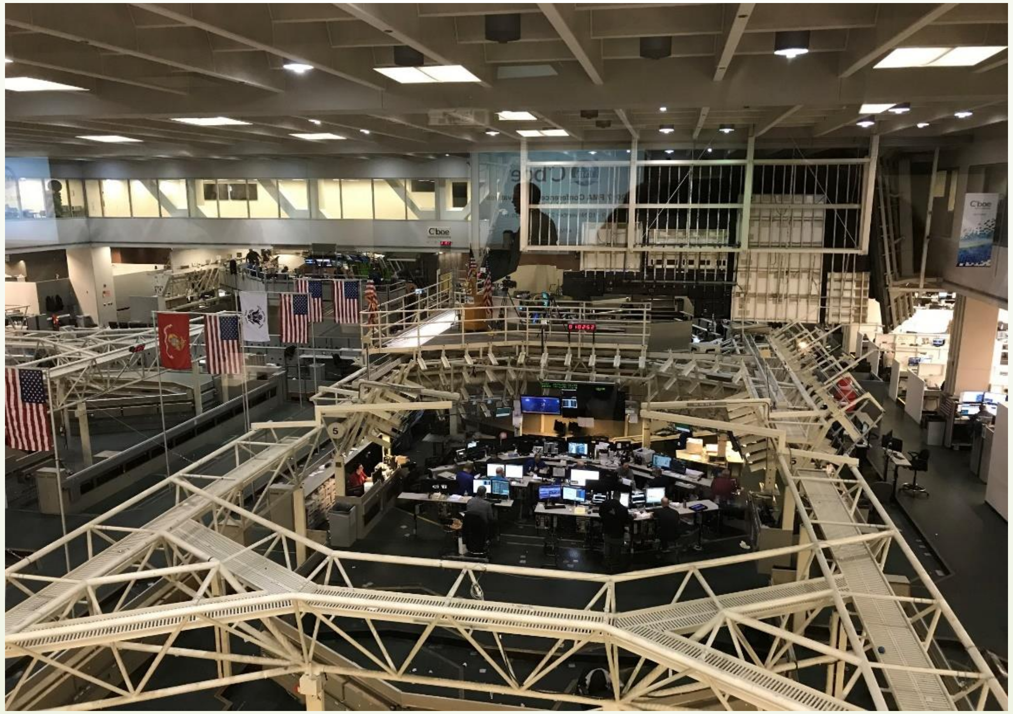
AAII San Diego Options Trading

https://aaiisandiego.com/sub-groups/options-trading/



Comments:

- The analysis is certainly not perfect … there was a lot of trading over the years
- Classification of trades is *really* not perfect:
  - Some trades start out as purely directional calls … then I later sold OTM calls on the position … then included puts when uncertainty increased etc.
- I've kept some details e.g. dollar amounts out for some privacy. Results are discussed per contract
- I tracked performance 'by trade'. A 'trade' sometimes goes on for many months, even multiple years, and sometimes has dozens of transactions involved

Key takeaways:

- I need to keep track of my trading better!
- 15.2% average annual return since 2012 after fees, commissions and (most) taxes (S&P 500 +- 10.5%)
- Clear evidence that I've become better at this over time
  - Hang in there!
  - Trading is a skill that can be learned like many other things. (In terms of technique, controlling behavioral mistakes. I don't think I've necessarily become better at guessing where prices are going!)
- I've certainly kept my broker and the Internal Revenue Service happy!
  - ...but, very difficult to change this when trading relatively often and short-term

Key takeaways:

- One specific strategy has worked very well for me, consistently well over time:
  - Debit spreads
  - By far my most consistent money maker
- Highly versatile strategy
  - …which also makes it complicated, and not very easy to describe in a ‘paint by numbers’ way

Trade categories

Long call: bullish, speculative. Includes synthetic stock trades.

Covered call: own asset, write call options

Dr spreads: buy one call (C1), sell another (C2), \$C1 > \$C2

Long straddles: buy call, buy put. Includes butterflies, or variations of butterflies (unbalanced, different expiries)

Put writes: selling OTM puts on asset

Long put: bearish, speculative.

Prot. Puts: buying of puts on existing positions to protect the downside (*not* bearish)

Cr spreads bear: buy one call (C1), sell another (C2), \$C1 < \$C2. Profits if price does *not rise above* certain price level.
Cr spreads bull: buy one call (C1), sell another (C2), \$C1 < \$C2. Profits if price does *not fall below* certain price level.

Short straddles: sell call, sell put. Includes strangles, iron condors.

Trade categories

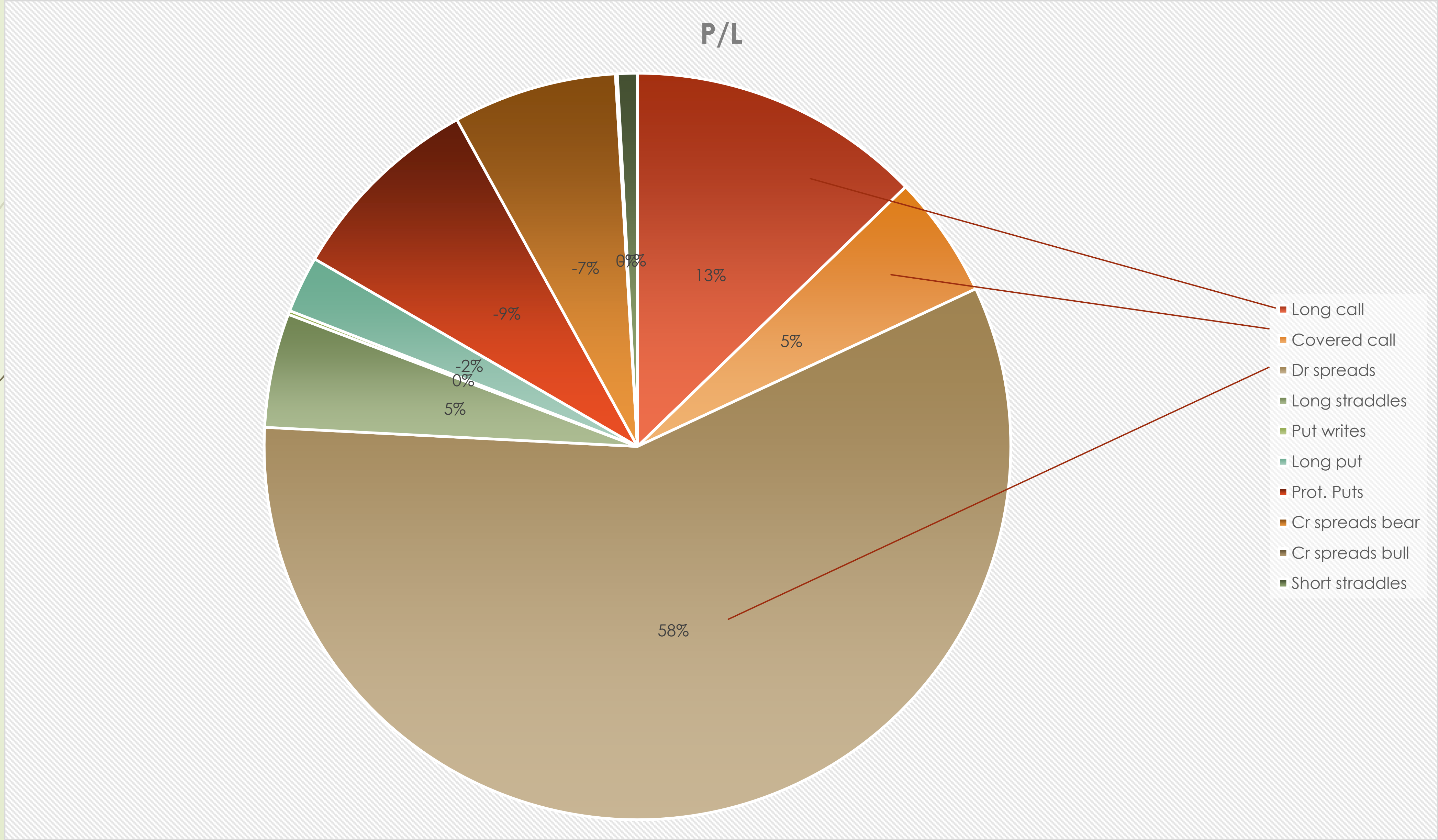
Paying for premium (time value decay hurts):

- Long call
- Debit spread (*time decay not always negative)
- Long straddle
- Long Put
- Protective put

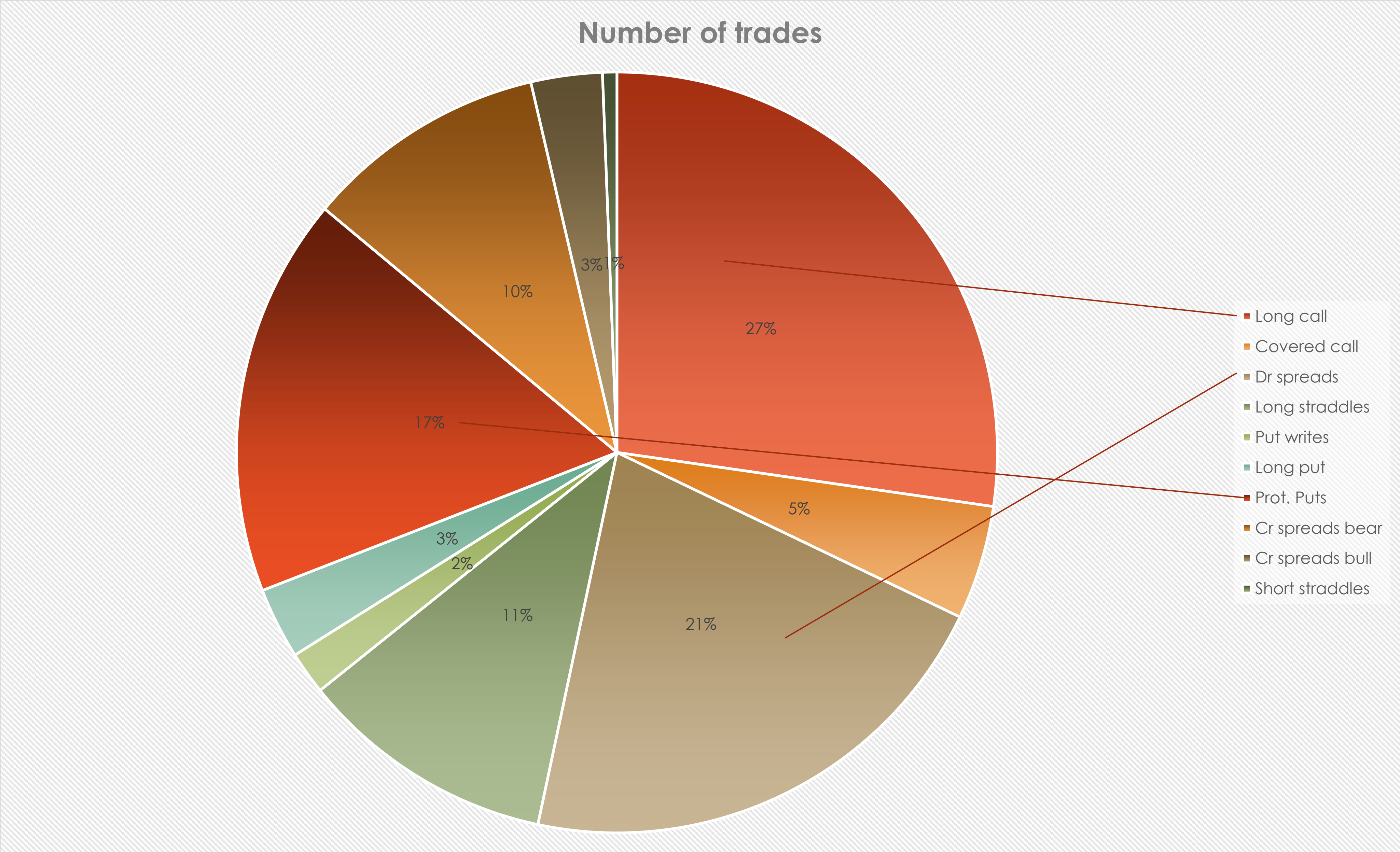
Receiving premium (time value decay is good):

- Put writing
- Credit spreads
- Short straddles
- Covered call

% P/L by strategy

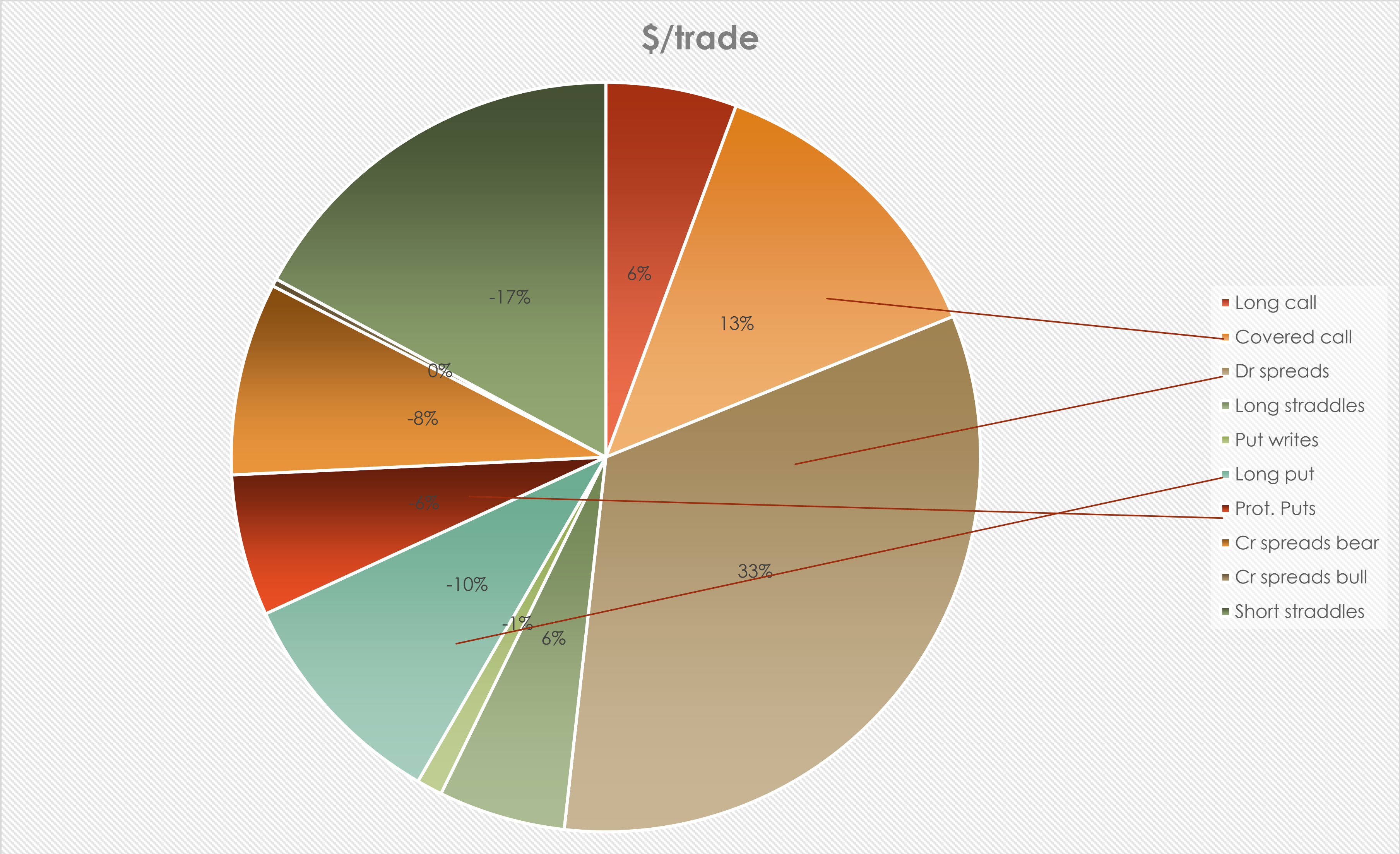


Number of trades

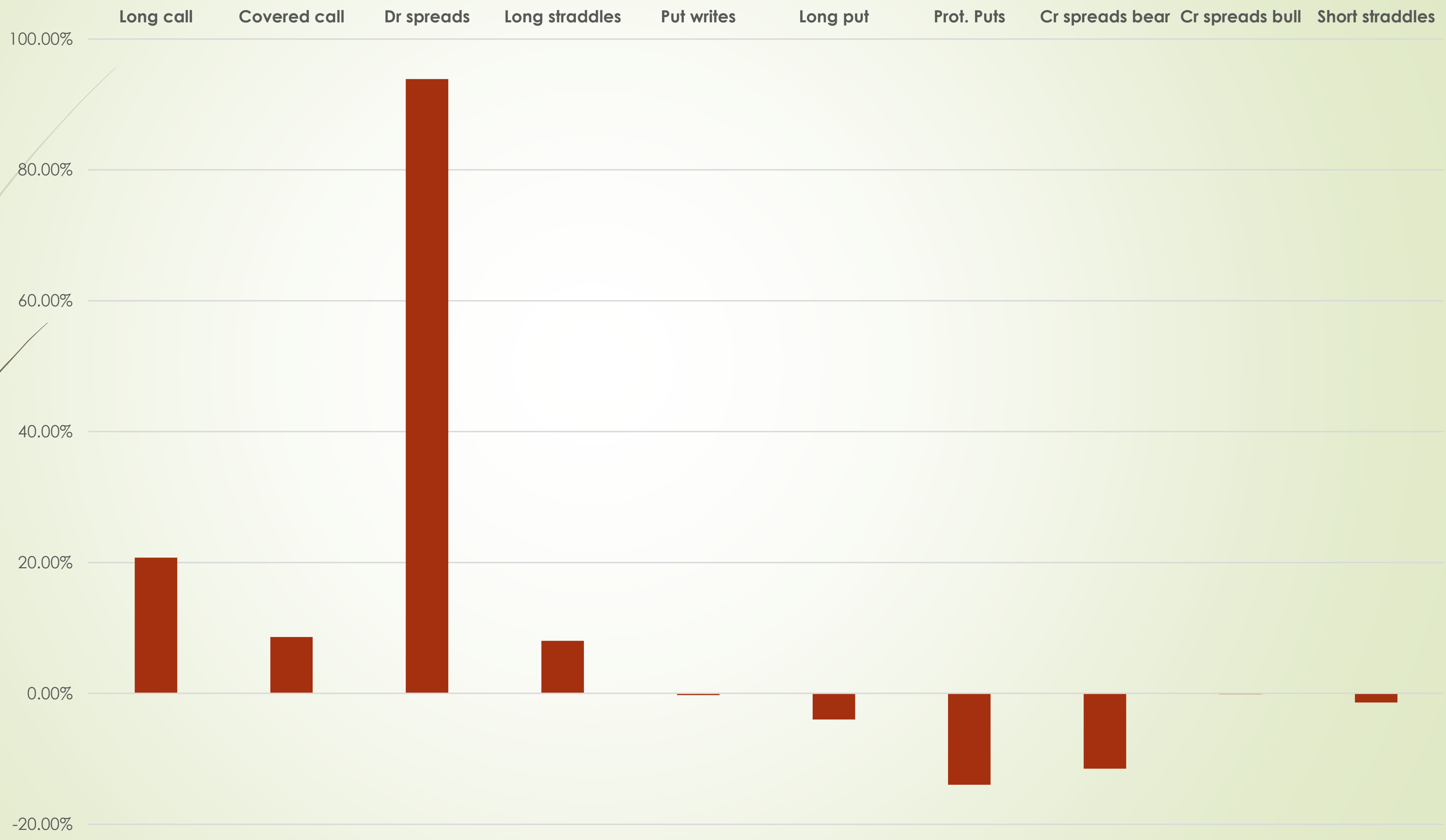


$ P/L by strategy

(to account for some strategies being used more than others)



% P/L by strategy



$ P/L by trade

Long call
Covered call
Dr spreads
Long straddles
Put writes
Long put
Prot. Puts
Cr spreads bear
Cr spreads bull
Short straddles
500.00%
400.00%
300.00%
200.00%
100.00%
0.00%
-100.00%
-200.00%
-300.00%

The most consistently profitable trade:

- Calendar spread
  - Buy *long-dated ITM* call option (on SPX, AMZN, others)
  - Sell *short-dated OTM* call option
    - Roll over the OTM call when it comes up to expiry

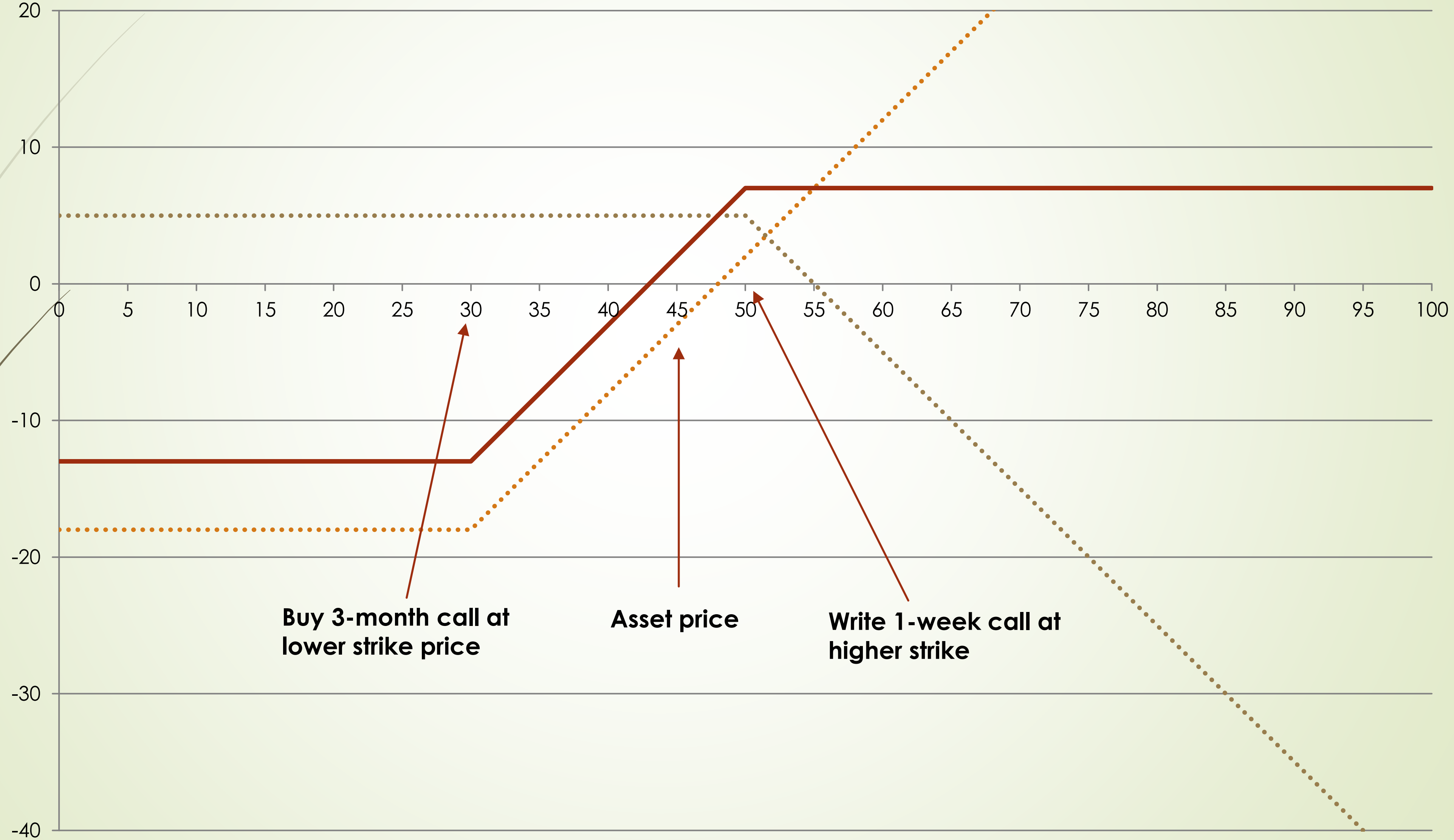
- The concept:
  - Profit from increase in price of asset
  - Write OTM options to help cover the time value cost of buying the call
  - Multiple call options over a period of time likely to have more time value than one call option which covers the entire time period
  - Allows flexibility to add puts for protection, or OTM put spreads (cheaper)
    - Some versions of this trade have involved dozens of instances of rolling over the short position and/or rolling up the long position
  - Does not require a high win rate to have overall success
    - Although writing the OTM contracts can cap the profits, generally the positive asymmetry of owning calls is maintained

- Other flexibility:
  - Unbalanced:
    - For example, buy 5 contracts of the ITM calls, sell 4 contracts of the OTM calls
    - Allows 1 or more contract to "run free" if there is a large runup in the price of the asset
      - (1 or more contract not capped)
- Caveats:
  - This timeframe has been an overall bull market, so a bullish direction strategy should have made money
  - A lot of investments look good during a sustained bull market!


S&P 500 (^GSPC)
SNP - SNP Real Time Price. Currency in USD
3,009.05 -74.71 (-2.42%)
At close: June 26 5:24PM EDT
Indicators
Comparison
Date Range
1D 5D 1M 3M 6M YTD 1Y 2Y 5Y Max
Interval 1W
Line
Draw
^GSPC 3041.310
yahoo!finance
3009.050
27.87B
3,250.000
2,750.000
2,500.000
2,250.000
2,000.000
1,750.000
1,500.000
1,250.000
2013 2014 2015 2016 2017 2018 2019 2020
MSFT

The most consistently profitable trade:

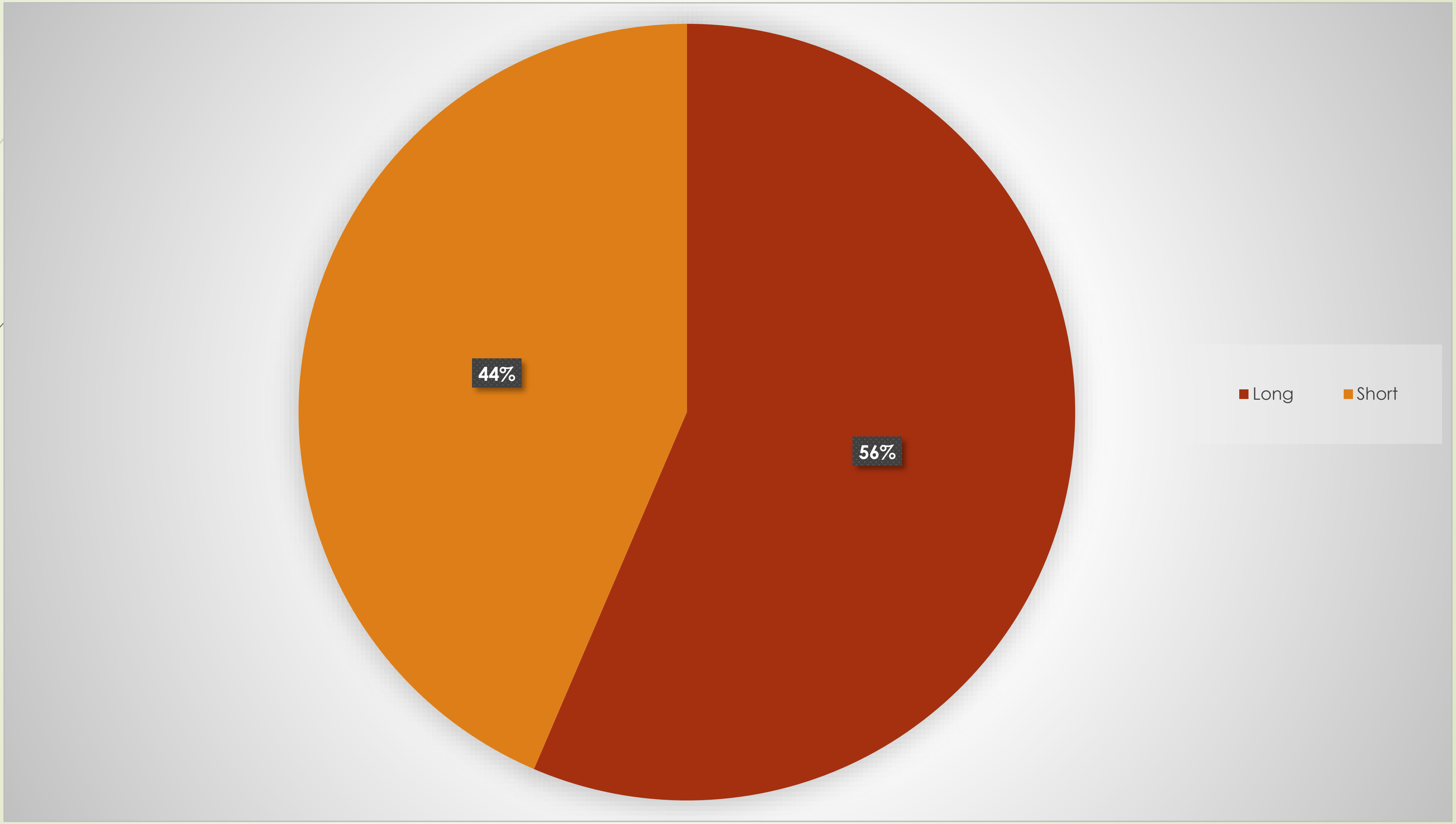
- Illustration of setup:



Best to worst: debit spread trades

- Win rate 18/35
- …but wins > losses when they happen
- Cut losses, let profits run ***really*** important

Long versus short



Lessons:

- Keep track of trading more closely as it's actually happening!
- My view:
  - Trades that are motivated as *directional* or long volatility work out better
  - Trades which are short volatility are a difficult way to make money, even though they seem to be incredibly popular in training seminars etc.
  - Short volatility: iron condors, OTM credit spreads etc. require routinely being better than the market at judging where prices will or won't move to. I think this is extremely difficult to get consistently correct
  - Directional trades, on the other hand, can be profitable even with a relatively low win rate, even below 50%. Therefore, there's no requirement to know more, or be better than, the market.
  - Keep the number of underlyers you have to follow to a minimum. Really get to know the nature of the assets: what price levels are common, feasible etc.
  - Main skill required for directional trading is tolerance for volatility … this is something that can become stronger with experience

Lessons:

- My impression is that most training programs for options trading actively discourage buying options/paying premium
- For me, it's worked out well
- Things to avoid:
  - Buying put options
  - Buying short-dated, OTM calls (this is definitely a loss-making proposition!)
  - Holding options too close to the expiry date
    - Time value becomes quite erratic close to expiry
    - Contracts become illiquid, bid-ask spreads widen
    - I've found it best to close or roll over a long position 25 to 30 days ahead of expiry
- It does require strong price movements to make money. Modest price increases of 3 to 5% often don't make money.