

# Make Money Trading Options

**Top-15 Option Trading Strategies**



*Larry Gaines – Founder & 25-Yr Veteran Options Trader, Austin, Texas, USA*

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Make Money Trading Options  
*Top-15 Option Trading Strategies*



## *Introduction*

### **Why Trade Options?**

Dear Options Trader,

Want to know the best strategies for trading options?  
Look no further.

This E-Book contains the best methods for trading stock options, commodities options, or any other options in the financial markets – period.

These are the same strategies I use to bank 4%, 17%, and 40% and more on my winning trades, while keeping my losing trades to a bare minimum. **That's how I consistently pull out triple-digit returns from the market every year** – and that is no-misprint.

(Cumulative 2011 Returns as of November 2011: 2,014%)

I've been trading the financial markets since the early 80's. I've traded millions of dollars in equities and derivatives both professionally and in my own personal account. I've traded for stocks, bonds, futures, Forex, and everything in between –

But **nothing beats the consistent returns of options.**

This E-Book is my contribution to your options trading success. Memorize these strategies. They are the backbone of any great options trader – and they will help you become a consistent options trader too.

All the Best on Your Options Trading Success,

*Larry Gaines*

Larry Gaines  
25-Year Veteran Options Trader  
Founder, [OptionsOnTheOpen.com](http://OptionsOnTheOpen.com)  
Austin, Texas

P.S. \*\*Don't forget to checkout [www.OptionsOnTheOpen.com](http://www.OptionsOnTheOpen.com) for FREE bi-weekly options trading tips videos – did I mention it was FREE?

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[www.OptionsOnTheOpen.com](http://www.OptionsOnTheOpen.com) "The Leader in Options Day Trading"

Larry Gaines – Founder & 25-Yr Veteran Options Trader, Austin, Texas, USA

## **Strategy #1**

### **Buy-Write or Covered Call**

**Construction** – Long stock, short one call for every 100 shares of stock owned.

**Function** – To enhance profitability of stock ownership and to provide limited downside protection against adverse stock movement.

**Bias** – Neutral to slightly bullish.

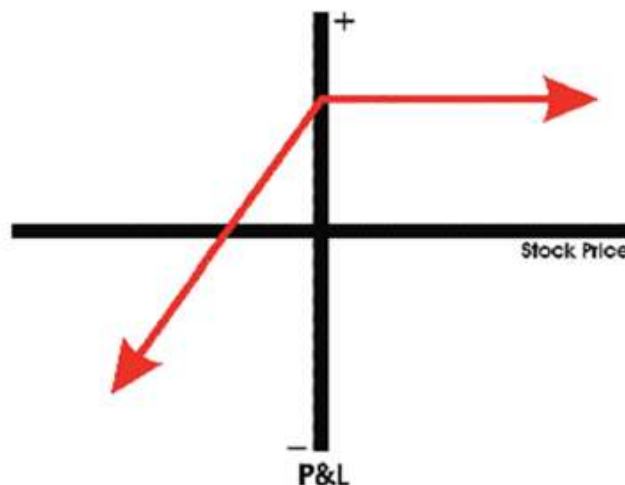
**When to Use** – When you feel the stock will trade up slightly or in a tight range for a period of time and you plan on holding the stock for longer term.

**Profit Scenario** – If stock rises, profit will be enhanced by premium received. If stock stagnates, you will profit from premium received from call sale.

**Loss Scenario** – If stock trades lower than the point defined by your purchase price minus the premium received from call sale you will lose dollar for dollar. Call premium received will act as an offset to the loss in the stock.

**Key Concepts** – If stock trades up aggressively, you will only profit up to a stock price defined by the strike price plus option price. If the stock continues higher above that point (breakeven), you will incur lost opportunity. Further, if stock closes above strike price, stock will be called away unless necessary adjustment is made. Philosophically identical to the Sell-Write position except in opposite direction. Time decay helps the position.

**Covered Call P&L Chart**



## Strategy #2 Sell-Write or Covered Put

**Construction** – Short stock, short one put for every 100 shares of stock shorted.

**Function** – To enhance profitability of short stock position and to provide limited protection against adverse stock movement.

**Bias** – Neutral to slightly bearish.

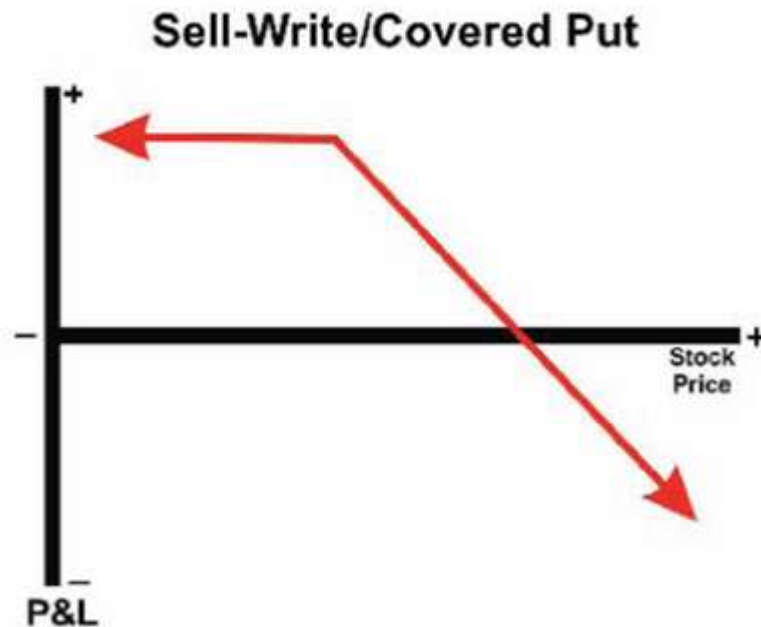
**When to Use** – When you feel the stock will trade slightly down or in a tight range for a period of time.

**Profit Scenario** – If stock falls, profit will be enhanced by premium received. If stock stagnates, you will profit from premium received from put sale.

**Loss Scenario** – If stock trades higher than the point defined by your stock sales price plus the premium received from put sale, you will lose dollar for dollar. Put premium received will act as stock loss offset.

**Key Concepts** – If stock trades down aggressively, you will only profit down to a stock price defined by the strike price minus option premium. If the stock continues down below that point (breakeven), you will incur lost opportunity.

Further, if stock closes below strike price, stock will be assigned to you unless necessary adjustment is made. Time decay helps the position. Philosophically identical to Buy-Write except in opposite stock direction.



## Strategy #3 Protective Put

**Construction** – Long stock, long 1 put per every 100 shares of stock

**Function** – To provide maximum downside protection for long stock position. Long stock insurance policy.

**Bias** – Bullish but cautious

**When to use** – When wishing to protect profits of long stock position while wishing to retain position. Also, to protect speculative stock purchases (i.e. purchasing stock on potential chart break out from present trading range according to Technical Analysis).

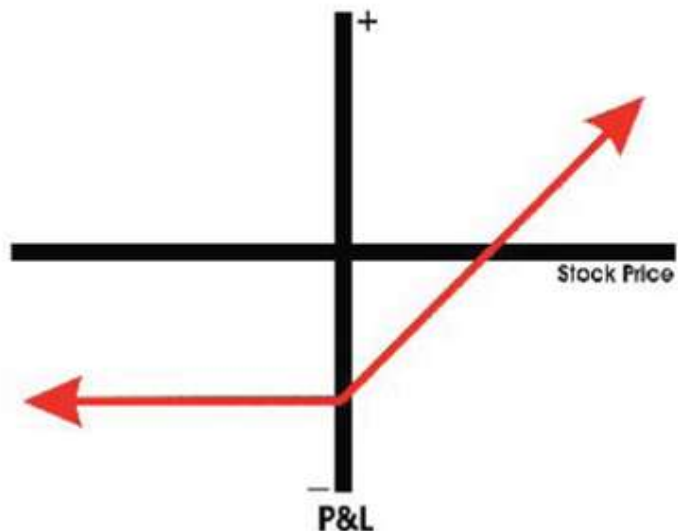
**Profit Scenario** – If stock continues to trade up by more than the amount paid for the puts. Once above that level, position makes dollar for dollar with stock.

**Loss Scenario** - If the stock trades down, loss will be felt until stock reaches point defined by puts strike price minus put price. At that level, position will cease losing. If stock stagnates, loss will equal put price due to decay.

**Key Concepts** – Due to the acquisition of time decay from the long put, the position is best used for protection of already existing profits, or when a potentially aggressive or explosive upside move in the near future is a good possibility. Other side of the Sell-Write position.

Philosophically identical to the Synthetic Put strategy except for anticipation of stock going up.

Protective Put Strategy P&L Chart



## **Strategy #4**

### **Collar**

**Construction** – Long stock, simultaneously long one out-of-the-money put and short one out-of-the-money call per every 100 shares of stock owned.

**Function** – Provide no-to-low cost maximum profit protection for a long stock position.

**Bias** - cautious or even short term bearish.

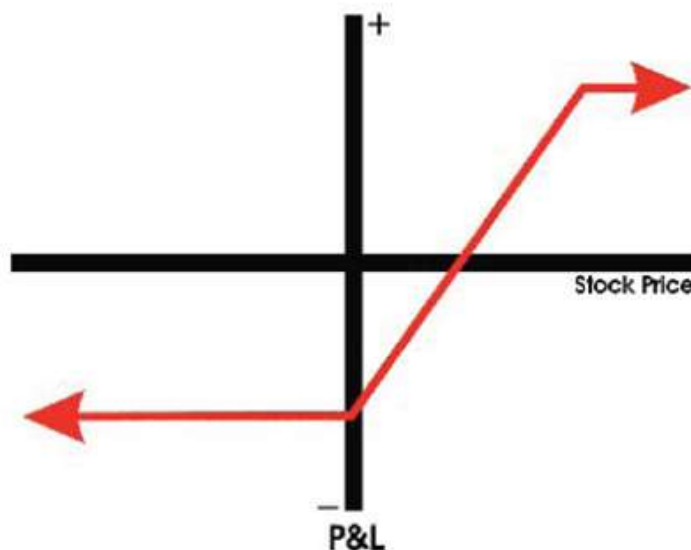
**When to Use** – When you feel that your long stock position may run into a tough period of time but you want to keep the position.

**Profit Scenario** – Depending on how you set up the collar and the prices of the put and call, you may make a very negligible amount. If the stock trades up, you may make a little.

**Loss Scenario** – Depending on how you set up the collar and prices of the put and call, you may lose a little money. If the stock trades down, you may also lose a little but the collar will limit it to a set amount regardless of how low the stock goes.

**Key Concepts** – Collars are not designed to make money. They are designed to provide maximum downside protection, similar to the protective put, but at a much better price. The premium received from the sale of the call will offset the amount paid for the put.

### **Collar Strategy P&L Chart**



## Strategy #5 Bull Spread

**Construction** – Long one call while simultaneously short one call with a higher strike in the same month. Or, short one put while simultaneously long one put with a lower strike in the same month.

**Function** – Low cost stock directional play which allows you two choices to put on the same trade. Long Vertical Call Spread or Short Vertical Put Spread.

**Bias** – Bullish

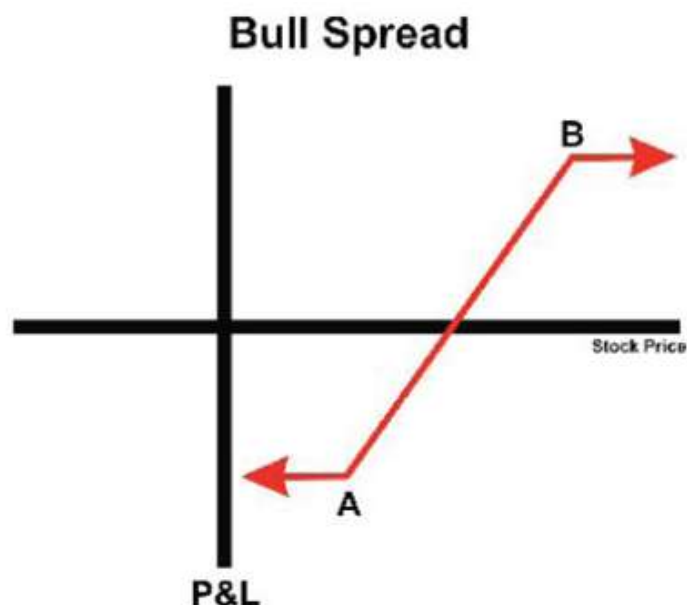
**When to use** – Use when you feel the stock is likely to rise but not too quickly nor explosively as this strategy has a limited profit potential. Also, when constructed properly, this spread can be used as a premium collection strategy.

**Profit Scenario** – If stock rises, profit will be defined by the increase in value of the long vertical call spread or, in the case of a short vertical put spread, its decrease in value.

**Loss Scenario** – If stock declines, loss will be defined by the decrease in value of the long vertical call spread, or in the case of a short vertical put call spread, its increase in value.

**Key Concepts** – The maximum value of a vertical spread will be equal to the difference between the two strikes, therefore both the buyer and the seller will have a limited profit and limited loss scenario.

Depending on which strikes you use, time decay can help or hurt the position. Thus, some vertical spreads can make money over time even if stock stays stagnant.



## Strategy #6 Bear Spread

**Construction** – Long one call while simultaneously short one call with a lower strike in the same month. Or, short one put while simultaneously long one put with a higher strike in the same month.

**Function** – Low cost stock directional play which allows you two choices to put on the same trade. Short Vertical Call Spread or Long Vertical Put Spread.

**Bias** – Bearish

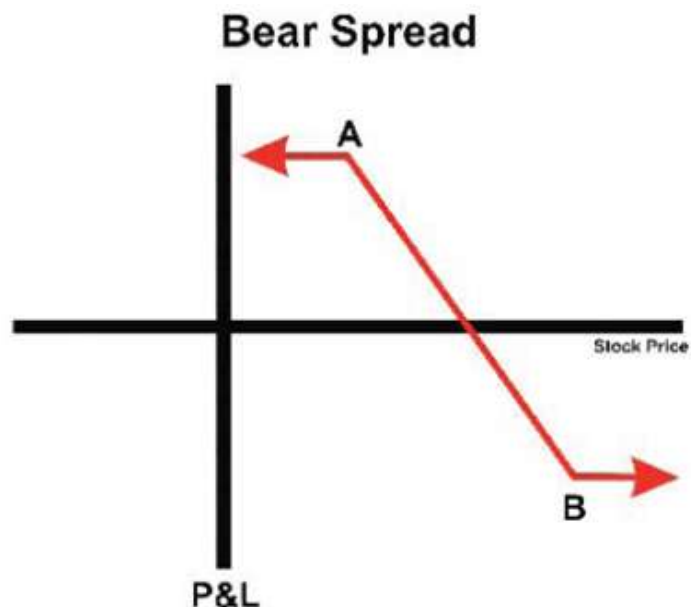
**When to use** – Use when you feel the stock is likely to decline but not too quickly nor explosively as this strategy has a limited profit potential. Also, when constructed properly, this spread can be used as a premium collection strategy.

**Profit Scenario** – If stock declines, profit will be defined by the decrease in value of the short vertical call spread or, in the case of a long vertical put spread, its increase in value.

**Loss Scenario** – If the stock rises, loss will be defined by the increase in value of the short vertical call spread, or, in the case of a long vertical put spread, its decrease in value.

**Key Concepts** – The maximum value of a vertical spread will be equal to the difference between the two strikes, therefore both the buyer and the seller will have a limited profit and limited loss scenario.

Depending on which strikes you use, time decay can help or hurt the position. Thus, some vertical spreads can make money over time even if stock stays stagnant.



## Strategy #7 Time Spread

**Construction** – Long one call in a further out month while simultaneously short one call with the same strike but in a closer expiration month.

**Function** – To collect time premium by taking advantage of options non-linear rate of decay.

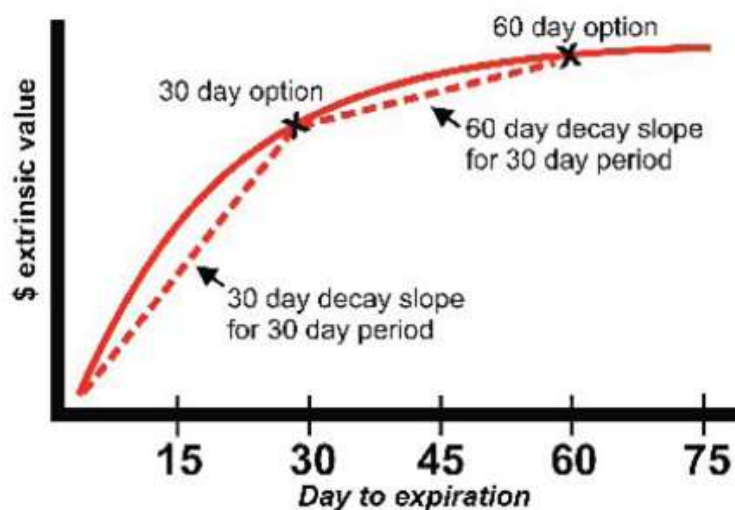
**Bias** – Neutral.

**When to use** – Best used during stagnant periods in order to collect premiums due to time decay. Unlike other premium collection strategies, the time spread offers a limited loss scenario in both directions.

**Profit Scenario** – If the stock remains stagnant, the position will profit by the nearer month option (which you are short) decaying at a faster rate than the further out month option (which you are long). When this occurs, the spread will widen thus creating a profit. Profit can also be attained if implied volatility increases.

**Loss Scenario** – If the stock moves away from the strike by either rising or falling, the spread will tighten, thus losing value and creating a loss.

**Key Concepts** – Time spreads are best done in at-the-money options where the extrinsic value is the highest which accentuates the rate of decay. Best results are found in stocks that are in a stagnant period as stock movement away from the strike will lead to losses.



## Strategy #8 Long Straddle

**Construction** – Long one call and one put with the same strike price, in the same expiration month and in a one to one ratio. Strike price used is normally at-the-money.

**Function** – To take advantage of large potential stock movements in either direction or if you anticipate an upward movement in implied volatility.

**Bias** – Volatile in either direction.

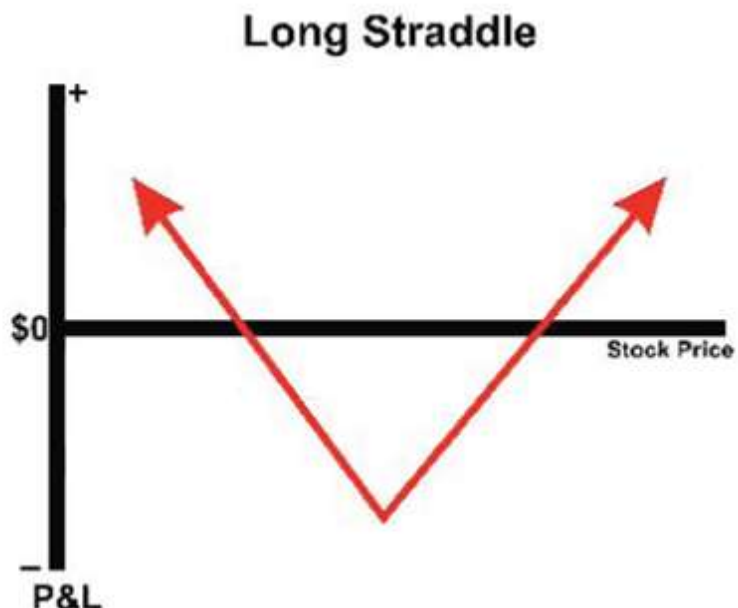
**When to Use** – Normally around news release time (i.e. earnings) when you feel that the news can effect the stock aggressively but aren't sure in which direction. Also, good to use when you feel implied volatility is likely to increase sharply.

**Profit Scenario** – Profit will be obtained in a dollar for dollar fashion if the stock closes outside of the parameters of the breakevens set forth by first adding the strike price to the amount paid for the straddle then subtracting the amount paid for the straddle from the strike price. Theoretically, unlimited potential reward.

**Loss Scenario** – Loss occurs if stock closes between break-even points as defined above. Maximum loss occurs if stock closes directly at the strike and lessens as stock closes closer to either of the breakeven points. Maximum loss is limited to price paid for straddle.

**Key Concept** – Because of large decay associated with this position, time sensitivity is critical.

Once anticipated movement occurs, it is critical to close down position in order to secure profit and eliminate further risk of substantial decay.



## Strategy #9 Short Straddle

**Construction** – Short one call and short one put with the same strike price, in the same expiration month in a one to one ratio. Strike price used is normally at-the-money

**Function** – To take advantage of a stock entering a stagnant or low volatility trading range.

**Bias** – Stagnant

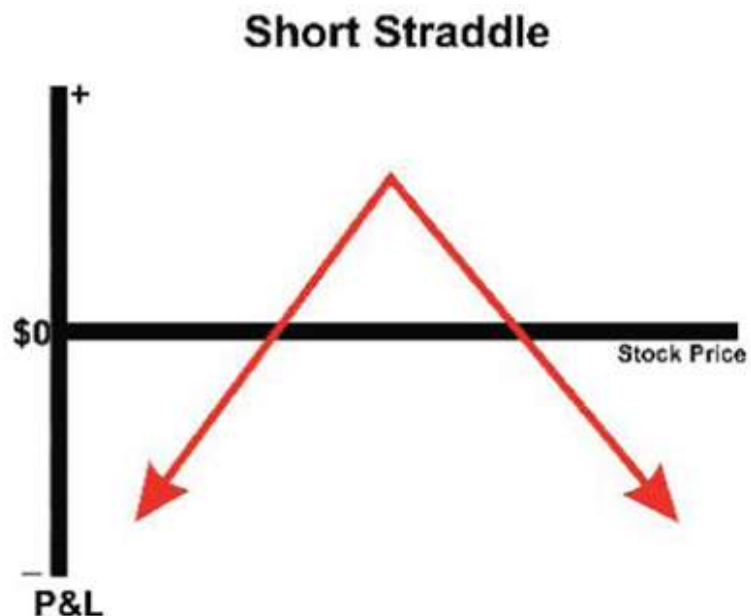
**When to Use** – Normally around a time away from expected news releases (i.e. earnings) when you feel that the lack news can lead to a period of stagnation or lack of movement of the stock without directional bias. Also, good to use when you feel implied volatility is likely to decrease sharply.

**Profit Scenario** – Profit will be obtained if the stock closes inside of the parameters of the breakevens set forth by first adding the strike price to the amount paid for the straddle then subtracting the amount paid for the straddle from the strike price. This strategy has a potential reward limited to the amount received from the sale.

**Loss Scenario** – Loss occurs if stock closes outside break-even points as defined above. Maximum loss occurs once the stock closes outside either of the breakeven points and increases as stock moves further away beyond either of the breakeven points.

**Key Concept** – Because of large decay associated with this position, time sensitivity is critical. The longer the stock remains stagnant or between the two break-even points, the better for the seller.

The passage of time aids this strategy. Due to the nature of the position, maximum loss is theoretically unlimited.



## Strategy #10 Long Strangle

**Construction** – Long one call and one put with different strike prices but in the same expiration month in a one to one ratio. Both options are usually out-of-the-money.

**Function** – To take advantage of large potential stock movements in either direction or if you anticipate an upward movement in implied volatility.

**Bias** – Volatile in either direction

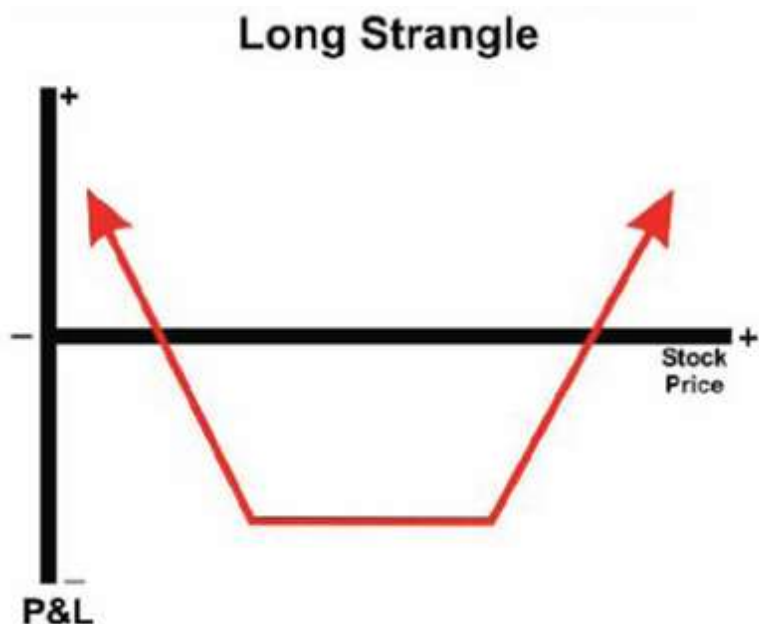
**When to Use** – Normally around news release time (i.e. earnings) when you feel that the news can affect the stock aggressively but aren't sure in which direction. Also, good to use when you feel implied volatility is likely to increase sharply.

**Profit Scenario** – Profit will be obtained in a dollar for dollar fashion if the stock closes outside of the parameters of the breakevens set forth by first adding the strike price of the call to the amount paid for the strangle then subtracting the amount paid for the strangle from the strike price of the put. Theoretically, unlimited potential reward.

**Loss Scenario** – Maximum loss occurs if stock closes between the break-even points as defined above. Maximum loss is limited to price paid for strangle.

**Key Concept** – Because of large decay associated with this position, time sensitivity is critical. Once anticipated stock or volatility movement occurs, it is critical to close down position in order to secure profits and eliminate further risk of substantial decay.

Philosophically identical to the straddle except the strangle's wider breakevens require a larger stock movement. The trade off for this is the lower cost of the strangle.



## Strategy #11 Short Strangle

**Construction** – Short one call and short one put with different strike prices, in the same expiration month and in a one to one ratio. Both options are usually out-of-the-money.

**Function** – To take advantage of a stock entering a stagnant or low volatility trading range.

**Bias** – Stagnant

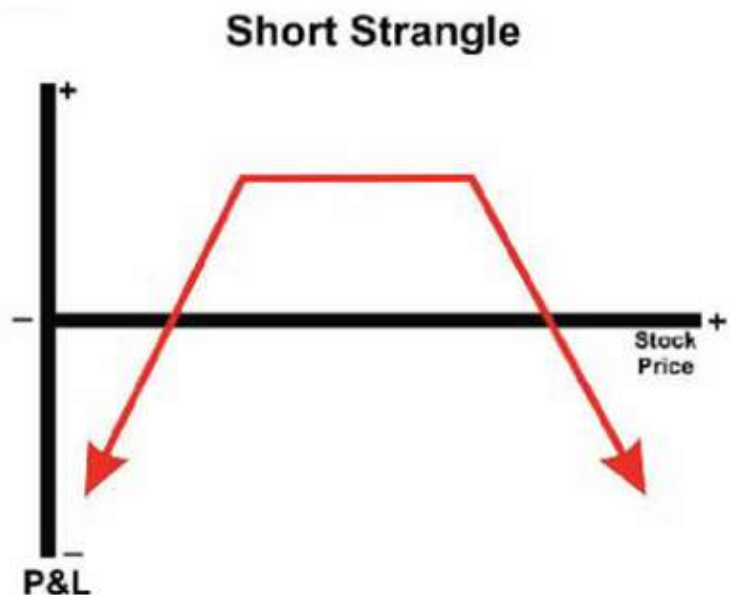
**When to Use** – Normally around a time away from expected news releases (i.e. earnings) when you feel that the lack news can lead to a period of stagnation or lack of movement of the stock without directional bias. Also, good to use when you feel implied volatility is likely to decrease sharply.

**Profit Scenario** – Profit will be obtained if the stock closes inside of the parameters of the breakevens set forth by first adding the strike price of the call to the amount paid for the strangle then subtracting the amount paid for the strangle from the strike price of the put. This strategy has a potential reward limited to the amount received from the sale.

**Loss Scenario** – Loss occurs if stock closes outside break-even points as defined above. Maximum loss occurs as stock continues to trade further outside and away from either breakeven point. Potential loss is theoretically unlimited.

**Key Concept** – Because of large decay associated with this position, time sensitivity is critical. The longer the stock remains stagnant or between the two break-even points, the better for the seller.

The passage of time aids this strategy as well as decreases in implied volatility. Due to the nature of the position, maximum loss is theoretically unlimited.



## Strategy #12 Long Butterfly

**Construction** – Short two calls (puts) of same month and strike while long a call (put) above and long a call below both equidistant from the strike of the two short calls (puts). In the case of an “Iron Butterfly,” short a straddle while long a strangle around it.

**Function** – Premium collection strategy with upside and downside protection. Also short volatility play.

**Bias** – Stagnant.

**When to Use** – When you feel the stock will trade in a very tight range near a strike price and stagnate there. Also if you feel the stock has a likely hood of a decrease in implied volatility. The butterfly allows you to take advantage of these potential situations while offering the investor a hedged position.

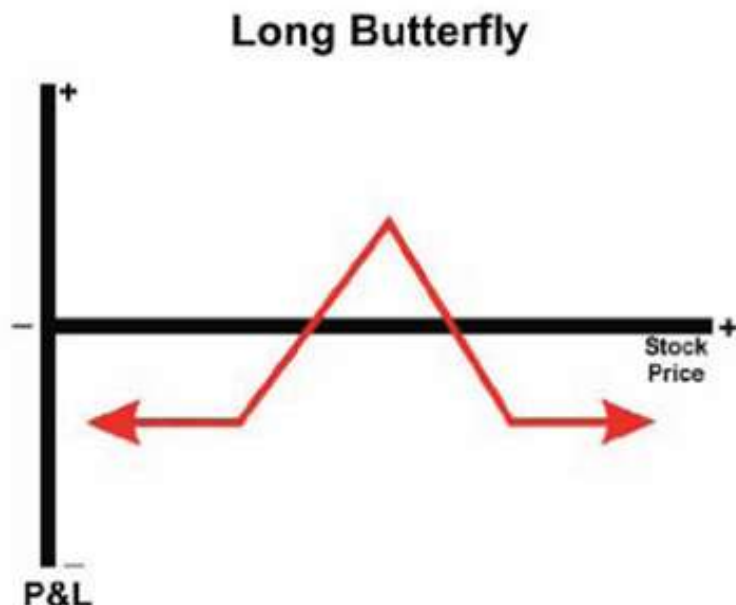
**Profit Scenario** – Maximum profit occurs when stock closes directly at the strike of the two short options and decreases as stock moves in either direction away from the strike.

**Loss Scenario** – Maximum loss occurs when stock closes at either strike of the long options. Maximum loss is limited.

**Key Concepts** – The long butterfly is an ideal strategy for premium collectors who seek to minimize potential losses in the event the stock moves adversely. This strategy can also take advantage of expected decreases in implied volatility. The strategy can be viewed as two separate trades.

In the case of a traditional butterfly, the position can be broken down into two vertical spreads, one long and one short with each sharing the same short strike, and having different but equidistant long strikes.

In the case of the Iron Butterfly, the position can be broken down to a short straddle surrounded by a long strangle. Butterflies are best entered into in further out months.



## Strategy #13 Short Butterfly

**Construction** – Long two calls (puts) of same month and strike while short a call (put) above and short a call (put) below both equidistant from the strike of the two long calls (puts). In the case of an "Iron Butterfly," long a straddle while short a strangle around it.

**Function** – Limited directional stock movement play. Also long volatility play.

**Bias** – Limited directional but in either direction.

**When to Use** – When you feel the stock will trade away from a strike but not aggressively. Also if you feel the stock has a likely hood of an increase in implied volatility. The short butterfly allows you to take advantage of these potential situations while offering the investor a hedged position.

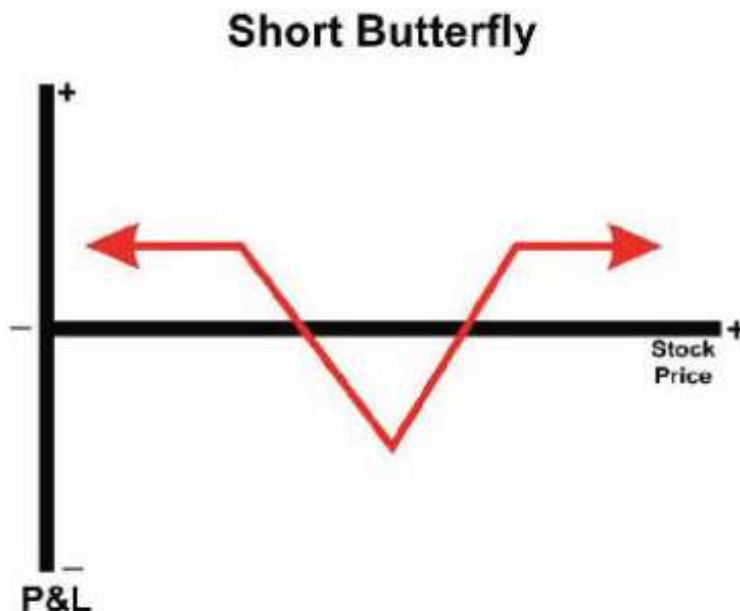
**Profit Scenario** – Maximum profit occurs when stock closes at or above the highest of the short strikes or at or below the lowest of the short strikes. The trade will also be profitable in event of increasing implied volatility.

**Loss Scenario** – Maximum loss occurs when stock closes at either strike of the long options. Maximum loss is limited.

**Key Concepts** – Short butterflies are an ideal strategy for long volatility players who seek minimizing potential loss in the event the stock moves adversely. The strategy can be broken down viewed as two trades.

In the case of a traditional butterfly, the position can be broken down into two conflicting vertical spreads, one long, and one short with each sharing the same short strike and different but equidistant long strikes.

The Iron Butterfly can be broken down to a long straddle surrounded by a short strangle. Butterflies are best entered into in further out months.



## Strategy #14 Long Condor

**Construction** – Short two calls (puts) of same month and adjacent strikes while long a call above the highest of the short call (put) strikes and long a call (put) below the lowest of the short call (put) strikes. Both short call (put) strikes must be equidistant from the strike of the two short calls (puts). In the case of an “Iron Condor,” short an interior strangle while long an exterior strangle around it.

**Function** – Premium collection strategy with upside and downside protection. Also a short volatility play.

**Bias** – Stagnant.

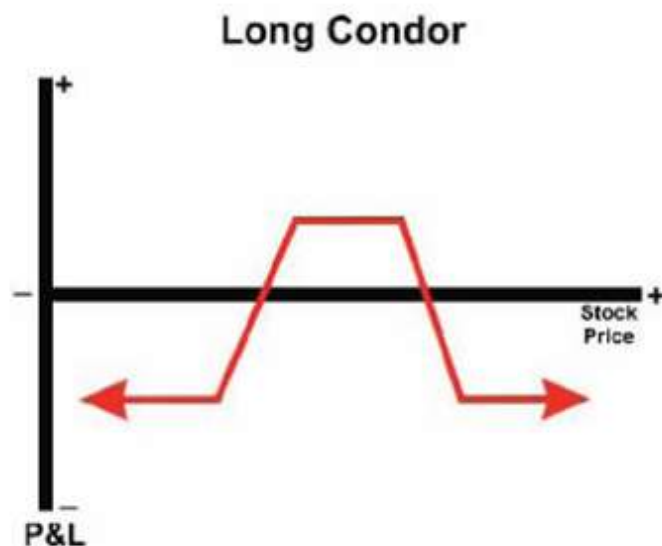
**When to Use** – When you feel the stock will trade in a very tight range between two strike prices and stagnate there. Also if you feel the stock has a likelihood of a decrease in implied volatility. The long condor allows you to take advantage of these potential situations while offering the investor a fully hedged position.

**Profit Scenario** – Maximum profit occurs when stock closes anywhere between the two short strikes and decreases as stock moves in either direction outside and away from the two short strikes.

**Loss Scenario** – Maximum loss occurs when stock closes at or above the highest strike of the long strikes or at or below the lowest of the long strikes. Maximum loss is limited.

**Key Concepts** – The long condor is an ideal strategy for premium collectors who seek to minimize potential losses in the event the stock moves adversely. This strategy can also take advantage of expected decreases in volatility. The strategy can be broken down and viewed as two trades.

In the case of a traditional condor the position can be broken down into two conflicting vertical spreads, one long and one short. In the case of an Iron Condor, the position can be broken down to a short interior strangle surrounded by a long exterior strangle. Condors are best entered into in further out months.



## Strategy #15 Short Condor

**Construction** – Long two calls (puts) of same month and adjacent strikes while short a call (put) above the highest of the short call (put) strikes and long a call (put) below the lowest of the short call (put) strikes. Both short call (put) strikes must be equidistant from the strike of the two short calls (puts). In the case of an “Iron Condor,” short an interior strangle while long an exterior strangle around it.

**Function** – Limited directional stock movement play. Also long volatility play

**Bias** – Limited directional but in either direction

**When to Use** – When you feel the stock will trade away from a range between two strikes but not aggressively. Also if you feel the stock has a likely hood of an increase in implied volatility. The short condor allows you to take advantage of these potential situations while offering the investor a hedged position.

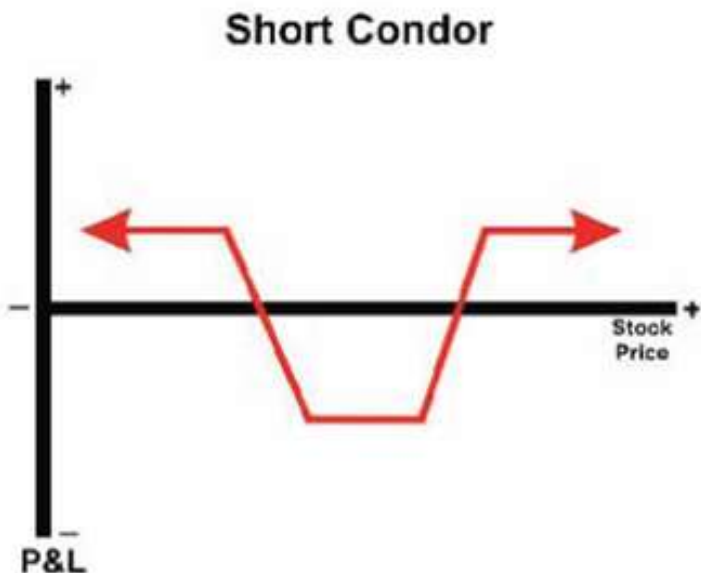
**Profit Scenario** – Maximum profit occurs when stock closes at or above the highest of the short strikes or at or below the lowest of the short strikes. The trade will also be profitable in event of increasing implied volatility.

**Loss Scenario** – Maximum loss occurs when stock closes at or above the highest strike of the long strikes or at or below the lowest of the long strikes. Maximum loss is limited.

**Key Concepts** – Short condors are an ideal strategy for long volatility players who seek to minimize potential losses in the event the stock moves adversely.

The strategy can be broken down viewed as two trades. In the case of a traditional condor, the position can be broken down into two conflicting vertical spreads, one long, and one short.

The Iron Condor can be broken down to a long interior strangle surrounded by a short exterior strangle. Condors are best entered into in further out months.





## ***About the Author***

**Larry Gaines, Founder**

[Options On the Open.com](http://www.OptionsOnTheOpen.com)

*'The Leader in Options Day Trading'*

Larry Gaines has been involved in trading and brokering commodities and financial markets for over twenty-five years.

He started his career trading tanker cargoes of foreign crude oil for a large independent oil company in the 80's. He quickly advanced his career to become an Executive Vice President of one of the largest international oil trading companies in the world.

In this position he managed their international oil trading and marketing for over ten years from their corporate office in Bermuda. During his tenure he traded and managed billions of dollars worth of oil, foreign exchange and financial market derivatives.

His trading group was one of the first to trade over the counter options on cargoes of foreign crude oil and traded millions of barrels of north sea Brent crude oil options.

He has been involved with a number of hedge funds on a consulting basis and in 2009 set up an over the counter crude oil options brokerage desk for the world's largest privately owned oil brokerage company.

Today, Larry trades options and futures and is the founder of Options on the Open, an options day trading site, which he established so he could share his years of trading knowledge and experience to teach its members how to achieve higher trading profit margins with smaller capital investments using options.

Larry lives in the Texas Hill country with his wife, two teenage boys and his yellow Lab.

