

Disclaimer



The views and opinions expressed in this presentation reflect those of the individual authors/presenters only and do not represent in any way Bourse de Montréal Inc.'s (the "Bourse") opinion or any of its affiliates. The presentation is not endorsed by the Bourse or its affiliates. The information provided in this presentation, including financial and economic data, quotes and any analysis or interpretation thereof, is provided solely on an information basis and shall not be interpreted in any jurisdiction as an advice or a recommendation with respect to the purchase or sale of any derivative instrument, underlying security or any other financial instrument or as a legal, accounting, tax, financial or investment advice. The Bourse and its affiliates do not endorse or recommend any securities referenced in this presentation. The Bourse recommends that you consult your own advisors in accordance with your needs. Although care has been taken in the preparation of these articles, the Bourse and/or its affiliates do not guarantee the completeness of the information contained in this presentation, and are not responsible for any errors or omissions in or your use of, or reliance on, the information. The Bourse reserves the right to amend, review or delete, at any time and without prior notice, the content of this presentation. The Bourse, its affiliates, directors, officers, employees and agents will not be liable for damages, losses or costs incurred as a result of the use of any information appearing in this presentation.

"S&P ®" and "Standard & Poor's ®" are registered trademarks of The McGraw-Hill Companies, Inc. and "TSX" is a trademark of TSX Inc. ("TSX"). The products mentioned in this presentation are not sponsored, endorsed, sold or promoted by S&P or TSX; and S&P and TSX make no representation, warranty or condition regarding the advisability of investing in them.





TMX

**Montréal
Exchange**



TMX | **Montréal
Exchange**



**Montréal
Exchange**

Selling Call Options



Toronto Stock Exchange | TSX Venture Exchange | **Montréal Exchange** | Natural Gas Exchange | Montréal Climate Exchange | Boston Options Exchange

Canadian Derivatives Clearing Corporation | TMX Datalinx | Equicom | PC Bond | Shorcan

Why Sell Call Options?



- Generate additional income.
- Profit from range-bound or bearish stocks.
- Use to exit a stock position.
- Hedge immediate downside risk in a stock.



Selling Covered Calls



- The option seller owns the stock.
- Obligated to sell that stock to the option buyer.
- Assumes the risk associated with the stock ownership.



Selecting Strike Prices



- In-the-money strikes:
 - Composed of both intrinsic and time value.
 - The intrinsic value is downside protection.
 - The deeper in-the-money, the more downside protection.



Selecting Strike Prices



- At-the-money strikes:
 - The stock price equals the strike price.
 - Made up entirely of time premium.
 - Achieve the greatest static return.



Selecting Strike Prices



- Out-of-the-money strikes:
 - Leave upside potential for stock up to the strike price sold.
 - Smaller premium.
 - Better potential return if the stock moves higher.



Selling Covered Calls



- XYZ is trading \$50.00
- 2-month call options with a strike price of \$50.00 are listed at \$2.50.
- Investor buys or already owns 1,000 shares of XYZ.
- Investor sells 10 call options and creates a cash flow of \$2,500.00.



Selling Covered Calls



Stock Price at Expiration	Profit / Loss
\$58.00	\$2,500.00
\$52.00	\$2,500.00
\$50.00 Strike	\$2,500.00
\$48.50	\$1,000.00
\$47.50	Break Even
\$46.00	- \$1,500.00
\$40.00	- \$7,500.00

Start Price →



Selecting Strike Prices



Call Option Strike Price	Call Premium	Adjusted Cost Base	Cash Flow Return
\$54.00	\$1.00	\$49.00	2.04%
 \$50.00	\$2.50	\$47.50	5.26%
\$46.00	\$5.00	\$45.00	2.22%

* Returns calculated using the adjusted cost base as the common denominator.



Covered Calls as an Income Strategy



- By selecting the at-the-money call option, \$2,500.00 in real cash flow was created.
- 5.26% cash flow in 2 months.
- Reduced the cost base of the investment.
- The covered call writer gives up profiting on share ownership above the \$50.00 strike price.

* Returns calculated using the adjusted cost base as the common denominator.



Covered Calls as an Exit Strategy



- To sell underlying shares at a target price.
- Reduces the cost base of the investment.
- Difficult to adjust the target once the strategy is in place.



Covered Calls for Hedging Risk

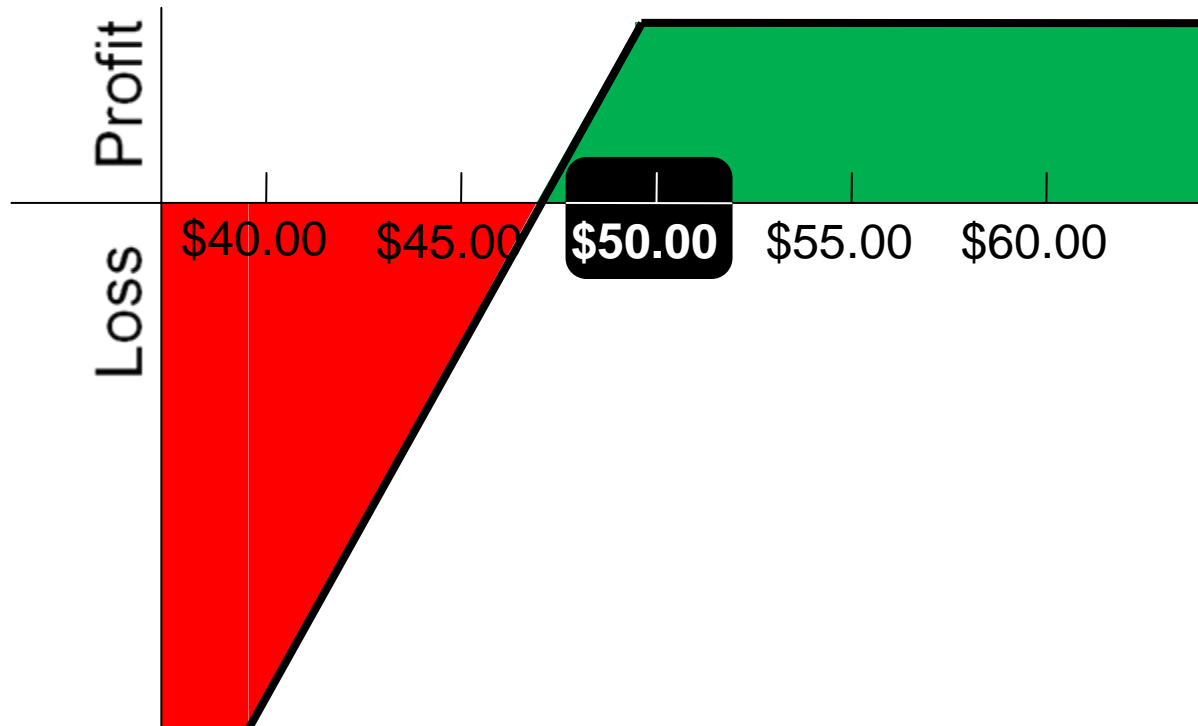


- If market weakness or little upside potential on a stock is anticipated.
- Reduces the cost base of the investment without selling the underlying stock.
- The deeper in-the-money, the more intrinsic value is captured to hedge the downside.



Synthetic Positions

Long Stock + Short Call = Short Put



Selling Naked Call Options



- The option seller does not own the stock.
- Is obligated to sell that stock to the option buyer.
- Creates an undefined risk.
- Risk profile similar to short selling a stock.



Naked Call Options



- XYZ is trading \$50.00.
- 2-month call options with a strike price of \$52.00 are trading at \$2.00.
- Investor sells 10 call options, collecting \$2,000.00.
- Does not own the shares - marked as naked.



Naked Call Options



Stock Price at Expiration	Profit / Loss
\$60.00	-\$6,000.00
\$58.00	-\$4,000.00
\$56.00	-\$2,000.00
\$54.00	Break Even
\$52.00 Strike	\$2,000.00
\$50.00	\$2,000.00
\$48.00	\$2,000.00
\$46.00	\$2,000.00

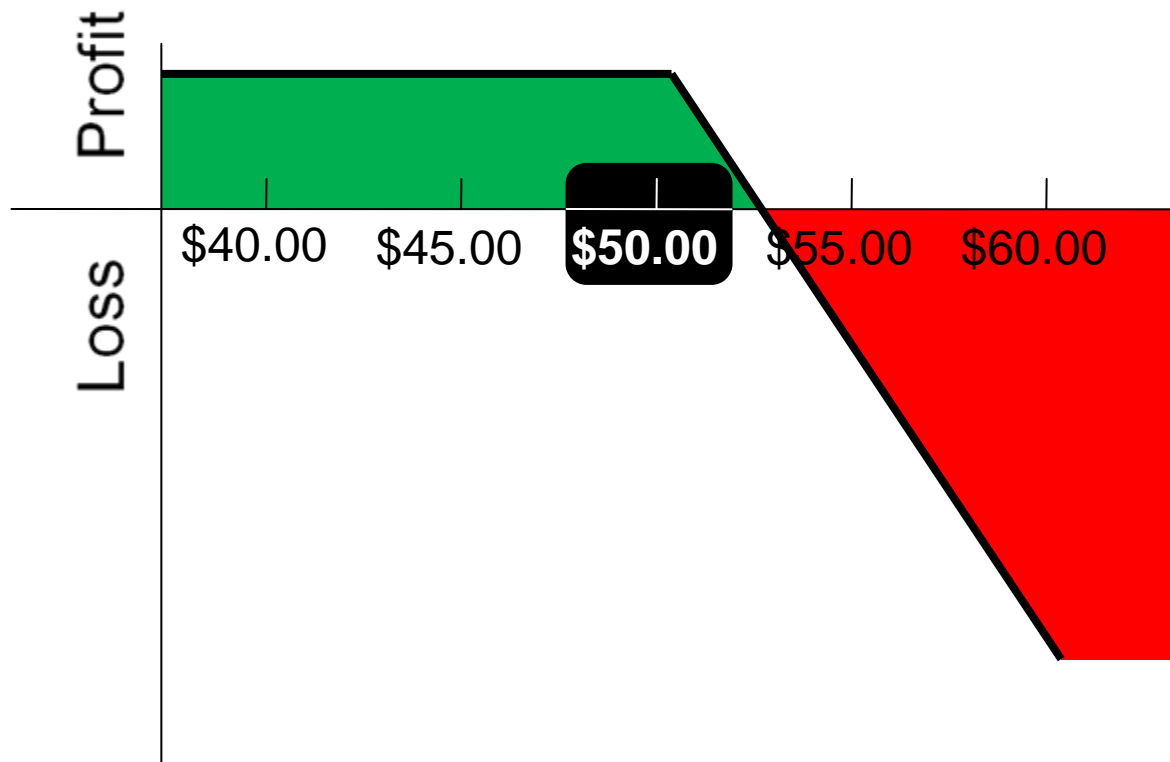


Start Price



Synthetic Positions

Short Call = Short Put + Short Stock





Jason Ayres, President
Optionsource.net

