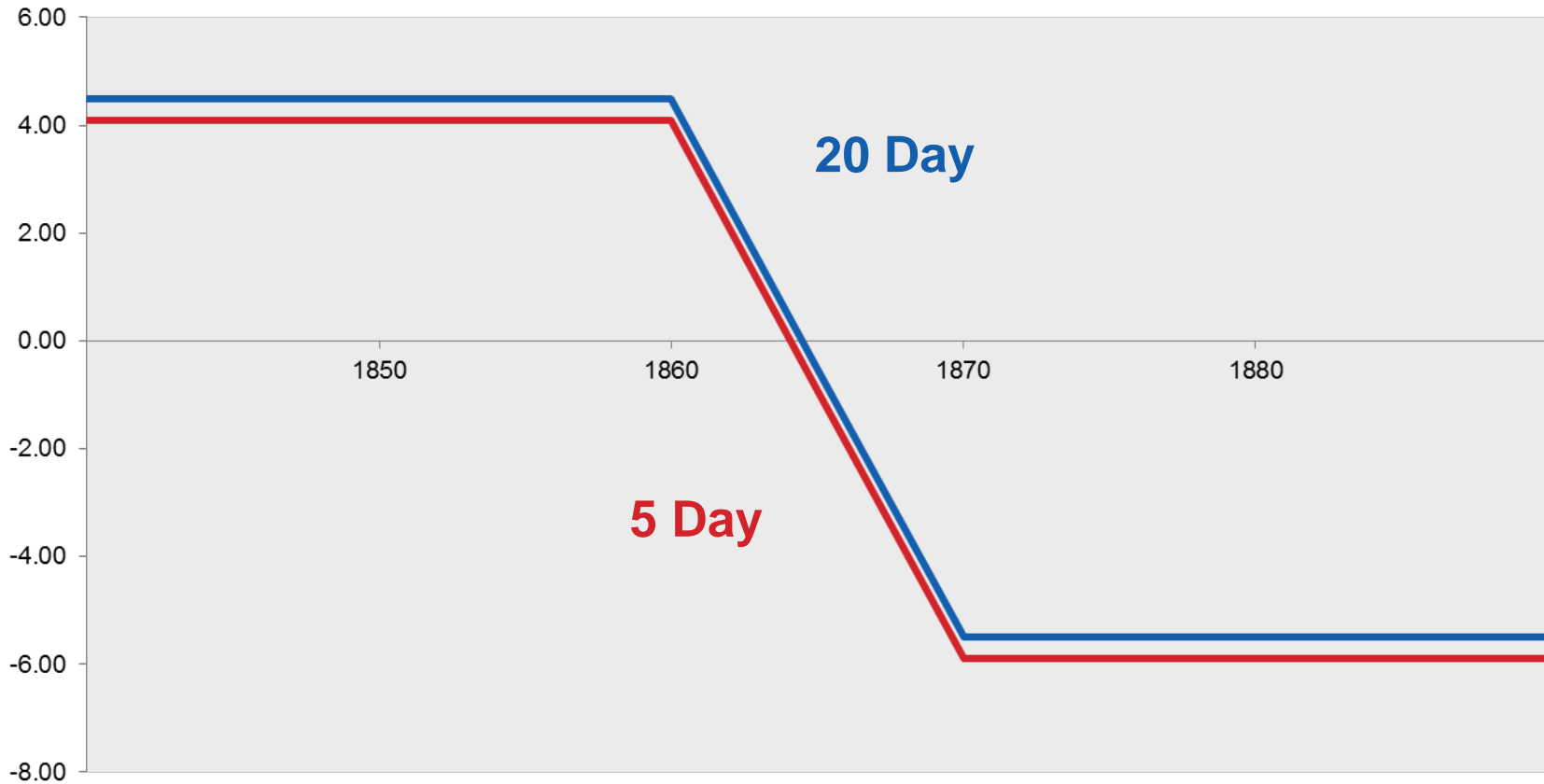
	SPX 1860 Call Bid	SPX 1870 Call Ask	Credit
5 Day	11.20	7.10	4.10
10 Day	15.50	11.30	4.20
15 Day	18.00	13.70	4.30
20 Day	21.90	17.40	4.50

Why do a 20 Day spread when you can do a 5 Day?

Credit Spreads

Vertical Spread

5 Day vs. 20 Day Payoff Diagram –



Credit Spreads

Iron Condor

- The S&P 500 is at 1857 and we have a neutral outlook for the equity market for the next four weeks
- Based on this outlook we check out putting on an iron condor

Buy 1 SPX 20 Day 1840 Put @ 19.30

Sell 1 SPX 20 Day 1850 Put @ 21.60

Sell 1 SPX 20 Day 1865 Call @ 19.10

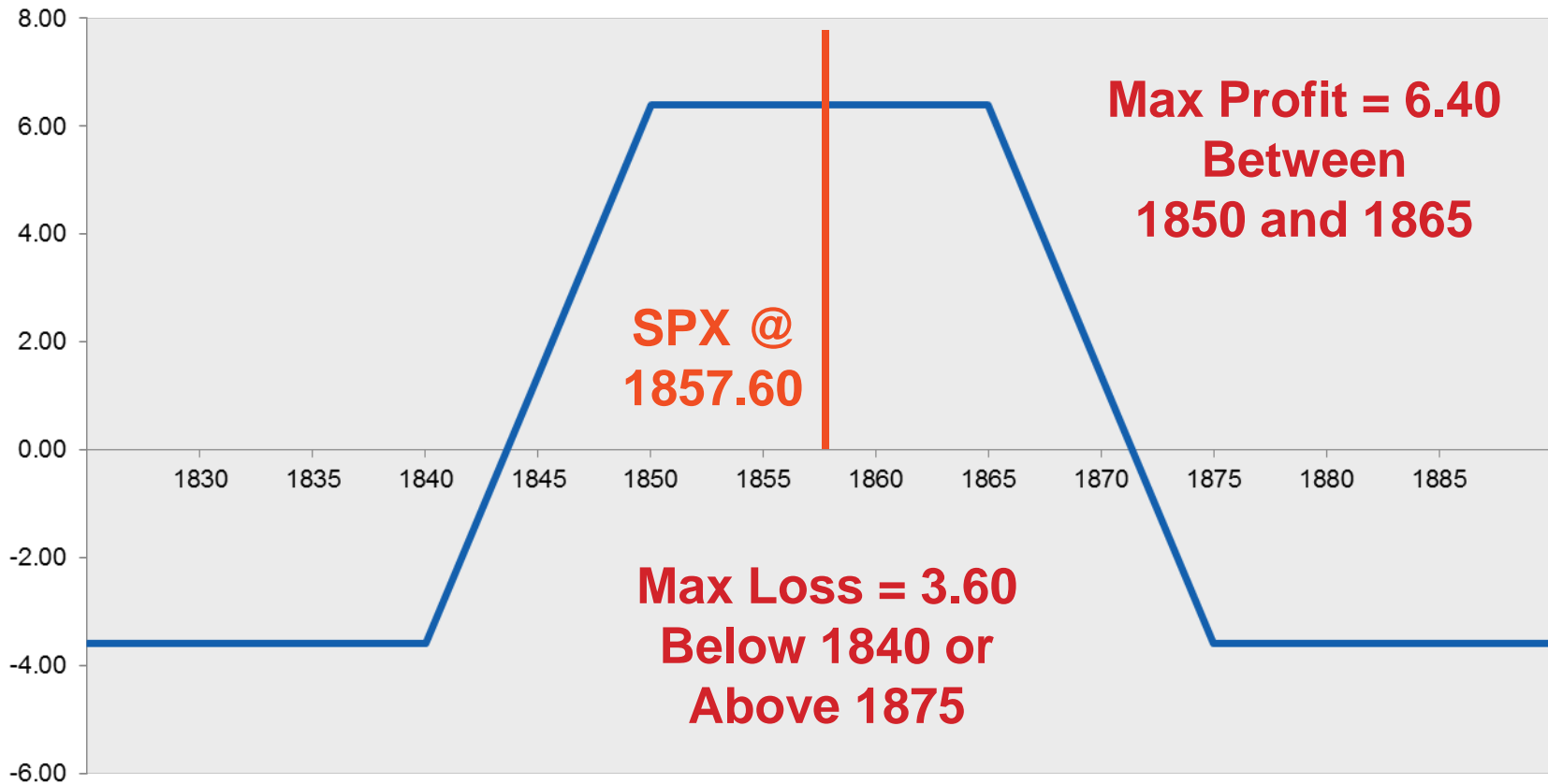
Buy 1 SPX 20 Day 1875 Call @ 15.00

Net Credit = 6.40

Credit Spreads

Iron Condor

Payoff Diagram –



Credit Spreads

Iron Condor

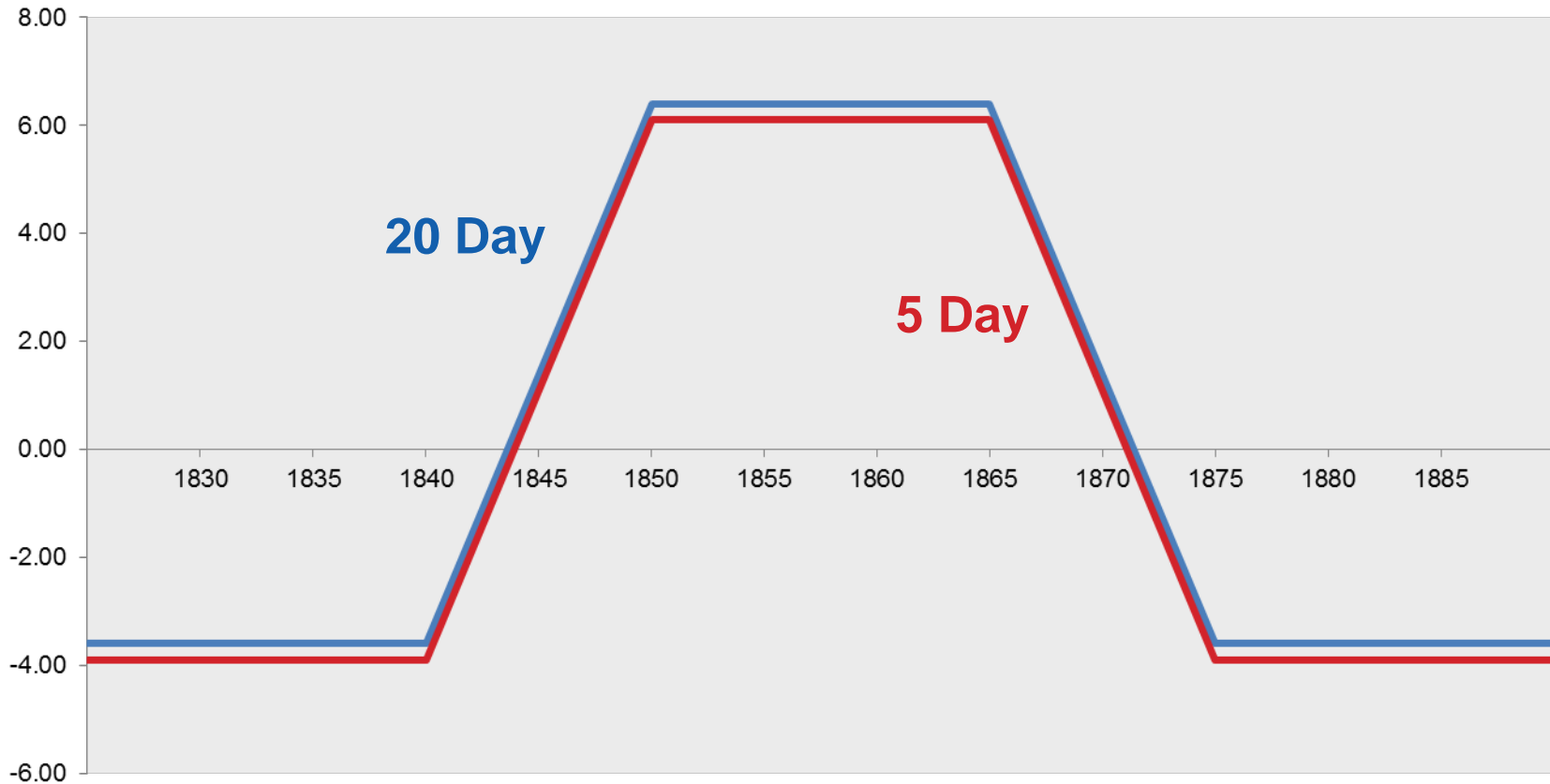
Weekly Expiration Comparison –

	SPX 1840 Put Ask	SPX 1850 Put Bid	SPX 1865 Call Bid	SPX 1875 Call Ask	Credit
5 Day	8.20	11.10	8.50	5.30	6.10
10 Day	12.80	15.00	13.00	9.00	6.20
15 Day	15.70	18.10	15.40	11.50	6.30
20 Day	19.30	21.60	19.10	15.00	6.40

Credit Spreads

Iron Condor

5 Day vs. 20 Day Payoff Diagram –



Credit Spreads

Spreads and Time Decay

- **Short dated SPX options offer flexibility in addition to more time decay benefits**
- **Traders may actually pin point their timing on trades using various SPX expiration dates**
- **Traders may also have more opportunities to execute trades around different outlooks**

Summary

Summary

- **Short dated or Weeklys options have experienced tremendous volume growth in the past few years**
- **These options give traders the ability to manage time decay – either from the long or the short side**
- **Even if a trader has an outlook that has a longer time frame than just a week or two, short dated options should be taken under consideration**

Questions / Contact

CBOE Weeklys Microsite

www.cboe.com/weeklys

CBOE Blog Site

www.optionshub.com

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