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IUR Capital

Option Strategies for Market Corrections

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Option Strategies for Market Corrections



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Options are leveraged products that involve risk and are not suitable for all investors. Before committing capital to any option strategies, read the “Characteristics & Risks of Standardized Options” provided by the Options Industry Council. For a copy call 312-542-6901.

A copy is also available at: <http://www.optionsclearing.com/publications/risks/riskstoc.pdf>

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Host Profile (Gareth Ryan)

- Founded IUR Capital Ltd in 2007, IUR Capital LLC in 2010
- IUR Capital is an investment advisor for institutional and retail investors
- Focused in exchange-traded option strategies

“Bear markets are the true test of every investor.”

(Me. Just now.)

How has your 2022 been so far?

- Nasdaq re-enters bear market in late April, worst month since 2008
- S&P 500 re-enters correction also in late April
- Volatility impacting risk assets the most since March 2020
- Treasury markets pricing in 150-200 bps in rate hikes in 2022
- Commodities remain in a “super-cycle” / Inflation at 40-year high
- US equity markets in a state of near-term “flux”
- Fed rate decision this week is a cross-asset market-moving event

(As of April 27, 2022)

Catalysts for the current market correction?



CBOE VIX.... If you haven't noticed, it's volatile out there

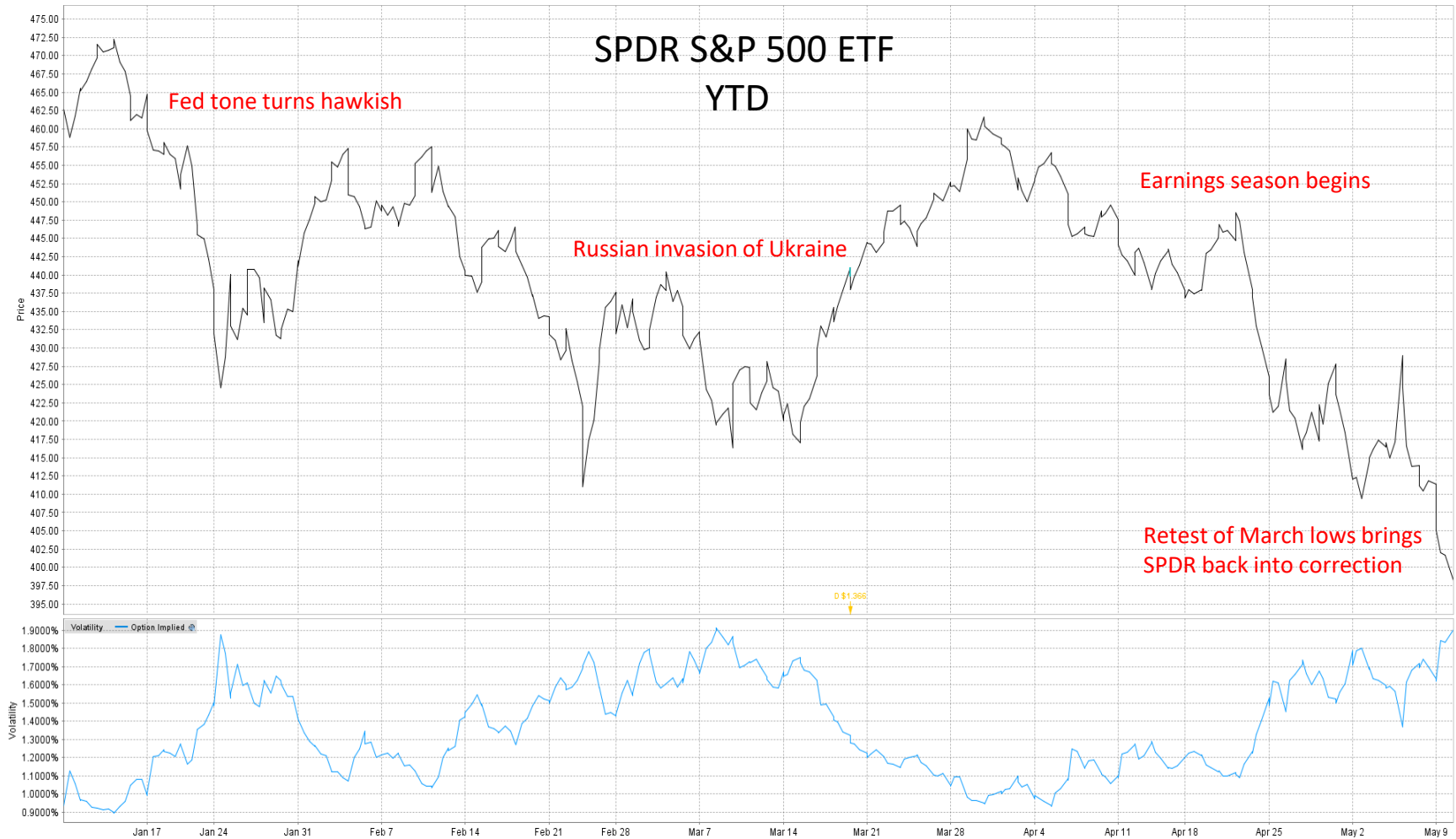
CBOE VIX YTD



Source: IBKR TWS (May 9,2022)

SPDR S&P 500 ETF....

1-2% daily moves are more common



Source: IBKR TWS (May 10, 2022)

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QQQ Powershares.... Steep declines into bear market

QQQ YTD

20% peak to trough in less than 4 months

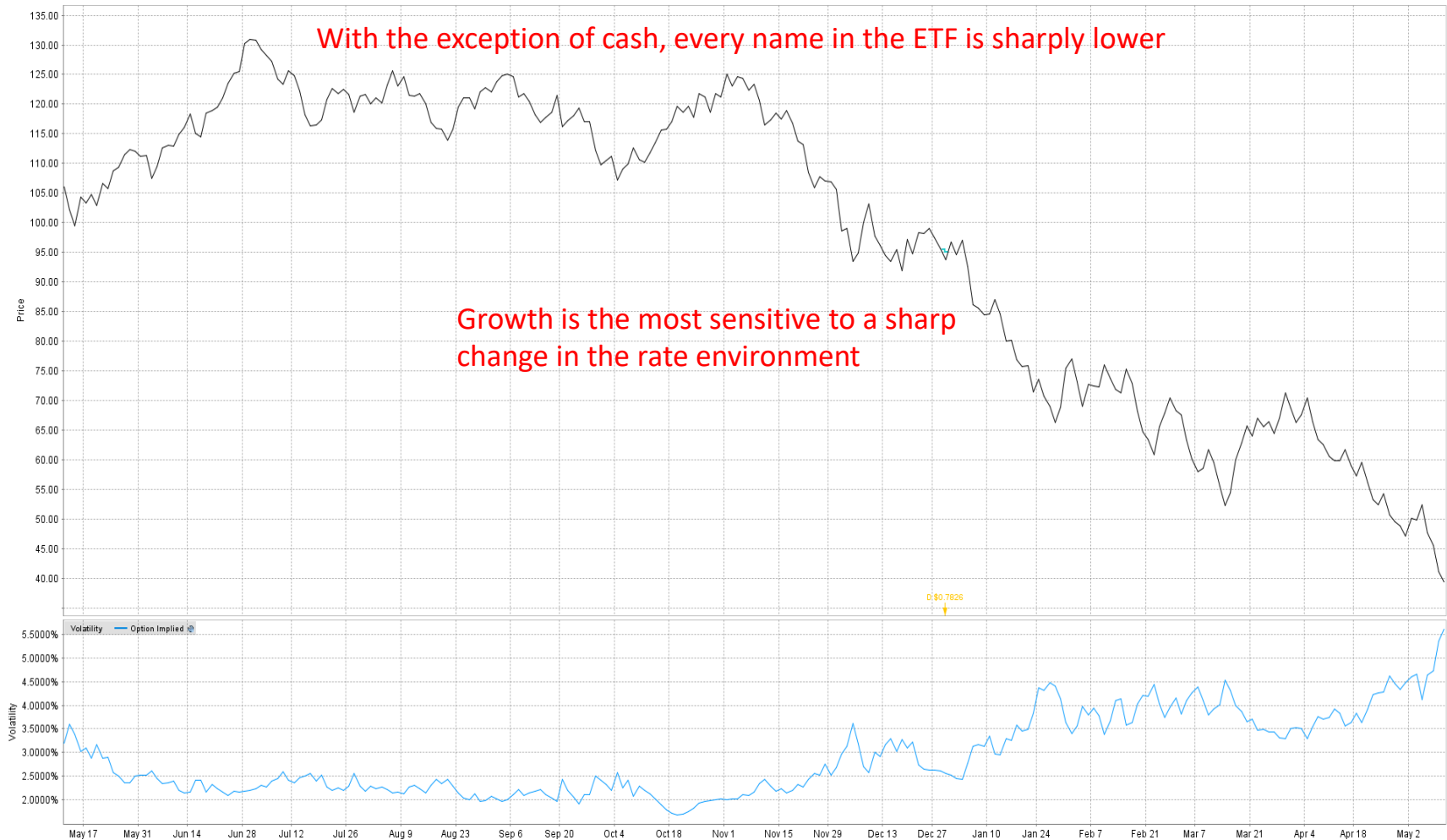
Lower lows for QQQ again
indicates further weakness



Source: IBKR TWS (May 9, 2022)

ARKK Funds ETF (12 Month)

A painful lesson for retail speculation..



Source: IBKR TWS (May 9, 2022)

Should we be a BUYER or SELLER of volatility at current levels?

Answers please in the Q&A Panel

Buying Puts =
Buying Volatility

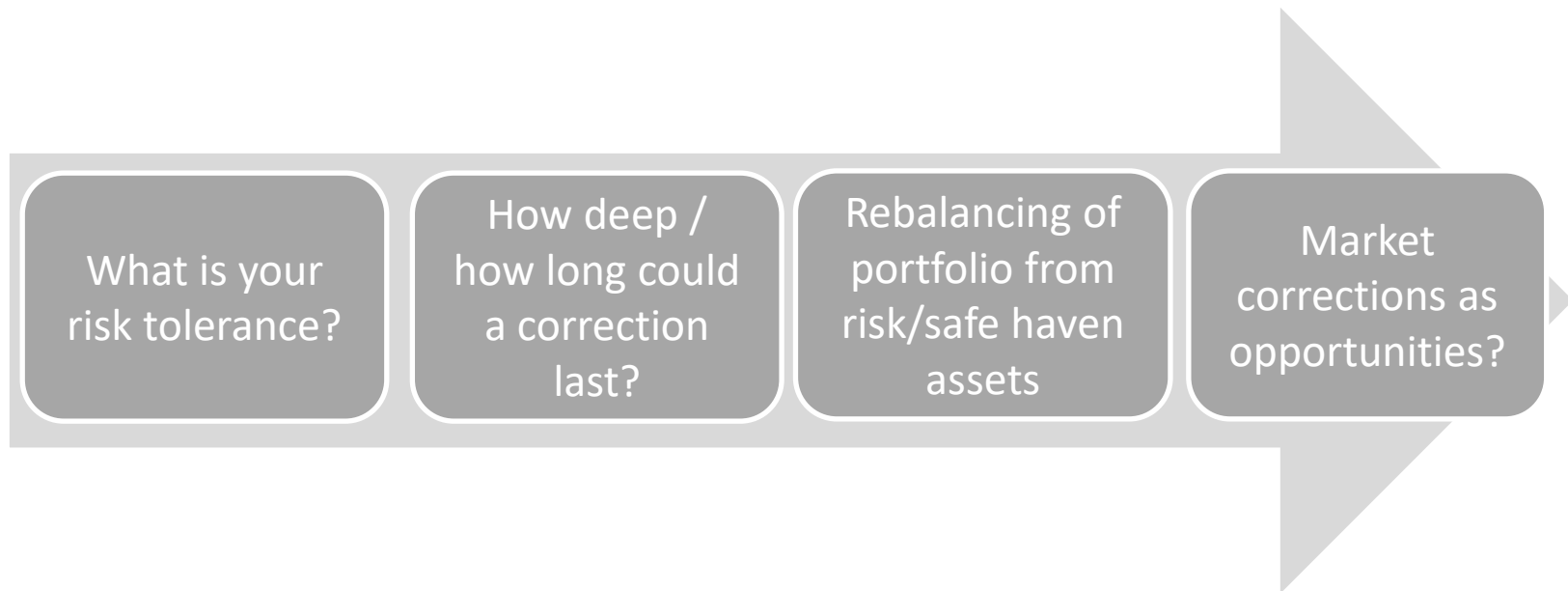
Selling Puts =
Selling Volatility

Questions to ask about option strategies during market corrections:

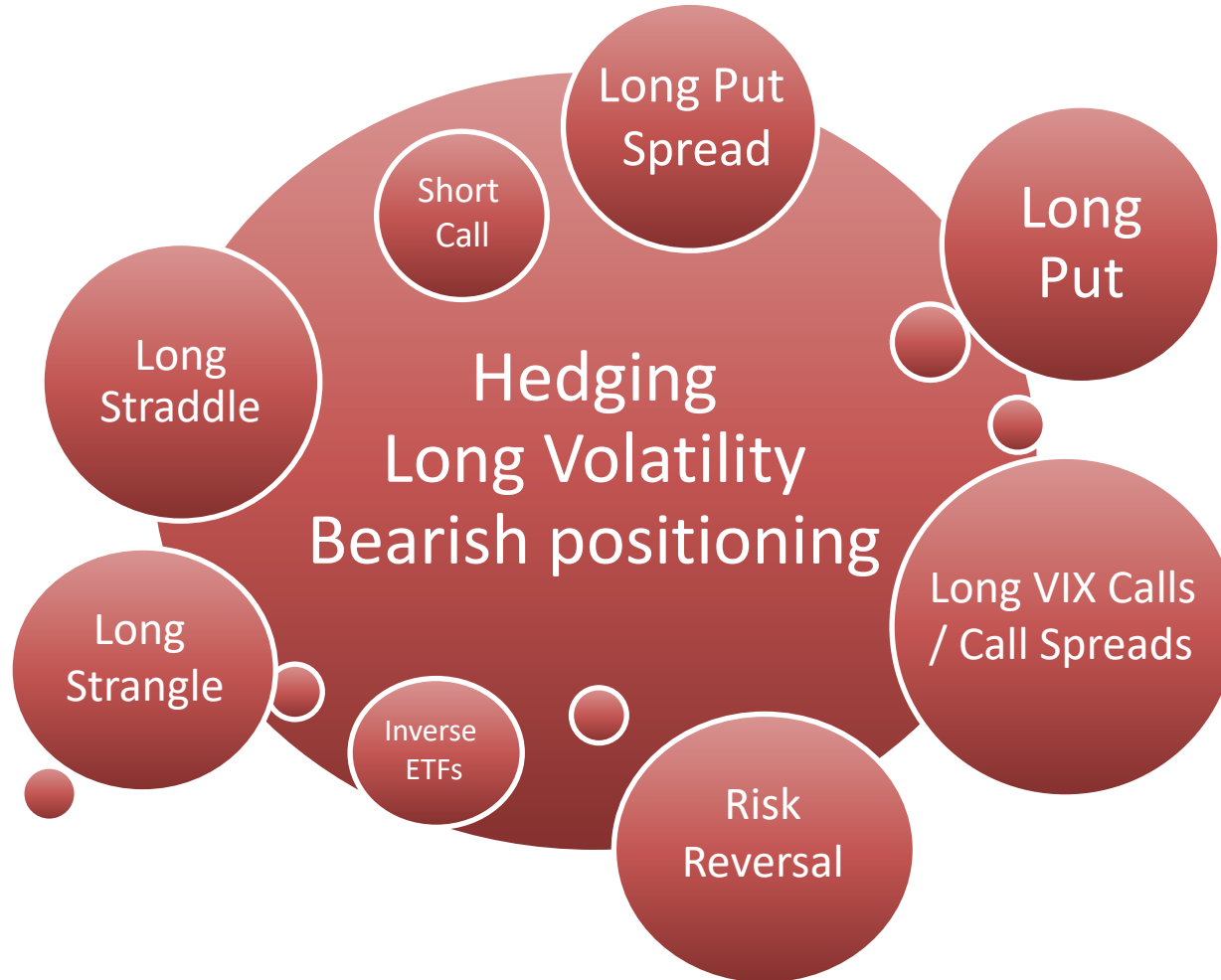
- What are the objectives for an equity/fixed income portfolio?
- How can option strategies achieve a “*net benefit*”?
- If seeking income with options, what risk/return profile is appropriate?
- If taking directional positioning with options, what strategies can we use?
- For hedging an equity position with options, how can we justify costs?
- Do we have sufficient knowledge of the various strategies available?

Options involve risk and are not suitable for all investors. Multiple leg strategies, including spreads, will incur multiple transaction costs

What should be my approach during an equity market correction?



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Risk/Return Profile must be understood for each strategy

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Puts – a quick review of the basics...

To be successful in buying put options, we need to be right about three things:

*The more bearish you are, the more willing you may be to purchase options that are far out-of-the-money. That means there might have to be a substantial decrease in the price of the underlying stock for you to break even or realise gain.

The potential for a stock to fall

The amount that the stock will fall

The time will take to happen

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Why use Puts as Insurance....

- Hedging a long equity portfolio
- Protection before a key event, which may significantly move your underlying
- If your underlying does have a near-term sell-off, puts will gain to mitigate unrealized loss on the equity portfolio
- How much protection are you seeking to hold? 50% of your portfolio

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Am I long vol or short vol?

Strategy	Vega	Rise in IV	Fall in IV
Long Call	Positive/Long	Gain	Loss
Short Call	Negative/Short	Loss	Gain
Long Put	Positive/Long	Gain	Loss
Short Put	Negative/Short	Loss	Gain

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Am I long vol or short vol? (Spreads)

Strategy	Vega	Rise in IV	Fall in IV
Long Strangle	Positive / Long	Gain	Loss
Long Straddle	Positive / Long	Gain	Loss
Credit Spread	Negative / Short	Loss	Gain
Debit Spread	Positive / Long	Gain	Loss
Butterfly Spread	Negative / Short	Loss	Gain
Calendar Spread	Positive / Long	Loss	Gain

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Potential Volatility Strategies

- Why the straddle or strangle?
- Speculating volatility of the stock
- Straddle BUYERS expect higher volatility
- Straddle SELLERS expect lower volatility
- Stranglers expect a similar movement, BUT with a different risk/return scenario

Options involve risk and are not suitable for all investors. Multiple leg strategies, including spreads, will incur multiple transaction costs

The Long Straddle

- Purchase of one call
- Purchase of one put
- Same strike price, underlying and expiry date.
- Risk Profile
- Maximum Risk – Net Debit
- Maximum Reward – Unlimited
- Downside Breakeven – Strike less net debit
- Upside Breakeven – Strike plus net debit

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The Long Straddle Example

- With XYZ stock trading at \$50.00
- Buy 1 XYZ 50 Call at \$3.20
- Buy 1 XYZ 50 Put at \$3.00
- Net Cost $\$6.20 * 100 = \620.00
- The “50 straddle” is purchased for a total cost of \$620 plus commissions.

Long Straddle P&L

Stock price	50 Call Profit/Loss	50 Put Profit/Loss	Net Profit/Loss
\$60.00	\$680	(\$300)	\$380
\$55.00	\$180	(\$300)	(\$120)
\$50.00	(\$320)	(\$300)	(\$620)
\$45.00	(\$320)	\$200	(\$120)
\$40.00	(\$320)	\$700	\$380

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Long Straddle P&L

	50 Call Profit/Loss	50 Put Profit/Loss	Net Profit/Loss
Stock Price	\$50.00	\$60.00	20%
Days to Expiration	60	32	
50 Call	\$320	\$1020	220%
50 Put	<u>\$300</u>	<u>\$15</u>	(95%)
50 Straddle	\$620	\$1035	67%

Options involve risk and are not suitable for all investors. Multiple leg strategies, including spreads, will incur multiple transaction costs

The Long Strangle Example

- XYZ stock trading at \$50.00
- Buy 1 XYZ 55 Call at \$1.40
- Buy 1 XYZ 45 Put for \$1.05
- Net Cost \$2.45
- The “45-55 Strangle” is purchased for a total of \$245 plus commissions.

Long Strangle P&L

Stock price	55 Call Profit/Loss	45 Put Profit/Loss	Net Profit/Loss
\$60.00	\$360	(\$105)	\$255
\$55.00	(\$140)	(\$105)	(\$245)
\$50.00	(\$140)	(\$105)	(\$245)
\$45.00	(\$140)	(\$105)	(\$245)
\$40.00	(\$140)	\$395	\$255

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Straddles vs Strangles

- Strangle – Maximum loss possible over wider range than straddle
- Straddle – Maximum loss only if stock = strike price at expiry
- Combination (strangle) – Maximum loss anywhere between two strikes at expiry

Use of index/index ETF products as underlying vehicles

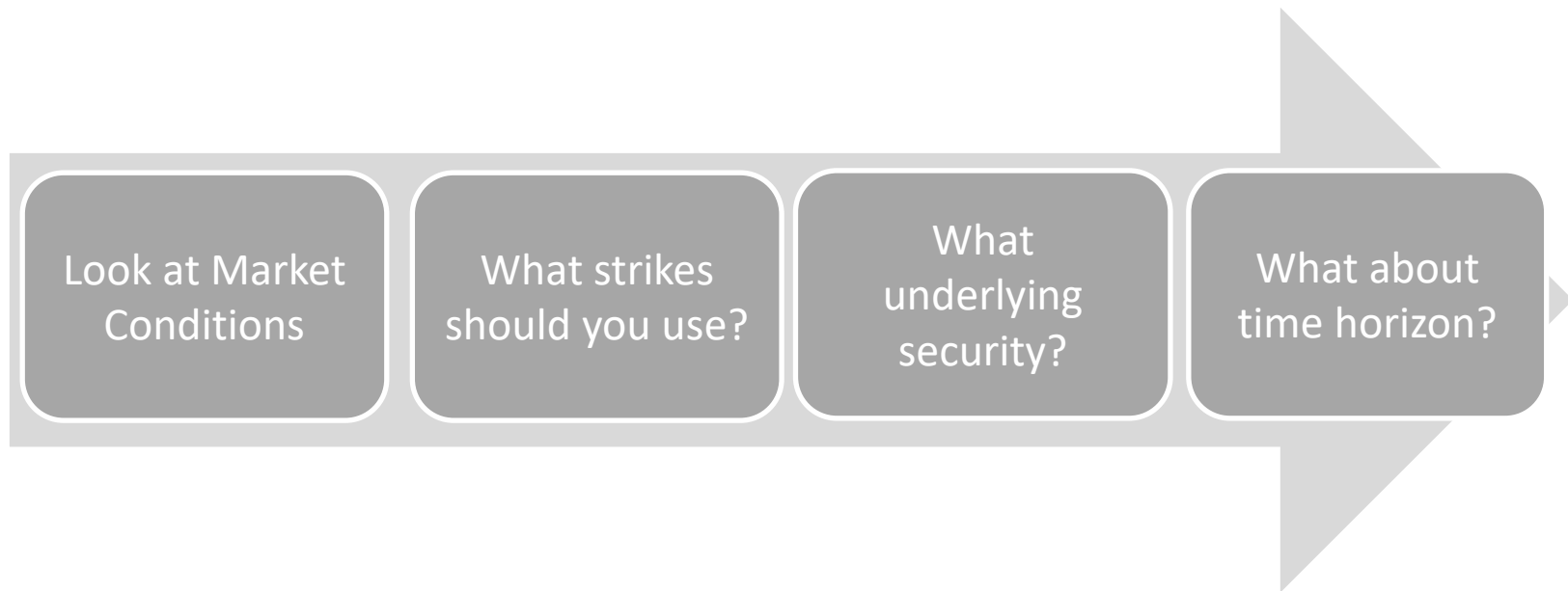
Ticker	Instrument	Style	Settlement
SPY	SPDR S&P 500 ETF	American	Physical
SPX	S&P 500 Index	European	Cash
IWM	Russell 2000 Index ETF	American	Physical
RUT	Russell 2000 Index	European	Cash

*Note that SPY / IWM ETF products have quarterly dividends.

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Making option-based strategies work in a portfolio.....



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Let's talk...

Email me gryan@iurcapital.com to request the slides or just to have a chat....