thinkMoney/24

random musings for traders at TD Ameritrade
Summer 2014

18/VOLATILITY'S LITTLE SECRET

24/HOW TO NEUTER YOUR TRADE

CHARTING FOCUS
32/CHARTS THAT RULE THE WORLD

10/**TIPS FOR TRADING WITH YOUR GUT**

TD Ameritrade

(See page 9 for details)

Contents

Photograph by
Fredrik Brodén

p. 10

Trading With A Sour Stomach
In bull markets, sometimes logic goes out the window. So the next time your gut is telling you to get into a trade despite your rules, pick a strategy that tempers your enthusiasm.

07 cont.

Contents

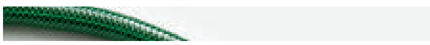
Cover photograph by
Fredrik Brodén

tdameritrade.com

Features

10/ Trading With A Sour Stomach
No matter how many rules you strictly follow, there's going to come a time when you just have to trust your gut on a bullish trade. But depending on how confident you are, you can tweak the downside risk to help you sleep better.

18/ News For Show, Vol For Dough
Headlines may come and go. But the volatility resulting from headlines is what can matter most to traders. And before you write off higher-volatility markets, here's a little secret you ought to know.



24/ How To Neuter Your Trade
At some point you may have heard an option trader boast about being a "delta neutral" or "market-neutral" trader. But what do these terms mean and are they really useful? Let's put the debate to rest.

32/ Special Focus: Charting for Everyone
CHARTS THAT RULE THE WORLD
No doubt you can find lots of charting programs out there. But seriously, why look further? Other than a back massage, thinkorswim® Charts can give you almost anything you need—even if you're not a chart reader.

PLUS:
THINKORSWIM CHARTS Q+A

Columns

16/News + Views
Retail options trading is caught in the crossfire of Congressman Camp's tax proposal. Should you be worried?
+ Ask the Suit

38/Capiche?
If you're buying ETFs that track futures like oil and volatility, beware of the "rolling penalty" that could be stealing your profits.

22/Evolution of the Trader
If you thought trading started under a buttonwood tree, you'd be wrong. Think monkeys, Darwin, and opposable thumbs.

40/Ask the Trader Guy
Our resident guru responds to why all options aren't created equal, how to size up your vertical spread, and false promises from a dumb clairvoyant.

28/Gear Head
Today's cool tool two-fer: A Dow-to-gold script from TD Ameritrade's "Mr. Script" and how to share a chart with your loved ones.

31/The Spotlight
Fun guy Mike Barwacz is making sure your Trading Desk confidant at TD Ameritrade has what it takes to answer your tough questions. And he can show you a good time doing it.

Miscellaneous

08/A Quick Howdy

15/Love Notes

42/The Token Glossary

TD Ameritrade Contact Info You Could Use
Client Services Representative: 800-669-3900
New Accounts: 800-454-9272

thinkorswim Support:
800-672-2098
thinkorswim@tdameritrade.com
Platform Feedback:
thinkorswimfeedback@tdameritrade.com
Tech Support:
thinkorswimtechsupport@tdameritrade.com
paperMoney Support:
thinkorswimpapermoney@tdameritrade.com
For all other inquiries:
tdameritrade.com/contact-us

General Mailing Address
200 S. 108th Ave
Omaha, NE 68154

Follow TD Ameritrade

And follow thinkorswim on Twitter, too:
@thinkorswim

BACK ISSUES OF THINKMONEY!
To view past issues of thinkMoney, hop on over to tdameritrade.com/thinkmoney. You'll be glad you did.

edit

A Quick Howdy

tdameritrade.com

thinkMoney®

EDITOR-IN-CHIEF
Kevin Lund

EDITOR
Thomas Preston

ASSISTANT EDITOR
Eileen Sutton

ART DIRECTOR
Tom Brown

DESIGNER
Jennifer Roberts

CONTRIBUTING WRITERS
Nicole Sherrod
John Brodemus
Chesley Spencer
Kira Brecht
Greg Loehr
David Kier

CHIEF PHOTOGRAPHER
Fredrik Brodén

CONTRIBUTING ILLUSTRATOR
Joe Morse

PUBLISHER
T3 Custom
Email: info@t3publishing.com
www.t3publishing.com

GOT FEEDBACK?
Talk to us about thinkMoney! Take our survey and you'll qualify for infinite brownie points. tdameritrade.com/tmsurvey or write to us at thinkmoney@tdameritrade.com

PHOTOGRAPH: FREDRIK BRODÉN

Me Go Trade

Let's face it. No matter how impressively automated your trading system is—custom scans, charts, half-eaten Twinkies—at the end of the day, it's really an educated guess where the stock you're coveting is going next. Though your indicators all point to up or down, you don't really know for sure—which means your level of confidence in the trade sits on a spectrum. Of sorts. In other words, it's more of a data-driven gut feeling that ultimately drives your decisions.

You may know which stock you want to trade. But choosing the right option strategy could make a huge difference in your probability of success, depending on how confident you are. And this is where gut meets science. In this month's cover feature, "Trading on a Sour Stomach" (page 10), we'll show you whether the difference between feeling a "sure thing" or just "meh" could dictate which strategy you may want to consider for a given trade.

But suppose you don't already have a system, and you're just discovering the thinkorswim® trading platform for the first time. Continuing our Special Focus on the finer tools of the platform, we'll dive into thinkorswim Charts (starting on page 32). Serving up nothing less than the kitchen sink, the Charts page has tools from which even the "I don't use charts" trader could benefit.

And of course, after you've pulled the trigger and entered a trade, at some point, you'll find yourself in one of two situations—facing a loss or staring at a profit—and not sure what to do next. "How to Neuter Your Trade" on page 24 is a must-read for you nail-biters that could provide some relief.

It's been said that trading can be traced back to our simian ancestors. As Trader Erectus once wrote on his cave wall while contemplating his next Paleo snack, "mmfph"—which was later translated to "Buy sparingly and sell often." We agree.

Happy trading!

Kevin Lund,
Editor-in-Chief, *thinkMoney*

1

important info

• Options transactions involve complex tax considerations that should be carefully reviewed prior to entering into any transaction.

• The risk of loss in trading securities, options, futures and forex can be substantial. Clients must consider all relevant risk factors, including their own personal financial situations, before trading. Options involve risk and are not suitable for all investors. See the Options Disclosure Document: Characteristics and Risks of Standardized Options. A copy accompanies this magazine if you have not previously received one. Additional copies can be obtained at tdameritrade.com or by contacting us.

• Trading foreign exchange on margin carries a high level of risk, as well as its own unique risk factors. Before considering trading this product, please read the Forex Risk Disclosure, available at http://www.nfa.futures.org/NFA-investor-information/publication-library/forex.pdf.

• A forex dealer can be compensated via commission and/or spread on forex trades. TD Ameritrade is subsequently compensated by the forex dealer.

• Futures and forex accounts are not protected by the Securities Investor Protection Corporation (SIPC).

• The information presented in this publication does not consider your personal investment objectives or financial situation; therefore, this publication does not make personalized recommendations. This information should not be construed as an offer to sell or a solicitation to buy any security. The investment strategies or the securities may not be suitable for you. Any and all opinions expressed in this publication are subject to change without notice.

TD Ameritrade, Inc. Member SIPC FINRA NFA

2

• Neither Investools® nor its educational subsidiaries nor any of their respective officers, personnel, representatives, agents or independent contractors are, in such capacities, licensed financial advisors, registered investment advisors or registered broker/dealers. Neither Investools nor such educational subsidiaries provide investment or financial advice or make investment recommendations, nor are they in the business of transacting trades, nor do they direct client futures accounts nor give futures trading advice tailored to any particula r client's situation. Nothing contained in this communication constitutes a solicitation, recommendation, promotion, endorsement or offer by Investools or others described herein, of any particular security, transaction, or investment. Investools Inc. and TD Ameritrade, Inc. are separate but affiliated companies that are not responsible for each other's services or policies.

3

Transaction costs (commissions and other fees) are important factors and should be considered when evaluating any options trade. For simplicity, the examples in these articles do not include transaction costs. At TD Ameritrade, the standard commission for online equity orders is $9.99, online option orders are $9.99 + $0.75 per contract. Orders placed by other means will have higher transaction costs. Options exercises and assignments will incur a $19.99 commission.

4

TD Ameritrade was evaluated against 19 others in the 2014 Barron's Online Broker Review, March 15, 2014, and was awarded 4.5 stars overall (along with 3 others). The firm was ranked 1st in the categories "Best for Long-Term Investing" and "Best for Novices." TD Ameritrade was also among those listed in the categories Best for Frequent Traders (ranked 4th), Best for Options Traders (ranked 2nd) and Best for In-Person Service (ranked 5th). Star ratings are out of a possible 5. Barron's is a trademark of Dow Jones. L.P. All rights reserved.

10

Gut-Trading Strategies

tdameritrade.com

TRADING WITH A SOUR STOMACH

IN THE WORLD of numbers and analysis, a gut feeling can seem squishy and out of place. But with trading and investing, there's no denying that our gut instinct can often help. It can make us confident or wary, no matter the analysis we used to determine a bullish or bearish directional bias. And for the record, it's not that our analysis is wrong. It's just that our gut remembers past winners and losers and a different part of the brain engages. It's right brain vs. left brain. In a word, our gut can provide a reality check. ● Now, some traders might use their gut as a "go, no-go" indicator. The "go" is all in with long stock, for example. The "no-go" is sit on your hands and do nothing. But there's a smarter approach that may help fine-tune your trading instincts. Figure out whether your gut is making you slightly confident, semi-confident, or very confident in your bias. Let's look at a few bullish strategies that may match what your gut might suggest. →

WORDS BY **THOMAS PRESTON**

NO MATTER HOW MANY TRADING SYSTEMS YOU TRY, THERE'S GOING TO COME A TIME WHEN YOU JUST HAVE TO TRUST YOUR GUT ON A BULLISH TRADE. BUT DEPENDING ON HOW CONFIDENT YOU ARE, YOU CAN TWEAK THE DOWNSIDE RISK TO HELP YOU SLEEP A LITTLE BETTER AT NIGHT.

12

Gut-Trading Strategies

Photograph by **Fredrik Brodén**

tdameritrade.com

THE SORT-OF-CONFIDENT BULLISH TRADE

SHORT, OUT-OF-THE-MONEY PUT VERTICAL

When looking at a stock, you might believe it will go up—at least that's what your analysis is telling you. But your gut isn't quite as psyched about it. It's telling you that the stock might not go up, and might drop. Since the out-of-the-money (OTM) put vertical has a defined max loss and defined max profit, it might be an appropriate strategy when you're sort of confident in the direction you think the underlying will go.

A bullish short OTM put vertical is made up of a short OTM put, and a long OTM put that's further OTM than the short put. This trade is designed to produce a credit, which is the max profit the trade can make(less transaction costs). The max loss is the difference between the strikes minus that credit (plus transaction costs).

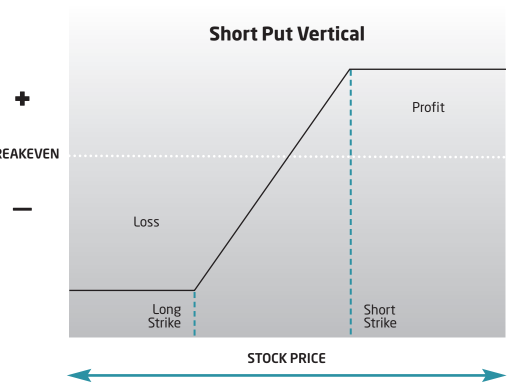


FIGURE 1: Short OTM put vertical. A smaller potential reward with higher probability of success than long verticals, when you're feeling so-so about the direction of the underlying. *For illustrative purposes only.*

What the short OTM put vertical does is potentially profit not only if the stock rallies, but also if it sits at its current price, or even drops a bit. More than a bit would mean the stock drops below the short strike plus the credit received, in order to incur a loss. As long as the price of the stock is higher than the strike price of the short put at the expiration of the options, this position can be profitable. A long stock position, for example, can't do that. If the price of the stock doesn't go up, or drops, the long stock position isn't profitable (not counting possible dividends). The short put vertical can also have a lower margin requirement than long stock. That means you don't need to tie up a lot of your trading capital in a sort-of-confident trade.

THE SEMI-CONFIDENT BULLISH TRADE

NAKED, SHORT OUT-OF-THE-MONEY PUT

Huh? a naked short option if you're only semi-confident? That may sound risky, but hey, at *thinkMoney*, we don't flinch. A short OTM put takes in a credit (the premium received for selling the put), which is its max potential profit (less transaction costs). The max potential loss is the strike price of the put minus the credit you realize for selling it. That's the loss that would occur if the price of the stock goes to zero. And it's that large potential loss that might be raising eyebrows for the semi-confident trader. The strategy also includes a high risk of purchasing the underlying stock at the strike price when the market price of the stock will likely be lower.

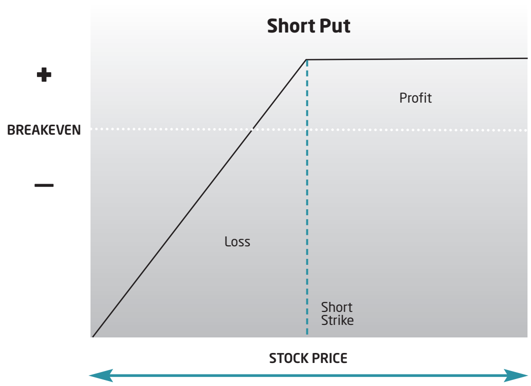


FIGURE 2: Short OTM put. Wee bit bigger potential reward, lots more risk. Still a higher probability of success than a long vertical position, since you could potentially make money even if the stock stands still. *For illustrative purposes only.*

But think about it. The short put has no more risk than long stock. The losses for both are large if the price of the stock drops sharply, let alone goes to zero. But here's an advantage for the short OTM put—the price of the stock can sit where it is, or even drop a bit by expiration, and the short OTM put can still be profitable. Long stock can't do that (save, for possible dividends). A short OTM put also has no greater margin requirement than long stock. In a margin account, the margin on a short put can be lower than on long stock, and in an IRA, the margin on a cash-secured short-put position and a long stock position can be roughly the same.

The short OTM put and the short OTM put vertical share some characteristics. So, what makes the short OTM put the choice for the semi-confident trade? The short OTM put can have a higher credit than a short-put vertical, and thus larger potential profit. If the short put of the short-put vertical and the short put are at the same OTM strike price and same expiration, the credit for the short OTM put vertical will be lower than the credit for the short-put. The difference is the cost of the long-put component of the short-put vertical. The short put gives you potentially more profit than a short-put vertical in exchange for a higher margin requirement and higher potential risk. That's why it may be a choice if you're a bit more confident in your bullish bias.

SEE GLOSSARY
PAGE 42

BEFORE YOU GUT
Find trades your gut feels good about. Fire up thinkorswim's "MOST ACTIVES" lists to get some ideas.
From the MarketWatch tab, go to the Quotes sub-tab. Click the little gear icon to the far right to see a menu of predefined lists, such as "Lovers and Losers" and "Top 10," featuring the day's hits and misses.

THE CONFIDENT BULLISH TRADE

LONG, AT-THE-MONEY CALL VERTICAL

A long at-the-money (ATM) call vertical could be the choice as a "very confident" trade. A bullish long ATM call vertical is made up of a long slightly, in-the-money (ITM) call and a short OTM call in the same expiration. You pay a debit when you do this trade, and the debit of the long ATM vertical is its max possible loss. The max potential profit is the difference between the strike prices, minus the debit paid, including transaction costs, and occurs when the stock price is higher than the strike price of the short OTM call at expiration. That means the price of the stock has to go higher for the ATM vertical to profit. It can't just stay at the same price or drop, like it can for the short OTM put, or short OTM put vertical. If the stock drops, the long ATM vertical will likely lose some money, and the max loss happens when the price of the stock drops below the strike price of the long call at expiration.

The long ATM call vertical may be a confident choice because it can have a higher delta than an OTM short put vertical, or even a short put—meaning, it can be more responsive to a rise in the stock price. But if you're so confident, why not just buy stock, or a long call for that matter? Neither caps your upside potential, so why choose it?

Compared to long stock, the long ATM call vertical can have less potential risk, for one. Nothing is guaranteed to go higher. If the stock does drop sharply, the loss on the long stock can be much greater than on the long vertical. Also, the long ATM call vertical can have a lower margin requirement than long stock. That means that you tie up less of your trading capital with verticals.

Compared to a long call, the long ATM vertical can be less sensitive to changes in volatility (vega) and time (theta), because the vertical has both a long and short option in it. The negative vega in the short option offsets the positive vega in the long option, resulting in a net-lower vega than a single long option. Likewise, the negative theta of the long option is offset by the positive theta of the short option, resulting in a net-lower time decay than a single long option.

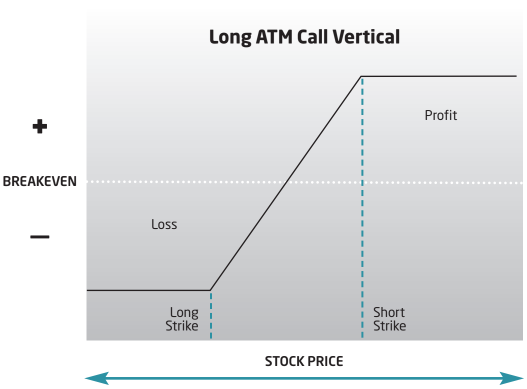


FIGURE 3: Long ATM call vertical. The lowest probability of success among the three strategies discussed here, but the greatest possible reward when you're feeling warm and fuzzy about the direction of the trend. *For illustrative purposes only.*

Important Information
Naked option strategies involve the highest amount of risk and are only appropriate for traders with the highest risk tolerance. Spreads and other multiple-leg option strategies can entail substantial transaction costs, including multiple commissions, which may impact any potential return. Supporting documentation for any claims, comparison, statistics, or other technical data will be supplied upon request.

THE KEY IS UNDERSTANDING THAT YOUR GUT drives strategy, not trade size. The smart way to implement confident analysis is with a strategy that not only reflects that confidence, but also can have lower risk, lower margin requirements, and opportunity to profit if you're directional bias proves wrong. Remember, your gut gets you in the game. Your brain hopefully gets you paid.

Access granted.

Get an exclusive look into how "The Suit" uses thinkorswim.

With the new sharing feature in thinkorswim, you'll discover how our experts use the platform and which tools they rely on most. You can also generate new ideas and share your platform setup with friends, followers, and the myTrade® community.

TD Ameritrade

Explore thinkorswim sharing:
tdameritrade.com/shareyourtos

15

Love Notes

lttrs.

Sweet tweets and quick quips from all of us

Photograph by **Fredrik Brodén**

Follow the "experts" on Twitter for all things markets, trading, and thinkorswim:
@TDANSherrod
@TDAJJKinahan
@thinkorswim

THE TWEETS

• **@TDANSherrod:** Today I'm working on our 2015 Strategic Plan. And I'm putting the things that my Twitter followers ask for FIRST.

• **@NewShoesHere:** Does the Strategic Plan include how to play pocket Aces under the gun? ☺

• **@TDANSherrod:** No but it does include a new tab called "High Probability Racehorse Handicapping."

• **@MichaelComeau:** Please add Pac-Man to the thinkorswim platform. I will trade more, I swear.

• **@TDANSherrod:** We already have Tetris. And Mine Sweeper.

• **@MichaelComeau:** Yes—but Pac-Man is a must. Come on, I'm not asking for Ms. Pac-Man here.

• **@panthersfan1234:** @JaviFusco Since you made it into a magazine, now you're never gonna shut up. Thanks a lot, @TDANSherrod… :D

DA QUIPS

• *On trading vanity*
It is quite possible that I just might be the best looking day-trader in all of Alabama, if not the world.
Joe

• *On take-backs*
There are no Mulligans in trading.
Pat

• *On disruptive technology*
I want a driverless car...so I can text while driving.
Brendan

• *On domestic finances*
If your husband defaults on you, you can always execute a swap.
Francine

• *On electric-car drawbacks*
Tesla. Where gas stations don't know your name.
Sam

• *On inter-market analysis*
I think Justin Bieber got arrested again. Not yet sure what impact it will have on crude.
Jack

• *On pragmatism*
The Millionaire Next Door is not trading the VIX, but he is wearing four sets of clothing on the plane.
Stacey

• *On predictive analysis*
Forecasting is the art of saying what will happen and then explaining why it didn't.
Skip

• *One from a famous dude:*
If past history was all there was to the game, the richest people would be librarians.
Warren Buffet

Important Information
These comments are excerpts from chat rooms, emails, and tweets submitted by TD Ameritrade clients, and their views may not reflect those of TD Ameritrade. Testimonials may not be representative of the experience of other clients and are no guarantee of future performance or success.

News+Views

A hodgepodge of stuff we thought you should know.

Photograph by **Fredrik Brodén**

tdameritrade.com

nws.

Ask The Suit

A little Q&A with **Nicole Sherrod**, Managing Director, Trader Group at TD Ameritrade

Q: What's new in the world of education at TD Ameritrade? Any new events coming up?

A: Yes! Here's a short list of some of the latest and greatest:

Market Drive events. My work BFF, JJ Kinahan, hooked us up with some amazing sponsor partners this year so we can bring our TD Ameritrade Market Drive events to even more cities and to larger venues. (Thanks CME, BlackRock, Barclay's, and CBOE!*)

If you're not familiar with these events, in a word, get off your derrière and go. "In a city near you" you'll get a day of royal treatment learning all kinds of thinkorswim® tips, as well as mingle with other trading fanatics. And, of course, you'll be inducted into our trading "inner circle." Find out more here: www.tdameritrade.com/registerformarketdrive.

thinkorswim Chat Rooms. Don't forget about the great education going on daily in thinkorswim Chat Rooms. If you're looking for something topical it's there, it's colorful, it's unedited. And our "on air" talent keeps stepping up their collective games to drive even more impact from these events. Just fire up thinkorswim, and select Support/Chat in the upper right of the screen. Then select the Chat Rooms tab.

And for the Ladies. Finally, there's one other thing that we're working on. You might not know this, but the readership of this esteemed publication skews to the male side. Yup, it's a fact that women are not as invested as men.

But we're going to change all that. That's right—developed by ladies for ladies, we're launching new educational content designed to empower women to focus on building even greater wealth and investing savvy investing in the markets (tdameritrade.com/up). Why say it here? Because I want you to share a link with the women you care about—your sisters, daughters, friends, mothers, and yes, even wives.

FOLLOW THE SUIT
Read more of Nicole's musings on her own blog at **tickertape-monthly.com/blog.**

Follow Nicole on Twitter: **@TDANSherrod**

*CME, BlackRock, Barclays, CBOE, and TD Ameritrade are separate and unaffiliated companies and are not responsible for each other's services or policies.

toys

Toys for Traders

A few of our latest trading faves

thinkorswim®

TRADE FLASH

This toy displays trade-related events as they happen—such as analyst up/downgrades, block trades, trade imbalances, events on the trading floor, and more. To trade on a "Flash," just click on the symbol in the Trade Flash feed and you'll be sent to the Trade tab.

MY TOOLS

Instead of scrounging around all the submenus for your favorite indicators or chart functions, this toy gives you easy access and one click for each of your faves. Apply it to one or all the charts, or just those detached. To turn on My Tools, bring up Chart Settings and look under the General tab, bottom right.

ISE SPREAD BOOK

This old tool has been turned back on to let you see all the working spread orders on the ISE that your peers are trading. Similar to the regular spread book, you can search for all types of spreads (verticals, butterflies, etc.) for any symbol traded there to analyze for your own purposes.

industry spotlight

If it Ain't Broke, Don't Tax It

Will a tax proposal that picks on retail option traders survive?

Words by
Rachel Koning Beals

Illustration by
Joe Morse

Can I interest you in a little light reading? House Ways and Means Committee Chairman Dave Camp, a Michigan Republican, has issued a 979-page door stop called the "Tax Reform Act of 2014." In his defense, an overly complex U.S. tax code requires nothing short of a beefy rewrite. And there among the fine print is the proposal he first pushed in January 2012, a "mark-to-market" treatment of certain derivatives that will snag listed options that retail investors favor in the sweeping list of changes. Essentially, the proposal calls for marking all derivatives to market in order to put a price on that investment, then tax it as income. This means investors would be required to pay taxes on gains, even if it's an open position. The Act calls for treating the option, including buying a put, as if it were sold on the last business day of the year. Toss in straddles with a derivative, and non-derivative, offsetting position — including stock that is not part of a qualified covered call — both sides would be marked to market.

The aim is to clean up and clarify taxation and regulation of the increasingly complex suite of derivatives products launched in the last decade. Guilty by association is the decades-old listed - options market. Options' tax treatment has been "well-settled" for 30 years, argues the Options Industry Council. Other potential problems, according to tax-law firm Chapman and Cutler: Valuation of lightly traded derivatives; attempting to price as individual products embedded derivatives whose "value" may depend on what happens with the entire trade; and perhaps most importantly, expecting investors to pony up taxes on money they don't actually have in hand.

AND THERE AMONG THE FINE PRINT OF THE "TAX REFORM ACT OF 2014," MARK-TO-MARKET TREATMENT WILL SNAG LISTED OPTIONS THAT RETAIL INVESTORS FAVOR IN THE SWEEPING LIST OF CHANGES.

Stay tuned. Camp has some bipartisan support, but the proposal faces a long road, especially in a mid-term election year that may give Congress a facelift. Picking on retail derivatives is just the tip of the iceberg for a proposal that takes on individual and corporate tax rates, and many more complexities. For now, a red pen awaits its call.

NEWS FOR SHOW, VOL FOR DOUGH

HEADLINES MAY COME AND GO. BUT VOLATILITY IN REACTION TO THOSE HEADLINES IS WHAT CAN MATTER MOST TO TRADERS. AND BEFORE YOU WRITE OFF HIGHER-VOLATILITY MARKETS, HERE'S A LITTLE SECRET YOU OUGHT TO KNOW.

WORDS BY **THOMAS PRESTON**

PHOTOGRAPHS BY **FREDRIK BRODÉN**

OUR TRADING DAYS ARE FILLED WITH NEWS—

good news, bad news, news you consider important, news you ignore. Of course, how you interpret news is up to you. But there's no mistaking the one signal—implied volatility—that can tell us how the market itself feels about news. Simply put, implied vol measures the magnitude of an index or stock's potential price change. It goes up when the market is uncertain or fearful about what a headline might mean for future price changes, and down when news makes the market confident.

Sometimes, though, market volatility itself becomes news. And talking heads sound the alarm when the VIX—the Chicago Board Options Exchange (CBOE) volatility index—spikes higher. The VIX might not be reacting to news at all. But scary headlines about volatility can make novice investors skittish and afraid to act.

Sure, it's a free country. And you can choose to trade or not, depending on your nervous system. But savvy traders understand that higher volatility may actually signal potential opportunities. In fact, veteran traders may use strategies that leverage the very thing that's often scary to novices. How? Because they understand that when the VIX is higher, options premiums don't just increase in lockstep. They do so exponentially.

LEG BONE CONNECTED TO THE SHIN BONE

Traders know the VIX is calculated using out-of-the-money (OTM) SPX options prices. Those prices move higher and the VIX goes up, when traders buy them as a hedge or speculation against a large SPX price change. When option prices move lower because traders are selling in expectation of smaller price changes, the VIX moves lower. The relationship is essentially mechanical.

Traders may have an idea that short-option strategies like short straddles, for example, present opportunities when implied vol is higher, and wait for a higher VIX before they either open positions or increase position size. The higher the volatility, the higher the credit received for a short straddle—all other things like SPX price, strike price, and time to expiration being equal. That higher credit can mean higher potential profits and wider break-even points for a short strangle, which is why the strategy may be more attractive when volatility is higher. That said, short strategies in higher volatility environments pose great risk due to the wild swings that could drive a short option deep in the money very quickly. For that reason, you will always need to be aware of the increased risks as volatility increases, but as it does, how much higher is the credit?

PUT TO THE TEST

Let's use some actual numbers for the dollar amount that a change in the VIX means to SPX prices. The difference between the VIX at 14, and the VIX at 20, is due to SPX option prices. But how much higher are the SPX options when the VIX is at 20, than when it was at 14? A little bit higher, a lot higher, or somewhere in between?

SEE GLOSSARY **PAGE 42**

To answer that, I did a little study using the thinkBack tool on the Analyze tab of thinkorswim®. thinkBack lets you look at end-of-day stock-and-option prices for every trading day going back to 2003. Set the date in the upper-right-hand corner to open up the stock and option prices for that date. It's very handy for this type of analysis.

I looked for trading days where the SPX prices were very close—only a few points difference—and where the expirations were the same number of days in the future. The dates I found were July 9, 2013, and October 8, 2013. That removed much of the influence of the SPX price, and days to expiration on the prices of SPX options. The main reason for any difference in the option prices would be volatility. So, same SPX price, same days to expiration. Only the VIX is different. Here's what I found:

9 DAYS TO EXPIRE

JUL. 9/13 SPX **1652** VIX **14.50**		OCT. 8/13 SPX **1655** VIX **20.34**
.20	**1500 put**	1.35
.25	**1525 put**	2.15
.50	**1550 put**	2.90
.95	**1575 put**	4.55
2.15	**1600 put**	6.95
5.25	**1625 put**	11.05
13.00	**1650 put**	18.55
3.60	**1675 call**	10.50
.65	**1700 call**	3.35
.15	**1725 call**	.95
.10	**1750 call**	.35
.05	**1775 call**	.10
.01	**1800 call**	.05

37 DAYS TO EXPIRE

JUL. 9/13 SPX **1652** VIX **14.50**		OCT. 8/13 SPX **1655** VIX **20.34**
2.85	**1500 put**	7.55
4.00	**1525 put**	9.95
5.65	**1550 put**	12.90
8.70	**1575 put**	17.00
12.90	**1600 put**	22.15
19.75	**1625 put**	28.95
28.70	**1650 put**	37.30
14.55	**1675 call**	25.70
6.35	**1700 call**	14.75
2.70	**1725 call**	7.45
.95	**1750 call**	3.30
.55	**1775 call**	1.20
.25	**1800 call**	.60

For illustrative purposes only. Not a recommendation.

The table above is divided into two sections showing SPX options with nine days to expiration, and 37 days to expiration. The strike prices are down the middle. On the left hand side are out-of-the-money SPX option prices, when the VIX was 14.50. On the right are out-of-the-money SPX option prices when the VIX was 20.34. The strike prices 1650 and lower, show SPX put prices, and the strike prices 1655 and higher, show SPX call prices. You want to look only at out-of-the-money options because their values are purely extrinsic, and clearly illustrate the impact of higher and lower volatility on their prices.

The VIX at 20.34 is 40% higher than the VIX at 14.50. You might think that the SPX option prices are higher by a similar amount but they're not. In the case of the 1500 puts with 9 days to expiration, with the VIX at 14.50 they were .20. But with the VIX at 20.34 they were 1.35, or rather 6.5x greater. The 1500 puts with 37 days to expiration were 2.85 with the VIX at 14.50, but 7.55 with the VIX at 20.34—more than 2.5x greater.

The 1650 puts with 9 days to expiration, which were closer to the money, were 13.00 with the VIX at 14.50, and 18.55 with the VIX at 20.34. That's 1.4x higher, which is closer to the increase in the VIX. The 1650 puts with 37 days to expiration were 28.70 with the VIX at 14.50 and 37.30 with the VIX at 20.34. That's about 1.3x higher.

FOLLOW THE RISK

This analysis illustrates the actual premium change for the SPX options that pushed the VIX from 14.50 to 20.34. And it's important to understand that relationship. It's not the VIX moving higher that makes the SPX option premiums go up. It's the SPX option premiums that make the VIX go up. In fact, the SPX options moved up a larger percentage, depending on their distance out of the money, than the VIX. The further out of the money the option was, the greater the percentage price change. The closer to the money the option was, the smaller the percent price change.

That means the VIX is really a shorthand for how much premium is available in SPX options. Because SPX options represent liquid and efficient markets, and they're used to calculate the VIX, the VIX is a responsive indicator of potential market risk. This is one good reason traders ought to check the VIX daily, arguably giving it even more attention than underlying trends.

Also, note the SPX was the same price, but the VIX was different, suggesting the SPX price itself isn't necessarily an indication of fear or confidence. That information is packed into the prices of the SPX options, and makes the VIX a forward-looking indicator.

DOES SELLING PREMIUM WHEN VOL IS HIGHER guarantee profits? Absolutely not. Is volatility the only thing to consider when trading? Nope. But this information is a kind of dollar validation for using volatility as a basis for a strategy. Arguably, you should be looking at the VIX even before looking at the price of S&P futures pre-market. For a well-capitalized trader who is comfortable employing short-option strategies, the potential reward for keeping a sharp eye on the VIX can mean you potentially don't make a little more. You can potentially make a lot more for the same level of risk.

mky.

22

The Centerfold

Illustration by
Joe Morse

Evolution of the Trader

The recent discovery of the "T-DNA," or trader's genetic code, has led scientists to piece together the *thinkMoney* family tree. Who knew we all share a double helix started by our favorite little creature way back when?

1st LEVEL:
Calliputibus Volarensis

OPPOSABLE THUMB CREATES ADVANTAGE OVER OTHER APES BY ALLOWING 5 LOTS


Vercentradavix
GALLIC KING OF TRADERS CORNERS MILK MARKET, SETS FRANCE UP AS CHEESE CAPITAL IN PERPETUITY
Eddie LongShanks
EDICT FORCING ENGLISH SUBJECTS TO TAKE OTHER SIDE OF ROYALS' LONG OPTION TRADES LEAVES STERN RULER PENNILESS BUT LOVED BY MILLIONS
Conan the Call Seller
BEARISH DRUID TRADER PAINTS SELF BLUE IN ATTEMPT TO CONFUSE COLOR-BLIND BULLS
St Constantine
PENCHANT FOR 17-LEGGED OPTION TRADES LEADS PUZZLED ROMAN TRADER TO RENAME HIS CITY "BYZANTIUM"
Gramma Gamma
NONAGENARIAN DOES PRECISE PORTFOLIO REBALANCES TO KEEP WHIPPERSNAPPERS AT BAY
Johnny McPublic
BUYS TOPS, SELLS BOTTOMS, REPEATS
Schuyler Faulding
CONSTANT PANIC AND DIRE WARNINGS LEAVE WANNA-BE BEAR WITH NO TIME TO ACTUALLY TRADE
Hans Beuterfliegen
DELIGHTS IN THE SIGHT OF A FLOCK OF ATM BUTTERFLIES EXPANDING AT EXPIRATION
Sidney Sigmastein
MUCH TO HIS MOTHER'S DISMAY, LIVES LIKE HE TRADES—AT THE THIRD STANDARD DEVIATION
Penny Wyde
WORKS LIMIT ORDERS SO AGGRESSIVELY THAT US MINT IS CONSIDERING SUB-$.01 INCREMENTS SO EXCHANGES CAN KEEP UP

HOW TO NEUTER YOUR TRADE

AT SOME POINT YOU MAY HAVE HEARD AN OPTIONS TRADER BOAST ABOUT BEING A "DELTA NEUTRAL" OR " MARKET NEUTRAL" TRADER. BUT WHAT DO THESE TERMS MEAN, AND ARE THEY REALLY USEFUL? LET'S PUT THE DEBATE TO REST.

WORDS BY **THOMAS PRESTON** PHOTOGRAPH BY **FREDRIK BRODÉN**

NEUTRAL.

The word conjures images of a discrete Switzerland and fifty shades of beige.

But add the terms "market" or "delta" and the real fun begins. Why? Because "market neutral" and "delta neutral" are trading terms—often confused, confusing, and used interchangeably. Is a market-neutral strategy always delta neutral? Or can a delta-neutral strategy be market neutral? Rather than get into a semantic argument, let's define them, then explore how you can apply them.

DELTA WHAT?

Delta neutral means that the delta of a portfolio or given position—how much money it will make or lose if a stock price changes $1.00, all other factors being equal—is zero, or close to zero.

A simple position like a straddle, or a portfolio holding a lot of different options, can have cumulative delta close to zero, and be considered delta neutral at the onset of a trade, but not likely for long. Delta-neutral trading kicks in when the need arises to "neutralize" deltas, or rather, reset the position's delta to zero. Market makers employ this technique when there's too much directional risk—or in trader-speak, too many positive or negative deltas (see sidebar, right)—in a given position. Market makers continuously buy and sell options, and perhaps hedge each option trade with stock. For them, their profits arise from the bid/ask spread, and they don't want to lose those profits if the stock or index moves in a given direction.

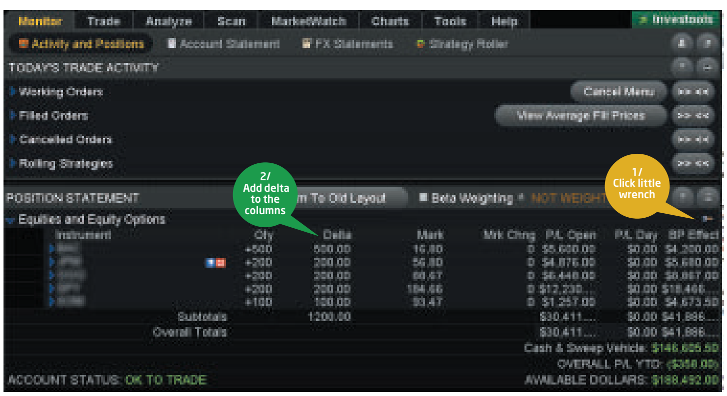
For example, if an order comes into an exchange to buy out-of-the-money (OTM) calls, the market maker takes the other side of the trade by shorting those calls. The short calls have negative delta, and can lose money if the stock rallies. The market maker may immediately buy stock shares to generate positive deltas, to offset the call's short deltas. If the stock rallies, he's hedged. Or, he might see an order for someone trying to buy puts. If he takes the other side of that trade by shorting puts, that too, could generate positive deltas to hedge the short calls. It's complicated, but being delta neutral keeps the market maker's directional risk low. In that sense, delta neutral is a response to a question about an existing position. How many deltas does that existing position have, and how can they be reduced? More on that later.

AS FOR MARKET NEUTRAL...

Market-neutral trading, however, is much closer to what retail traders—you and me—do. We might create a specific strategy as a market-neutral trade, if we believe the stock price or index will stay in a range, or at least not move past certain price levels. The market bias is neither bullish nor bearish, and the expectation is the stock won't move much at all. Hence, it's market neutral. For example, think short strangles or iron condors. These market-neutral strategies typically start without a bias, and result in positions that we choose

SEE GLOSSARY PAGE 42

FIGURE 1: Checking deltas. To view the deltas of each position or your entire portfolio in thinkorswim, 1) click the little "wrench"-looking thingy in the upper right of the Position Statement section of the Monitor page. Then 2) add "delta" in the menu of options to add to the columns. *For illustrative purposes only.*



NEUTRAL JARGON

DELTA
One of the option "greeks" that is the measure of expected change in an option's price per $1 move in the underlying. Long calls and short puts have negative (-) deltas, while long puts and short calls have positive (+) deltas. The maximum deltas a single US option contract can have is 100. The total sum of all positions in a portfolio is the portfolio delta.

DELTA NEUTRAL
A position or option portfolio in which the total net deltas of all the legs of every positions combined equal zero. For example, an at-the-money straddle is a delta neutral position because the call, carrying a delta of 50 offsets the put, with a delta of -50, for a net delta of 0. Since delta is always changing as the market moves, market makers and option traders will often reduce ("hedge") their deltas with an offsetting position, such as long puts against long calls or long stock; and short puts against short stock.

MARKET NEUTRAL
A style of trading in which a trader attempts to capture profits from a stock or index trading within a specific range. Though some market neutral strategies, like the straddle, start off as delta neutral, that's not always the case.

based on price, probability, or potential return vs risk.

Now, market-neutral strategies often have very low deltas, at least when trades are initiated. How so? A short strangle, for example, composed of a short out-of-the-money (OTM) call, and short OTM put in the same expiration, can have a very low delta, if the call's and put's strike prices are roughly the same number of points OTM. The short call has a negative delta, and the short put has a positive delta.

Combining the negative delta of the short call and the positive delta of the short put, the delta of the short strangle is close to zero. But a near-zero delta doesn't always mean market neutral. For example, consider a long at-the-money (ATM) call vertical in options with single points between strikes. The long ATM call option might have a delta of .50, and the short-call option at the first OTM strike might have a delta of .46. The net delta is .04, which is pretty small. But that long-call vertical has a decidedly bullish bias, and is not market neutral. It could lose money if the stock just sits where it is. So, small delta doesn't mean market neutral.

By the way, you can always see the delta of your current positions on the Monitor page of the thinkorswim® platform (see Figure 1). It's one of the columns in the "Position Statement" section of that page. To add delta, click on the little "wrench" icon in the upper-right-hand of the Position Statement section, and find "delta" from the list of available columns.

RUBBER, MEET ROAD

So, hopefully you now understand the difference between delta neutral and market neutral, but how can you use it? Is delta neutral solely for market makers? No. Retail traders, too, can employ delta-neutralizing strategies in an effort to protect profits and reduce losses. Unlike a market maker who neutralizes delta—i.e., gets the delta of a trade close to zero, on a trade-by-trade basis—retail traders may just want to reduce delta on a losing trade to help defend against further losses, or on a winning trade to potentially capture profits. Let's see how.

Important Information
Multiple-leg option strategies can entail substantial transaction costs, including multiple commissions, which may impact any potential return. These are advanced option strategies and often involve greater risk, and more complex risk, than basic options trades.

Consider a scenario with a stock price at $50 and a short 47 strike put for a 1.00 credit. This strategy loses if the stock price drops, and profits if the stock price rises. It has a positive .30 delta when you first put the trade on, and a breakeven point at $46.

Defend against losses. If the stock drops to $48, the put will likely be losing money, and its delta rises to, say .45. Your strategy now has more delta (directional) risk to it, with the potential to lose a growing amount of money if the stock continues to drop.

Now, you could just buy back the short put, but maybe you think the stock might stop dropping, or even rally a bit. A way to "defend" the short put would be to reduce the higher delta by selling a call against it. If the 50 call has a .35 delta, selling it for 1.20 would generate negative -.35 deltas, and leave you with a short 47/50 strangle with a current delta of positive .10. Selling the call also adds to the credit of the overall strategy, which increases the potential profit to 2.20 (minus transaction costs), and lowers the downside breakeven point to $44.80. Yes, you are adding risk to the position if the stock rallies sharply. But if the stock continues to drop, you could roll the short call to a lower strike to realize even more credit, which would lower the downside breakeven point further.

Capturing profits. On the other hand, let's say the stock rallies from $50 to $53, and the short 47 put is now profitable with a delta of .15. Rather than adding upside risk by shorting a call to reduce the already-lower delta, you might buy the 48 put with a delta of .20, for example, if it's trading for less than the credit you took in for selling the 47 put. If you can buy the 48 put for .75, you'd not only reduce your delta from +.15 down to -.05, you'd also have the long 47/48 put vertical on for a net .25 credit (minus transaction costs).

THESE ARE TWO SIMPLE EXAMPLES of reducing a position's delta. You can use verticals or other spreads, for example, to reduce delta in a defined risk way. But if you understand the logic of choosing a specific option or spread based not only on how much it neutralizes the delta of a position, but also on how it can potentially enhance or improve the resulting cumulative position, you'll be able to think more strategically about individual positions, and even your entire portfolio.

28

Trader Tools

thinkorswim scripts and gadgets

Gear Head

For your inner trading nerd, one part thinkScript, and one part gadget. Enjoy.

1

gear

COOL SCRIPT #1
THE DOW-TO-GOLD RATIO

• Words by **David "Mr. Script" Kier**

When asked to describe a widespread problem and then offer a solution I thought they meant for something like global warming. But alas, it was to solve a problem related to thinkorswim using thinkScript®, the do-almost-anything-we-didn't-think-of tool. If you're new to thinkScript, see the left sidebar to learn more.

For my first trick, I want to show you how to build a chart that displays the ratio of the Dow Jones Industrial average to the price of gold. Despite the name, the "Dow-to-Gold Ratio" is used by many traders to tell how overpriced the S&P 500 (SPX) might be. (See Figure 1.) You can see historically as the SPX hit new highs, gold was also at highs, and the ratio remained relatively low. But at the time of writing, as SPX continues to rise, gold is going down. So SPX is becoming expensive valued in gold as well as U.S. dollars.

BUILD-A-RATIO

The Dow-to-gold ratio has been used to analyze everything from stock-market moves to predicting upcoming interest-rate decisions. We aren't going to delve into Dow-to-gold theories, but rather describe how to see this ratio on thinkorswim. The problem we face is you can't enter ratios in the symbol entry box on thinkorswim. So we need to think outside the (symbol entry) box to solve this one.

Starting on the thinkorswim Charts tab, bring up a one-year daily chart of the S&P 500 index by entering SPX in the symbol box. We're going to build a study for a lower sub-graph of the chart in which the displayed data will be independent of the charted symbol—meaning, you can change the symbol without changing the new study. Once you see an SPX chart, fire up the thinkScript Editor by following the sidebar "Scripting from the Charts." Then enter the following script:

```
1. #hint: Ratio Chart
2. declare lower;
3. Input symbol_1 = "/YM";
4.  Input symbol_2 = "/GC";
5. Plot ratio = close(symbol_1) / close(symbol_2);
6. ratio.AssignValueColor(if ratio > = ratio[1] the
Color.UPTICK else Color.DOWNTICK);
```

After you've entered the above code, press Apply and OK and you'll see a chart similar to Figure 2, with the Dow-to-gold indicator at the bottom.

Now let's break down the code line by line to help you figure out how you got there.

FIGURE 1: How overpriced is it? The Dow-to-Gold ratio (the lower indicator above) helps you see how overpriced the SPX (upper chart) might be relative to the ratio. *For illustrative purposes only.*

NEW TO SCRIPTING?
You can find help to get started in two places:

1/ The **thinkorswim Learning Center** at tlc.thinkorswim.com. Select the Charting tab, then thinkScript in the submenu.

2/ Read our **Scripting Special Focus** in thinkMoney, Winter 2014, by going to tdameritrade.com/thinkmoney.

3/ Listen to Mr. Script's weekly show in the **thinkScript Lounge** of the thinkorswim Chat Rooms. From thinkorswim, click the Chat icon at the top (2nd icon from the right) >Chat >thinkScript Lounge.

Watch It!
For a more detailed walk-through on the **Sharing Center**, watch the video in the Learning Center.

1. Line one is a note which doesn't affect your script but is used to keep track of each section's goal. In our example we created "fancy note" by using the key word hint. This tells the thinkScript Editor to place the little help bubble next to our custom script in the Edit Studies and Strategies.

2. Line two tells the script this is a study by default that belongs on a lower subgraph. This is used with studies that don't relate, or will not scale, to the chart's price graph.

3. Lines three and four allow you to change the raio symbols without editing the script.You can customize these two inputs in the study parameters similar to how you customize pre-defined studies. Since we are building the Dow-to-gold ratio, I used the futures for each of these specific products.

FIGURE 1: Share Your Awesomeness. Set up a chart with all your favorite indicators and share it with friends and loved ones. *For illustrative purposes only.*

4. Line five is the math, the heart and soul of the script. We are simply taking the first input symbol and dividing it by the second, thus making it a ratio.

5. Line six makes the study pretty. The AssignValueColor function allows us to color the line as the ratio changes. If the ratio moves up, we color the line as our Uptick. And if it moves down, as our Downtick.

Congrats, you have your own Dow-to-gold ratio chart. And since you solved this in a smart way, you now create any ratio chart you desire simply by editing the symbols in lines 3 and 4. If you're new to scripting, be sure to read our primer on scripting in thinkMoney, Winter 2014 issue. We may not have solved global warming today, but we did make one small step for a legion of traders!

2 THINKORSWIM SHARING

ONE WORLD. LET'S SHARE IT

• Words by **Chesley Spencer**

With over a bajillion possible customizations available, thinkorswim can be a little intimidating. Users often ask "how do I set up my platform like [insert celebrity trader here]?" Trying to replicate another trader's setup used to be quite the exercise, but now it's as easy as a button click.

The Sharing Center enables users to share and consume a dozen different flavors of platform customizations by way of a web link. Each one of these platform functions has its own "Share" option that, when clicked, will generate a link to a web address which can then be given to anyone. Users can share their workspaces, watchlists, order or alert templates, trade grids, charts, scan queries, thinkScripts (studies, strategies, columns, and alerts), or flexible grids.

As we mentioned, each sharable function has its own share button, generally located where that function is set up. For example, the button for a single chart is at the top of the chart's border. The grid sharing button is in the grid menu, etc. Figure 1 shows many, but not all, of the locations where these links can be created.

Once you select a share function, a new window you'll see with the option to share the content directly with myTrade®, or to create an HTML link which can then be posted anywhere you like on the Internet. Keep in mind: you'll need a myTrade username to create a link (so others can see the source). This can be created under the Tools tab in myTrade. From myTrade, click on "Settings," edit your Display Name, then click "Update Settings."

When shared content is loaded into the platform, it will either save a copy to load later (such as a Workspace), or pop-out in a discrete window (such as a chart). This way, you'll always have the chance to save your setup.

2014 INVESTOOLS INVESTOR EDUCATION CONFERENCE
AUGUST 18-20 | DALLAS, TEXAS

ATTACK THE MARKET FROM ALL SIDES.

Turn education into action at the 2014 Investools Investor Education Conference.
Strategy-building breakout sessions. Insight from industry pros. Networking with like-minded traders.

AUGUST 18-20, 2014 | DALLAS HYATT REGENCY

FEATURED KEYNOTE SPEAKERS

T. Boone Pickens
Visionary Entrepreneur

Get the latest on the energy market—and why you should care.

Ken Fisher
Forbes *Columnist*

Find out how a veteran money manager is handling today's market.

Learn more at
investoolsconferences.com/thinkmoney

Investools
from TD Ameritrade
Holding Corp.

31 spot

Associate Spotlight

A chat with a TD Ameritrade VIP making waves

Interview by **Kira Brecht**

Illustration by **Joe Morse**

Meet the Mayor

TD Ameritrade's Mike Barwacz runs the innovative Trading Desk with old-school principles.

"Hey kid, you wanna come work for me?"

That was thinkorswim® founder Tom Sosnoff, talking to Mike Barwacz thirty years ago on the trading floor of the Chicago Board Options Exchange (CBOE). Happily for us, Barwacz said yes, and first clerked for Sosnoff before moving into the OEX pit as a market maker in his own right. Back then, Barwacz took a lot of grief for his trading badge which read "SYZ" (pronounced "size")—an ironic acronym since he started as a one- and two-lot trader.

As fate would have it, the acronym spoke volumes about Barwacz's ambition and drive. Still a passionate trader geek, he's now Director of TD Ameritrade's Trade Desk and oversees teams in Chicago, Fort Worth, and Canada. Not surprising, he draws heavily on 22 years of knowledge and wisdom from the trading floor to ensure trade-desk reps have the right stuff to talk to clients about even the most complex options strategies.

Barwacz is called the unofficial mayor of Chicago for good reason, and walking the CBOE trading floor with him takes some time. He seems to know everyone and loves to talk trading strategies. We wondered how his years on the floor helped shape who he is today.

Mike, tell us about those early days at the CBOE.

It was the mid-1980s and options were getting hot. That was the buzz. At one point the OEX (S&P 100) was the biggest pit in the world and had almost 600 guys. Tom Sosnoff, JJ Kinahan and I, we all stood very close to each other. We were like family. The best days were when you really couldn't leave, because there was so much paper (orders), and you were sweating through your coat. It was great. The energy, the competitiveness, having a broker yell something out, and you being the first on the ticket.

You were at thinkorswim in the early days, right?

I joined thinkorswim (when it was an independent brokerage) in 2007 and helped guide the Chicago office through TD Ameritrade transition after the merger. Hiring people from the floor is what made thinkorswim so special. Floor traders are a different breed. We have a different gene. As competitive as it was, there was also honor and etiquette, which we took off the floor as well. We knew how to talk to clients and explain things in a clear, simple manner. That's the benefit of coming to TD Ameritrade. It's like a family here.

What are your three trading rules to live by?

Don't panic, manage your winners, learn from your mistakes.

What's the bigger goal ahead for Trade Desk?

At the time TD Ameritrade bought thinkorswim, about 6% of their trades were options. Now, it's 40%. We wanted customer-service reps to be able to answer complex phone calls about option strategies. So, in the last year and a half, we've combined trade desks into the "One Trader Group," and taken reps through a rigorous training. We make sure all our trade-desk reps trade, or paper trade. They've got to have skin in the game. We hire people who are passionate about trading.

I heard a rumor you like to "initiate" unsuspecting guests?

Well, I've been called the "Entertainment Committee." So yeah, if you're visiting TD Ameritrade's Chicago office on business, I'd likely be the one showing you around. We might make it over to the Motel Bar for an introductory shot of Malört (an infamously terrible-tasting, Chicago-made liquor, by the way). That's all I'm going to say.

SPCL FOCUS

CHARTS THAT RULE THE WORLD

NO DOUBT YOU CAN FIND LOTS OF CHARTING PROGRAMS OUT THERE. BUT SERIOUSLY, WHY LOOK FURTHER? OTHER THAN A BACK MASSAGE, THINKORSWIM® CHARTS CAN DO ALMOST ANYTHING YOU'D NEED A CHART TO DO—EVEN IF YOU'RE NOT A CHART READER.

WORDS BY
THOMAS PRESTON
PHOTOGRAPH BY
FREDRIK BRODÉN

NORTH
ATLANTIC
OCEAN
SOUTH
ATLANTIC
OCEAN
PACIFIC
Norwegian Sea
North Sea
Mediterranean Sea
Caribbean Sea
Gulf of Mexico
Strait
UNITED STATES
7
6
5
4
3½
3
4½
2
1
0
Dallas
Chicago
Toronto
Québec
New York
Washington, D.C.
Island of Newfoundland
St. Pierre and Miquelon (FRANCE)
Bermuda (U.K.)
MEXICO
Mexico
THE BAHAMAS
CUBA
JAMAICA
DOMINICAN REPUBLIC
BELIZE
GUATEMALA
HONDURAS
EL SALVADOR
NICARAGUA
COSTA RICA
PANAMA
Caracas
TRINIDAD AND TOBAGO
VENEZUELA
GUYANA
SURINAME
French Guiana (FRANCE)
Bogota
COLOMBIA
ECUADOR
GALAPAGOS ISLANDS (ECUADOR)
PERU
Lima
Manaus
BRAZIL
Brasília
São Paulo
BOLIVIA
PARAGUAY
URUGUAY
Buenos Aires
Santiago
ARGENTINA
CHILE
Easter Island (CHILE)
ARCHIPIELAGO JUAN FERNÁNDEZ (CHILE)
AZORES (PORT.)
MADEIRA ISLANDS (PORT.)
CANARY ISLANDS (SPAIN)
CAPE VERDE
Ascension (St. Helena)
St. Helena (St. Helena)
St. Helena (U.K.)
TRISTAN DA CUNHA (St. Helena)
Gough Island (St. Helena)
NORWAY
SWEDEN
FINLAND
IRELAND
UNITED KINGDOM
London
DENMARK
NETH.
GERMANY
POLAND
BELGIUM
LUX.
CZ. REP.
AUS.
HUNG.
Paris
FRANCE
SWITZ.
ROMANIA
BULGARIA
ITALY
Rome
GREECE
ALB.
SER.
EST.
LAT.
LITH.
RUS.
BELARUS
PORTUGAL
SPAIN
Barcelona
Algiers
TUNISIA
MALTA
Casablanca
MOROCCO
ALGERIA
LIBYA
Western Sahara
MAURITANIA
MALI
NIGER
CHAD
SENEGAL
THE GAMBIA
GUINEA-BISSAU
GUINEA
SIERRA LEONE
LIBERIA
CÔTE D'IVOIRE
BURKINA FASO
GHANA
TOGO
BENIN
NIGERIA
Lagos
CAMEROON
CENTRAL AFRICAN REPUBLIC
EQUATORIAL GUINEA
Gulf of Guinea
SAO TOME AND PRINCIPE
Annobon (EQ. GUI.)
GABON
REP. OF THE CONGO
DEM. REP. OF THE CONGO
Kinshasa
Kisangani
ANGOLA
NAMIBIA
BOTSWANA
SOUTH AFRICA

WANT TO KNOW A LITTLE SECRET? When the thinkorswim® platform was first built, it didn't have charts. It's not that the development team couldn't build chart functionality. It's just that as ex-market makers, we didn't think to add them because we hadn't really used them.

Then two things happened. One, customers started to ask for charts. And two, we figured out some cool chart functionality that would help traders who didn't do technical analysis.

I won't bore you with how to interpret the hundreds of technical studies or chart drawings the platform supports. You'll find volumes of books on that subject. I want to focus on the stuff you may not have seen—the cooler stuff that's easy to overlook.

Let's shine a light on some of the features that chartists and non-chartists alike can use in day-to-day trading. These instructions will be based on the Charts page unless otherwise noted.

OVERLAYS

An overlay is when you have two or more different stocks or indices displayed on the same chart. It's a way to see relative performance—whether one is over- or under-performing another. It can be a measure of relative strength, and it's also handy if you're doing pairs trades. (See Figure 1.)

Here's how you do it:

1— Look in the upper-right-hand corner for the Studies button. Click on it, then hold the cursor over "Add Study" to see the expanded menu.

2—Hold the cursor over "Compare With" at the bottom of that menu. You'll see for example a list of default index symbols like DJX and SPX, as well as "Custom Symbol" at the top. If you click on one of the index symbols, or enter another symbol when you click on "Custom Symbol," a chart for that symbol is overlaid on the chart.

For example, if you have a chart for DJX and you select SPX from the list of indices, an SPX line chart will be displayed along with the DJX chart. The vertical axis on the left-hand-side will be scaled for the overlay symbol so the high-and-low range fits on the same chart as the original symbol. That's how the SPX, whose price is 10x the price of the DJX, can be displayed on the same chart. You can also go back to the "Compare With" menu and add more indices or custom symbols.

To take overlays one step further, click on the "Style" button in the upper-right-hand corner, then click on "Settings." Now in the "Chart Settings" window, click on the "Price Axis" tab and check the "Show Price as Percentage" box. That switches the vertical axis on the left-hand side of the chart to show the percentage change each symbol has had from the first date on the left-hand side of the chart, to the current day. This makes it easier to compare performance of two symbols with different prices.

BACKTESTING*

You can test trading strategies based on technical indicators, and see the profit-and-loss performance right on the charts. The charts have what we call "Strategies," which are simulated long-and-short entry and closing points determined by a technical indicator. You can code your own strategy, which is beyond the scope of this article, but I'll show you how to get started:

1—Click on the "Edit Studies" icon in the upper-right-hand corner.

FIGURE 1: Comparing Notes. Use the overlay function in thinkorswim, to compare two stocks, or in this case a stock to the SPX (pink line).

For illustrative purposes only.

FIGURE 2: Real test, fake money. Backtest a strategy first. Then view the entry and exit points on the chart, as well as a p/l before committing real dollars.

For illustrative purposes only.

More on Charts, Please...
If you're looking for even more awesomeness to squeeze out your thinkorswim Charts, learn more at the thinkorswim Learning Center. Go to: **tlc.thinkorswim.com** then click Charts.

2—In the window that pops up, click the "Strategies" tab on the upper-left corner.

3—On the left-hand-side you'll see a list of the default strategies available. To make the strategies "work," you need to add commands that will show both "long entry" (LE) and "short entry" (SE), at a minimum.

4—For practice, look for the "BollingerBandsLE" and "BollingerBandsSE" strategies in the list. Those are the long-entry and short-entry commands based on Bollinger bands. Double click on each one and it will be added to the list of studies and strategies on the charts in the main body of the "Edit Studies and Strategies" window.

5—Click the "Apply" button in the lower-right-hand corner of the window, then the "OK" button.

You should see "BollingerBandsLE" and "BollingerBandsSE" labels on the chart, indicating simulated buying and selling 100 shares of stock based on the Bollinger Band test. To see the profit and loss of those simulated trades, place the cursor directly on one of the labels, and right click to open a new menu. Click on "Show Report" in that menu to open the "Strategy Report" window. There you'll find the buy-and-sell signals, and profit-and-loss data for the strategy.

And by the way, if you want to buy or sell the chart's stock shares for real, right click in the chart's main body and select "Buy" or "Sell" from the drop-down menu. Plus, on the far-right-hand side of the chart window, you'll see tabs for "Trade," "Time and Sales," "Level II," etc. This lets you add windows with those features next to the chart window. That can basically set up charts as your go-to page for stock and futures trading needs.

LOOKING INTO THE FUTURE

OK, not even thinkorswim has a crystal ball. But Charts let you see future dates to the right of the current date. This helps you locate upcoming earnings and dividend dates, for example, as well as helps you extend drawings like trend lines into the future so you can identify possible price targets. The process?

1— Click on the "Style" button in the upper-right-hand corner and click on the "Settings" choice in the drop-down menu.

2— Click on the "Time Axis" tab in the "Chart Settings" window.

3— Now look for the "Expansion Area" control. You can enter a number in the field for "bars to the right"—say, 50—then click the "Apply" button on the window's bottom-right-hand corner.

That will add empty space to the right of the current date on the chart (see Figure 3). Once you've done that, you can extend a trend line or other drawing into that space. Place the cursor directly on the trendline and right click. Select "Extend to Right" from the drop-down menu and you'll see that line in those future dates.

A study that's built specifically for those future dates is the Probability of Expiring Cone (Figure 3 also). This draws the upper-and-lower bounds of a stock's or index's price range that theoretically encompasses a level of probability.

One way to add the cone study is to click on the

FIGURE 3: Peeking at the Future. By adjusting the chart to stop 50 bars from the right (shaded area), you can view future earnings and dividend dates. Add a probability cone (pink curve line) to estimate the probability range in which a stock will trade prior to those dates.

For illustrative purposes only.

"Edit Studies" icon in the upper-right-hand corner and find "ProbabilityofExpiringCone" from the list of studies on the window's left-hand side. Double click to add it to the list of chart studies. You'll also find two fields to edit for the study. The "period" is the number of future dates for which the probability cone is calculated, and the "prob range," is the probability the projected range covers. The default "prob range" is 68%, which corresponds roughly to one standard deviation. Set it to 95% to see a cone that covers two standard deviations, or 99%, to see a cone that covers three standard deviations.

THESE FEATURES REALLY JUST SCRATCH the surface of charting functionality. But hopefully you now have an idea of their scope and how to access them. Each of the described menus has other choices that lead you to other functions. Go ahead and continue to explore the charts to see just how hard you can make them work for you.

Important Information

**Backtesting is the evaluation of a particular trading strategy using historical data. Results presented are hypothetical, they did not actually occur and they may not take into consideration all transaction fees or taxes you would incur in an actual transaction. And just as past performance of a security does not guarantee future results, past performance of a strategy does not guarantee the strategy will be successful in the future. Results could vary significantly, and losses could result.*

myTrade is a service of myTrade, Inc., a separate but affiliated firm. In order to use the service, you must create a myTrade profile, and conform to the myTrade terms of use.

TD Ameritrade is not responsible for the services of myTrade, or content shared through the service.

Supporting documentation for any claims, comparison, statistics, or other technical data will be supplied upon request.

FIGURE 1:
Legal Hacking.
Scanning for trades with Stock Hacker is as simple as choosing the list, then your parameters, and sorting how you want the results to show. *For illustrative purpose only.*

FIGURE 2:
Chart the Trade.
Once you find a stock in Stock Hacker, right click and choose "TOS Chart." Then answer the questions above. *For illustrative purpose only.*

How to...Find and Chart Your Next Trade

It's easier than you think. Just ask three questions.

WORDS BY
DAVID KIER

chrts

Often, too many indicators can lead to indecision and antacids. But there's a more logical approach to finding a potential trade and plotting a chart using just a few indicators to answer some important questions you might have about what a stock may do next.

STEP 1: SCAN THE UNIVERSE

Using Stock Hacker in the Scan tab of thinkorswim® trading platform, refer to Figure 1. There you can scan the world of stocks with your own criteria, containing the list of stocks to scan, your filters, and all the price data your heart desires. Then…

1— Choose the subset of stocks you would like to scan from the drop-down next to the words "Scan in." There, you can see predefined categories as well as all your personal watch lists, and GICS classified industry lists.

2— Choose All Optionable if you only want to see stocks with listed options.

3— Select "Add Stock Filter" below the "Scan in" drop down to add a stock filter to the existing set of criteria.

4— Choose Last and enter a minimum and maximum price of the stock.

5— Now click the "Add Study Filter" button. Use the drop down to select the "Price Performance" group and choose "Price Direction." The default inputs for this filter are "CLOSE" and "increased," which we'll keep. But you might want to increase the number of bars of data to more than 3.

6— Sort for the most heavily traded by choosing the "sorted by" dropdown to the left of the scan button. Select "Basic Price & Quote" menu and choose "Volume."

7— In the next menu choose “Descending.” Then press “Scan.”

The results will appear at the bottom of the screen like orderly soldiers. If you’re not happy with them, you can always edit the filters.

STEP 2: MASTER THE UNIVERSE
Okay, maybe not the actual universe, but you can attempt to determine where the stocks in your world are going by charting them in the thinkorswim Charts. Just right click on any symbol in the scan results and choose “TOS Charts.”

If you’ve never charted, you should try to answer three basic questions:

1— What’s the trend?
2— How strong is the trend?
3— Where do I get in?

To help us with these questions, we’ll add three studies: simple moving average, volume, and Relative Strength Index, and make a couple of minor adjustments to the parameters.

Referring to Figure 2, change your chart to a one-year daily chart. Then, from the studies menu in the upper right corner of your chart, add SimpleMovingAvg and RSI-Wilder. Click on the SimpleMovingAvg and edit the length of the study to 50. You don’t have to add volume since it is already turned on by default. However, if your volume isn’t displayed you can add it within the Settings menu.

Once you’ve got thinkorswim Charts set up, you can answer the three questions.

One: Is the stock clearly trading above the simple moving average (blue line in chart) or has it recently crossed above the line?
Two: does the indicator line in the RSI-Wilder cross from below the 30 line to above the 30 line recently?
Three: is the volume increasing or higher than normal (bars are higher than prior bars, indicating more traders committing to the trade)?

WHILE THERE’S NEVER A GUARANTEE that a trend will continue, if you’ve answered “yes” to all three of these, then there’s a good chance you may have filtered for a stock or two smack dab in the heart of a bullish run. Happy trading!

Q+A

FAQs.

Q: How can I synchronize drawings across multiple chart windows with the same symbol?
A: If you have a drawing like a trend line or a price level on a chart, you can have that appear at the same price level on another chart, even if it has a different time scale. Click on the “Style” button, then click on “Settings.” In the “General” tab of the “Chart Settings” window, you’ll see “Synchronize” with a checkbox for “Drawings” and “Crosshair Position” in the middle of the left-hand side. If those are checked, you can get a drawing displayed on a daily chart and a minute chart, for example, that have different price scales without your having to recreate the drawing.

Q: I’ve set up my charts just how I like them. How do I save the settings and have them open as my default?
A: Once you have the time frame, technical studies, colors, and other settings established for each new chart, click on the “Style” button, then click on “Set Chart Default” from the drop-down menu. Now you can close the thinkorswim platform and reopen it with your favorite chart settings loaded as a default.

Q: How can I share my chart settings with someone else?
A: You can share your charts on the thinkorswim platform with anyone else who uses the platform. Click the “Share” button in the upper-right-hand corner. This opens a window with a choice to share the chart you’re currently on via email, Facebook, Twitter, or myTrade®. If you choose email, Facebook, or Twitter, you can copy and paste a link. As long as the other person has the thinkorswim platform open, the link will open up a chart window with your symbol, studies, and settings.

PRECISION CHARTING
HOW TO EDIT YOUR STUDIES

In thinkorswim Charts, if you click on the “Studies” button in the upper-right-hand corner and hold the cursor over “Add Study,” you’ll see dozens and dozens of different technical-analysis tools you can add to a chart. But if you know your studies, you’ll know that most of them have parameters that can be changed—things like the number of data bars used in the study, or like the K period and D period in Stochastics, for example. There’s a fast way to edit those inputs and parameters.

1– In the upper-right-hand corner, look for the “Edit Studies” icon that looks like a test tube releasing a drop of liquid. It’s a couple inches to the left of the “Studies” button.

2– Click on that icon to open the “Edit Studies and Strategies” window.

3– In that window’s main area, you’ll see any studies you’ve loaded on the chart. Hold the cursor over the study you want to edit and click the “gear” icon on the right-hand side. That opens the controls to change the study’s inputs, as well as color formats.

Capiche

Pearls from a veteran floor trader

cap.

Words by
Greg Loehr

• These days, trading terms may not be as complicated as "supercalifragilisticexpialidocious." But close. Like flying nannies, market words are weird and wonderful. Understanding references like "contango" and "backwardation" could hold the secret to your success when you try to make sense of price moves in ETF products whose values are tied to futures contracts.

Remember a futures contract is an agreement to buy or sell something—like oil, for instance—at some time in the, well, future. In general, futures prices differ from "spot prices," which represent real-time cash prices.

If a future price trades higher than the spot, this is called "contango." If a future price trades lower than the spot, this is called "backwardation." Note the following table.

30-day future price—contango	**$105**
Cash (spot) price	**$100**
30-day future price—backwardation	**$95**

For illustrative purposes only.

As an example, crude oil is said to be "in contango" when longer-dated contracts trade at increasingly higher premiums over cash. This premium exists to cover the costs, for instance, of paying the storage for the oil between now and a futures expiration. As the contract gets closer to expiration, this premium begins to "decay," until the price of the expiring future matches the cash.

For instance, assume a cash price of $100 per barrel, and $105 for a 30-day futures contract. If oil's cash price remains unchanged, then 30 days later the expiring futures contract will also be worth $100. If you had bought the futures contract, you just lost $5.

Burned by Oil Rolls

If you're trading futures-based ETFs, beware of the "rolling risk"

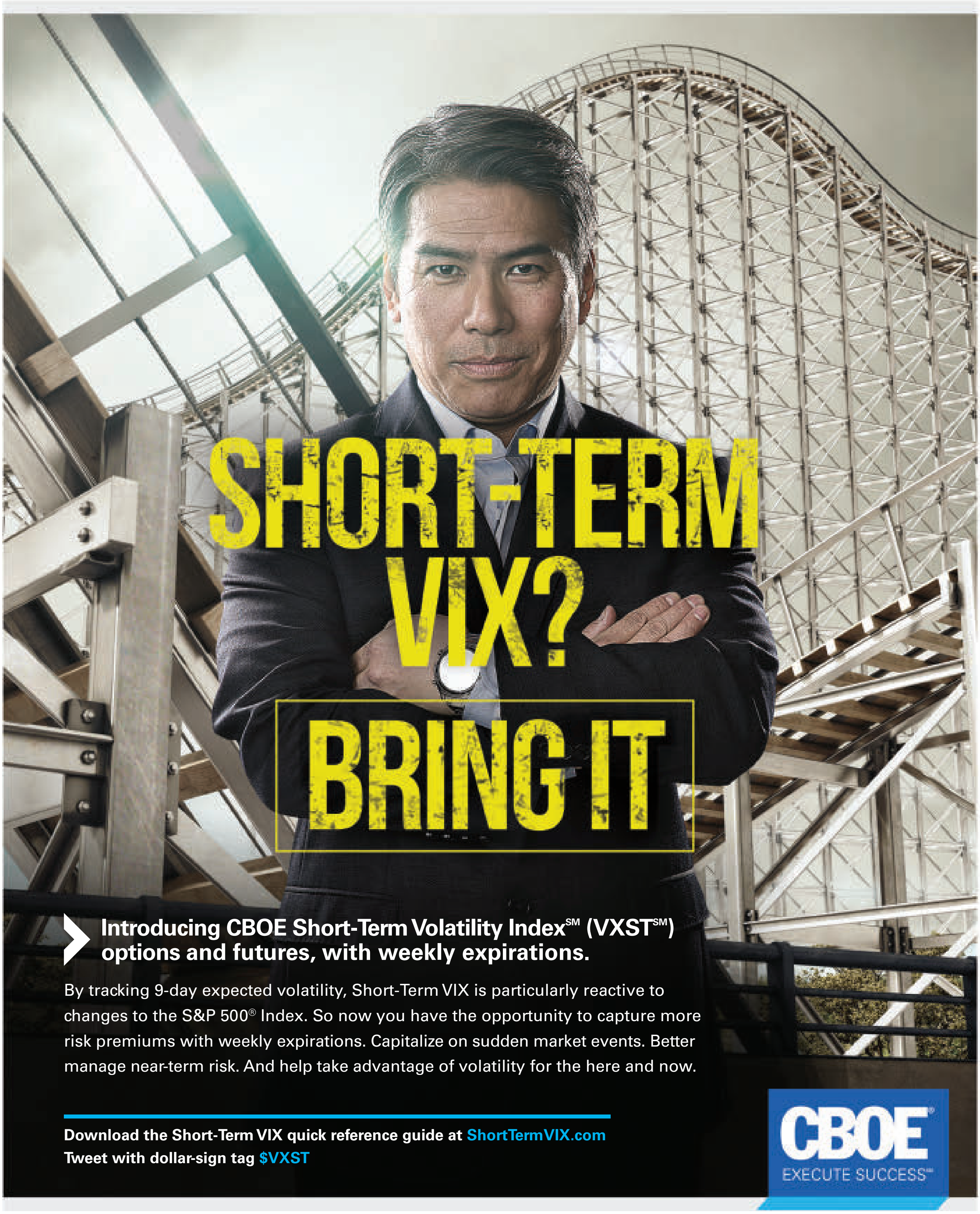
Just a Spoonful of Sugar...

What does this have to do with your trading life? Even though you're trading an ETF, in reality you're trading futures contracts (at least through the fund manager) because products such as oil ETFs—derive their prices from futures. The goal of an oil ETF isn't simply to track the price of oil. It's to track the price of oil using near-month oil futures.

As a fund's near-term futures contracts approach expiration, those contracts need to be rolled over into longer-term futures expirations so the fund avoids being forced into taking physical delivery of all that crude.

And when the market is in contango, guess what? You end up paying more for the longer-term contract than what you receive from selling the shorter-term contract, and the net price of your investment goes down. This is called "roll decay," and with oil futures expiring every month, this decay can really add up.

REMEMBER THAT just because a market is in contango, and longer-term futures cost more than shorter-term contracts, that doesn't necessarily ground your investment. It's just a headwind to keep track of. Given that the value of oil, volatility, or whatever it is you're trading, could go up, this change in the cash price might be enough to offset 'roll decay'. Or it might not. You may not have to clean chimneys, but watch the words that make the market. And above all, always work to understand the products you're trading.


SHORT-TERM
VIX?
BRING IT
Introducing CBOE Short-Term Volatility Index℠ (VXST℠)
options and futures, with weekly expirations.
By tracking 9-day expected volatility, Short-Term VIX is particularly reactive to changes to the S&P 500® Index. So now you have the opportunity to capture more risk premiums with weekly expirations. Capitalize on sudden market events. Better manage near-term risk. And help take advantage of volatility for the here and now.
Download the Short-Term VIX quick reference guide at ShortTermVIX.com
Tweet with dollar-sign tag $VXST
CBOE®
EXECUTE SUCCESS℠

40

Ask the Trader Guy

Rescuing traders, one question at a time.

Photograph by **Fredrik Brodén**

Q: Hey, Trader! When I look at options, I usually see that out-of-the-money (OTM) puts have a higher price than OTM calls that are the same distance out of the money. And sometimes I see stocks whose OTM calls are higher than the OTM puts. What's going on and why?

T: That, my friend, is volatility skew in action. Vol skew, for short, is when the implied volatilities of the options in a particular expiration aren't all the same. If you look at a graph of the implied vols, they usually slope up, and away, from the ATM strikes. And the slope is often steeper for the OTM puts than the OTM calls. This is because investors often buy OTM puts as a hedge against long stock, and sell OTM calls as either a covered call, or to finance buying the put. That buying-and-selling pressure drives the implied vols of the puts higher than the calls, which in turn makes the puts look more expensive than the calls. But when calls are more expensive than the puts, the slope of the call skew is steeper than the put skew, and that can happen when the stock has a lot of speculative activity. Investors who believe a stock might make a big move higher may buy calls, which can drive those particular values, and implied vols, higher.

Q: Why do my AAPL* options look so strange after the stock split 7-1?

T: No matter how strange things look, remember that the split itself doesn't change the value of your position.

That said, let's look at an AAPL option pre- and post-split. If the August 560 put is trading for $14.00 and has .33 delta pre-split, it would be worth about $100 more if AAPL dropped $3.00 (with all other things being equal) and the 560 put rose to $15.00. Post-split, the price of AAPL was 1/7th of the pre-split price, and all the option strike prices were adjusted down to 1/7th, too. So, the 560 put turned into the 80 put and might be worth about $2.00. But the single 560 put turned into seven 80 puts. A single 560 put at $14.00 has a $1400 value, and 7 80 puts at $2.00 also have a $1400 value. Now, the delta of the 80 put will still be about the same as the 560 put, .33. And if AAPL drops the same percentage post-split as pre-split, a $3.00 drop would be about $.43. That means the 80 put would increase by about .142. Since you have 7 of the 80 puts, 7 x $14.20 = $99.40, which is nearly the same as the pre-split change in value. That means the risk of your position doesn't change from pre- to post-split.

Q: Hey, Trader! Greetings! My name is Zyphro and I come from the year 2514. I wish to bestow upon you all the Fed announcements from your time until mine so your future self can be wealthy!

T: Um, thanks Zyphro, but even if I knew what the Fed numbers were going to be, I'd still have no idea which way the market would move. Seriously, that stuff is a coin flip. Interpreting Janet Yellen's statements is a job all by itself. I'm too busy actually trading. But if you know the future, can you tell me if this burrito I'm about to eat will keep me up all night?

Bring out the option trading machine in you.

Stay on top of the option market with **thinkorswim**® platform tools.

You eat iron condors for breakfast. You straddle the market like it's nobody's business. When it comes to option trading, you think you know it all, right? Think again. There's a world of option opportunity out there. And we keep bringing you the innovative tools to help take it on. Slice and dice data like never before with option statistics. Scan thousands of optionable stocks in seconds with dynamic scanning. It's no wonder why *Barron's* named us among the "Best for Options Traders" five years in a row.*

TD Ameritrade

Learn more at tdameritrade.com/options

42

The Token Glossary

Terms you might stumble across in this issue.

tdameritrade.com

gls

found on page:
26

Long Straddle

• A market neutral, defined risk position, composed of an equal number of long calls and puts of the same strike price. The strategy assumes the market will break out one way or another, in which case, a profit occurs when one side of the trade gains more than the other side loses. Breakeven points are calculated by adding and subtracting the total debit to and from the strike price of the options.

found on page:
13

Theta

• A measure of an option's sensitivity to time passing one calendar day. For example, if a long put has a theta of -.02, the option premium will decrease by $2.

VEGA

• A measure of an option's sensitivity to a 1% change in implied volatility. For example, if a long option has a vega of .04, a 1% increase in implied volatility will increase the option premium by $4.

Delta

• A MEASURE OF AN OPTION'S SENSITIVITY TO A $1 CHANGE IN THE UNDERLYING ASSET. ALL ELSE BEING EQUAL, AN OPTION WITH A 50 DELTA (ALSO WRITTEN AS .50) FOR EXAMPLE, WOULD GAIN 50 CENTS PER $1 MOVE UP IN THE UNDERLYING. LONG CALLS AND SHORT PUTS HAVE POSITIVE (+) DELTAS, MEANING THEY GAIN AS THE UNDERLYING GAINS IN VALUE. LONG PUTS AND SHORT CALLS HAVE NEGATIVE (–) DELTAS, MEANING THEY GAIN AS THE UNDERLYING DROPS IN VALUE.

20 & 27
found on page:

Short Straddle/Strangle

• A market-neutral strategy with unlimited risk, composed of an equal number of short calls and puts of the same strike price (straddle) or two different strike prices (strangle), resulting in a credit taken in at the onset of the trade. The strategy assumes the underlying will stay within a certain range, in which case, as time passes and/or volatility drops, the options can be bought back cheaper than the credit taken in, or expire worthless; resulting in a profit. Breakeven points of either strategy at expiration is calculated by adding the total credit received to the call strike and subtracting the total credit received from the put strike.

found on page:
12, 20, 26 & 38

SHORT

• To short is to sell an asset, such as an option or stock that you don't own in order to collect a premium. The idea being that if you believe the price of the asset will decline, you can buy back (or "cover") your short at a lower price later. Your potential profit would be the difference between the higher price you shorted at and the lower price you covered.

12, 21, 26 & 38
found on page:

OUT OF THE MONEY (OTM)

• An option whose premium is not only all "time" value, but the strike is away from the underlying equity. For calls, it's any strike higher than the underlying. For puts, it's any strike that's lower.

13 & 27
found on page:

AT THE MONEY (ATM)

• An option whose strike is "at" the price of the underlying equity. Like out-of-the-money options, the premium of an at-the-money option is all "time" value.

found on page:
13

IN THE MONEY (ITM)

• An option whose premium contains "real" value, i.e. not just time value. For calls, it's any strike lower than the price of the underlying equity. For puts, it's any strike that's higher.

Article Disclaimers

Important info that you need to know.

tdameritrade.com

important info

1/ GENERAL DISCLAIMER

The information contained in these articles is not intended to be investment advice and is for illustrative purposes only. Be sure to understand all risks involved with each strategy, including commission costs, before attempting to place any trade. Clients must consider all relevant risk factors, including their own personal financial situations, before trading. Past performance of a security or strategy does not guarantee future results or success. Transaction costs (commissions and other fees) are important factors and should be considered when evaluating any options trade. Options involve risk and are not suitable for all investors. Supporting documentation for any claims, comparisons, statistics, or other technical data will be supplied upon request. It is not possible to invest directly in an index.

2/ OPTIONS STRATEGIES

Trading options involves unique risks and is not suitable for all investors. Mini-options do not reduce the per share cost or price of options.

The long put strategy provides only temporary protection from a decline in the price of the corresponding stock. Should the long put position expire worthless, the entire cost of the put position would be lost.

A long call option position places the entire cost of the option position at risk. Should an individual long call position expire worthless, the entire cost of the position would be lost.

Spreads, condors, butterflies, straddles, and other complex, multiple-leg option strategies can entail substantial transaction costs, including multiple commissions, which may impact any potential return. These are advanced option strategies and often involve greater risk, and more complex risk, than basic options trades. Be aware that assignment on short option strategies discussed in this article could lead to unwanted long or short positions on the underlying security.

The naked put strategy includes a high risk of purchasing the corresponding stock at the strike price when the market price of the stock will likely be lower. Naked option strategies involve the highest amount of risk and are only appropriate for traders with the highest risk tolerance.

Naked option strategies involve the highest amount of risk and are only appropriate for traders with the highest risk tolerance.

The risk of loss on an uncovered call option position is potentially unlimited since there is no limit to the price increase of the underlying security.

Option writing as an investment strategy is absolutely inappropriate for anyone who does not fully understand the nature and extent of the risks involved.

A covered call strategy can limit the upside potential of the underlying stock position, as the stock would likely be called away in the event of substantial stock price increase. Additionally, any downside protection provided to the related stock position is limited to the premium received. (Short options can be assigned at any time up to expiration regardless of the in-the-money amount.)

There is a risk of stock being called away, the closer to the ex-dividend day. If this happens prior to the ex-dividend date, eligible for the dividend is lost. Income generated is at risk should the position moves against the investor, if the investor later buys the call back at a higher price. The investor can also lose the stock position if assigned.

The maximum risk of a covered call position is the cost of the stock, less the premium received for the call, plus all transaction costs.

Rolling strategies can entail substantial transaction costs, including multiple commissions, which may impact any potential return. You are responsible for all orders entered in your self-directed account.

Supporting documentation for any claims, comparisons, statistics, or other technical data will be supplied upon request.

thinkMoney from TD Ameritrade
200 S. 108th Ave
Omaha, NE 68154

PRSRT STD
US Postage
Paid
TD Ameritrade

The risk of loss in trading securities, options, futures, and forex can be substantial. Clients must consider all relevant risk factors, including their own personal financial situations, before trading. Options involve risk and are not suitable for all investors. See the Options Disclosure Document: Characteristics and Risks of Standardized Options. A copy accompanies this magazine if you have not previously received one. Additional copies can be obtained at tdameritrade.com or by contacting us. Trading foreign exchange on margin carries a high level of risk, as well as its own unique risk factors. Please read the following risk disclosure before considering trading this product: Forex Risk Disclosure (www.nfa.futures.org/NFA-investor-information/publication-library/forex.pdf). A forex dealer can be compensated via commission and/or spread on forex trades. TD Ameritrade, Inc., member FINRA/SIPC/NFA.TD Ameritrade is a trademark jointly owned by TD Ameritrade IP Company, Inc. and The Toronto-Dominion Bank.

SUSTAINABLE FORESTRY INITIATIVE
Certified Chain of Custody
Promoting Sustainable Forestry
www.sfiprogram.org
SFI-00993