

MONTREAL EXCHANGE

**Options
Strategies
Quick Guide**

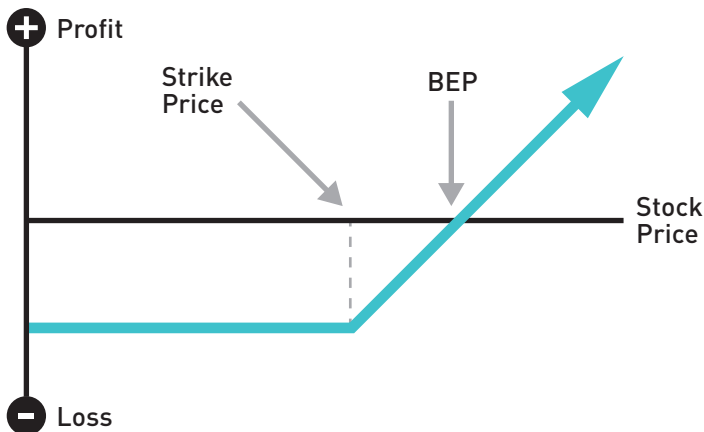


TABLE OF CONTENTS

How to use this book	4
Terms and definitions	5
Bullish Strategy	7
Long call	8
Bull call spread	9
Bull put spread	10
Covered call / Buy write	11
Protective / Married put	12
Cash-secured short put	13
Bearish Strategy	14
Long put	15
Bear put spread	16
Bear call spread	17
Neutral Strategy	18
Collar	19
Short straddle	20
Short strangle	21
Iron condor	22
Calendar spread	23
Covered combination / Covered strangle	24
Long call butterfly	25
Volatility Strategy	26
Long straddle	27
Long strangle	28
Call backspread	29
Put backspread	30

HOW TO USE THIS BOOK

- Each strategy has an accompanying graph showing profit and loss at expiration.
- The vertical axis shows the profit/loss scale.
- When the strategy line is below the horizontal axis, it assumes you paid for the position or had a loss.
- When it is above the horizontal axis, it assumes you received a credit for the position or had a profit.
- The dotted line indicates the strike price.
- The intersection of the strategy line and the horizontal axis is the break-even point (BEP) not including transaction costs, commissions, or margin (borrowing) costs.
- These graphs are not drawn to any specific scale and are meant only for illustrative and educational purposes.
- The risks/rewards described are generalizations and may be lesser or greater than indicated.



TERMS AND DEFINITIONS

Break-Even Point (BEP): The stock price(s) at which an option strategy results in neither a profit nor loss.

Call: An option contract that gives the holder the right to buy the underlying security at a specified price for a certain, fixed period of time.

In-the-money: A call option is in-the-money if the strike price is less than the market price of the underlying security. A put option is in-the-money if the strike price is greater than the market price of the underlying security.

Long position: A position wherein an investor is a net holder in a particular options series.

Out-of-the-money: A call option is out-of-the-money if the strike price is greater than the market price of the underlying security. A put option is out-of-the-money if the strike price is less than the market price of the underlying security.

Premium: The price a put or call buyer must pay to a put or call seller (writer) for an option contract. Market supply and demand forces determine the premium.

Put: An option contract that gives the holder the right to sell the underlying security at a specified price for a certain, fixed period of time.

Ratio Spread: A multi-leg option trade of either all calls or all puts whereby the number of long options to short options is something other than 1:1. Typically, to manage risk, the number of short options is lower than the number of long options (i.e. 1 short call: 2 long calls).

Short position: A position wherein the investor is a net writer (seller) of a particular options series.

Strike price or exercise price: The stated price per share for which the underlying security may be purchased (in the case of a call) or sold (in the case of a put) by the option holder upon exercise of the option contract.

Synthetic position: A strategy involving two or more instruments that has the same risk/reward profile as a strategy involving only one instrument.

Time decay or erosion: A term used to describe how the time value of an option can “decay” or reduce with the passage of time.

Volatility: A measure of the fluctuation in the market price of the underlying security. Mathematically, volatility is the annualized standard deviation of returns.

BULLISH STRATEGY





BULLISH STRATEGY

LONG CALL

Example: Buy call

Market Outlook: Bullish

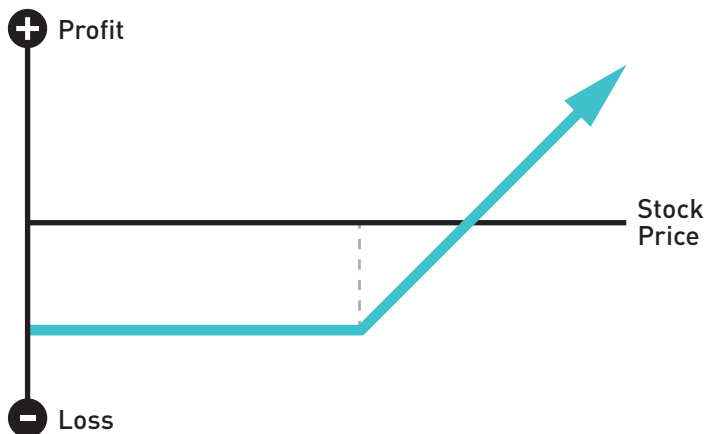
Risk: Limited

Reward: Unlimited

Increase in Volatility: Helps position

Time Erosion: Hurts position

BEP: Strike price plus premium paid



BULLISH STRATEGY

BULL CALL SPREAD

Example: Buy 1 call; sell 1 call at higher strike

Market Outlook: Bullish

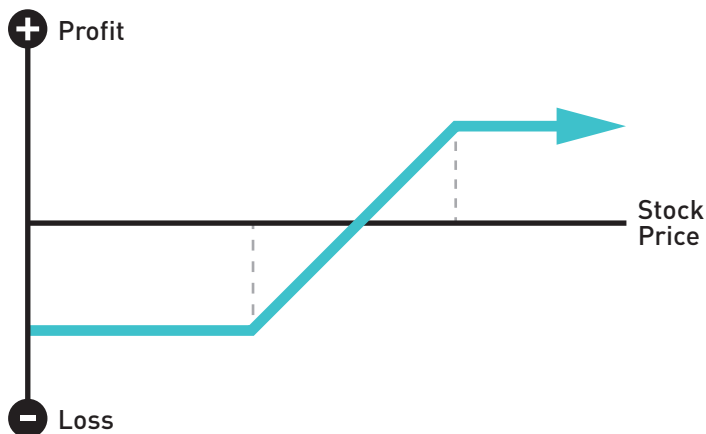
Risk: Limited

Reward: Limited

Increase in Volatility: Helps or hurts depending on strikes chosen

Time Erosion: Helps or hurts depending on strikes chosen

BEP: Long call strike plus net premium paid



BULLISH STRATEGY

BULL PUT SPREAD

Example: Sell 1 put; buy 1 put at lower strike with same expiry

Market Outlook: Neutral to bullish

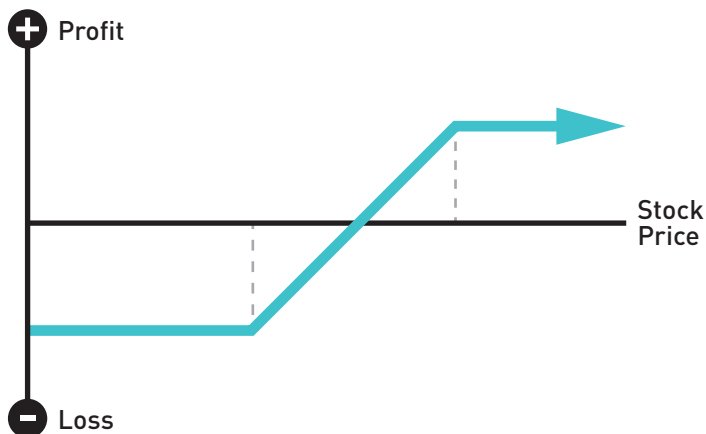
Risk: Limited

Reward: Limited

Increase in Volatility: Typically hurts position slightly

Time Erosion: Helps position

BEP: Short put strike minus credit received



BULLISH STRATEGY

COVERED CALL / BUY WRITE

Example: Buy stock; sell calls
on a share-for-share basis

Market Outlook: Neutral to slightly bullish

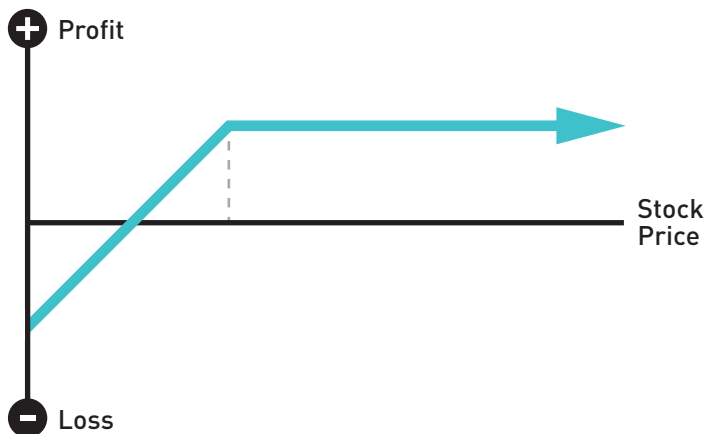
Risk: Limited, but substantial
(risk is from a fall in stock price)

Reward: Limited

Increase in Volatility: Hurts position

Time Erosion: Helps position

BEP: Starting stock price minus
premium received



BULLISH STRATEGY

PROTECTIVE / MARRIED PUT

Example: Own 100 shares of stock; buy 1 put

Market Outlook: Cautiously bullish

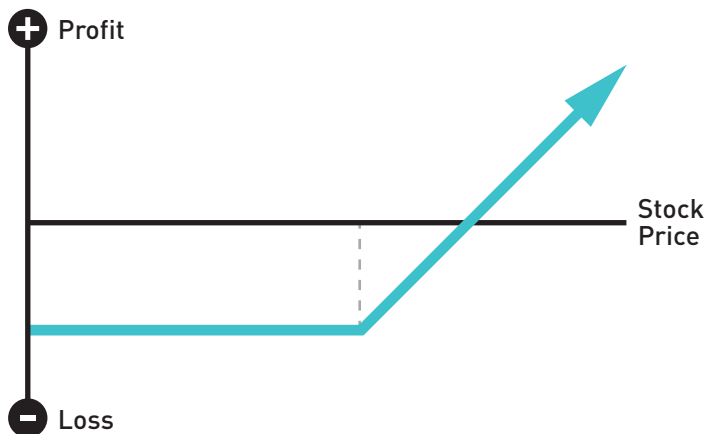
Risk: Limited

Reward: Unlimited

Increase in Volatility: Helps position

Time Erosion: Hurts position

BEP: Starting stock price plus premium paid



BULLISH STRATEGY

CASH-SECURED SHORT PUT

Example: Sell 1 put; hold cash equal to strike price x 100

Market Outlook: Neutral to slightly bullish

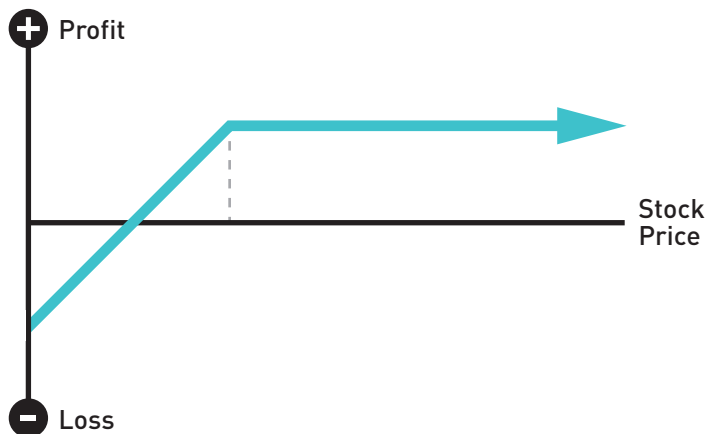
Risk: Limited, but substantial

Reward: Limited

Increase in Volatility: Hurts position

Time Erosion: Helps position

BEP: Strike price minus premium received



BEARISH STRATEGY



BEARISH STRATEGY LONG PUT

Example: Buy put

Market Outlook: Bearish

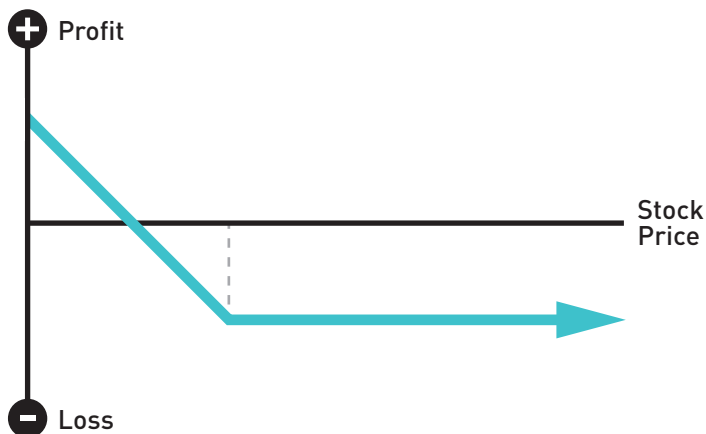
Risk: Limited

Reward: Limited, but substantial

Increase in Volatility: Helps position

Time Erosion: Hurts position

BEP: Strike price minus premium paid



BEARISH STRATEGY

BEAR PUT SPREAD

Example: Sell 1 put; buy 1 put at higher strike

Market Outlook: Bearish

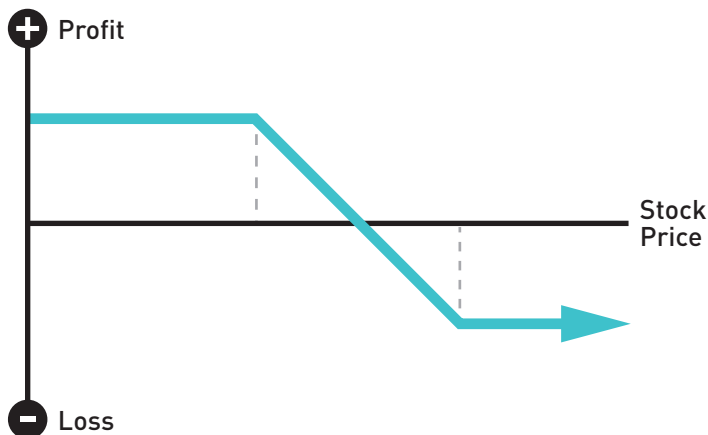
Risk: Limited

Reward: Limited

Increase in Volatility: Helps or hurts depending on strikes chosen

Time Erosion: Helps or hurts depending on strikes chosen

BEP: Long put strike minus net premium paid



BEARISH STRATEGY

BEAR CALL SPREAD

Example: Sell 1 call; buy 1 call at higher strike

Market Outlook: Neutral to bearish

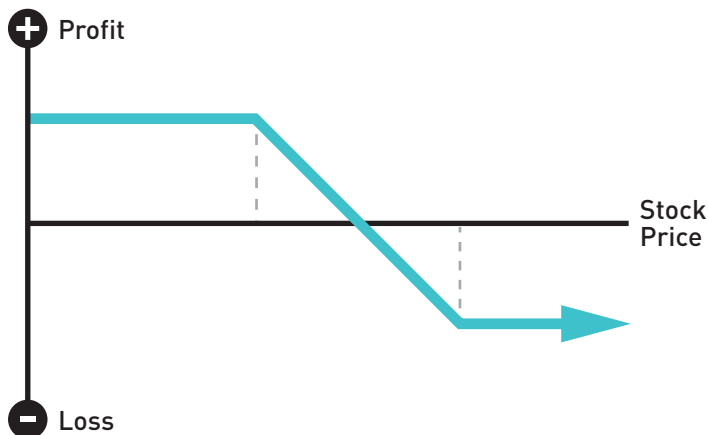
Risk: Limited

Reward: Limited

Increase in Volatility: Typically hurts position slightly

Time Erosion: Helps position

BEP: Short call strike plus credit received



NEUTRAL STRATEGY





NEUTRAL STRATEGY

COLLAR

Example: Own stock, protect by purchasing 1 put and selling 1 call with a higher strike

Market Outlook: Neutral to slightly bullish

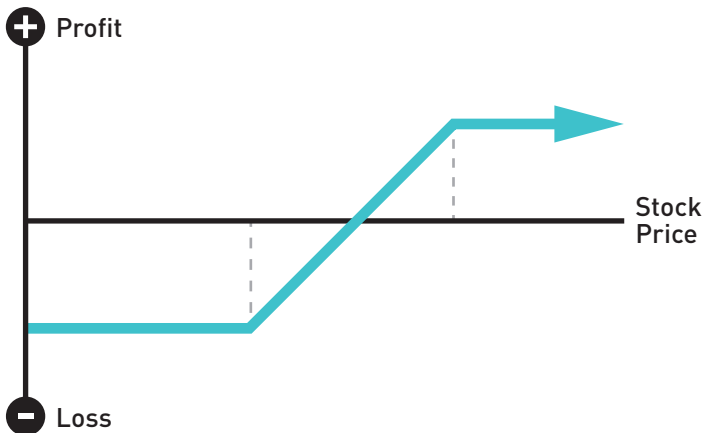
Risk: Limited

Reward: Limited

Increase in Volatility: Effect varies, none in most cases

Time Erosion: Effect varies

BEP: In principle, breaks even if, at expiration, the stock is above/(below) its initial level by the amount of the debit/(credit)





NEUTRAL STRATEGY

SHORT STRADDLE

Example: Sell 1 call; sell 1 put at same strike

Market Outlook: Neutral

Risk: Unlimited

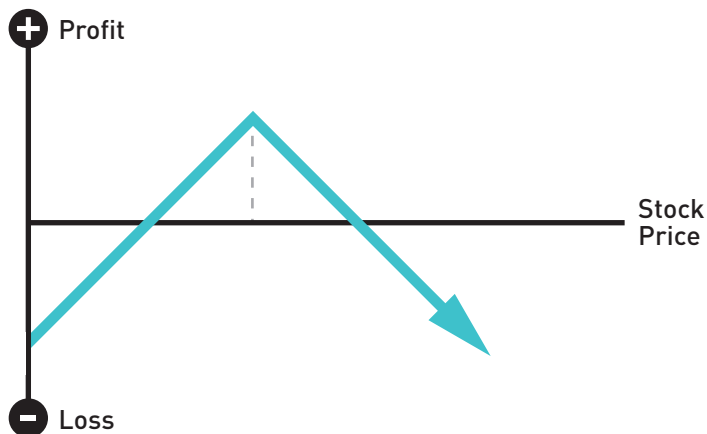
Reward: Limited

Increase in Volatility: Hurts position

Time Erosion: Helps position

BEP: Two BEPs

1. Call strike plus premium received
2. Put strike minus premium received





NEUTRAL STRATEGY

SHORT STRANGLE

Example: Sell 1 call with higher strike;
sell 1 put with lower strike

Market Outlook: Neutral

Risk: Unlimited

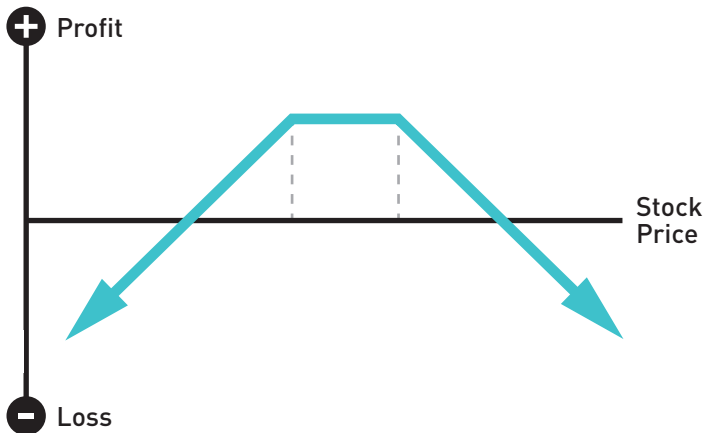
Reward: Limited

Increase in Volatility: Hurts position

Time Erosion: Helps position

BEP: Two BEPs

1. Call strike plus premium received
2. Put strike minus premium received



→ NEUTRAL STRATEGY

IRON CONDOR

Example: Sell 1 call; buy 1 call at higher strike; sell 1 put; buy 1 put at lower strike; all options have the same expiry. Underlying price typically between short call and short put strikes.

Market Outlook: Range bound or neutral

Risk: Limited

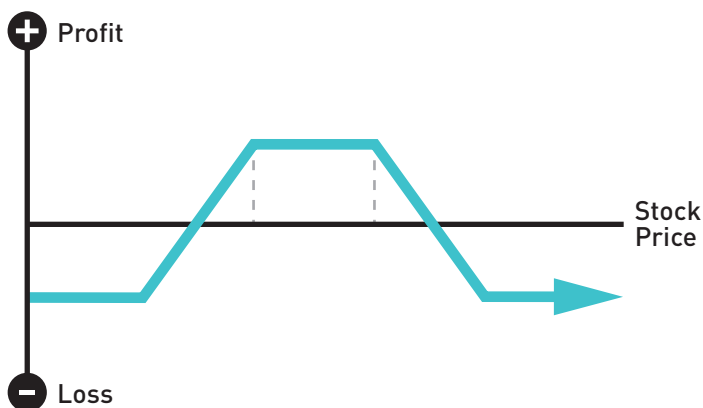
Reward: Limited

Increase in Volatility: Typically hurts position

Time Erosion: Helps position

BEP: Two BEPs

1. Short call strike plus credit received
2. Short put strike minus credit received



NEUTRAL STRATEGY

CALENDAR SPREAD

Example: Sell 1 call; buy 1 call at same strike but longer expiration; also can be done with puts

Market Outlook: Near term neutral (if strikes = stock price); can be slanted bullish (with OTM call options) or bearish (with OTM put options)

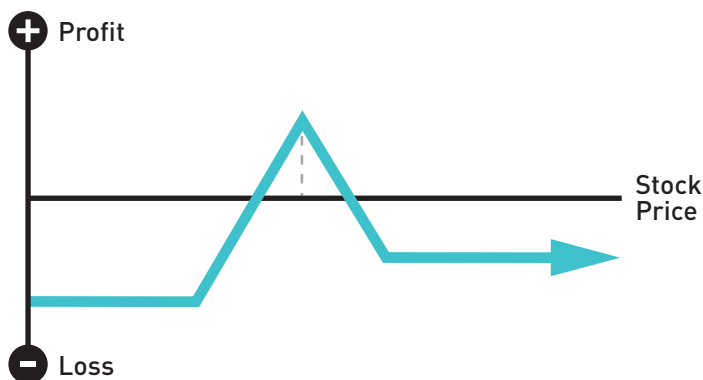
Risk: Limited

Reward: Limited; substantial after near term expiry

Increase in Volatility: Helps position

Time Erosion: Helps until near term option expiry

BEP: Varies; after near term expiry long call strike plus debit paid or (if done with puts) long put strike minus debit paid





NEUTRAL STRATEGY

COVERED COMBINATION / COVERED STRANGLE

Example: Own stock; sell one call; sell one put; underlying price typically between short call and short put strikes

Market Outlook: Range bound or neutral, moderately bullish; willing to buy more shares and sell existing shares

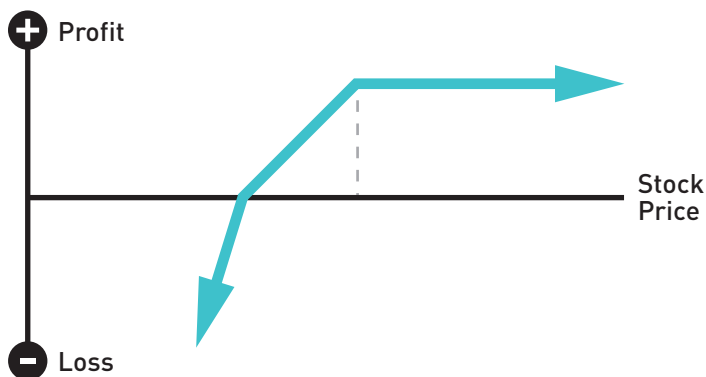
Risk: Limited, but substantial

Reward: Limited

Increase in Volatility: Typically hurts position

Time Erosion: Typically helps position

BEP: Initial stock price (or average price if assigned) minus net premium received



NEUTRAL STRATEGY

LONG CALL BUTTERFLY

Example: Sell 2 calls; buy 1 call at next lower strike; buy 1 call at next higher strike (the strikes are equidistant)

Market Outlook: Neutral around strike

Risk: Limited

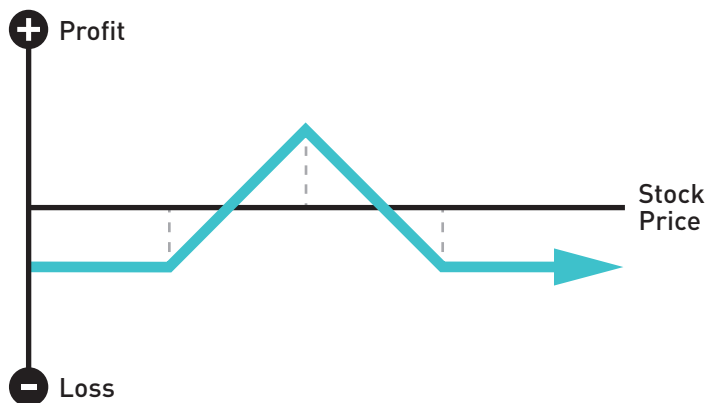
Reward: Limited

Increase in Volatility: Typically hurts position

Time Erosion: Typically helps position

BEP: Two BEPs

1. Lower long call strike plus net premium paid
2. Higher long call strike minus net premium paid



VOLATILITY STRATEGY





VOLATILITY STRATEGY

LONG STRADDLE

Example: Buy 1 call; buy 1 put at same strike

Market Outlook: Large move in either direction

Risk: Limited

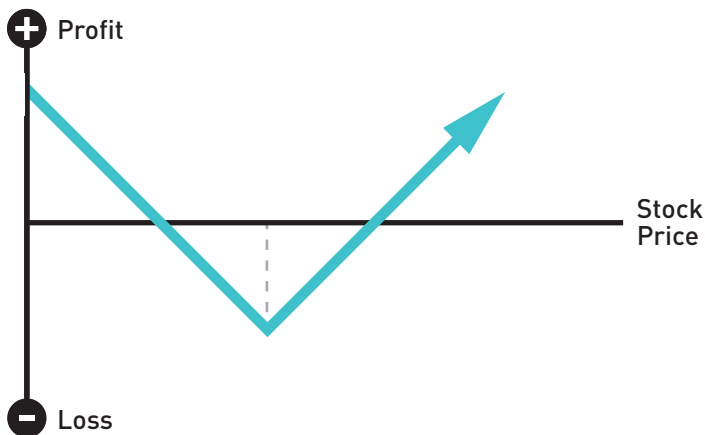
Reward: Unlimited

Increase in Volatility: Helps position

Time Erosion: Hurts position

BEP: Two BEPs

1. Call strike plus premium received
2. Put strike minus premium received





VOLATILITY STRATEGY

LONG STRANGLE

Example: Buy 1 call with higher strike;
buy 1 put with lower strike

Market Outlook: Large move in either direction

Risk: Limited

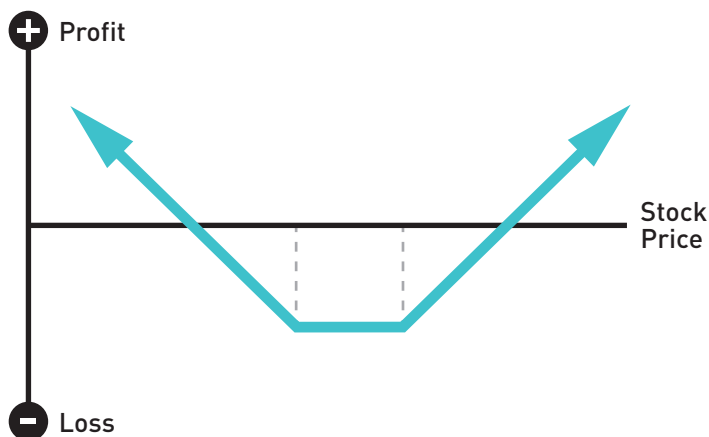
Reward: Unlimited

Increase in Volatility: Helps position

Time Erosion: Hurts position

BEP: Two BEPs

1. Call strike plus premium received
2. Put strike minus premium received





VOLATILITY STRATEGY

CALL BACKSPREAD

Example: Sell 1 call; buy 2 calls at higher strike

Market Outlook: Bullish

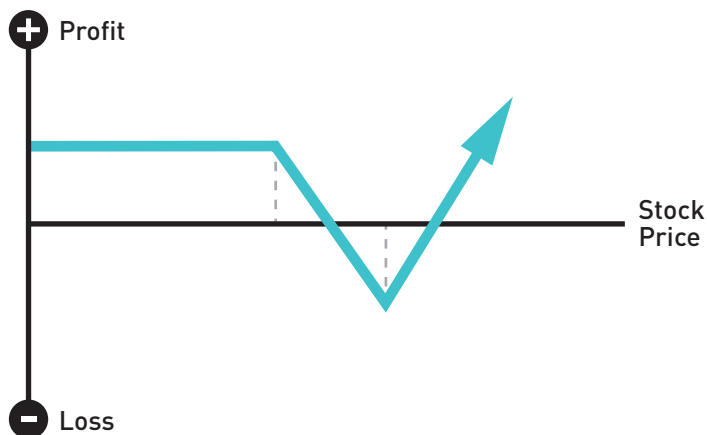
Risk: Limited

Reward: Unlimited

Increase in Volatility: Typically helps position

Time Erosion: Typically hurts position

BEP: Varies, depends if established for a credit or debit. If done for a credit, two BEP's with the lower BEP being the short strike plus the credit





VOLATILITY STRATEGY

PUT BACKSPREAD

Example: Sell 1 put; buy 2 puts at lower strike

Market Outlook: Bearish

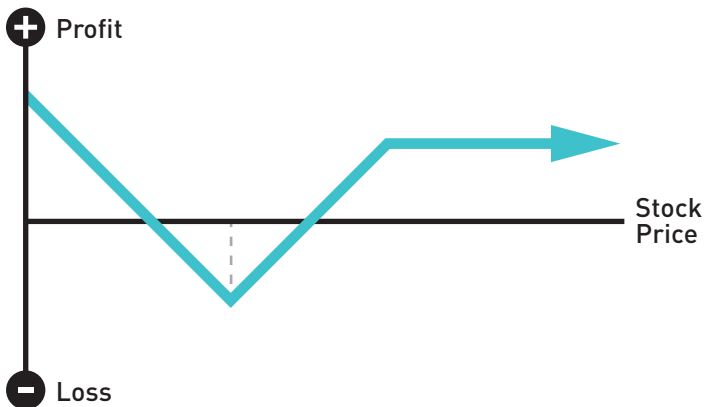
Risk: Limited

Reward: Limited, but substantial

Increase in Volatility: Typically helps position

Time Erosion: Typically hurts position

BEP: Varies, depends if established for a credit or debit. If done for a credit, two BEP's and the lower BEP is the short strike minus the credit



This document is made available for general information purposes only. The information provided in this document, including financial and economic data, quotes and any analysis or interpretation thereof, is provided solely for information purposes and shall not be construed in any jurisdiction as providing any advice or recommendation with respect to the purchase or sale of any derivative instrument, underlying security or any other financial instrument or as providing legal, accounting, tax, financial or investment advice. Bourse de Montréal Inc. recommends that you consult your own advisors in accordance with your needs before making decision to take into account your particular investment objectives, financial situation and individual needs. Although care has been taken in the preparation of this document, Bourse de Montréal Inc. and/or its affiliates do not guarantee the accuracy or completeness of the information contained in this document and reserve the right to amend or review, at any time and without prior notice, the content of this document. Neither Bourse de Montréal Inc. nor any of its affiliates, directors, officers, employees or agents shall be liable for any damages, losses or costs incurred as a result of any errors or omissions in this document or of the use of or reliance upon any information appearing in this document.

For more information

Richard Ho






Senior Manager, Business Development, Equity Derivatives

T: +1 514 871-7889

info@tmx.com



Follow us:

-  m-x.ca/twitter
-  m-x.ca/linkedin
-  m-x.ca/facebook
-  m-x.ca/rss
-  optionmatters.ca

m-x.ca/options