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GFM Asset Management

How Conservative Investors Can Hedge Risk & Enhance Yields With Options

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GFM
ASSET MANAGEMENT

Options 101 For Risk-Concerned Investors

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Image credit: My own photo, taken in a market in Urumqi on 15 August 2017

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About Tariq Dennison TEP CFP^{CM}

- Independent Adviser Managing accounts on Interactive Brokers Platform
 - US RIA: GFM Asset Management LLC
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- 23 years global markets experience
 - Commerzbank (NY, London, Frankfurt)
 - Bear Stearns (NY)
 - J.P. Morgan (NY)
 - Canadian Imperial Bank of Commerce
 - Societe Generale (HK)
- Masters in Financial Engineering
 - University of California at Berkeley
- Lecturer at ESSEC Business School
 - Fixed Income
 - Alternative Investments
- Author of "Invest Outside the Box"



Outline of Options 101

- Right into some sample screens
- 5 Simple Sample Option Trades
 - Buy Call
 - Buy Put
 - Protective Put
 - Put Write
 - Covered Call Write
- 1 Sample Spread Trade

Outline of Action Part

- Understanding the options
 - ETF vs index
 - Exchanges & hours
 - Sizes & currencies
- Sample long and short trading strategies

For illustration, I'll use one name traded on 3 markets in TWS

The screenshot shows a search results list in a dark theme. The search term 'bhp' is entered in a search bar at the bottom. The results are categorized by instrument type. The following table summarizes the visible entries:

Instrument Type	Company Name	Market
Stock (SMART)	BHP GROUP LTD-SPON ADR	NYSE
Options	BHP GROUP LTD-SPON ADR	NYSE
CFD	BHP GROUP LTD-SPON ADR	NYSE
Stock (SMART)	BHP GROUP LTD-SPON ADR	FWB
Stock (SMART)	BHP GROUP PLC	LSE
Options	BHP GROUP PLC	LSE
Warrants	BHP GROUP PLC	LSE
Structured Products	BHP GROUP PLC	LSE
CFD	BHP GROUP PLC	LSE
Stock	BHP GROUP PLC	JSE
CFD	BHP GROUP PLC	JSE
Stock (SMART)	BHP GROUP LTD	ASX
Options	BHP GROUP LTD	ASX
Warrants	BHP GROUP LTD	ASX
CFD	BHP GROUP LTD	ASX
Bonds	Corporate Fixed Income	

Any stock, options or futures symbols displayed are for illustrative purposes only and are not intended to portray recommendations.

BHP (ASX) Option Chain on TWS, 10 June 2021

BHP ASX PUT/CALLs (Side by Side) 48.30 -0.37 (-0.76%)

AUG 19 '21 BHP 100 70 DAYS | **SEP 16 '21 BHP 100 98 DAYS** | SEP 16 '21 BHP.E 100 98 DAYS | MORE

TABBED VIEW PUT/CALL 3.5 SD ASX TRADING CLASS IV: 30.0%

CALLS						PUTS								
OPTN ...	VOLUME	BID	ASK	DELTA	IMPLD...	ASK S...	STRIKE	OPTN ...	VOLUME	BID	ASK	DELTA	IMPLD...	ASK S...
30			x	0.874			41		200	0.930	x 1.135	-0.208	33.3%	200
			x	0.860			41.5		200	1.035	x 1.250	-0.227	32.8%	200
40			x	0.845			42	2.11K	200	1.150	x 1.370	-0.245	32.5%	200
			x	0.826			42.5	467	200	1.280	x 1.505	-0.267	32%	200
50			x	0.807			43		200	1.425	x 1.655	-0.289	31.9%	200
750			x	0.788			43.5	20	200	1.580	x 1.810	-0.312	31.7%	200
681			x	0.766			44	1.74K	200	1.745	x 1.985	-0.336	31.3%	200
468			x	0.743			44.5		200	1.930	x 2.170	-0.361	30.9%	200
670			x	0.720			45	1.62K	200	2.125	x 2.365	-0.386	30.8%	200
468	200	3.920	x 4.570	0.694	30%	200	45.5	8	200	2.340	x 2.580	-0.413	30.5%	200
3.67K	200	3.825	x 4.055	0.667	30%	200	46	3.00K 250	200	2.565	x 2.805	-0.440	30.4%	200
768	200	3.520	x 3.745	0.639	30.1%	200	46.5	5	200	2.810	x 3.050	-0.467	30.3%	200
1.78K	200	3.215	x 3.440	0.611	29.8%	200	47	500	200	3.065	x 3.310	-0.495	30%	200
1.05K	200	2.915	x 3.150	0.581	29.5%	200	47.5		200	3.330	x 3.585	-0.524	29.9%	200
2.05K	200	2.650	x 2.890	0.551	29.4%	200	48		200	3.615	x 3.880	-0.552	29.8%	200
115	200	2.400	x 2.640	0.521	29.2%	200	48.5		200	3.915	x 4.190	-0.579	29.6%	200
1.51K	200	2.160	x 2.400	0.491	29.7%	200	49		200	4.225	x 4.510	-0.604	29.5%	200
531	200	1.930	x 2.175	0.461	28.7%	200	49.5	200	200	4.555	x 4.845	-0.632	29.5%	200
3.61K	200	1.735	x 1.980	0.430	28.7%	200	50	670	200	4.900	x 5.195	-0.659	29.4%	200
790	400	1.365	x 1.610	0.370	28.3%	200	51	200	200	5.465	x 6.215	-0.711	30%	200
840	200	1.105	x 1.315	0.317	28.3%	200	52	95		x		-0.751		
11	200	0.850	x 1.050	0.266	28.1%	200	53			x		-0.793		

OFF Strategy Builder

Any stock, options or futures symbols displayed are for illustrative purposes only and are not intended to portray recommendations.



We'll get to this later

Details of one option contract

DESCRIPTION		File	Configure
Stock Description			
BHP GROUP LTD			
Security Type	OPT		
Underlying	BHP STK		
Contract Month	SEP21		
Expiration Date	SEP 16 '21		
Last Trading Date	SEP 16 '21 16:20 AEST		
Strike	50		
Right	Call		
Currency	AUD		
Multiplier	100		
Exchange	ASX		
Trading Class	BHP		
Symbol	BHPUL9		
Sector	Basic Materials		
Industry	Mining		
Category	Diversified Minerals		
Product Type	Equity		
Settlement Method	Physical Delivery		
Exercise Style	American		
Trading Schedule: June 10, 2021 Calendar			
Total Available Hours	10:00 - 16:20 (08:00 - 14:20 your time)		
Exchange Time Zone	(UTC+10:00) Australia/NSW		
<i>Note: Trader Workstation follows timezone adjustments for daylight savings time</i>			

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BHP's UK and US Listed Options



BHP LSE PUT/CALLS (Side by Side) C2131.00

JUL 16 '21 BTB 1000 36 DAYS	AUG 20 '21 BTB 1000 71 DAYS	SEP 17 '21 BTB 1000 99 DAYS	OCT 15 '21 BTB 1000 127 DAYS	MORE
CALLS				
OPTN ... VOLUME	BID x ASK	DELTA	IMPLD... ASK S...	STRIKE
41	490.0 x 500.5	0.938	41	1650
41	443.0 x 454.0	0.923	41	1700
41	396.5 x 407.0	0.897	41	1750
41	351.5 x 362.5	0.873	41	1800
41	308.0 x 319.0	0.836	41	1850
41	267.0 x 277.5	0.798	41	1900
41	228.0 x 239.0	0.747	41	1950
41	191.5 x 203.0	0.692	41	2000
41	159.0 x 170.0	0.630	41	2050
41	129.5 x 141.0	0.568	41	2100
41	104.5 x 115.5	0.502	41	2150
41	83.5 x 94.0	0.437	41	2200
41	65.5 x 76.0	0.375	41	2250
41	51.0 x 60.5	0.317	51	2300
41	39.0 x 47.0	0.264	10	2350
41	29.0 x 38.0	0.221	10	2400
41	21.5 x 30.5	0.183	10	2450
41	16.0 x 25.0	0.150	41	2500
51	8.5 x 16.5	0.103	10	2600
41	4.5 x 11.5	0.076	41	2700
41	2.5 x 8.0	0.055	41	2800
41	1.0 x 6.5	0.044	41	2900

Strategy Builder

BHP PUT/CALLS (Side by Side) C74.42

JUN 18 '21 8 DAYS	JUL 16 '21 36 DAYS	AUG 20 '21 71 DAYS	SEP 17 '21 99 DAYS	MORE
CALLS				
OPTN ... VOLUME	BID x ASK	DELTA	IMPLD... ASK S...	STRIKE
31	32.10 x 37.00		161	40
61	29.60 x 34.50		117	42.5
30	27.10 x 31.90		1	45
1	24.70 x 29.40		15	47.5
2	22.20 x 27.00		33	50
7	17.20 x 22.00		28	55
139	12.60 x 17.50		142	60
2	10.30 x 15.00		94	62.5
192	8.40 x 13.00		210	65
210	6.20 x 11.00		223	67.5
3	4.50 x 9.00		1,125	70
20	2.85 x 7.50		1,217	72.5
52	3.80 x 4.60		1,405	75
28	2.85 x 3.70		1,109	77.5
2	2.00 x 2.35		468	80
1,151	1.15 x 3.20		1,474	82.5
26	0.95 x 1.20		26	85
185	0.70 x 0.90		538	87.5
39	0.50 x 0.85		1,558	90
1	0.25 x 0.40		298	95
	x 2.30		1,274	100
	x 2.20		1,282	105

Strategy Builder

DESCRIPTION File Configure

Stock Description

BHP GROUP PLC

Security Type **OPT**
 Underlying **BHP STK**
 Contract Month **SEP21**
 Expiration Date **SEP 17 '21**
 Last Trading Date **SEP 17 '21 16:30 BST**
 Strike **2350**
 Right **Call**
 Currency **GBP**
 Notation **Price quotes are displayed in pence per rules**
 Multiplier **1000**
 Exchange **ICEEU**
 Trading Class **BTB**
 Symbol **BTB SEP21 23.5 C**
 Sector **Basic Materials**
 Industry **Mining**
 Category **Diversified Minerals**
 Product Type **Equity**
 Settlement Method **Physical Delivery**
 Exercise Style **American**

Trading Schedule: June 10, 2021 [Calendar](#)
 Total Available Hours 08:00 - 16:30 (15:00 - 23:30 your time)
 Exchange Time Zone (UTC+00:00) GB-Eire
 Note: Trader Workstation follows timezone adjustments for daylight savings time

DESCRIPTION File Configure

Stock Description

BHP GROUP LTD-SPON ADR

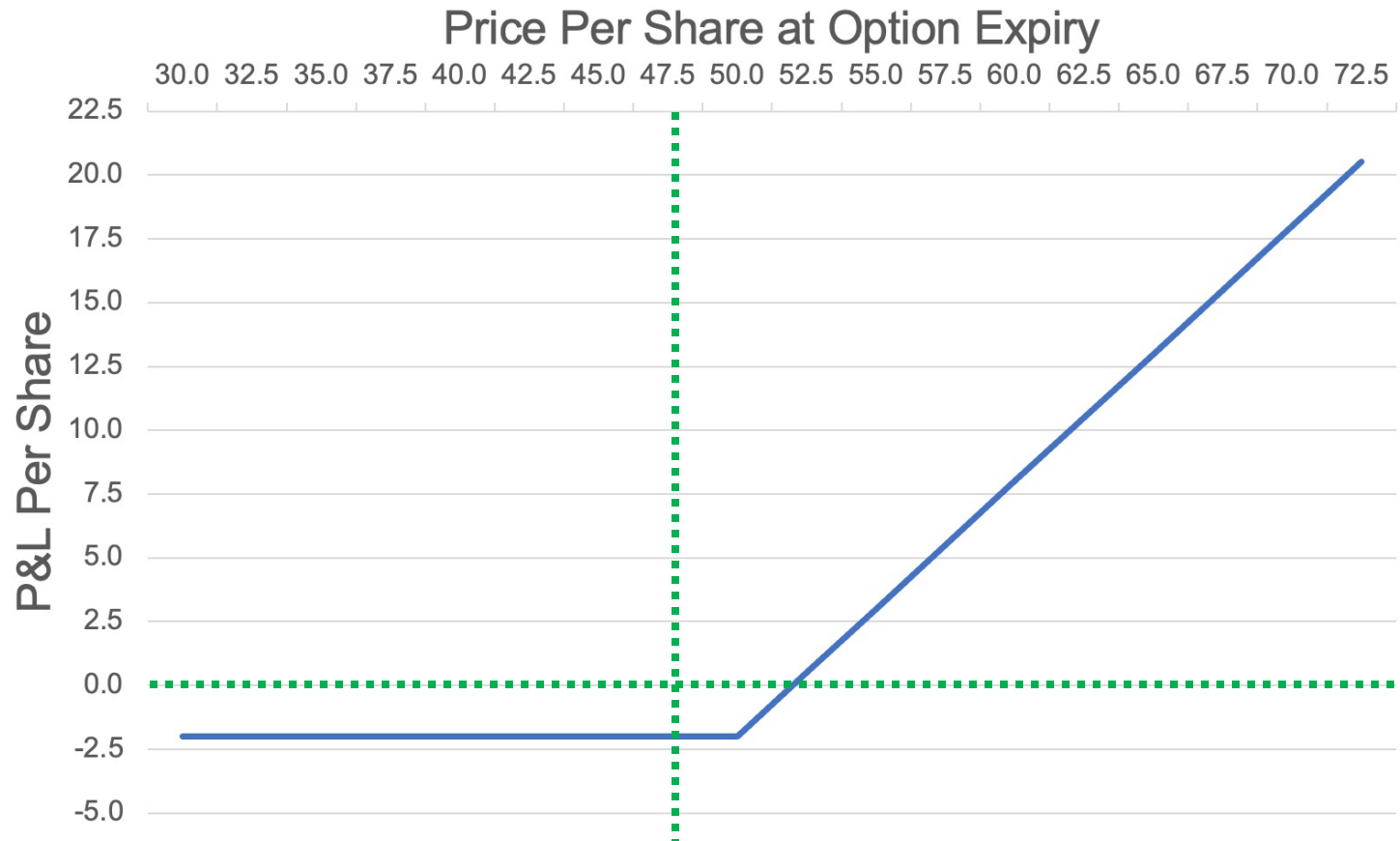
Security Type **OPT**
 Underlying **BHP STK**
 Contract Month **SEP21**
 Expiration Date **SEP 17 '21**
 Last Trading Date **SEP 17 '21**
 Strike **80**
 Right **Call**
 Currency **USD**
 Multiplier **100**
 Exchange **SMART**
 Trading Class **BHP**
 Symbol **BHP 210917C00080000**
 Sector **Basic Materials**
 Industry **Mining**
 Category **Diversified Minerals**
 Product Type **Equity**
 Settlement Method **Physical Delivery**
 Exercise Style **American**

Trading Schedule: June 10, 2021 [Calendar](#)
 Total Available Hours 09:30 - 16:00 (21:30 - 04:00 your time)
 Exchange Time Zone (UTC-05:00) US/Eastern
 Note: Trader Workstation follows timezone adjustments for daylight savings time

Example #1: Buy 50-Strike Call @\$200

Delta = 0.43

Final Price	P&L*
30.0	-2.0
32.5	-2.0
35.0	-2.0
37.5	-2.0
40.0	-2.0
42.5	-2.0
45.0	-2.0
47.5	-2.0
50.0	-2.0
52.5	0.5
55.0	3.0
57.5	5.5
60.0	8.0
62.5	10.5
65.0	13.0
67.5	15.5
70.0	18.0
72.5	20.5



* Per Share → Multiply x100 for P&L per ASX or US contract

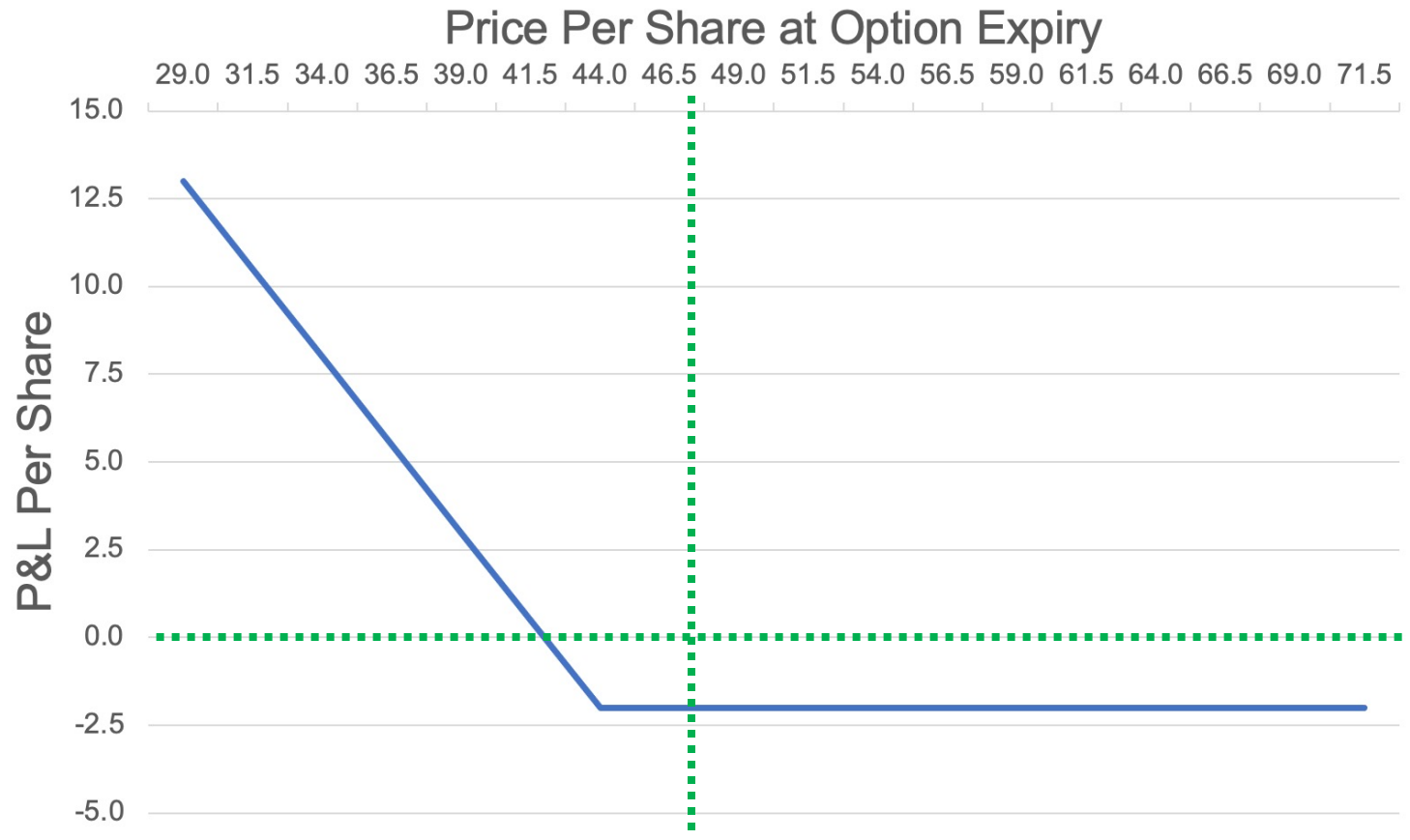
Things to know about buying calls outright

- “43 delta” can be interpreted as implying 43% chance this option will NOT expire worthless (→ 100% loss of \$200/contract premium)
- Even though relatively likely, \$2/share is also the maximum you can lose
- Traditional application by conservative investors: keep most money in bonds, and spend the interest on options for measured upside with limited downside

Example #2: Buy 44-Strike Put @\$200

Delta = 0.34

Final Price	P&L*
29.0	13.0
31.5	10.5
34.0	8.0
36.5	5.5
39.0	3.0
41.5	0.5
44.0	-2.0
46.5	-2.0
49.0	-2.0
51.5	-2.0
54.0	-2.0
56.5	-2.0
59.0	-2.0
61.5	-2.0
64.0	-2.0
66.5	-2.0
69.0	-2.0
71.5	-2.0



* Per Share → Multiply x100 for P&L per ASX or US contract

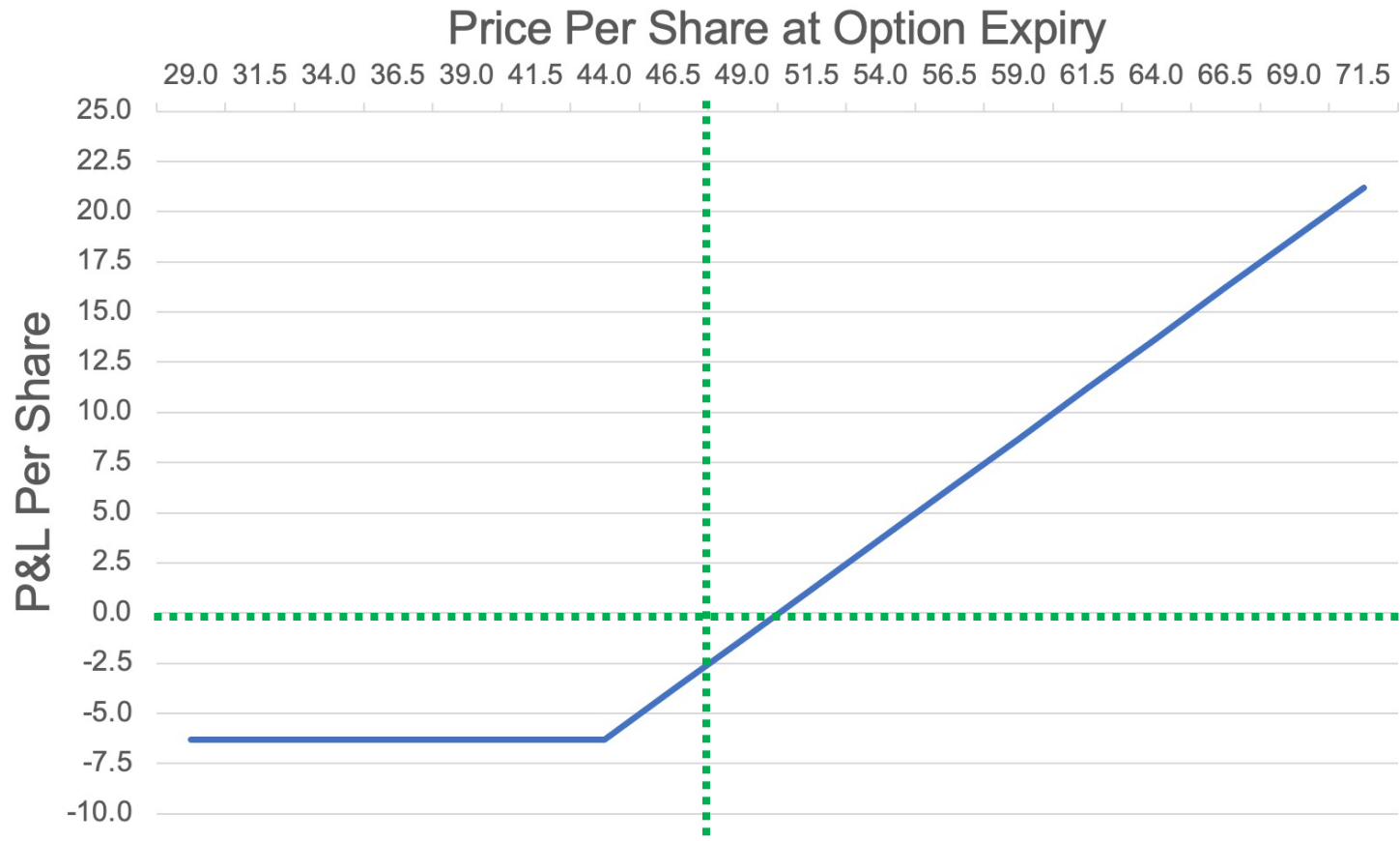
Why buy puts?

- Simplest and most measured way to make money from the decline of a stock's price
 - No stock borrowing required
 - Loss limited to premium paid
- Often bought on ETFs to hedge against broader market declines
- Conservative investors also buy puts on shares they own in this next example...

Example #3: Buy stock @\$4,830 + Buy 44 Put @\$200

Stock Delta (= 1.00) - Option Delta (= 0.34)

Final Price	P&L*
29.0	-6.3
31.5	-6.3
34.0	-6.3
36.5	-6.3
39.0	-6.3
41.5	-6.3
44.0	-6.3
46.5	-3.8
49.0	-1.3
51.5	1.2
54.0	3.7
56.5	6.2
59.0	8.7
61.5	11.2
64.0	13.7
66.5	16.2
69.0	18.7
71.5	21.2



* Per Share → Multiply x100 for P&L per ASX or US contract

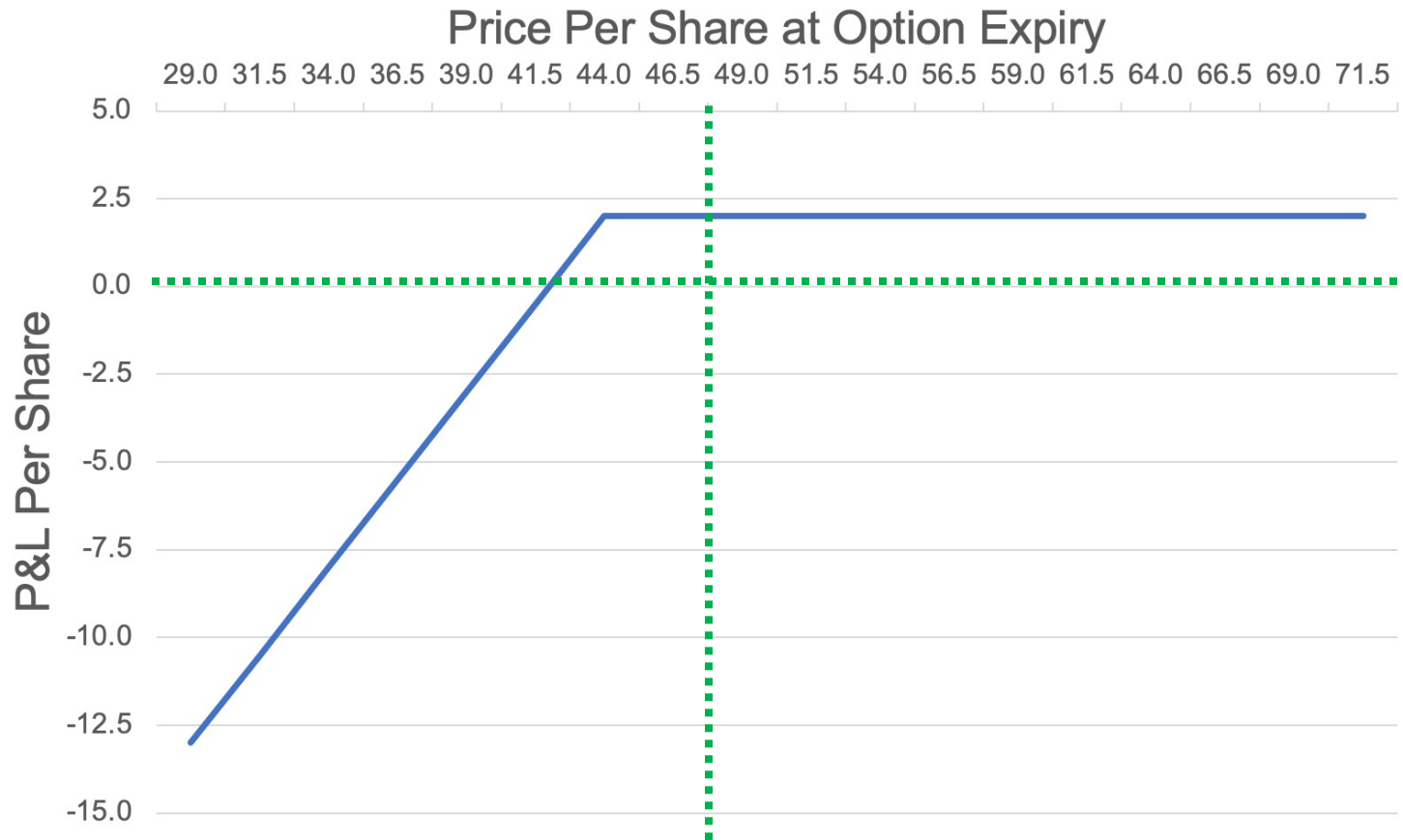
Look familiar?

- Being long stock + buying protective put is economically equivalent to simply being long a call at the same strike
- Main difference between the two:
 - Financing (the amount of cash required)
 - Dividends (physical vs implied)
- This is called “put-call parity”, the same principal that lets you buy a call + sell a put of the same price to mirror a long position.
- Speaking of selling options...

Example #4: Sell 44 Put @\$200

Option Delta = 0.34

Final Price	P&L*
29.0	-13.0
31.5	-10.5
34.0	-8.0
36.5	-5.5
39.0	-3.0
41.5	-0.5
44.0	2.0
46.5	2.0
49.0	2.0
51.5	2.0
54.0	2.0
56.5	2.0
59.0	2.0
61.5	2.0
64.0	2.0
66.5	2.0
69.0	2.0
71.5	2.0



* Per Share → Multiply x100 for P&L per ASX or US contract

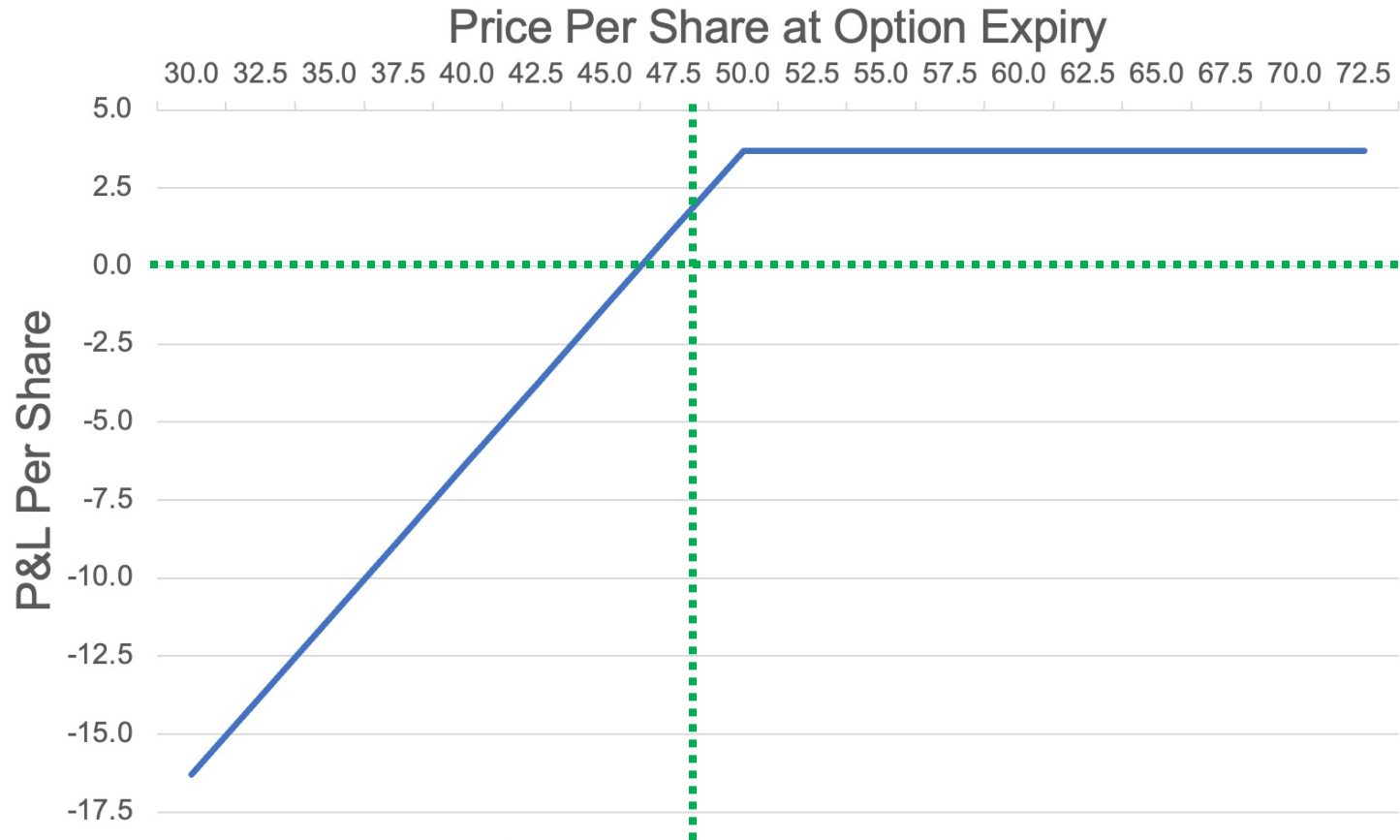
How conservative investors use this strategy

- Generally “cash secured” put writes
- Often used to set a price and time an investor would be happy to buy the stock if the price falls down to or below that level.
- The premium pays the investor to wait, and can also be compared to the coupon on a high yield bond

Example #5: Sell “Covered” 50 Call @\$200

Option Delta = 0.43, Reference stock value \$4,830

Final Price	P&L*
30.0	-16.3
32.5	-13.8
35.0	-11.3
37.5	-8.8
40.0	-6.3
42.5	-3.8
45.0	-1.3
47.5	1.2
50.0	3.7
52.5	3.7
55.0	3.7
57.5	3.7
60.0	3.7
62.5	3.7
65.0	3.7
67.5	3.7
70.0	3.7
72.5	3.7



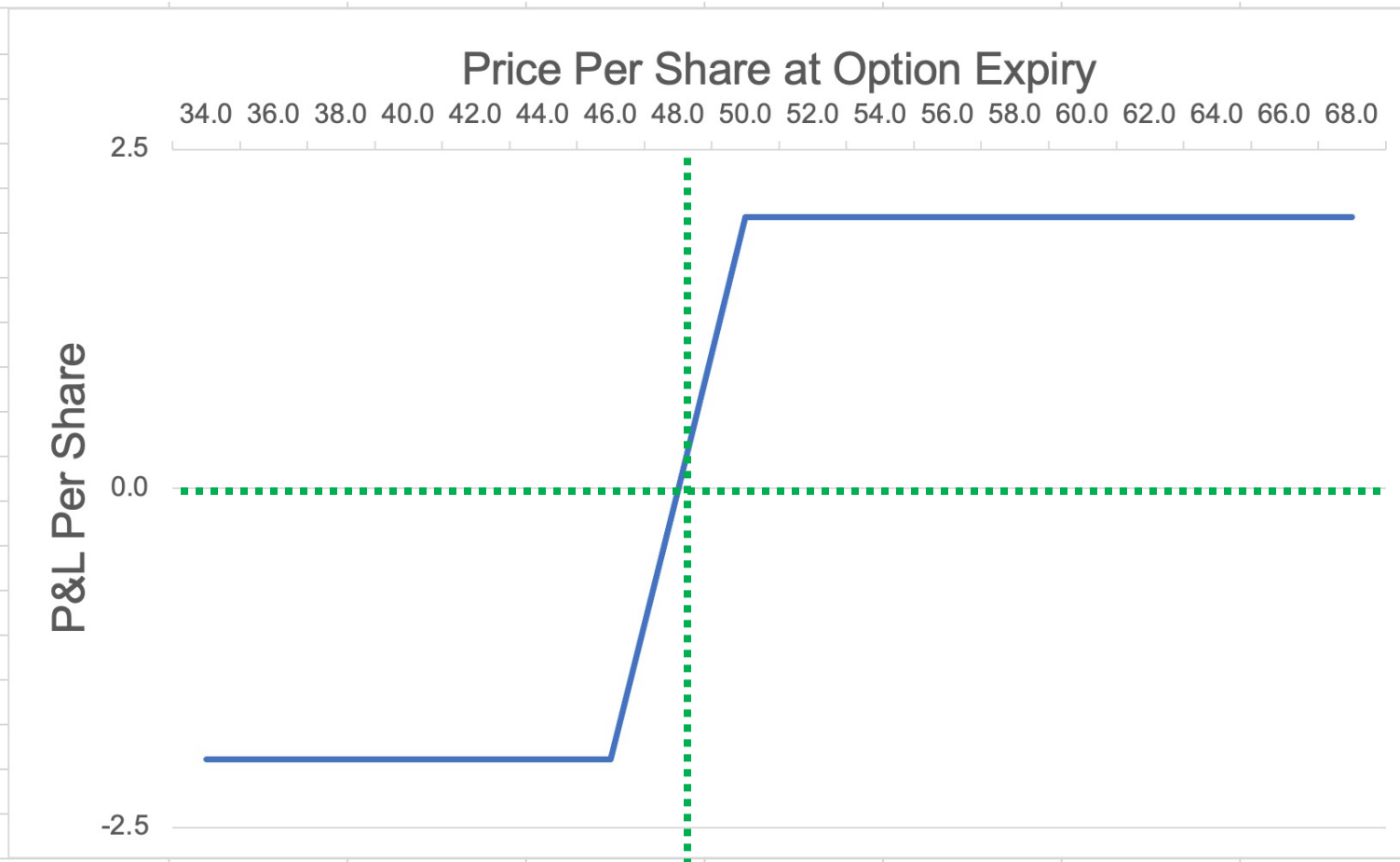
* Per Share → Multiply x100 for P&L per ASX or US contract

Covered Calls = Popular With Dividend Investors

- Call premium sometimes viewed as a “bonus dividend”, providing a bit of a cash buffer against declines.
- Capping the upside can be seen as making it more like a preferred stock.
- Sometimes a way of monetizing high valuations, but must be willing to give up upside if the stock keeps going!
- Many investors roll these regularly

Sample Spread: Buy 46-50 Call Spread @\$200

Final Price	P&L*
34.0	-2.0
36.0	-2.0
38.0	-2.0
40.0	-2.0
42.0	-2.0
44.0	-2.0
46.0	-2.0
48.0	0.0
50.0	2.0
52.0	2.0
54.0	2.0
56.0	2.0
58.0	2.0
60.0	2.0
62.0	2.0
64.0	2.0
66.0	2.0
68.0	2.0



* Per Share → Multiply x100 for P&L per ASX or US contract

More on call spreads and put spreads

- Highly dependent on “skew” pricing
- Longer-term, these are how many insurance and annuity companies offered guarantees with capped market exposure
- Shorter-term, these can look like a “bet”, but the “odds” should be measured against your estimated probabilities of what the asset will do

IBKR has a powerful "Strategy Builder"

Turn this on in a TWS Option Chain

MHI INDEX Calls and Puts
C28497.00

MAR 30 '21
6 DAYS
APR 29 '21
36 DAYS
JUN 29 '21
97 DAYS
SEP 29 '21
189 DAYS
MORE ▾

TABBED VIEW ▾
3.5 SD ▾
HKFE ▾
MHI ▾
10

CALLS						PUTS					
OPTN ...	VOLUME	BID	SIZE	ASK	STRIKE	OPTN ...	VOLUME	BID	SIZE	ASK	STRIKE
				x	0.743			35		904 x 967	25600
				x	0.728		1	20		980 x 1018	25800
4				x	0.712		28	4	20	1045 x 1084	26000
				x	0.696		24	5	20	1114 x 1153	26200
				x	0.679		15	20		1189 x 1228	26400
				x	0.662		13	20		1266 x 1307	26600
	2			x	0.644		12	20		1349 x 1392	26800
9				x	0.625		9	2	20	1435 x 1480	27000
				x	0.607		4	20		1526 x 1573	27200
	20	1478 x 1530			0.588	19.7%	20			1622 x 1696	27400
6	1	20	1383 x 1433		0.569	19.7%	20	7	7	1725 x 1799	27600
6	6	20	1293 x 1340		0.549	19.5%	20			x	27800
9		20	1207 x 1252		0.528	19.5%	20			x	28000
7		20	1126 x 1169		0.508	19.5%	20			x	28200
8		20	1051 x 1092		0.488	19.4%	20			x	28400
6		20	979 x 1009		0.467	19.2%	20			x	28600
15		20	911 x 950		0.448	19.4%	20			x	28800
8		7	839 x 908		0.428	19.5%	35			x	29000

Strategy Builder

ACTN	RT	LST TRD DAY	STRIKE	TYPE	DELTA	THETA	BID/ASK	SIZE	PAYOFF
× Leg 1	Sell	1 SEP 29 '21	29800	Call	0.354	-3.879	622 x 683	7x7	
× Leg 2	Buy	1 SEP 29 '21	27600	Put	-0.431	-4.148	1725 x 1799	7x7	
× Leg 3	Sell	1 SEP 29 '21	26000	Put	-0.288	-3.859	1045 x 1084	20x20	
Total					-0.498	3.591	-42 x 132	7x7	

Clear All Legs + PROFILE + Add to Watchlists

Order Entry LMT QTY 1 LMT ... 0.00 DAY advanced Margin Impact: 26,995 HKD Submit Order

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Using Fundamentals To Decide On Strike / Expiry




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Things to consider when buying vs selling options

- Option buyers expect a large move (more important than direction), option sellers expect moves to be relatively small or range bound
- “Time decay” mean long option positions lose value (and short option positions gain value) every day the asset doesn’t move
- Is your trade part of a long-term strategy, or something more timely and tactical?

Many options markets on IBKR

COUNTRY/REGION	MARKET CENTER DETAILS
 United States	Bats EDGX Options Exchange
	Bats Global Markets (BATS)
	Boston Options Exchange (BOX)
	CBOE C2 (CBOE2)
	Chicago Board Options Exchange (CBOE)
	GEMINI
	ISE Mercury
	ISE Options Exchange (ISE)
	MIAX EMERALD
	MIAX Options Exchange
	MIAX PEARL
	NASDAQ OMX (NASDAQOM)
	NASDAQ OMX BX Options Exchange
	NYSE American (AMEX)
NYSE Arca (PSE)	
Philadelphia Stock Exchange (PHLX)	
 Canada	Montreal Exchange (CDE)
 Mexico	Mexican Derivatives Exchange (MEXDER)

COUNTRY/REGION	MARKET CENTER DETAILS
 Belgium	Euronext Brussels (BELFOX)
 France	Euronext France (MONEP)
 Germany	EUREX (DTB)
 Italy	Borsa Italiana (IDEM)
 Netherlands	Euronext NL Derivatives (FTA)
 Spain	Spanish Futures & Options Exchange (MEFF)
 Sweden	Nasdaq OMX - Stockholm (OMS)
 Switzerland	EUREX (SOFFEX)
 United Kingdom	Intercontinental Exchange (ICEEU)

COUNTRY/REGION	MARKET CENTER DETAILS
 Australia	Australian Stock Exchange (ASX)
 Hong Kong	Hong Kong Futures Exchange (HKFE)
	Hong Kong Stock Exchange (SEHK)
 India	National Stock Exchange of India (NSE)
 Japan	Osaka Exchange (OSE.JPN)
 Singapore	Singapore Exchange (SGX)
 South Korea	Korea Stock Exchange (KSE)

Source: Interactive Brokers

There are of course a LOT more to options strategies, but hopefully provides a solid “101” starter or refresher



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Questions?



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Cross-Index Spreads

- Can offer far more precise risk/reward spread trades than outright futures or ETFs
- Nearly limitless combinations
- Easier between “less different” options (e.g. FX, hours, index vs physical).

Risks

- Being wrong
- Pushing margin limits
- HKD vs USD basis
- Futures liquidity may take time to develop (which is why I’m not yet sampling a momentum strategy)