BUBBA AND BADGER'S OPTION TRADES AND METHOD TO EXECUTE

We offer a number of trades on our option show using weekly options as our focus. This pamphlet breaks down the trades and how they are executed. The trades in Blue designate a credit, Red designate a debit spread. Earnings trades are considered to be neutral and will be in Green.

DIRECTIONAL TRADES

OUTRIGHT BUY OF A PUT OR CALL

Buying an outright Call or Put offers the best chance to cash a **big** trade, but it still has a number of problems. First you must overcome the premium you pay for the option. Second in low volatility environments you can be right on the direction of the trade but still lose money. Suggest these trades in high volatility environments.

EXAMPLE OF HOW TO EXECUTE

Select a Call or Put that is **AT THE MONEY** (.50) delta or no more than +/- one strike. "Buy to open" (limited risk unlimited reward) the selected option. When you get a profit target or reversal signal "Sell to close". Your profit or loss is the difference between the price you paid for the option and where you sold it. The amount of change in the underlying stock has no effect on the trade, only the price differential in the option. **NEVER SELL NAKED OPTIONS** (unlimited risk limited reward) "Sell to open".

SELL A CREDIT SPREAD (VERTICAL BULL AND BEAR SPREADS)

The credit spreads also known as vertical spreads can help you to make more money in any type of market. The credit spread combines the power of time decay with the ability to withstand some adverse price movement and still make money.

The reward in the spread is the amount of "credit" you receive when you sell the option nearest to the money and buy the one that is further away. The risk is the difference between the credit you receive and the spread between the two strikes.

EXAMPLE: Sell the STOCK SYMBOL 90-95 call spread for a credit of 2.20

You would sell the **STOCK SYMBOL 90 call** and buy the **STOCK SYMBOL 95call**, and you would receive a credit of 2.20 ($220 a contract). It doesn't matter what the prices of the sale and buy are as long as they have a difference of 2.20 in the premium. If you sell the 90 call @ 2.80 you would buy the 95 call @.60. If you sell the 90 call @ 4.40 you would buy the 95 call @ 2.20 the difference is 2.20 in both cases.

The risk in the spread is limited to the "credit" minus the difference between the strikes. So in our example of the **STOCK SYMBOL** 90-95 call spread we subtract the credit of 2.20 from the difference between the strikes of 5.00 and we have a risk of 2.80 (5.00 -2.20= 2.80). In order for the trade to be cashed the price at expiration must be 92.20 or less.

Selling the credit put vertical is just the mirror image of the call spread.

EXAMPLE: Sell the STOCK SYMBOL 90-85 put spread for a credit of 2.20

You would sell the **STOCK SYMBOL 90 put** and buy the **STOCK SYMBOL 85 put**, and you would receive a credit of 2.20 ($220 a contract). It doesn't matter what the prices of the sale and buy are as long as they have a difference of 2.20 in the premium. If you sell the 90 call @ 2.80 you would buy the 95 call @.60. If you sell the 90 call @ 4.40 you would buy the 95 call @ 2.20 the difference is 2.20 in both cases.

The risk in the spread is limited to the "credit" minus the difference between the strikes. So in our example of the **STOCK SYMBOL 90-85 put** spread we subtract the credit of 2.20 from the difference between the strikes of 5.00 and we have a risk of 2.80 (5.00 -2.20= 2.80). In order for the trade to be cashed the price at expiration must be 87.80 or greater.

SELLING A 60 40 CREDIT SPREAD (VERTICAL SPREAD)

This is a more aggressive directional credit spread. You sell the option that has a .60 delta and buy one that has .40 delta. This trade has a bigger risk as if it goes slightly against you it will lose more money. Offsetting the risk is that it also has more reward when it goes in your favor.

You get two chances to cash this spread. If the trade goes in the price direction as expected or it moves against you less than the premium that you have received.

This type of trade will work in any market condition. It is particularly attractive using weekly options because you have the opportunity to do it each week, which means that theoretically you can cash the trade 52 times a year.

ONE BY TWO FOR EVEN (BACKSPREAD)

This is a directional spread that allows you unlimited reward with limited risk. You buy two options of the same serial and sell one closer to the money. The risk is limited to the spread between the two options you buy and the one you sell.

EXAMPLE: Sell the STOCK SYMBOL 90-85 put one x two spread for even.

The first step is to sell the 90-85 put credit spread. Once you have established the credit buy the other put. In some cases this can be done for an outright credit. As an example if you sell the 90 put @ 1.60 and buy the 85 put @ .75 you would have a credit of .85 the cost of the other put would be .75 giving you the 1x2 for a .10

credit. In other cases you may have to pay a slight debit. In any case the spread is limited to the risk of the price between the two strikes. The reward is unlimited The reward is unlimited you would keep the spread in place until you get a reversal signal or a closing signal. You buy back the credit spread and sell the extra put.

EXAMPLE: Sell the STOCK SYMBOL 80-85 call one x two spread for even.

The call spread is a mirror image of the put spread. The first step is to sell the 80-85 call credit spread. Once you have established the credit buy the other call. In some cases this can be done for an outright credit. As an example if you sell the 80 call @ 1.60 and buy the 85call @ .75 you would have a credit of .85 the cost of the other call would be .75 giving you the 1x2 for a .10 credit. In other cases you may have to pay a slight debit. In any case the spread is limited to the risk of the price between the two strikes. The reward is unlimited you would keep the spread in place until you get a reversal signal or a closing signal. You buy back the credit spread and sell the extra call.

OFFSTRIKE HORIZONTAL SPREAD (FREE ROLL)

EXAMPLE: Buy the STOCK SYMBOL 80-95 horizontal call spread

Buy the deferred (anchor) 80 call and sell the weekly 95 call for a debit. The object of this spread is to take advantage of the time decay in the weekly option to finance the premium in the deferred call. You can cash this trade two ways. The market moves in your favor and the 95 call goes out worthless or at a large debit to the 80 anchor call, or you continue to roll back the 95 call until you have paid for the 80 call and you get a “free roll” on the 80 call which you own for zero premium.

EXAMPLE: Buy the STOCK SYMBOL 95-80 horizontal put spread

This is the mirror image of the call spread. Buy the deferred (anchor) 95 put and sell the weekly 80 put for a debit. The object of this spread is to take advantage of the time decay in the weekly option to finance the premium in the deferred call. You can cash this trade two ways. The market moves in your favor and the 80 put goes out worthless or at a large debit to the 95 anchor put , or you continue to roll back the 80 put until you have paid for the 95 put and you get a “free roll” on the 95 put which you own for zero premium.

EARNINGS TRADES (NEUTRAL)

STRADDLE VERSUS STRADDLE

This trade is used during earnings season to try and capture the extra premium (risk of price movement) in the front straddle. The trade is executed by buying a deferred straddle (anchor) and selling a straddle in the expiring weekly option. The trade will always be a debit trade. Depending on how far the anchor is from the front it will allow for the ability to “roll back” the premium for more than one period.

EXAMPLE: Buy the STOCK SYMBOL 80-80 weekly 45 day straddle spread

The trade can be executed in two ways. Buy the deferred 80 straddle and sell the weekly straddle as a spread. When the trade is executed in this manner all four legs are executed simultaneously. Buy the deferred 80/ weekly call spread, and then buy the deferred 80/ weekly put spread.

STRANGLE VERSUS STRADDLE OR STRADDLE VERSUS STRANGLE

EXAMPLE: Buy the STOCK SYMBOL 80-straddle sell weekly 75-85 strangle

The trade can be executed in several ways. Buy the deferred 80 straddle and sell the weekly 75/85 strangle. Buy the deferred 75 weekly 80 put spread. Buy the deferred 85 weekly 80 call spread. In some cases this may not be a debit spread depending on premium levels, if it is done as a credit all the better.

EXAMPLE: Buy the STOCK SYMBOL 75-85 strangle sell weekly 80 straddle

The trade can be executed in several ways. Buy the deferred 75-85 strangle and sell the weekly 80 straddle. Buy the deferred 75 weekly 80 put spread. Buy the deferred 85 weekly 80 call spread. In some cases this may not be a debit spread depending on premium levels, if it is done as a credit all the better.

INSIDE OUTSIDE SPREAD

EXAMPLE: Buy STOCK SYMBOL 55-85 strangle sell weekly 60-80 strangle

This trade is initiated using options that are outside the expected range (EV) of the weekly straddle. It can be initiated in several ways. Buy the deferred 55 85 put spread, sell the deferred 85 80 call spread. Buy the horizontal 55 60 put spread, buy the horizontal 85 80 call spread. In some cases the trade can be done for a credit, all the better. The trade can be managed by buying it back or allowing the inside strangle to go out worthless and roll the strangle back until you own the strangle for free.

Sticking with these simple trades will give you the power to consistently cash trades in any market conditions.