1 The Options Industry Council

Options involve risks and are not suitable for everyone. Individuals should not enter into options transactions until they have read and understood the risk disclosure document, *Characteristics and Risks of Standardized Options*, available by visiting OptionsEducation.org. To obtain a copy, contact your broker or The Options Industry Council at One North Wacker Drive, Chicago, IL 60606. Individuals should not enter into options transactions until they have read and understood this document.

In order to simplify the computations used in the examples in these materials, **commissions, fees, margin interest and taxes have not been included.** These costs will impact the outcome of any stock and options transactions and must be considered prior to entering into any transactions. Investors should consult their tax advisor about any potential tax consequences.

Any strategies discussed, including examples using actual securities and price data, are strictly for illustrative and educational purposes and should not be construed as an endorsement, recommendation, or solicitation to buy or sell securities. Past performance is not a guarantee of future results.

2 The Options Industry Council

3rd Party Presenter Disclaimer Slide

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For the sake of simplicity, **the examples about to be presented do not take into consideration commissions and other transaction fees, tax considerations, or margin requirements**. These are factors that may significantly affect the economic consequences of a given strategy, and they should be considered before making actual investments.

Any strategies discussed, including examples using actual securities and price data, are strictly for illustrative and educational purposes only and are not to be construed as an endorsement, recommendation, or solicitation to buy or sell securities. Past performance is not a guarantee of future results.

The strategy suggestions presented during this discussion are the ideas of the presenter and not those of The Options Industry Council or OCC. Also, OIC makes no recommendation with respect to any financial education firm. OIC does not control, nor has it developed or reviewed the relevant content, and does not make any warranty, express or implied, as to the accuracy, usefulness, timeliness or even the continued availability or existence of information created or maintained by others. Opinions expressed by others are not necessarily those of OIC, nor does OIC endorse, warrant, or guarantee products, services or information described or offered by such firms.

3 Who We Are

About OIC

The Options Industry Council (OIC) is an industry resource funded by OCC, the world's largest equity derivatives clearing organization and sole central clearinghouse for U.S. listed options, and the U.S. options exchanges. OIC's mission is to provide free and unbiased education to investors and financial advisors about the benefits and risks of exchange-traded equity options. Managed by OCC, OIC delivers its education through the Options Education Program, a structured platform offering live seminars, self-directed online courses, mobile tools, podcasts, webinars and live help. OIC's resources can be accessed online at www.OptionsEducation.org or via mobile app for iOS.

About OCC

OCC is the world's largest equity derivatives clearing organization and the foundation for secure markets. Founded in 1973, OCC operates under the jurisdiction of both the U.S. Securities and Exchange Commission (SEC) as a Registered Clearing Agency and the U.S. Commodity Futures Trading Commission (CFTC) as a Derivatives Clearing Organization. OCC now provides central counterparty (CCP) clearing and settlement services to 19 exchanges and trading platforms for options, financial futures, security futures and securities lending transactions. More information about OCC is available at www.theocc.com.

4 U.S. Listed Options Exchanges

Cboe

BOX OPTIONS EXCHANGE

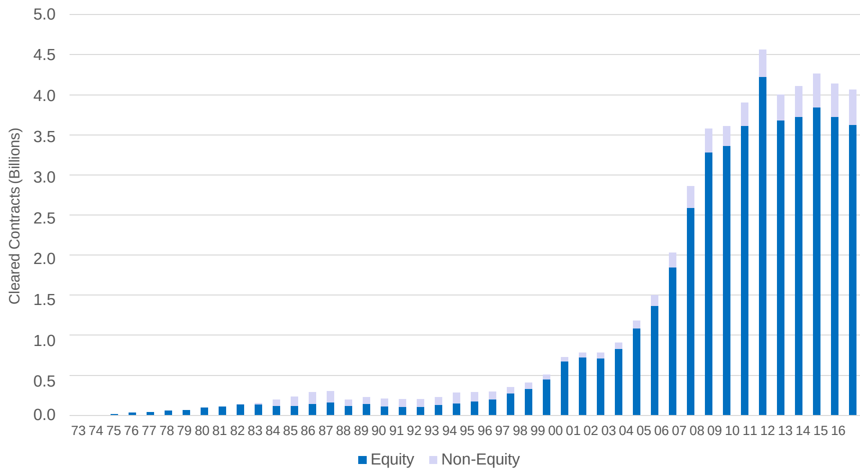
MIAX Options

Nasdaq

NYSE

5 Annual Options Volume 1973-2016

OCC Annual Contract Volume by Contract Type



6 Presentation Overview

- Why Options?
- Covered Calls
- Buying Puts
- Collars
- Summary

Why Options?

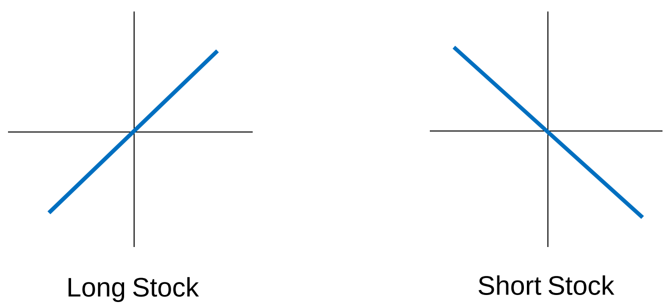
8

Why Options?

- Options give you more ways to implement your market research
- Options make it possible to target a variety of investment objectives:
  - ***Risk Reduction***
  - ***Income Generation***
  - ***Stock Acquisition***
- Options offer **FLEXIBILITY!**

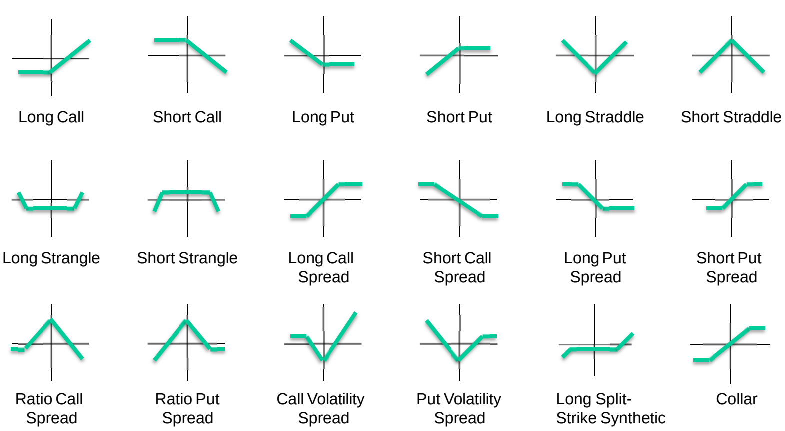
9 Long Stock vs. Short Stock

In a world without options, stock investors have limited choices.



10 Flexibility

With options, these are some of the available choices.

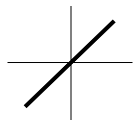


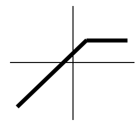
Covered Call

12 Covered Call Definition

- Covered call: investor simultaneously
  - Writes (sells) one or more equity call contracts
  - Buys equivalent number of underlying shares
  - One short call for each 100 long shares
  - "Covered write" or "buy-write"
- If stock already owned when call is written
  - "Overwrite"

13 Covered Call Writer's Risk?


Long Stock


Covered Call

- Where's the risk with a covered call?
  - Risk is in the long stock
- Upside stock profit potential is limited
  - Assignment → stock sold at strike price
  - Short call loss reduces long stock profit

14 Why Write Covered Calls?

- Primary goal – increase returns
  - Call premium received and kept (assigned or not)
  - Generate additional income (over any dividends)
- Investor's forecast
  - Neutral to bullish on the underlying stock
  - Within a small price range over strategy's lifetime
- Call premium's limited downside benefits
  - Lowers stock's break-even point (BEP)
  - Reduces cost basis for long stock by call premium amount

15 Covered Call Writer's Obligations?

- Like any call writer (short call position)
  - Has the obligation to sell underlying shares
  - At strike price
  - If assigned
- Assignment (your potential obligation)
  - Possible at any time before expiration
  - Equity options are American-style
- In return for this obligation
  - Call writer receives and keeps option premium

16 Covered Call: Profit and Loss at Expiration

- Upside <u>profit</u> potential is <u>limited</u>
  - Strike price – stock price paid + call premium received
  - If assigned stock sold at strike price
- Break-even point
  - Stock price paid – call premium received
- Downside <u>loss</u> potential is <u>substantial</u>
  - Downside risk is with stock
  - Option in this case offers only limited protection
  - Entire stock cost less call premium received is the risk

17 Covered Call Example

You own 100 XYZ shares trading at $42.00

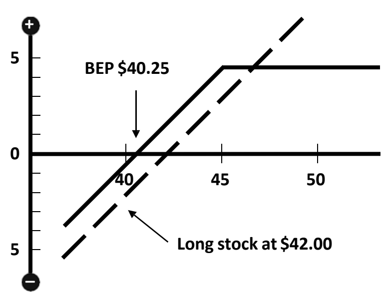
- Neutral to moderately bullish over next few months
- Want to generate income in a stable market
- You have target sale price for stock

Sell 1 90-day XYZ 45 call at $1.75

- Total premium received = $175.00

18 Covered Call Example

Own 100 shares XYZ at $42.00
Sell 1 XYZ 45 call at $1.75



Break-even at Expiration:
Stock Price Paid –
Call Premium Received
$42.00 – $1.75 = $40.25

Maximum Profit if Assigned:
Effective Stock Sale Price –
Stock Price Paid
($45.00 + $1.75) – $42.00 = $4.75
$475.00 Total

Puts

20 Why Buy Puts?

- You are bearish on a particular stock
  AND
- You are looking to benefit from falling prices with
  - A small cash outlay AND
  - A limited, pre-defined risk

21 Buying Puts

The put buyer:

- Has the right to sell stock
- At an agreed upon price (the strike price)
- Until the expiration date
- For this right the put buyer pays a premium

22 Put Buying Example

- Stock XYZ:
  - Is trading at $36.00
- View
  - You are bearish on the stock
  - You want to limit risk
- Action
  - You buy a 3-month, 35 strike put for $2.25 per share ($225 per option)

23 Example

Buy 35 strike put at $2.25

Break-even at expiration:

Strike Price – Option Premium

$35.00 – $2.25 = $32.75

24 Example

Buy 35 strike put at $2.25

Stock Price at Expiration	Long 35 Put Value at Expiration	Long 35 Put Initial Cost	Total Profit/(Loss)
$40.00	0	($2.25)	($2.25)
$35.00	0	($2.25)	($2.25)
$32.75	$2.25	($2.25)	0
$30.00	$5.00	($2.25)	$2.75
$25.00	$10.00	($2.25)	$7.75

Collar

26 Why Use a Collar?

- Stock, ETF or Index buyer with unrealized gains wants
  - downside protection – long put
  - some upside participation – limited by short call
- Key benefits
  - put cost fully or partially paid by call premium received
  - objectives met whether share price up or down
  - receive any dividend if not assigned on short call

27 Before You Use a Collar

- Downside protection needed?
  - select appropriate put strike price
  - consider time frame
- Upside participation on the underlying?
  - select appropriate call strike price
  - be happy with share sale price if assigned
- Balance two factors:
  - put premium paid and protection provided – risk
  - call premium received and upside potential – reward

28 Collar: Two Strategies in One

- The 100 shares of stock play a part in both
- On the downside you have a protective put
  - OTM put purchased
  - Grants right to sell shares at put’s strike until expiration
  - OTM call will expire worthless
- On the upside you have a covered call
  - OTM call sold
  - Upside profit limited by call’s strike price if assigned
  - OTM put will expire worthless

29 Motivations

- Stock investor has unrealized profits
  - Wants downside protection for all or part
  - Cost of put more than willing to pay for insurance
- Investor feels some upside profit potential remains
  - Sells OTM call
  - Offsets all or part of put cost with premium received
- Investor accepts tradeoff
  - Limited upside worth downside protection desired

30 Investor's Choices Before Expiration

- Avoid assignment
  - Close short call → left with protective put
- No longer feels protection necessary
  - Sell put → left with covered call
- Beware of exercising put without closing call
- Roll position
  - Out and down
  - Out and up

Summary

32

Long Calls vs. Short Calls

Long calls	Short calls
Owns the right to buy the stock	Has obligation to potentially sell the stock
Can buy stock if holder chooses to exercise	Must sell stock if seller is assigned (result of holder exercise)
Profits if stock rises, loses if stock falls	Profits if stock falls, loses if stock rises
Can lose value as time passes (potentially leading to losses)	Can lose value as time passes (potentially leading to profits)

33 Long Puts vs. Short Puts

Long puts	Short puts
Owns the right to sell the stock	Has obligation to potentially buy the stock
Can sell stock if holder chooses to exercise	Must buy stock if seller is assigned (result of buyer exercise of the put)
Profits if stock falls, loses if stock rises	Profits if stock rises, loses if stock falls
Can lose value as time passes (potentially leading to losses)	Can lose value as time passes (potentially leading to profits)

34 Many Uses for Options

- Risk management
- Generating income
- Leverage
- Improving the risk-reward of investments
- Portfolio diversification

35 The Options Education Program

Whether you're an options novice or just deployed an iron condor, the Options Education Program has you covered.

- Take the MyPath assessment so you can learn at your own pace online and customize your own curriculum for your skill level.
- Download our podcasts and videos and learn options on your own time.
- Attend seminars and webinars and hear first hand about options strategies.
- Get all your options-related questions answered by our leading professionals at Investor Services.

36 How Financial Advisors Use and Think About Exchange-Listed Options

- Download the entire 15-page Cerulli Associates research study at www.optionseducation.org

37 IWI Course

INVESTMENTS & WEALTH INSTITUTE™ formerly IMCA | In Partnership With OIC The Options Industry Council

Fundamentals of Exchange-listed Options Course

Results of a quantitative study conducted by the Options Industry Council (OIC) showed that advisors have low confidence levels about using options. The OIC and Investments & Wealth Institute, formerly IMCA, have partnered on the new **Fundamentals of Exchange-listed Options** online course to help advisors overcome confidence hurdles when using options.

The course is designed to provide advisors with essential, foundational options knowledge and skills, as well as practical strategies that can be put to work immediately. Using easy-to-understand examples and demonstrations and ongoing high-level support from the OIC and Institute, the course dives into options markets; risk, reward, and probability; option behavior; option spreads; volatility trading; and portfolio management using options.

Add value to your business and clients' portfolios by boosting your options IQ.

Learn more about this exciting new course at www.investmentsandwealth.org/FELO

38 For More Information

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