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HOW TO GAIN DISCIPLINE & COURAGE THROUGH  
KNOWLEDGE & STRATEGY

## Solving The 5 Pitfalls of: **Covered Calls**

### How To Trade For Income



**by: Lan H. Turner**

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# Covered Calls & The Loop

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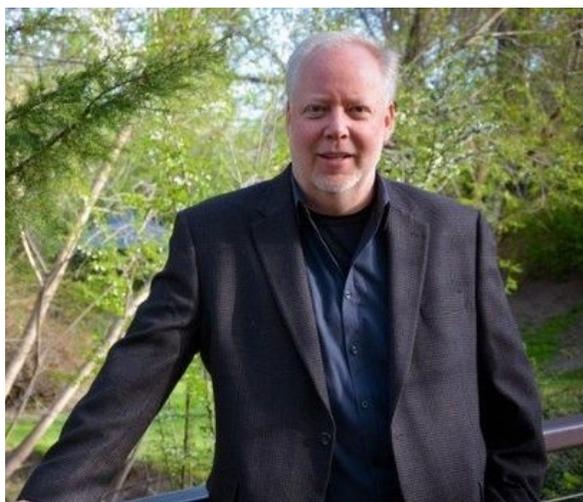
Trading For Income

## Trading Covered Calls & The Loop

A Comprehensive Guide to Trading Covered Calls For Income

By: Lan H. Turner

### About the Author



Lan H Turner has over 28 years of experience in the financial industry as a seasoned trader and educator in Stocks, Futures, Forex, and Options. With a background in teaching at prestigious institutions such as the Chicago Board of Trade, Chicago Mercantile Exchange, and currently at Dixie State University, Mr. Turner brings a wealth of knowledge and expertise to the world of trading education.

As the founder of [TradeMentors.com](http://TradeMentors.com) and co-founder of [CommodityTradingSchool.com](http://CommodityTradingSchool.com), Mr. Turner has been dedicated to providing educational resources and mentoring to traders worldwide. His major contributions include

developing the award-winning live trading platforms known as Track 'n Trade, along with the research tools known as TradeMiner. Mr. Turner established Gecko Software, an engineering firm, and Gecko Financial Services, a boutique brokerage firm known for its safe and friendly approach. He also founded PitNews Press, a publishing house focused entirely on the financial industry.

With a passion for sharing knowledge, Mr. Turner has authored numerous publications, delivered public speeches, and created a number of comprehensive trading courses. His expertise spans teaching live trading seminars, creating proprietary indicators, and developing fast-paced, educational boot camp videos and training courses available on the website [Tools4Traders.ORG](http://Tools4Traders.ORG) and on Amazon.

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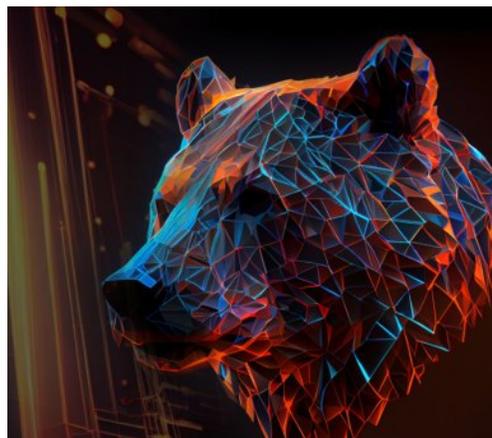
#### Trading Covered Call Options

Options are financial derivatives that grant the buyer the right, but not the obligation, to buy or sell an underlying asset (such as shares of a stock) at a predetermined price, known as the strike price, on or before a specific date, known as the expiration date. There are two types of options: calls and puts. Buying a call option gives you the right to buy the underlying asset, while buying a put option gives you the right to sell it. Conversely, selling or writing an option is the act of granting this right to a buyer, and in return, you collect a fee or premium.



A covered call strategy involves owning (or buying) the underlying asset, such as shares of a stock, and selling call options on the same asset. The idea is to generate additional income (the premium from selling the call options) while holding the asset. The term "covered" comes from the fact that the potential obligation of selling the asset, if the option buyer exercises their right, is "covered" by the asset you already own.

1. Advantages and disadvantages of covered calls:
  - a. Advantages: This strategy allows you to generate income through the premiums collected from selling call options, thereby lowering the overall cost of owning the asset. It can also provide some downside protection, as the premium received can offset some potential losses if the asset's price decreases.
  - b. Disadvantages: The main drawback is that you limit your potential upside. If the asset's price significantly increases, you'll miss out on those potential profits because you're obliged to sell the asset at the lower strike price. Also, if the asset's price drops significantly, the premium collected might not be enough to offset the loss.
2. Think of covered call trading as similar to owning a rental property. When you own a rental property, you collect rent from your tenants. In the case of covered calls, the shares you own are like your property, and the premium you collect from selling the call options is akin to the rent. Just like how rent can provide a steady income stream from a rental property, the premiums from covered calls can generate a consistent return from your stock holdings.
3. Stay vigilant, just like real estate, if you don't manage the risks properly, you could potentially face losses.



This approach is not about hitting home runs, but rather about generating consistent returns over time. By managing the risks and being patient, you can potentially achieve higher returns than traditional investing. Once you master this skill, you can actually use it for monthly income, as many other traders do.



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#### II. Understanding the Covered Call Strategy

1. **What is a call option, premium, and option expiration?:** A call option is a financial contract that gives the buyer the right, but not the obligation, to purchase the underlying asset (such as a stock, or futures contract) at a specific price, known as the strike price, by a predetermined date, known as the expiration date. The premium is the cost of this right, paid by the option buyer to the option seller. When an option reaches its expiration date, it is either exercised (if it's in-the-money, profitable), or it expires worthless (if it's out-of-the-money, not profitable).
2. **Example of a Standard Covered Call Strategy:** Let's consider an investor who owns 100 shares of XYZ Company, currently trading at \$50 per share. The investor decides to sell a covered call with a strike price of \$55 and a premium of \$2 per share.
  - a. **Monthly Return:** If the call option expires worthless (stock price remains below \$55), the investor keeps the premium of \$2 per share, resulting in a 4% return ( $\$2 / \$50$ ).
  - b. **Annualized Return:** Assuming this strategy is repeated monthly, the annualized return would be approximately 48% ( $4\% \times 12$ ).
    - i. **Outcome 1: Stock Closes Below the Strike Price**
      1. If the stock price remains below the strike price of \$55 by the expiration date, the call option expires worthless, and the investor keeps the premium. They can then choose to sell another covered call for the next month if desired.
    - ii. **Outcome 2: Stock Closes Above the Strike Price**
      1. If the stock price closes above the strike price of \$55, the call option may get exercised, and the investor's shares may be called away. They will still keep the premium received, but they will miss out on potential additional stock price appreciation.
3. **Outcome 1: Stock closes below the strike:** Now, let's consider a scenario where you continue this strategy for three consecutive months with the same stock and similar outcomes each month.
  - a. **Month One:** You own 100 shares of XYZ Corp at \$50 per share. You sell a call option with a \$55 strike price, earning a premium of \$200. The stock price stays below \$55, so the option expires worthless. Your profit is \$200.
  - b. **Month Two:** You still own your 100 shares, and again sell a call option with a \$55 strike, earning another \$200 premium. The stock price remains below \$55, so this option also expires worthless. Your profit for this month is \$200, and the cumulative profit is now \$400.
  - c. **Month Three:** You continue the same strategy, earning another \$200 premium. However, this time, the stock price increases above \$55. The option is exercised, and you sell your 100 shares for \$55 each. You make a profit of \$5 per share (totaling \$500) plus the \$200 premium, making your profit for this month \$700. The cumulative profit for the three-month period is \$1,100.
  - d. In both scenarios, you generate income from premiums, and potentially from selling your shares if the stock price rises above the strike price. You can use these profits to reinvest or to offset any potential decrease in the stock's price.
4. **Outcome 2: Stock closes above the strike:** If XYZ Corp's price rises above \$55 (the strike price of your call option), the buyer of the call option will likely choose to exercise it. As



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the option writer, you're obligated to sell your 100 shares of XYZ Corp at the strike price of \$55 per share. You'll miss out on any additional profit that could have been made from selling the shares at a higher market price. However, you keep the \$200 premium and make an additional \$500 from selling your shares ( $\$55 - \$50 = \$5$  profit per share, multiplied by 100 shares).

#### 5. Example of a covered call strategy executed over multiple months

Month	Action	Stock Price	Strike Price	Premium Received	Shares Called Away	Profit
1	Buy 100 shares of XYZ Corp & sell call	\$50	\$55	\$200	No	\$200
2	Sell call	\$52	\$57	\$200	No	\$200
3	Sell call	\$54	\$59	\$200	No	\$200
4	Sell call	\$56	\$61	\$200	No	\$200
5	Sell call	\$62	\$67	\$200	Yes	\$1200

#### 6. Explanation of accumulated profits

- a. Month 1: You purchase 100 shares of XYZ Corp at \$50 per share and simultaneously sell a one-month call option with a strike price of \$55, receiving a premium of \$200.
- b. Month 2: The stock's price has increased to \$52 but is still below your calls strike price. Your option expires worthless. You sell another one-month call option with a higher strike price of \$57 and again receive a premium of \$200.
- c. Month 3: The stock's price has risen to \$54, still below your calls strike price. The option again expires worthless. You sell a third one-month call option with a strike price of \$59, receiving another premium of \$200.
- d. Month 4: The stock's price has now reached \$56, but remains below your calls strike price. The option expires worthless once more. You sell a fourth one-month call option, this time with a strike price of \$61, and receive yet another premium of \$200.
- e. Month 5: The stock's price rallies to \$62. Your call option with a strike price of \$61 is exercised, and you sell your 100 shares at the strike price. Your profit from selling the shares is \$1,100 ( $\$61$  selling price -  $\$50$  purchase price =  $\$11$  profit per share, multiplied by 100 shares), and you keep the \$200 premium. This month's total profit is \$1,300.
- f. In total, over this five-month campaign, you have made a profit of \$2,100 from selling premiums and the stock itself. If the initial investment was \$5,000 (100 shares at \$50 each), this represents a return on investment of 42% over five months. Annualized, this return rate would be approximately 100.8% if you were able to maintain similar results throughout the year.



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#### III. Understanding the Underlying Stock

The importance of choosing the right stock: Choosing the right stock to execute a covered call strategy is crucial. The success of your strategy greatly depends on the underlying asset, in this case, the stock.



- 1. Fundamental Analysis:** First, you should conduct a thorough fundamental analysis of the stock. This includes evaluating the company's financial health, its market position, industry trends, and any news or events that could potentially impact its stock price. A stable company with steady earnings growth can be a good candidate for a covered call strategy.
- 2. Dividend Yield:** Stocks with a decent dividend yield can be beneficial for a covered call strategy. It's like having an additional income stream, apart from the premium received from selling call options.
- 3. Stock Volatility:** Stocks with high volatility can provide higher premiums due to the increased risk associated with them. However, they also come with a greater chance of price movements that could lead to the early exercise of the option. On the other hand, very low volatility might result in very low premiums. Therefore, choosing a stock with moderate volatility can be ideal for covered call writing.
- 4. Liquidity:** The stock chosen should have good liquidity to ensure ease of trading. Also, the options associated with that stock should be liquid enough to allow for easy entry and exit.
- 5. Market Outlook:** Your overall market outlook or bias towards the stock should be either neutral or slightly bullish. As you'll be obligated to sell your shares if the stock price increases above the strike price, the stock shouldn't be one that you anticipate will have a significant bullish run in the short term.
  - a. Remember,** when implementing a covered call strategy, it's about consistent income generation and risk management, not chasing the highest possible returns. Therefore, choosing the right stock is a crucial first step.
- 6. Technical Analysis:** Besides fundamental analysis, technical analysis also plays a crucial role in determining the best stocks for covered calls. By studying chart patterns, technical indicators, and price trends, you can identify optimal entry and exit points for your trades.



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7. **Support and Resistance Levels:** Understanding where the key support and resistance levels are can help you select a suitable strike price for your calls. Generally, resistance levels could serve as a good benchmark for the strike price as stocks often struggle to break through these levels.
8. **Trend Analysis:** Analyzing the overall trend of the stock is important. Ideally, for covered call strategies, a sideways or slightly uptrending market works best.
9. **Indicators:** Utilize indicators such as the Relative Strength Index (RSI), Moving Averages, or Bulls 'n Bears to gauge the stock's momentum and volatility. Overbought conditions may signal a good time to sell covered calls as the stock may struggle to rise much further.
10. **Volume Analysis:** A sudden increase in volume can signify a strong move. It's important to be aware of such changes as they could affect the likelihood of option assignment.
11. **By combining both fundamental and technical analysis, you increase your chances of executing a successful covered call strategy. It's not just about picking the right stock, but also about choosing the right time to enter and exit your positions.**





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IV. The Role of Volatility in Covered Calls: Volatility is a statistical measure of the dispersion of returns for a given stock or market index. In most cases, the higher the volatility, the riskier the security. In the context of options, volatility is a very crucial element as it directly impacts the pricing of options. There are two types of volatility you should understand:

- **Historical Volatility:** This refers to the past fluctuations of a stock. It's calculated based on the standard deviation of the stock's daily price changes in the past.
  - **Implied Volatility:** This refers to the market's forecast of a likely movement in a security's price. It's directly reflected in the pricing of options. The higher the implied volatility, the higher the expected movement (up or down), and thus, the higher the option premium.
1. **Volatility and Option Premiums:** The level of implied volatility in the market affects the premium of an option. When implied volatility is high, option premiums are higher because there's a greater expected range of movement in the stock's price. This higher range of movement increases the probability that an option could finish in-the-money at expiration.
    - a. Conversely, when implied volatility is low, option premiums are lower because there's a smaller expected range of movement in the stock's price, thereby reducing the chance that an option could finish in-the-money.
    - b. As a covered call seller, you want to sell options when implied volatility (and hence premiums) is high. However, keep in mind that high volatility also suggests a higher risk of large price swings, which could lead to early assignment. Thus, managing volatility is a careful balance in a covered call strategy.
  2. **Using the Volatility Index (VIX) as a guide:** The Volatility Index, or VIX, often referred to as the "fear gauge," is an index that measures the market's expectation of future volatility. It's calculated from the implied volatilities of a wide range of S&P 500 index options. This makes the VIX a valuable tool for traders to gauge market sentiment and potential future volatility.

Here's how you can use the VIX in your covered call strategy:

- **High VIX values:** High VIX values typically indicate increased fear among investors, translating to higher market volatility. When the VIX is high, option premiums are also inflated due to the increased volatility. This could present more lucrative opportunities for covered call writers since they can collect higher premiums. However, it's important to remember that a higher VIX also means larger potential price swings in the underlying stock, which could lead to early assignment.
- **Low VIX values:** On the contrary, a low VIX suggests complacency among investors, implying lower volatility. In these circumstances, the premiums received from writing covered calls would be lower. However, the risk of large price swings (and therefore early assignment) is also reduced.

By keeping an eye on the VIX, you can have a better understanding of the broader market sentiment and adjust your covered call strategy accordingly. Remember, however, the VIX is just one tool of many, and should be used in conjunction with other analysis techniques and indicators such as Bulls 'n Bears to make well-rounded trading decisions.



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### V. Mistakes to Avoid in Covered Call Trading

#### 1. Mistake #1: Selling covered calls on a bearish market:

- a. Examples and Outcomes: Suppose you have shares in Company A, which currently trades at \$50, and you expect the price to decline in the coming months. You decide to sell a covered call with a strike price of \$55, expiring in a month, for a premium of \$2. Three possible outcomes might occur:
  - i. Outcome 1: The stock price falls, as expected. The option expires worthless, and you keep the premium. However, the decline in the stock's value exceeds the premium received, resulting in a net loss.
  - ii. Outcome 2: The stock price stays around \$50. The option expires worthless, you keep the premium, and your stock position remains relatively unchanged.
  - iii. Outcome 3: Unexpectedly, the stock price rises to \$55. The option gets exercised, your shares get called away, and you accidentally make max profit.



Chart Figure #1: Don't put on a covered call in a bearish market

- b. Persisting in a covered call trade despite bearish indicators: The primary risk of selling covered calls is the potential decrease in the underlying stock's price. If bearish indicators emerge after initiating a covered call trade, it's crucial not to be blinded by the small premium from the call. Recognize the bearish signals and consider exiting the trade.



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- c. One of the greatest misconceptions about covered calls is the belief that the goal is to avoid having your shares called away. However, in reality, getting your shares called away is actually the desired outcome and can lead to the largest profit. Many covered call traders mistakenly view it as a negative event, but in fact, it represents the culmination of a successful trade and the realization of the maximum profit potential.



2. **Mistake #2: Strategies for Exiting and Finding New Opportunities:** Recognizing when to exit a trade is as essential as knowing when to enter. Many traders hang onto a position too long. If the stock shows bearish signals, it might be in your best interest to exit the position, even if it means buying back the call option at a higher price. You can then search for new opportunities in markets exhibiting neutral to bullish trends.
3. **Mistake #3: Selling a covered call on a strongly bullish stock:** If you're highly bullish on a stock, selling a covered call might cap your potential upside. For instance, let's say you own shares of Company B, currently trading at \$100. You're highly optimistic about the company and sell a call option with a strike price of \$105 for a premium of \$3. If the stock





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price soars to \$120, your profit is limited to \$105 plus the \$3 premium, missing out on the additional \$15 increase.

4. Mistake #4: Selling a new covered call below the initial purchase price of the stock after a market fall.
  - a. Examples and Outcomes: For instance, you bought 100 shares of Company C at \$75. You sold a covered call, but then the stock price dropped to \$70. If you sell a new covered call with a strike price below \$75 (your initial stock purchase price), you risk locking in a loss if price rebounds and the option gets exercised.
  - b. Strategies for Proper Placement and Timing: It's important to adjust the strike price and expiration of your new covered call to align with your updated view of the stock. Consider selling a covered call with a strike price at or above your initial stock purchase price, even if it means choosing a longer expiration date or skipping a month.



Chart Figure #2: Never sell (roll for more time) below your initial long entry.

5. Mistake #5: Selling covered calls on a stock with a significant unrealized capital gain
  - a. Example and Outcomes: Imagine you bought shares of Company D a few years ago at \$20, and they are now worth \$80 each. If you sell a covered call and it gets exercised, you will realize a large capital gain, which could lead to a significant tax



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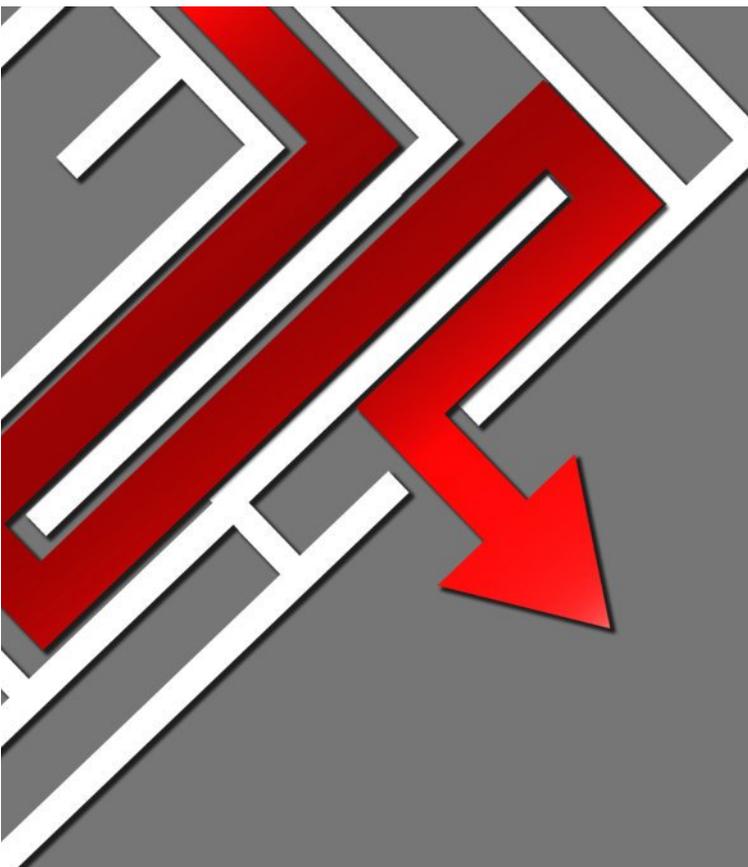
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liability. The option premium you received might not be enough to offset this tax burden.

- i. Note, if you're trading in a tax free self directed IRA or 401k, this is not an issue for you. Go ahead, and sell, sell, sell like hell.
- ii. On the other hand, if you're trying to liquidate a large position, and you know you're going to be hit with a large tax bill, you can sell a call to help cover your tax liability.

**VI. Exit Strategies:** Explanation of different exit strategies, including rolling out, rolling up, and unwinding the position.

A critical aspect of trading covered calls is knowing when and how to exit your position. Depending on market conditions and the performance of your underlying stock, you might choose to employ one of the following exit strategies:



1. **Rolling Out:** This strategy involves buying back the short call and selling another one with a later expiration date. Traders usually do this when they believe the stock has more upside potential in the coming months.
  - a. **When to Use:** This strategy is best used when the stock price remains under the strike price as the expiration date approaches. If you believe the stock has more room to grow in the future, rolling out allows you to collect another premium and keep the position open.
2. **Rolling Up:** In this strategy, you buy back the short call and sell another one with a higher strike price. This is used when the stock price has moved significantly above the calls strike price, and you believe it will continue to rise.
  - a. **When to Use:** This strategy is ideal when the stock price has significantly exceeded the calls strike price, and you believe it will continue to rise. Rolling up enables you to collect additional premium while also raising the price at which your stock might get called away.
3. **Unwinding the Position:** This involves selling the stock and buying back the short call. Traders use this strategy when they no longer believe in the upside of the stock or want to prevent further losses.
  - a. **When to Use:** This strategy is used when the outlook on the stock becomes bearish or when you want to free up capital for other trades. It is also used when the stock price has fallen significantly below the cost basis, and there is little chance of recovery in the near term. Unwinding allows you to cut your losses and move on to new opportunities.



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#### VII. Other Risks in Covered Call Trading

##### 1. Impact of dividend dates and ex-dividend dates:



- a. One important factor to consider in covered call trading is the impact of dividend and ex-dividend dates. When a company announces a dividend, it also announces a date by which an investor must own shares to qualify for the dividend payout. This is called the ex-dividend date.
- b. If you have sold a covered call and the ex-dividend date is approaching, there's a risk that your stock may be assigned early if the dividend amount is greater than the remaining time value of the call option. This is because the call option buyer may exercise the option to qualify for the dividend.
- c. It's essential to be aware of these dates to manage your strategy effectively. If early assignment due to an upcoming dividend is a risk, you might choose to close out the position or roll it out to a later expiry.

##### 2. Risk of early assignment:

- a. Early assignment is a risk inherent in covered call trading. While options usually aren't exercised until they are close to or at expiration, there's always a chance that the holder of the option will choose to exercise it early.
- b. Early assignment generally occurs when a stock is due to pay a dividend and the dividend amount is greater than the extrinsic value (time value) left in the options. However, it can also happen if the stock has made a significant move upwards and the call buyer wants to capture that gain.
- c. The risk of early assignment is not necessarily a negative. If the call is exercised early, you receive the strike price for your stock, which was part of your initial strategy. However, it does mean you might miss out on additional potential gains if the stock price continues to rise, and it may have tax implications.
- d. By monitoring your positions and the market closely, you can manage the risk of early assignment. If the risk becomes high, one strategy is to buy back the sold call and sell another one with a later expiration or higher strike price, in what's known as "rolling" the option. This can help to avoid early assignment.
- e. Keep in mind that assignment is ultimately controlled by the option holder and you can't prevent it if the holder decides to exercise. Therefore, the risk of early assignment should be factored into your overall trading strategy and risk management plan.



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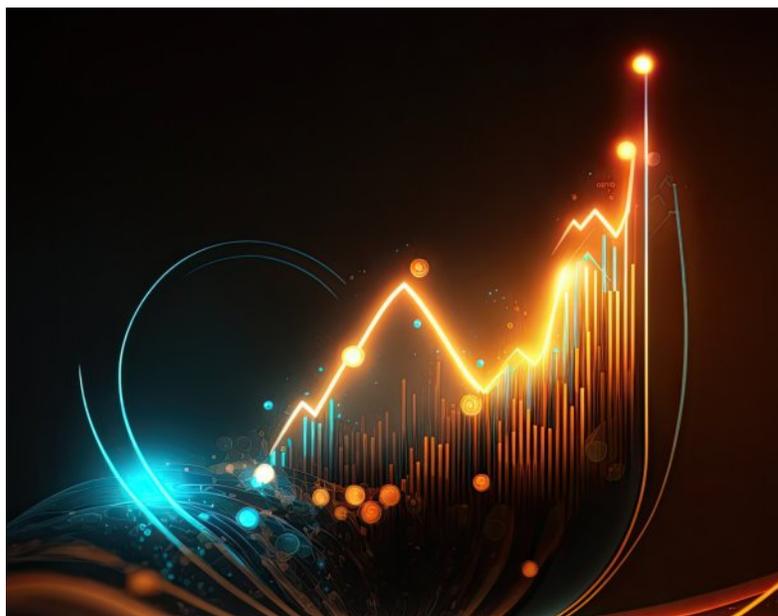
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### VIII. Strategies to Enhance Covered Call Trading

#### 1. Introduction to Synthetic Covered Calls (Poor Man's Covered Call)

- i. The Synthetic Covered Call, also known as a Poor Man's Covered Call, is a creative alternative to traditional covered calls. It mirrors the profit and loss potential of a standard covered call, but involves significantly less capital. Here's how it works:
  - ii. Instead of owning the underlying stock, you own a long-term (usually LEAPS - Long-term Equity Anticipation Securities) in-the-money call option.
  - iii. You then sell shorter-term out-of-the-money call options against this long-term option.
- a. Advantages:
- i. **Less Capital Intensive:** The strategy requires less capital upfront compared to traditional covered calls.
  - ii. **Time Decay:** The strategy capitalizes on the slower time decay of longer-term options and the faster time decay of shorter-term options. This potentially allows for more returns on capital over time.
- b. Risks:
- i. **Long-term Option Value:** If the underlying stock goes down, the long-term option could decrease in value, potentially losing more than the premium received from the short-term option.



#### 2. Strategy to Increase Call Option Value and Trading Frequency

- a. To boost potential returns from covered call trading, you could consider increasing the value of the call options you sell and your trading frequency.
- i. **Increasing Option Value:** Consider selling options that are slightly in-the-money or at-the-money, instead of out-of-the-money. This provides more premium upfront but increases the risk of the stock being called away. (Which isn't necessarily a bad thing, depending on how you've structured your strategy.)
  - ii. **Increasing Trading Frequency:** Actively manage your positions by closely monitoring the market and your underlying stocks. If opportunities arise, you could buy back a call and sell another one, a strategy referred to as "rolling" the option.
    1. **Rolling Options:**
      - a. **Rolling Out:** If you believe the stock will continue to appreciate, roll out to a later expiry.
      - b. **Rolling Up:** If the stock has risen significantly and you want to secure more potential upside, roll up to a higher strike price.

#### 3: Advantages of Having a Higher Likelihood of Early Exercise

In the world of covered call trading, the potential for early exercise by the option buyer often raises questions and concerns among traders. However, it's essential to recognize



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that early exercise can be advantageous for covered call sellers and can align with specific trading objectives. Let's explore the benefits of having a higher likelihood of early exercise and how it can enhance your covered call trading strategy.

**1. Capturing Gains:** One of the primary advantages of early exercise is that it allows the option buyer to capture gains when the stock price rises above the strike price. As the seller of the covered call, this results in having your shares called away at the strike price. While this may seem like a drawback at first, it's crucial to consider the profit potential embedded in the trade.

When the stock price rises above the strike price, the option buyer exercises their right to buy the shares from you at the agreed-upon strike price. As the seller, you benefit from selling the shares at the strike price, which may be higher than the stock's original purchase price. This can result in a profitable outcome, aligning with your intention of generating income from the covered call trade.

**2. Opportunity to Generate More Premium:** Having your shares called away early creates an opportunity to sell another covered call on a new batch of shares. This ongoing cycle of selling covered calls, having them exercised, and then selling new covered calls can lead to consistent premium income. By continually engaging in covered call trades, you have the potential to earn regular income from the premiums received.



Moreover, this process can enhance your overall return on investment (ROI) by repeatedly collecting premiums and participating in stock appreciation. As long as you continue to select appropriate strike prices and manage risk effectively, you can take advantage of the premium income and potential for capital appreciation.

**3. Aligning with Trading Goals:** The advantages of early exercise in covered call trading are best leveraged when aligned with your specific trading goals and risk tolerance. It's essential to consider your objectives carefully before selecting the strike price and expiration date for your covered call trades.

For example, if your primary objective is to generate income and capture gains from premium collection, selling at-the-money or near-the-money covered calls might be more suitable. On the other hand, if you prefer to retain your shares and participate in stock appreciation, selling out-of-the-money covered calls may be a better fit.

By having a balanced approach and aligning your covered call trading strategy with your financial goals, you can optimize your potential returns and manage risk effectively.



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#### IX. Choosing the Right Strike Price for Selling Covered Calls

Determining which strike price to sell for your covered calls is a crucial decision that could significantly impact the profitability of your trade. In this section, we will explore the benefits and risks associated with selling at-the-money (ATM), near-the-money (NTM), and out-of-the-money (OTM) call options.

1. **At-The-Money Call Options (ATM):** Selling an ATM call option means the strike price is equal to the current market price of the underlying stock.
  - a. **Advantages:**
    - i. **Higher Premium:** Since the strike price is very close to the stock's current trading price, the premium received will be higher compared to an OTM call.
    - ii. **Immediate Profit Potential:** If the stock price doesn't move much or falls, you keep the entire premium.
  - b. **Disadvantages:**
    - i. **Limited Upside:** If the stock price rises significantly, your profit is capped at the strike price plus the premium received.
    - ii. **Higher Risk of Assignment:** There is a higher likelihood of the option being exercised, and you may have to sell your stock.
2. **Near-The-Money Call Options (NTM):** Selling a NTM call option means the strike price is slightly above (for call options) the current market price of the underlying stock.
  - a. **Advantages:**
    - i. **Balanced Premium and Upside Potential:** This provides a balance between receiving a reasonable premium and leaving room for potential stock price appreciation.
  - b. **Disadvantages:**
    - i. **Risk of Assignment:** The closer the strike price to the current stock price, the higher the chance of the option being exercised.
3. **Out-Of-The-Money Call Options (OTM):** Selling an OTM call option means the strike price is above the current market price of the underlying stock.
  - a. **Advantages:**
    - i. **Profit from Stock Appreciation:** You allow room for the stock to appreciate up to the strike price. If the stock price stays below the strike price, you keep the premium and still own the stock.
  - b. **Disadvantages:**
    - i. **Lower Premium:** Premiums for OTM options are usually less than ATM or NTM options.
    - ii. **Less Downside Protection:** The lower premium provides less downside protection if the stock's price drops.
4. **In-The-Money Call Options (ITM):** Believe it or not, there are scenarios where you might consider selling an ITM call option, which means the strike price is below the current market price of the underlying stock. (Most traders will never do this, but let's mention it here none-the-less.)
  - a. **Advantages:**
    - i. **Higher Premium:** ITM options typically carry higher premiums due to their intrinsic value.



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- ii. **Partial Downside Protection:** The premium received from selling an ITM call provides some downside protection against potential stock price declines.
- b. **Disadvantages:**
  - i. **Increased Risk of Assignment:** Selling ITM calls increases the likelihood of early assignment, as the option buyer may exercise the option to capture the intrinsic value.
  - ii. **Greater Chance of Losing the Stock:** If the stock price rises above the strike price, there is a higher probability of the stock being called away.

While selling ITM covered calls can generate higher premiums and offer partial downside protection, it's important to carefully assess the risk of assignment and consider the potential impact on your overall investment strategy.

While these are general guidelines, the choice of strike price should be tailored to each investor's individual risk tolerance and market outlook. It's important to remember that there's no one-size-fits-all answer in options trading. The key is to find a strategy that aligns with your investing goals and risk tolerance.





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### X. Understanding the Value of Covered Call Options and Expiration

Let's delve deeper into understanding the value of covered call options and the implications of holding the option until expiration. In this real-world example let's illustrate how the option's value may change over time and what happens if you hold the option until expiration.

**A Real-World Covered Call Trade Example:** In this example we sold the call option with 22 days until expiration, therefore we're four days into the trade.

- Stock Symbol: VLO
- Stock 100 Share Purchase Price: \$124.88
- Sold Call Strike Price: \$130.00
- Option Premium: \$198.00
- Days Till Expiration: 18

#### The Changing Value of the Covered Call Option:

- When you sell a covered call, you receive the option premium upfront. In this case, you received \$198.00.
- The value of the option may fluctuate based on changes in the underlying stock price and other market factors.
- As the stock price approaches or exceeds the strike price of \$130, the value of the call option may decrease, leading to a loss in the market value of the option.



#### Holding the Option Until Expiration:

- Regardless of the changing market value of the option during the holding period, you will keep the full premium of \$198 if the option expires worthless (i.e., the stock price remains below \$130 at expiration).
- The goal of selling covered calls is to generate income through the option premium and potentially have your shares called away at a profit.
- In this example, if the stock price remains below \$130 at expiration, you'll keep the full \$198 premium, achieving a return of approximately 1.58% on the \$12,488 investment (100 shares of VLO at \$124.88 each).



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Implications of Exiting Early vs. Holding Until Expiration:

- **Exiting early:** If you decide to liquidate your position before expiration, the value of the option will be subject to current market conditions and may result in a gain or loss compared to the initial premium received.
- **Holding until expiration:** By holding the option until expiration, you lock in the full premium as profit if the option expires worthless. This allows you to achieve the desired income from the trade.

Here's an example of exiting early, and what you can expect.

- If you choose to liquidate your covered call position before expiration, you won't have to give back the entire \$198 premium you received upfront. The -\$75.00 loss you see in the option's market value is a reflection of the change in the option's price since you sold it.
- When you sell a covered call, you collect the premium immediately, and that premium is yours to keep, regardless of how the option's market value changes. If you decide to exit the trade early, you can do so by buying back the call option in the market. If the option's market value is -\$75.00 compared to the premium you initially received, you would pay \$75.00 to buy back the option.
- So, in this scenario, if you choose to liquidate your position after four days and the option is showing a -\$75.00 loss, you would effectively return \$75.00 of the \$198.00 premium you initially received, and you'd keep the difference of  $\$198.00 - \$75.00 = \$123.00$ . This would result in a net profit of \$123.00 from the covered call trade, considering the \$198 premium you received at the start.
- Remember that the value of the option can fluctuate based on changes in the stock price, market conditions, and other factors. Exiting early allows you to capture the current market value of the option, but you still retain the premium received upfront as profit.

Evaluating Early Exit in Covered Call Trading

In covered call trading, it is essential to be prepared for various market scenarios, including the possibility of early exit from your covered call position. Early exit decisions depend on several factors, such as the stock's performance, the time remaining until expiration, and your outlook for future market movements. In this section, we will explore the concept of early exit using a real-life example from our covered call strategy.

**Example: Valero Energy Corp (VLO) Covered Call Trade**

Let's revisit our previous example of a covered call trade in Valero Energy Corp (VLO). You purchased 100 shares of VLO at \$124.88 and sold a covered call with a strike price of \$130 for a premium of \$198. As the stock price surged to \$129 in just four days, the value of the call option decreased, showing a -\$75 loss in the option's market value.





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#### Understanding Early Exit and Its Implications

In this situation, you face an important decision: whether to continue holding the covered call until expiration or opt for early exit. Let's consider the implications of each choice:

##### 1. Holding Until Expiration:

- a. If you decide to hold the covered call until expiration (18 days away), you retain the \$198 premium you received upfront.
- b. Regardless of the current value of the option (in this case, showing a -\$75 loss), you will keep the entire premium at expiration.

##### 2. Opting for Early Exit:

- a. If you choose to exit the trade early, you can buy back the call option at the current market value, which is showing a -\$75 loss.
- b. By buying back the option, you effectively return \$75 of the \$198 premium you initially received.
- c. After early exit, you still retain the difference between the premium received and the loss incurred, resulting in a net profit of \$123 ( $\$198 - \$75$ ).

#### Considering Future Market Movements

The decision to opt for early exit depends on your outlook for the stock's future performance. If you believe that the stock's price will continue to rise, and you want to participate in additional upside potential, you may consider liquidating the covered call position. By doing so, you secure the profit earned from the premium and allow your shares to benefit from the further increase in stock price.

However, if you have a different market outlook or if the stock has reached your desired target price, you might choose to hold the covered call until expiration. By doing this, you can maximize the premium received and potentially allow the stock to be called away at the strike price, realizing your maximum profit.



Let's suppose I sold a covered call option for \$183.00, but due to a decline in the underlying market, in my trading software, my current gain on the option shows as \$89.50. If I choose to liquidate the covered call, will I receive the \$183.00 from selling the call, and on top of that, the \$89.50 currently showing in my account as the option's value?

- No, if the underlying market falls and your gain on the option shows \$89.50, it means that the current market value of the option is \$89.50 less than the premium you received when you initially sold the call for \$183.00. If you choose to liquidate the covered call at this



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point, you will buy back the call option at its current market value of \$89.50, and you would effectively give back \$89.50 of the \$183.00 premium you initially received.

- After liquidating the covered call, you would still retain the difference between the premium received and the loss incurred, which is \$93.50 (\$183.00 - \$89.50). In this case, you would realize a net profit of \$93.50 on the covered call trade, despite the underlying market's decline.
- Remember, the premium you initially received is separate from the current market value of the option. The current value represents the loss or gain in the option's price due to changes in the stock's performance and market conditions.

What's the Takeaway?:

- It's essential to understand that the market value of the option during the holding period doesn't overly affect the final outcome if the option expires worthless.
- Covered call trading is a strategy aimed at generating income and managing potential risks. The option premium received is yours to keep, regardless of how the market value of the option changes over time.
- By learning to analyze stock price movements, market conditions, and expiration dates, traders can make informed decisions about their covered call trades and maximize their potential returns.
- In covered call trading, early exit decisions depend on your evaluation of the stock's future performance and your specific investment goals. Remember that the premium received upfront is yours to keep regardless of market fluctuations. By understanding the implications of early exit and considering your market outlook, you can make informed decisions to optimize your covered call trading strategy.





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XI. Using Technical Analysis in Covered Call Trading: Technical analysis is a valuable tool for covered call traders as it can provide insights into price movements and help in formulating effective strategies. In this section, we will introduce the concepts of reading charts, utilizing Fibonacci retracements and extensions, and understanding Elliott Wave theory.

1. Introduction to Reading Charts: Reading charts involves analyzing historical price data and identifying patterns and trends to make informed trading decisions. Key elements of chart analysis include:
  - a. Support and Resistance Levels: These are price levels at which the stock tends to find support or face resistance.
  - b. Trend Lines: These are lines drawn to connect consecutive highs or lows, indicating the direction of the trend.
  - c. Chart Patterns: Patterns such as triangles, double tops or bottoms, head and shoulders, and more can provide indications of potential price movements.
  - d. Moving Averages: These lines smooth out price fluctuations and help identify the overall trend.
2. Utilizing Fibonacci Retracements and Extensions: Fibonacci retracements and extensions are based on mathematical ratios that are often observed in price movements. Key levels used in Fibonacci analysis include:
  - a. Fibonacci Retracement Levels: These levels (38.2%, 50%, and 61.8%) indicate potential support or resistance areas where price pullbacks may find support or face resistance before continuing in the original direction.
  - b. Fibonacci Extension Levels: These levels (127.2%, 161.8%, and 261.8%) suggest potential price targets for upward moves after a retracement.
    - i. Incorporating Fibonacci & Elliott Wave analysis into covered call trading can help identify potential entry or exit points and determine optimal strike prices for selling covered calls. If you understand these concepts, you'll do much better at trading covered calls, and trading in general.

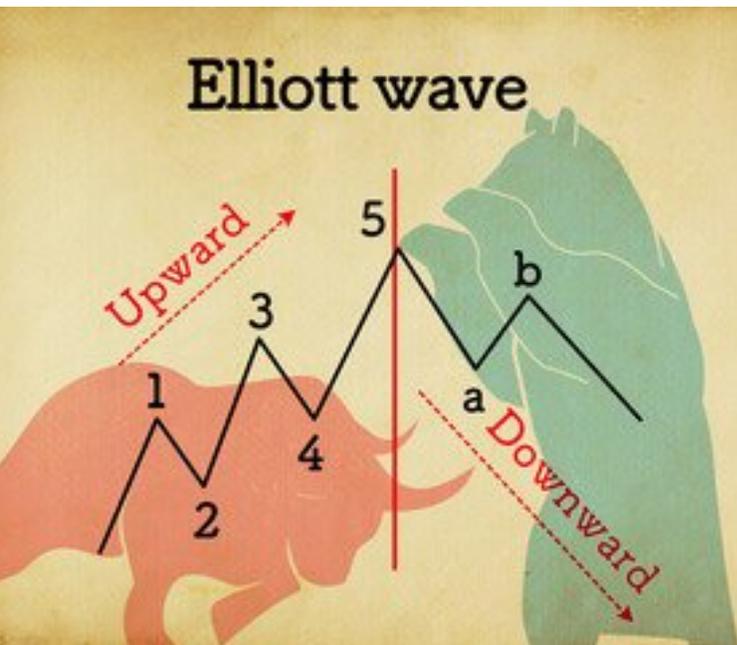




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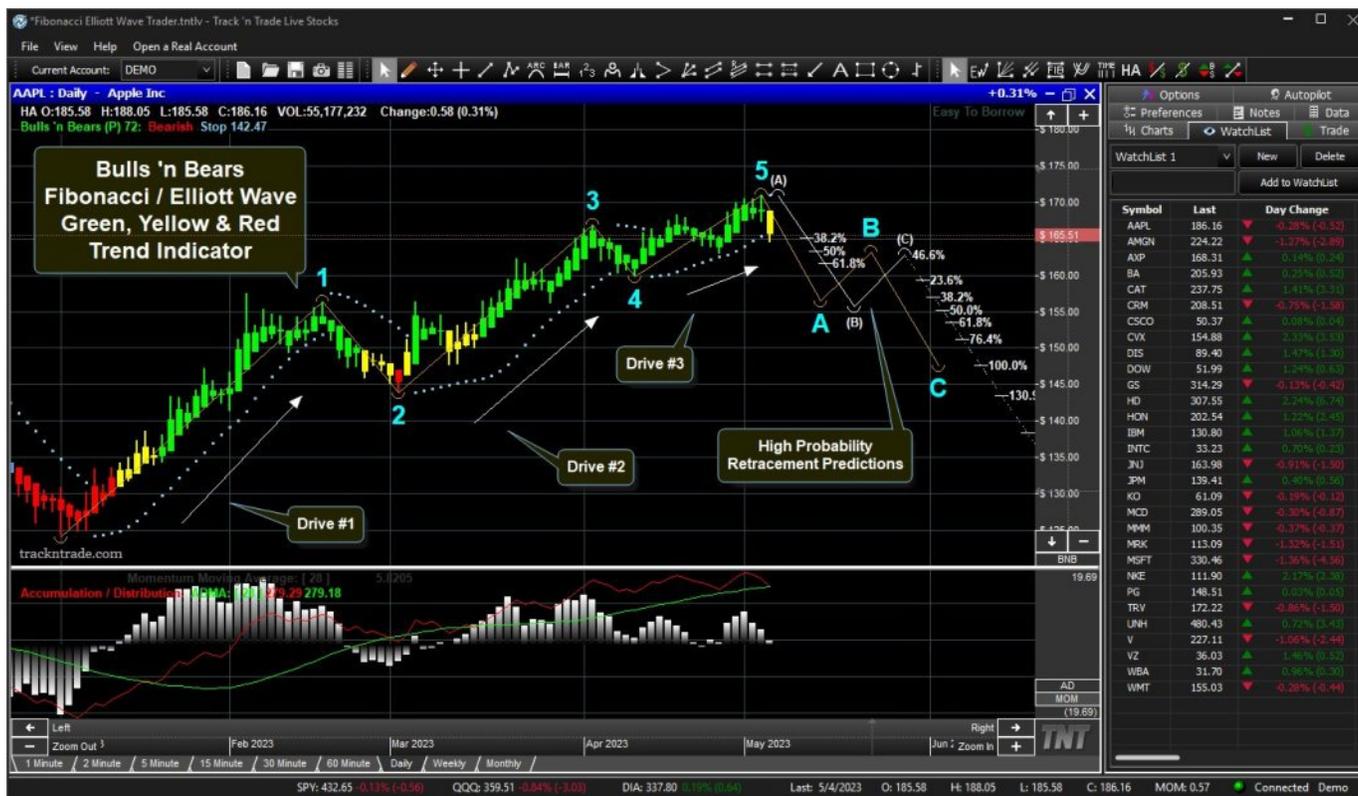
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1. Understanding Elliott Wave Theory: Elliott Wave theory is a technical analysis approach that seeks to identify and predict market trends based on repetitive wave patterns. The theory suggests that markets move in a series of five waves in the direction of the trend, followed by three waves in a corrective pattern. Covered call traders can utilize Elliott Wave theory to:

- a. Identify Trend Reversals: The completion of a five-wave pattern followed by a three-wave correction can signal a potential trend reversal, helping traders adjust their covered call strategies accordingly.
- b. Confirm Trend Continuation: If the market is in a strong trend, Elliott Wave analysis can help confirm the continuation of the trend, supporting the decision to sell covered calls.
- c. The single best tool devised to help traders identify these patterns of Fibonacci and Elliott Wave have been melded together in the proprietary indicator known as The Bulls 'n Bears; you can find it in Track 'n Trade Live, Stocks & Futures.

While technical analysis tools can be powerful aids in covered call trading, it's important to note that no analysis method is foolproof. These tools should be used in conjunction with other fundamental and risk management considerations to make well-informed trading decisions.





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#### XII. Using a Broker and Understanding Fees: What to Look for in a Broker when Planning to Trade Options.



1. When choosing a broker for options trading, it's important to consider the following:
  - a. **Options Trading Platform:** Ensure that the broker offers a user-friendly platform with advanced options trading tools and features that suit your trading style and needs. I recommend Stocks and Commodities seven time reader's choice award winning platform from Gecko Software, Track 'n Trade LIVE; you can search and find them online.
  - b. **Options Contract Availability:** Verify that the broker provides a wide range of options contracts on different underlying assets to maximize your trading opportunities.
  - c. **Commission Structure:** Evaluate the broker's commission structure to understand the costs associated with trading options.
  - d. **Margin Requirements:** If you plan to engage in more advanced options strategies that involve margin, check the broker's margin requirements and ensure they align with your trading objectives and risk tolerance.
  - e. **Customer Support:** Assess the quality and availability of customer support services provided by the broker, as prompt assistance can be crucial when trading options.
    - i. I recommend Gecko Financial Services online at: [www.GeckoFS.com](http://www.GeckoFS.com)
2. **How Commission Fees can Impact Returns:** Commission fees can significantly impact your overall returns, especially for frequent options traders. It's essential to understand how commission fees work and consider them in your trading strategy. Here are some important points to consider:
  - a. **Per-Contract vs. Per-Trade Fees:** Some brokers charge a commission fee per contract, while others charge a flat fee per trade. Consider your trading volume and frequency to determine which fee structure is more cost-effective for your trading style.
  - b. **Trade Size Considerations:** Take into account the number of contracts you typically trade in each transaction. Higher trade sizes may attract higher commission fees, potentially impacting your returns.
  - c. **Comparison Shopping:** Compare commission fees across different brokers to find competitive rates. However, keep in mind that low fees should not be the sole determining factor; also consider the quality of the broker's services and platform.
  - d. **Fee Negotiation:** In some cases, brokers may offer fee discounts based on trading volume or if you negotiate directly with them. Don't hesitate to explore such options if you have substantial trading activity.

Understanding commission fees and factoring them into your trading strategy is crucial for maximizing your potential returns and managing your overall trading costs effectively.



# Covered Calls & The Loop

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XIII. Summary: This skill of trading covered calls is not just a useful addition to your investing toolbox, but it can also form a vital component of your income strategy. Consider each stock you own as a separate property in your investment portfolio. As with real estate, the more properties you have, the greater your potential for income.

Instead of physically acquiring more real estate and navigating through the complexities associated with property management, simply accumulate more shares of suitable stocks and start writing covered calls on them. This is akin to renting out additional properties to tenants. The principles of the real estate rental market apply here: you want to have as many 'properties' (stocks) generating 'rent' (premiums) as possible.



Just like the occasional vacancy in your rental properties, there will be months where your covered call strategy might not pan out as expected. This is a normal part of the process and not dissimilar to having a vacant property until you find a new tenant.

Just as real estate income is subject to taxes, so too are your profits from covered call strategies. Both activities involve a careful balance of risk and reward, and both require thoughtful management to achieve long-term success.

Moreover, both strategies involve the cyclical nature of markets – just as property markets have their ups and downs, so do stock markets. A seasoned landlord knows not to panic if the property market temporarily dips, and similarly, a savvy covered call trader understands the ebb and flow of the stock market and uses it to their advantage.

In essence, think of covered call trading as a form of real estate investment but without the need for property maintenance, the handling of tenants, or geographical limitations. Instead, you have a global market at your fingertips, and your income is generated from the strategic selling of options rather than physical rent.



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#### Covered Call Trading with Commodity Futures: Expanding Your Trading Horizons

Covered call trading is not limited to traditional stocks and options. It can also be successfully applied to commodity futures, particularly index futures. Trading covered calls in the futures market offers several advantages and opportunities that traders should consider. Here are some key points to keep in mind:

- **No Pattern Day Trading Rules:** Unlike stock trading, commodity futures trading is not subject to the pattern day trading rules imposed by the U.S. Securities and Exchange Commission. Traders can actively participate in covered call strategies without limitations on the number of day trades made within a certain timeframe.
- **Leveraged Accounts:** Commodity futures trading allows for leverage, which means traders can control a larger position with a smaller amount of capital. This leverage can enhance potential returns when implementing covered call strategies.
- **Mini and Micro-Mini Markets:** The futures market offers mini and micro mini contracts, designed specifically for smaller account holders. These contracts allow traders with limited capital to participate in covered call trading with reduced exposure and risk.
- **Fast Execution and Liquidity:** Commodity futures markets are known for their high liquidity and fast execution. Traders can quickly enter and exit positions, allowing for efficient implementation of covered call strategies.
- **Diversification Opportunities:** Trading covered calls with commodity futures provides an additional avenue for diversifying an investment portfolio. By incorporating futures contracts based on different underlying commodities or indices, traders can achieve broader exposure to various market sectors.
- **Potential for Enhanced Returns:** The leverage available in commodity futures trading, combined with the premium collected from selling covered calls, can potentially result in enhanced returns compared to traditional stock trading.
- **Hedging and Risk Management:** Commodity futures can serve as effective hedging instruments, allowing traders to manage risk associated with their underlying stock positions. By selling covered calls on futures contracts, traders can protect against adverse price movements and potentially offset losses in their stock portfolio.



When considering covered call trading, don't overlook the advantages of the commodity futures market. Explore the many opportunities it offers, especially the absence of pattern day trading rules, leverage, mini and micro-mini markets, fast execution, and the potential for enhanced returns. Including futures as a part of your overall trading strategy can provide a dynamic and diversified approach to your portfolio.



# Covered Calls & The Loop

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#### Covered Call Trading Checklist; The Gouge

1. **Select the Underlying Stock**
  - a. Choose a stock that aligns with your investment goals and risk tolerance.
  - b. Consider factors such as liquidity, volatility, and market trends.
2. **Evaluate Stock Charts**
  - a. Analyze the stock's price movement using technical analysis tools; Fibonacci Projections are key in determining which strike price to choose.
  - b. Identify key support and resistance levels, trends, and market indicators.
3. **Determine Strike Price and Expiration**
  - a. Select an appropriate strike price based on your risk-reward preferences.
  - b. Choose an expiration date that allows sufficient time for your strategy to unfold; 30 days (monthly income) 90 days (quarterly growth).
4. **Assess Premium and Potential Returns**
  - a. Calculate the premium you will receive for selling the covered call.
  - b. Evaluate the potential returns, (\$ & %) both monthly and annualized, based on the premium and stock price.
5. **Place the Covered Call Trade**
  - a. If you don't already own the stock, purchase the desired number of shares.
  - b. Sell a call option at the chosen strike price and expiration, collecting the premium.
6. **Set Risk Management Parameters**
  - a. Determine the maximum acceptable loss and set a price alert accordingly.
  - b. Establish a plan for managing the trade if the stock price moves unfavorably.
7. **Monitor the Position**
  - a. Keep a close eye on the stock's price movement and market conditions.
  - b. Regularly review the performance of the covered call position.
8. **Implement Exit Strategies**
  - a. Consider rolling out, rolling up, or unwinding the position.
  - b. Have a plan for exiting the trade if the stock price reaches the strike price.
9. **Track and Evaluate Performance**
  - a. Maintain a record of each covered call trade, including entry and exit points, premiums collected, and overall returns.
  - b. Calculate multiple trades as a single P&L equity run; no single trade makes or breaks your strategy.
10. **Continued Education and Adaptation**
  - a. Stay updated on market trends, news, and economic indicators.
  - b. Continuously learn and refine your covered call trading strategies.

By following this checklist, you can ensure that you have considered all the necessary steps before executing a covered call trade. It's meant to serve as a quick reference guide to help you make more informed decisions; reference this checklist prior to putting on each trade.

# THE FIBONACCI EFFECT

HOW TO GAIN DISCIPLINE & COURAGE THROUGH  
KNOWLEDGE & STRATEGY

# The LOOP



# How The Wealthy Retire

by: **Lan H. Turner**



# Covered Calls & The Loop

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#### The Loop - Enhancing Covered Calls with The Loop Strategy

##### I. Introduction to The Loop Strategy

###### A. Recap of The Covered Call Strategy

###### Definition and Purpose

A covered call strategy is an options strategy that involves holding a long position in an underlying asset, such as a stock, and simultaneously selling (or "writing") call options on that same asset. The purpose of this strategy is to generate additional income from the asset, especially in flat or moderately bullish market conditions. By selling the call option, the investor collects a premium, which provides income regardless of how the underlying asset performs.

###### Components

The key components of a covered call strategy include:

- **Underlying Asset:** The investor must own the underlying asset (e.g., shares of a stock) on which the call options are written.
- **Call Options:** The investor sells call options on the underlying asset. The options have a specific strike price and expiration date.
- **Premium:** The income received from selling the call options, known as the premium, is collected upfront by the investor.
- **Obligation:** By selling the call options, the investor takes on the obligation to sell the underlying asset at the strike price if the options are exercised.

###### Benefits and Risks

###### Benefits:

- **Income Generation:** The premium collected from selling the call options provides immediate income.
- **Downside Protection:** The premium received can offset potential losses in the underlying asset to some extent.
- **Profit in Flat Markets:** Even if the underlying asset doesn't appreciate, the investor can still profit from the premium.

###### Risks:

- **Limited Upside Potential:** If the underlying asset's price rises significantly above the strike price, the investor must sell it at the strike price, missing out on additional gains.
- **Potential Losses:** If the underlying asset's price falls, the premium may not be enough to offset the losses.
- **Obligation to Sell:** If the options are exercised, the investor must sell the underlying asset, potentially at an undesirable time.

The covered call strategy is a popular and relatively conservative options strategy that can provide consistent income and some downside protection. However, it does come with risks, particularly the limitation of upside potential and the obligation to sell the underlying asset if the options are exercised.



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#### The Evolution from Covered Calls to The Loop Strategy

The covered call strategy has a long history in the financial markets, dating back to the early days of options trading. It has been a staple strategy for individual investors, portfolio managers, and institutions alike. Traditionally, the covered call strategy has been used to generate additional income on a stock portfolio, especially in flat or moderately bullish markets. It's often considered a conservative strategy, as it can provide some downside protection through the premium received from selling the call options.

**The Birth of The Loop:** The Loop Strategy is an evolution of the traditional covered call strategy, with a unique twist that adds further dimensions to the approach. While the covered call strategy focuses on selling call options on owned shares, The Loop introduces the concept of selling cash-secured puts to buy back shares that were taken away when the covered call got exercised. This "looping" process creates a continuous cycle of income generation and strategic buying and selling of the underlying asset.

#### Comparison

##### Covered Call Strategy:

- **Focus:** Primarily on selling call options on owned shares.
- **Income Generation:** Through the premium received from selling call options.
- **Risk Management:** Limited to the selection of strike prices and expiration dates.
- **Flexibility:** Limited flexibility in reacting to market changes or exercising additional strategies.

##### The Loop Strategy:

- **Focus:** Includes selling cash-secured puts to repurchase shares, in addition to selling covered calls.
- **Income Generation:** Enhanced income potential through both covered calls and cash-secured puts.
- **Risk Management:** More comprehensive risk management through continuous monitoring and strategic adjustments.
- **Flexibility:** Greater flexibility to adapt to market conditions and integrate with other investment strategies.



The Loop Strategy builds on the foundational principles of the covered call strategy but introduces additional layers of complexity and opportunity. By incorporating the selling of



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cash-secured puts and creating a continuous cycle, The Loop offers enhanced income potential, more robust risk management, and greater flexibility in adapting to various market conditions.

#### C. Benefits and Objectives of Implementing The Loop

**Income Generation:** The Loop Strategy is designed to provide consistent income through the selling of options, both covered calls and cash-secured puts. Here's how it works:

- **Covered Calls:** By selling call options on owned shares, investors collect a premium, providing immediate income.
- **Cash-Secured Puts:** After a covered call is exercised and shares are assigned, The Loop introduces the selling of cash-secured puts. This allows investors to collect additional premiums and potentially repurchase the shares at a more favorable price.
- **Continuous Cycle:** The Loop creates a continuous cycle of income generation by repeatedly selling covered calls and cash-secured puts, maximizing the income potential.



#### Risk Management

The Loop Strategy also emphasizes risk management within options trading:

- **Controlled Risk:** By using cash-secured puts (as opposed to naked puts), investors ensure that they have the funds to fulfill the obligation if the put options are exercised.
- **Strategic Adjustments:** The Loop allows for strategic adjustments based on market conditions, underlying asset performance, and individual risk tolerance. This can include rolling options, selecting specific strike prices, or diversifying underlying assets.
- **Downside Protection:** Similar to covered calls, the premiums received in The Loop provide some downside protection, offsetting potential losses in the underlying asset.

#### Flexibility

The flexibility of The Loop is one of its standout features:

- **Market Conditions:** The Loop can be adapted to various market conditions, from bullish to flat or even moderately bearish scenarios.
- **Underlying Assets:** The strategy can be applied to different underlying assets, such as individual stocks, ETFs, or indices, allowing for diversification.
- **Integration with Other Strategies:** The Loop can be combined with other investment or trading strategies, providing a multifaceted approach to portfolio management.

In summary, The Loop Strategy offers a unique and appealing approach to options trading, with the potential for consistent income generation, robust risk management, and remarkable flexibility. By creating a continuous cycle of selling covered calls and cash-secured puts, The Loop allows investors to capitalize on various market conditions and align the strategy with their individual goals and risk tolerance.



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#### Strategic Advantages

The strategic advantages of The Loop over traditional strategies include:

- **Enhanced Income Generation:** By incorporating both covered calls and cash-secured puts, The Loop offers multiple avenues for income generation, potentially increasing overall returns.
- **Improved Risk Control:** The Loop's continuous monitoring and strategic adjustments allow for more precise risk control, aligning the strategy with individual risk tolerance and market conditions.
- **Versatility:** The Loop's design allows for adaptation to various market scenarios and underlying assets, providing a versatile strategy that can be tailored to specific investment goals.

#### Practical Applications

The versatility of The Loop can be seen in various trading scenarios:

- **Bullish Markets:** In bullish markets, The Loop can capitalize on upward momentum through covered calls while preparing to repurchase shares through cash-secured puts if needed.
- **Flat Markets:** During flat markets, The Loop can generate consistent income through premiums, even if the underlying asset's price remains stagnant.
- **Diversified Portfolio:** The Loop can be applied to a diversified portfolio, using different underlying assets to create multiple income streams and reduce concentration risk.
- **Integration with Other Strategies:** The Loop can be combined with other trading or investment strategies, such as hedging or technical analysis, to create a comprehensive and multifaceted approach.

In conclusion, The Loop Strategy offers a distinct and innovative approach to options trading, setting it apart from traditional strategies like The Wheel. Its unique features, strategic advantages, and versatile practical applications make it a valuable tool for investors seeking consistent income, controlled risk, and adaptability to various market conditions.

## II. Closing the Loop: Selling Cash-Secured Puts: Cash-Secured Puts vs. Naked Puts

### Definition

- **Cash-Secured Puts:** A cash-secured put involves selling a put option with the cash on hand to purchase the underlying asset if the option is exercised. The investor has the necessary funds to fulfill the obligation of buying the asset at the strike price.
- **Naked Puts:** A naked put, on the other hand, is the selling of a put option without owning the underlying asset or having the cash to buy it if the option is exercised. It's called "naked" because the seller is exposed to significant risk if the underlying asset's price falls sharply.





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#### Requirements

- **Cash-Secured Puts:** The main requirement for selling cash-secured puts is having sufficient cash reserves to purchase the underlying asset at the strike price if the option is exercised. This ensures that the investor can fulfill the obligation without additional borrowing or liquidation of other assets.
- **Naked Puts:** Selling naked puts doesn't require the investor to have the cash or underlying asset on hand. However, it often requires higher margin requirements and a more extensive approval process with the brokerage due to the increased risk.

#### Comparison

##### Risk Profile:

- **Cash-Secured Puts:** Lower risk, as the investor has the cash to fulfill the obligation. The risk is limited to the potential decline in the underlying asset's price minus the premium received.
- **Naked Puts:** Higher risk, as the investor is exposed to potentially unlimited losses if the underlying asset's price falls significantly, and they don't have the cash to buy it.

##### Potential Benefits:

- **Cash-Secured Puts:** More conservative and controlled, providing a way to potentially buy the underlying asset at a discount or simply earn the premium if the option expires worthless.
- **Naked Puts:** Potentially higher returns due to leveraging, but with significantly increased risk and potential for substantial losses.

In summary, cash-secured puts and naked puts are strategies that involve selling put options, but they differ significantly in their risk profiles and requirements. Cash-secured puts are a more conservative approach, requiring sufficient cash reserves and offering controlled risk. In contrast, naked puts are a more aggressive strategy, with higher potential returns but also increased risk and requirements.

## B. Identifying Opportunities for Selling Cash-Secured Puts within The Loop

### Market Analysis

Analyzing market conditions is essential to identify opportunities for selling cash-secured puts within The Loop Strategy:

- **Trend Analysis:** Understanding the overall market trend helps in selecting the right underlying assets. In a bullish or flat market, cash-secured puts can be an effective way to generate income or potentially acquire assets at a discount.
- **Volatility Analysis:** Higher volatility often leads to higher option premiums, making it an attractive time to sell cash-secured puts. However, it also increases risk, so careful analysis and risk management are crucial.
- **Economic Indicators:** Monitoring economic indicators and news can provide insights into potential market movements, guiding the decision to sell cash-secured puts.

**Selection Criteria:** The underlying assets and strike prices is vital within The Loop Strategy:

- **Underlying Asset Selection:** Look for assets with strong fundamentals, liquidity, and alignment with your investment goals. The Loop may focus on specific sectors, industries, or individual stocks that fit the overall strategy.



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- **Strike Price Selection:** The choice of strike price should balance potential income (higher with lower strike prices) with the desire to own the underlying asset at that price if the option is exercised.
- **Expiration Date:** Selecting the appropriate expiration date allows control over the potential obligation period and can be aligned with the overall market outlook.

#### Timing

Timing plays a crucial role in selling cash-secured puts within The Loop:

- **Entry Timing:** Identifying the optimal time to sell cash-secured puts requires monitoring market conditions, underlying asset performance, and volatility. Timing the entry can maximize premium income and align with strategic goals.
- **Integration with The Loop:** In The Loop Strategy, timing the sale of cash-secured puts after a covered call exercise is essential to create a continuous cycle. This timing ensures that the strategy adapts to market changes and maintains alignment with the overall investment approach.

In conclusion, identifying opportunities for selling cash-secured puts within The Loop Strategy involves careful market analysis, clear selection criteria for underlying assets and strike prices, and strategic timing. By integrating these elements, The Loop can effectively leverage cash-secured puts to enhance income generation, manage risk, and adapt to various market conditions.

#### C. Risk Management and Mitigation with Cash-Secured Puts

##### Risk Identification

Selling cash-secured puts within The Loop Strategy involves several potential risks:

- **Assignment Risk:** If the put option is exercised, the seller must buy the underlying asset at the strike price, potentially at a higher price than the current market value.
- **Market Risk:** A significant decline in the underlying asset's price can lead to losses, even though the risk is limited to the difference between the strike price and the asset's price minus the premium received.
- **Opportunity Risk:** By setting aside cash to secure the put, the investor may miss other investment opportunities.
- **Liquidity Risk:** If the underlying asset lacks liquidity, it may be challenging to manage the position effectively.





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### Monitoring

Continuous monitoring and adjustment are vital to managing risks effectively within The Loop:

- **Regular Review:** Regularly reviewing the positions, market conditions, and underlying asset performance allows for timely adjustments.
- **Adaptive Strategy:** The Loop Strategy should be adaptive, allowing for changes in strike prices, expiration dates, or underlying assets based on market trends and individual risk tolerance.
- **Use of Technology:** Utilizing trading platforms and tools that provide real-time data and alerts can enhance monitoring and facilitate prompt decision-making.

In summary, risk management and mitigation with cash-secured puts within The Loop Strategy require careful identification of potential risks, implementation of specific mitigation strategies, and continuous monitoring and adjustment. By recognizing and addressing the inherent risks of selling cash-secured puts, The Loop can maintain its strategic objectives while controlling exposure and potential losses.

### D. Generating Consistent Income with Cash-Secured Puts

#### Income Potential

Selling cash-secured puts within The Loop Strategy offers significant income potential:

- **Premium Collection:** By selling cash-secured puts, investors collect a premium upfront, providing immediate income. This premium is kept regardless of whether the option is exercised.
- **Continuous Cycle:** Within The Loop, the continuous cycle of selling covered calls and cash-secured puts creates ongoing opportunities for income generation.
- **Potential Asset Acquisition:** If the put is exercised, the investor may acquire the underlying asset at a favorable price, potentially leading to further income through dividends or future price appreciation.

### Strategy Optimization

Optimizing the strategy for maximum income involves several considerations:



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- **Strike Price Selection:** Choosing strike prices that balance income potential (higher premiums for lower strike prices) with the willingness to own the underlying asset can optimize returns.
- **Expiration Date Selection:** Selecting optimal expiration dates allows control over the income frequency. Shorter expirations may provide more frequent income opportunities, while longer expirations may offer higher premiums.
- **Market Timing:** Timing the sale of cash-secured puts based on market conditions, volatility, and underlying asset performance can enhance income potential.
- **Risk Management:** Balancing income generation with risk control ensures that the strategy remains sustainable and aligned with overall investment goals.



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#### Real-Life Examples

Illustrating how consistent income can be achieved with The Loop may involve specific case studies or examples:

#### Example 1: Monthly Cash-Secured Puts on a Stable Dividend-Paying Stock

**Scenario:** You identify a stable dividend-paying stock that aligns with your investment goals. You decide to implement The Loop Strategy, focusing on selling monthly cash-secured puts to generate consistent income and potentially acquire the stock at a discount, then selling covered calls to continue the collection of monthly income.

#### Steps and Strategy:

- 1. Identifying the Stock:** You select a stock with a strong track record of paying dividends and stable price performance; something you might like to hold long-term.
- 2. Selling Cash-Secured Puts:** Each month, you sell cash-secured puts on the selected stock, choosing a strike price that represents a favorable purchase price. (Several strikes out of the money, as discussed.) You collect the premium upfront, providing immediate income.
- 3. Risk Management:** You ensure that you have sufficient cash reserves to purchase the stock if the put is exercised; monitor the stock price and performance to manage risk.
- 4. Stock Acquisition:** If the stock's price falls below your strike price, the put may be exercised, and you then acquire the stock at the strike price.
- 5. Dividend Collection and Covered Call Selling:** Once the stock is acquired, you benefit from the regular dividend payments, adding to the income generated through premiums. Simultaneously, you start selling covered calls on the stock, further enhancing income potential.
- 6. Continuing The Loop:** Each month, continue selling covered calls against your shares. If the covered call is exercised and the stock is called away, you return to selling cash-secured puts, maintaining the income stream and aiming to reacquire the stock. This looping process of selling covered calls until the stock is called away, then selling cash-secured puts to reacquire the stock, which forms the core of The Loop Strategy.





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### Trading For Income

Outcome: Through this approach, you achieve several key objectives:

Don't let stock selection become a stumbling block. I've written extensively on how to select the right stock, but to simplify the process, consider this: just pick the top 10 stocks by distribution in the Dow, S&P 500, and Nasdaq. These are likely to be your best-performing stocks for the Loop strategy, and the fundamental analysis has already been done for you. If the share prices of these stocks are too high for your portfolio, then pick the top ten stocks within the Russell 2000 by distribution. This way, you can focus on implementing the Loop strategy effectively, rather than getting bogged down in stock selection.

1. **Consistent Income:** By selling cash-secured puts and covered calls regularly, you generate regular income through premium collection, which allows you to purchase more shares, compounding your growth.
2. **Potential Asset Acquisition:** You occasionally acquire the stock at a discount, benefiting from both the lower purchase price and ongoing dividend payments.
3. **Alignment with Investment Goals:** The strategy aligns with your desire for stable income and long-term holding of dividend-paying stocks. The looping nature of the strategy allows for continuous income generation and potential asset acquisition at favorable prices, along with dividend income.
4. **Reinvesting Earnings and Portfolio Expansion:** Reinvest your earnings to acquire additional shares. As your portfolio grows, you can begin trading additional shares or diversify into multiple markets. Keep in mind that one option contract represents 100 shares. It's through the continued acquisition of additional shares that you can achieve compounded growth. This reinvestment strategy not only enhances your income potential but also helps diversify your portfolio, spreading risk across different assets.

**Summarization:** This example demonstrates how The Loop Strategy, which involves selling monthly cash-secured puts and covered calls on a stable dividend-paying stock, can create a consistent and diversified income stream. By carefully selecting the underlying asset, strike prices, and expiration dates, and integrating the strategy with overall investment goals, you can successfully leverage The Loop for both income generation and potential asset acquisition. This looping process of selling covered calls until the stock is called away, then selling cash-secured puts to reacquire the stock, forms the core of The Loop Strategy. It's a dynamic approach that allows for continuous income generation, potential asset acquisition at favorable prices, and the flexibility to adapt to various market conditions.





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#### Example 2: Managing a Diversified Portfolio Using The Loop Strategy Across Various Sectors

**Scenario:** As a trader with a large sum of money or portfolio manager overseeing a diversified investment portfolio, you're seeking to enhance income generation while effectively managing risk. You decide to integrate The Loop Strategy across various sectors, utilizing cash-secured puts and covered calls to create diversified income streams and compound your investments.

#### Steps and Strategy:

1. **Sector Analysis:** You identify various sectors that offer opportunities for income generation and risk diversification, such as technology, healthcare, consumer goods, and financials.
2. **Selection of Underlying Assets:** Within each sector, you select stable and liquid stocks or ETFs that align with the portfolio's overall objectives.
3. **Implementing The Loop Strategy:** You sell cash-secured puts on the selected assets, ensuring that the strike prices and expiration dates align with the portfolio's income needs and risk profile. Once the puts are exercised and you acquire the stocks, you start selling covered calls on them, further enhancing income potential.
4. **Diversification:** By implementing The Loop across various sectors, you create multiple income streams, reducing dependence on any single sector or asset.
5. **Adaptive Management:** You continuously monitor market trends, economic indicators, and sector performance, adapting the strategy as needed. This may include adjusting strike prices, expiration dates, or underlying assets to respond to changes.
6. **Risk Control:** You ensure that sufficient cash reserves are maintained to fulfill potential obligations and employ risk mitigation strategies, such as diversification and stop orders, to control exposure.
7. **Integration with Portfolio Goals:** The Loop Strategy is integrated with the portfolio's overall investment goals, balancing income generation with capital appreciation, risk management, and long-term growth.





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Outcome:

Through this approach, you achieve several key objectives:

1. **Diversified Income Streams:** By implementing The Loop across various sectors, you generate consistent and diversified income through premium collection.
2. **Adaptation to Market Trends:** The adaptive nature of the strategy allows you to respond to market changes, optimizing income potential and risk control.
3. **Alignment with Portfolio Objectives:** The integration of The Loop with the portfolio's broader investment goals ensures that the strategy enhances overall performance without compromising long-term objectives. The looping process of selling covered calls until the stock is called away, then selling cash-secured puts to reacquire the stock, forms the core of The Loop Strategy. It's a dynamic approach that allows for continuous income generation, potential asset acquisition at favorable prices, and the flexibility to adapt to various market conditions.

**Summarization:** This example illustrates how a portfolio manager, or a trader with a large sum of money to invest can successfully integrate The Loop Strategy across various sectors to create diversified income streams through cash-secured puts. By carefully selecting underlying assets, adapting to market trends, and aligning the strategy with the portfolio's overall goals, the manager leverages The Loop to enhance income generation, manage risk, and contribute to the portfolio's long-term success, compounding growth through the reinvestment and acquisition of additional shares.



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#### Example 3: Using The Loop to Enhance Your Retirement Income

**Scenario:** As an individual investor nearing or in retirement, you're seeking to enhance your retirement income without taking on excessive risk. You decide to implement The Loop Strategy, focusing on carefully selecting strike prices and expiration dates to align with your income needs and risk tolerance.

#### Steps and Strategy:

1. **Income Needs Assessment:** You identify your monthly or annual income needs in retirement, considering living expenses, healthcare costs, and other financial goals.
2. **Risk Tolerance Evaluation:** Understanding your risk tolerance, you ensure that The Loop Strategy aligns with your comfort level, particularly regarding potential obligations to buy underlying assets.
3. **Selection of Underlying Assets:** You choose stable and income-generating stocks or ETFs, possibly focusing on dividend-paying assets that align with your long-term investment strategy.
4. **Selling Cash-Secured Puts:** You sell cash-secured puts on the selected assets, choosing strike prices that represent a favorable purchase price and expiration dates that align with your income frequency needs.
5. **Strike Price and Expiration Date Alignment:** You carefully select strike prices and expiration dates to balance income generation with the potential obligation to buy the underlying assets. This alignment ensures that the strategy fits your income needs and risk.
6. **Continuous Monitoring:** You regularly monitor the positions, market conditions, and underlying asset performance, making adjustments as needed to maintain alignment with income needs and risk tolerance.
7. **Selling Covered Calls:** Once the puts are exercised and you acquire the stocks, you start selling covered calls, further enhancing income potential. If the covered call is exercised and the stock is called away, you return to selling cash-secured puts, maintaining the income stream and aiming to reacquire the stock.
8. **Integration with Overall Retirement Strategy:** The Loop Strategy is integrated with your broader retirement investment plan, ensuring that it complements other income sources such as Social Security, pensions, or annuities.

#### Outcome:

Through this approach, you achieve several key objectives:

1. **Enhanced Retirement Income:** By implementing The Loop, you generate consistent income through premium collection, supplementing other retirement income sources.
2. **Risk Alignment:** By carefully selecting strike prices and expiration dates, you control potential obligations and align the strategy with your risk tolerance.
3. **Flexibility:** The Loop Strategy offers flexibility to adapt to changing income needs or market conditions, allowing you to optimize the strategy over time.

**Summarization:** This example illustrates how you can successfully use The Loop Strategy to enhance retirement income, carefully aligning strike prices and expiration dates with income needs and risk tolerance.



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By integrating The Loop with your overall retirement investment plan and making thoughtful selections, you create a sustainable and adaptable approach to income generation that supports your retirement lifestyle. The looping process of selling covered calls until the stock is called away, then selling cash-secured puts to reacquire the stock, forms the core of The Loop Strategy. It's a dynamic approach that allows for continuous income generation, potential asset acquisition at favorable prices, and the flexibility to adapt to various market conditions.



# The Covered Call Strategies within The Loop

In our earlier discussion on covered calls, we delved into the nuances of selecting the right strike price, especially when considering at-the-money and near-the-money options. As we integrate these concepts into The Loop strategy, it's essential to reemphasize their significance.

Selling at or near-the-money covered calls within The Loop can enhance income generation. The larger premiums collected provide a buffer against market volatility, and the potential for early exercise can lead to more frequent income opportunities. By revisiting and integrating these covered call strategies, you can strategically position yourself within The Loop for optimal returns.

Remember, the key is to align your strategy with your objectives. Whether you prioritize consistent premium collection, potential stock appreciation, or a combination of both, The Loop offers the flexibility to tailor your approach based on market conditions and personal preferences.

## IV. The Loop in Action

### A. Scenario 1: Covered Call Exercise and Share Assignment Steps to Handle Covered Call Exercise

#### Notification:

When a covered call is exercised, the process typically begins with the following steps:

- **Receiving Notification:** The trader will receive a notification from their broker that the call option has been exercised. This notification may come via email, a message on the trading platform, or a phone call.



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- **Understanding the Obligation:** The exercise of the covered call means that the trader is obligated to sell the underlying shares at the strike price. It's essential to understand the details, including the number of shares, strike price, and settlement date.

#### Share Assignment

The share assignment process involves several key aspects:

- **Selling the Shares:** The shares are automatically sold at the strike price, and the proceeds are credited to the trader's account.
- **Adjustment to Portfolio:** The sale of the shares will change the composition of the trader's portfolio. Depending on the size and importance of the position, this may have significant implications.
- **Tax Considerations:** The sale of the shares may trigger capital gains or losses, depending on the original purchase price. It's essential to consider the tax implications and consult with a tax professional if needed.

#### Immediate Actions

Once the covered call has been exercised and the shares assigned, immediate actions may include:

- **Assessing the Overall Position:** The trader should review their overall portfolio to understand the impact of the share assignment. This includes assessing cash balances, diversification, and alignment with investment goals.
- **Considering The Loop Strategy:** If implementing The Loop, the trader may consider selling cash-secured puts to potentially buy back the shares or invest in other opportunities.
- **Monitoring Market Conditions:** Understanding the current market conditions and trends can guide the next steps, whether it's re-entering the position, adjusting other positions, or taking different investment actions.
- **Communication with Broker:** Depending on the broker's procedures and the trader's preferences, further communication or actions may be required to confirm the transaction or make additional trades.

#### Conclusion

Handling a covered call exercise and share assignment within The Loop Strategy requires understanding the notification process, managing the share assignment, and taking immediate actions to align with the trader's objectives and market conditions. By carefully navigating these steps, the trader can seamlessly transition from the covered call exercise to the next phase of The Loop, maintaining control over their portfolio and continuing to pursue their investment goals.



# Covered Calls & The Loop

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### Determining the Need for Implementing The Loop

#### Evaluation:

Determining whether to implement The Loop after a covered call exercise involves a thorough evaluation:

- **Reviewing Portfolio Objectives:** Assessing the overall investment goals and how The Loop aligns with those objectives is crucial. This includes considering income needs, risk tolerance, and long-term strategies.
- **Analyzing the Specific Situation:** Understanding the specific circumstances of the covered call exercise, such as the underlying asset, strike price, and market conditions, helps in evaluating the appropriateness of The Loop.

#### Considerations

Key considerations in determining the need for implementing The Loop include:

- **Market Conditions:** Assessing the current market trends and future outlook helps in deciding whether selling cash-secured puts (part of The Loop) is a viable strategy.
- **Underlying Asset Performance:** Evaluating the performance and prospects of the underlying asset that was assigned can guide whether re-entering the position through The Loop is desirable.
- **Risk Tolerance:** Understanding the investor's risk tolerance ensures that The Loop's potential obligations align with their comfort level.
- **Cash Reserves:** Ensuring sufficient cash reserves to fulfill potential obligations if the cash-secured puts are exercised is vital.
- **Alignment with Overall Strategy:** Considering how The Loop fits within the broader investment strategy and portfolio composition is essential.

#### Decision-making Process

A step-by-step guide to making the decision to implement The Loop may include:

1. **Assess the Covered Call Exercise:** Understand the details of the covered call exercise, including the underlying asset, strike price, and implications for the portfolio.
2. **Analyze Market Conditions:** Evaluate the current market trends and how they may impact the decision to sell cash-secured puts.
3. **Review Underlying Asset:** Analyze the performance and prospects of the underlying asset to determine whether re-entering the position is desirable.
4. **Evaluate Risk and Cash Position:** Assess risk tolerance and ensure sufficient cash reserves to meet potential obligations.
5. **Consider Overall Portfolio Alignment:** Ensure that implementing The Loop aligns with overall investment goals, portfolio composition, and long-term strategies.
6. **Make the Decision:** Based on the evaluation and considerations, decide whether to implement The Loop, and if so, plan the specific details such as strike prices, expiration dates, and underlying assets.

#### Conclusion

Determining the need for implementing The Loop after a covered call exercise requires a thoughtful evaluation, consideration of key factors, and a systematic decision-making process.



# Covered Calls & The Loop

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#### B. Scenario 2: The Loop Implementation and Benefits

##### Selling Cash-Secured Puts After Covered Call Exercise

###### Strategy Overview

- **Integration with The Loop:** Selling cash-secured puts is a key component of The Loop Strategy, especially after a covered call exercise. It allows the investor to potentially re-acquire the underlying asset at a favorable price or generate income through premiums.
- **Alignment with Objectives:** This approach aligns with various investment objectives, such as income generation, risk management, and strategic re-entry into underlying positions.

###### Execution

- **Selecting Strike Prices:** Choosing the appropriate strike prices involves assessing the underlying asset's value, market conditions, and your willingness to acquire the asset.
- **Choosing Expiration Dates:** Selecting optimal expiration dates balances the desire for premium income with the likelihood of assignment.
- **Executing the Trade:** The investor sells the cash-secured puts through their brokerage platform, ensuring that sufficient cash reserves are available to meet potential obligations.

##### Analyzing Market Conditions for Cash-Secured Put Sales

###### Market Analysis Tools

- **Technical Analysis:** Utilizing charts, trend lines, and technical indicators to assess price momentum, support and resistance levels, and potential entry points.
- **Fundamental Analysis:** Evaluating the underlying asset's financial health, industry trends, and economic factors to gauge its long-term prospects.

###### Timing

- **Alignment with The Loop:** Timing the sale of cash-secured puts to align with The Loop's objectives, such as maximizing premium income or targeting specific entry points for the underlying asset.
- **Market Conditions:** Considering broader market trends, volatility, and sector dynamics to optimize the timing of cash-secured put sales.

##### Calculating Potential Returns and Risks with The Loop Strategy

###### Return Calculations

- **Premium Income:** Calculating the potential income from selling cash-secured puts, considering the premiums received, strike prices, and expiration dates.
- **Total Return:** Assessing the total potential return within The Loop, including premiums, potential capital gains, and dividends if the underlying asset is re-acquired.

###### Risk Assessment

- **Assignment Risk:** Evaluating the likelihood of assignment and the implications for the portfolio, including potential obligations to buy the underlying asset.
- **Market Risk:** Assessing broader market risks that may impact the underlying asset's price and the overall strategy.

###### Performance Metrics



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- **Success Metrics:** Tracking key performance metrics such as return on capital, win/loss ratio, and consistency of income generation.
- **Ongoing Evaluation:** Regularly reviewing and adjusting The Loop Strategy based on performance metrics, market conditions, and alignment with overall investment goals.

**Conclusion:** Implementing The Loop through selling cash-secured puts after a covered call exercise involves a strategic overview, detailed execution, market analysis, and careful calculation of potential returns and risks. By understanding and applying these aspects, an investor can leverage The Loop to enhance income, manage risk, and create a versatile investment approach that adapts to various market conditions.



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### Trading For Income

#### IV. Risk Considerations and Management

##### A. Understanding Assignment Risk with Cash-Secured Puts

###### Definition

- **Assignment Risk:** Assignment risk refers to the possibility that the seller of a put option (in this case, a cash-secured put) will be obligated to buy the underlying asset at the strike price if the option is exercised by the buyer. In the context of cash-secured puts, this risk is managed by having sufficient cash reserves to fulfill the obligation.

###### Scenarios

- **In-the-Money Puts:** If the underlying asset's price falls below the strike price of the cash-secured put, the option may be exercised, triggering the assignment risk.
- **Volatility:** Sudden market volatility can cause rapid price changes, increasing the likelihood of assignment.
- **Dividend Payments:** If the underlying asset pays a dividend, it may affect the option's exercise probability, impacting assignment risk.
- **Impact on The Loop Strategy:** Assignment risk within The Loop Strategy can lead to the acquisition of the underlying asset, affecting portfolio composition, cash reserves, and overall strategy alignment.

###### Mitigation

- **Choosing Appropriate Strike Prices:** Selecting strike prices that align with the investor's willingness to acquire the underlying asset can help manage assignment risk.
- **Monitoring Positions Closely:** Regularly tracking the underlying asset's price, market conditions, and option's value allows for timely adjustments to mitigate assignment risk.
- **Diversification:** Spreading the strategy across various underlying assets can reduce the impact of assignment on the overall portfolio.
- **Using Stop Orders:** Implementing stop orders to close the position if certain conditions are met can provide additional risk control.
- **Understanding Expiration Dynamics:** Being aware of the time decay and exercise dynamics as the option nears expiration can guide decisions to close or adjust the position.

##### Understanding Expiration Dynamics

###### Time Decay

- **Definition:** Time decay, also known as theta, refers to the reduction in an option's value as it approaches its expiration date. All else being equal, an option will lose value over time, and this effect accelerates as the expiration date nears.
- **Impact on Cash-Secured Puts:** For sellers of cash-secured puts, time decay can be beneficial as it erodes the value of the option, potentially allowing the seller to keep the entire premium if the option expires worthless.
- **Management within The Loop:** Being aware of time decay allows the investor to make informed decisions about when to sell or close the position. For example, an investor might choose to close the position early to capture most of the premium while reducing the risk of assignment



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#### Exercise Dynamics

- **Definition:** Exercise dynamics refer to the factors that influence the likelihood of an option being exercised by the buyer. For cash-secured puts, this includes the relationship between the underlying asset's price and the strike price, volatility, dividends, and market expectations.
- **Scenarios for Exercise:** As the expiration date nears, the probability of exercise may increase if the option is in-the-money (underlying asset's price is below the strike price). Conversely, if the option is out-of-the-money (above the strike price), the likelihood of exercise decreases.
- **Managing Exercise Risk:** Understanding exercise dynamics enables the investor to assess the risk of assignment and make strategic decisions. This might include closing the position to avoid assignment or adjusting the strike price in a subsequent trade to align with market conditions and investment goals.

#### Integration with The Loop Strategy

- **Strategic Alignment:** By understanding expiration dynamics, an investor can align the timing and execution of cash-secured puts with The Loop's overall objectives, such as consistent income generation and risk management.
- **Adaptation to Market Conditions:** Awareness of time decay and exercise dynamics allows for flexibility and adaptation to changing market conditions, enhancing the responsiveness and effectiveness of The Loop Strategy.
- **Informed Decision Making:** Combining insights into time decay and exercise dynamics with other factors such as market analysis, risk tolerance, and portfolio composition guides informed decision-making within The Loop, optimizing outcomes and aligning with long-term investment goals.

**Conclusion:** Understanding assignment risk with cash-secured puts is essential for effectively implementing The Loop. This risk management approach enhances the robustness and adaptability of The Loop, allowing for strategic income generation while maintaining control over potential obligations.

## B. Maintaining Adequate Cash Reserves and Margin Requirements

### Cash Reserves

- **Importance:** Maintaining sufficient cash reserves is crucial when selling cash-secured puts within The Loop Strategy. Cash reserves ensure that the investor can fulfill the obligation to buy the underlying asset if the option is exercised, thus reducing the risk of forced liquidation or other adverse actions by the broker.
- **Alignment with The Loop:** In The Loop Strategy, cash reserves align with the goal of potentially re-acquiring the underlying asset at a favorable price or simply collecting premiums. Adequate cash reserves provide flexibility and control over the investment process.

### Margin Requirements

- **Definition:** Margin requirements refer to the amount of capital that must be maintained in the account when selling options, including cash-secured puts. These requirements are set by regulatory authorities and individual brokers and are designed to manage risk.
- **Variation Across Brokers and Market Conditions:** Margin requirements can vary significantly across different brokers and may change based on market volatility and other



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conditions. Understanding these variations is essential for compliance and effective risk management.

- **Impact on The Loop:** Within The Loop Strategy, margin requirements influence the ability to sell cash-secured puts and the overall capital efficiency of the strategy. Meeting margin requirements ensures uninterrupted execution of The Loop and alignment with regulatory guidelines.

#### Best Practices

- **Regular Monitoring:** Continuously monitoring cash reserves and margin levels to ensure compliance with requirements and readiness to execute The Loop Strategy.
- **Understanding Broker Policies:** Familiarizing oneself with the specific margin requirements and policies of the chosen broker, including how they may change during periods of high volatility.
- **Maintaining a Buffer:** Keeping a buffer of cash reserves beyond the minimum required can provide additional flexibility and reduce the risk of a margin call or forced liquidation.
- **Integrating with Overall Portfolio Management:** Aligning cash reserve and margin management with overall portfolio objectives, risk tolerance, and investment strategy, including The Loop.
- **Seeking Professional Guidance:** Consulting with financial professionals or utilizing broker tools to understand and manage cash reserves and margin requirements effectively.

**Conclusion:** Maintaining adequate cash reserves and understanding margin requirements are fundamental aspects of selling cash-secured puts within The Loop Strategy. By recognizing the importance of these factors, understanding variations across brokers, and implementing best practices, an investor can ensure compliance, reduce risk, and optimize the execution of The Loop. This disciplined approach to cash and margin management enhances the robustness and effectiveness of The Loop as a strategic investment tool.



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#### C. Monitoring Market Conditions and Making Timely Adjustments within The Loop Market Analysis

- **Continuous Assessment:** Successful implementation of The Loop Strategy requires ongoing analysis of market conditions, including trends, volatility, economic indicators, and sector dynamics.
- **Technical Analysis:** Utilizing charts, patterns, and technical indicators to gauge price momentum and potential entry or exit points for cash-secured puts.
- **Fundamental Analysis:** Assessing the underlying asset's financial health, industry trends, and macroeconomic factors to understand its long-term prospects within The Loop.
- **Sentiment Analysis:** Monitoring market sentiment, news, and events that may influence the underlying asset's price and the broader market.

#### Timely Adjustments

- **Rolling Options:** If a cash-secured put is approaching expiration and is in-the-money, an investor may choose to "roll" the option to a later expiration date, adjusting the strike price as needed.
- **Closing Positions:** Deciding when to close positions, either to take profits, prevent losses, or realign with The Loop's objectives.
- **Adapting to Market Changes:** Making strategic adjustments to The Loop in response to significant market changes, such as shifts in volatility, interest rates, or major economic events.
- **Alignment with The Loop's Goals:** Ensuring that all adjustments align with the overall goals of The Loop Strategy, such as consistent income generation, risk management, and strategic re-entry into underlying positions.

#### Tools and Resources

- **Trading Platforms:** Utilizing advanced trading platforms that offer real-time market data, technical analysis tools, and risk management features tailored to options trading.
- **Market Research Services:** Subscribing to market research and analysis services that provide insights into market trends, economic indicators, and sector analysis.
- **Educational Resources:** Leveraging educational materials, webinars, and courses that focus on options trading, risk management, and strategic investment approaches like The Loop.
- **Professional Guidance:** Consulting with financial professionals or investment advisors who have expertise in options trading and can provide personalized guidance within The Loop Strategy.
- **Automated Tools:** Employing automated tools and algorithms that can assist in monitoring market conditions, generating alerts, and executing predefined strategies within The Loop.

**Conclusion:** Monitoring market conditions and making timely adjustments within The Loop is a dynamic and essential aspect of the strategy. By conducting continuous market analysis, making strategic adjustments, and utilizing a range of tools and resources, an investor can navigate the complexities of the market and optimize The Loop's performance. This proactive approach enhances the adaptability, effectiveness, and resilience of The Loop Strategy, aligning it with long-term investment goals and market realities.



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#### D. Legal and Regulatory Considerations

##### Regulations

- **General Options Trading Regulations:** Options trading is governed by various regulatory bodies, such as the Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA) in the U.S. These regulations cover aspects like disclosure, suitability, margin requirements, and fair practices.
- **Specific Considerations for The Loop Strategy:** While The Loop Strategy may not have specific regulations, adherence to general options trading rules and guidelines is essential. This includes understanding margin requirements, risk disclosures, and suitability assessments.
- **International Considerations:** If trading across international markets, understanding and complying with local regulations and exchange rules is vital.

##### Compliance

- **Record-Keeping:** Maintaining accurate and comprehensive records of all trading activities, including transactions within The Loop Strategy, is a regulatory requirement. This includes trade confirmations, account statements, and correspondence.
- **Reporting Requirements:** Depending on jurisdiction and account type, there may be reporting requirements for tax purposes, including gains, losses, and specific option-related forms.
- **Broker Compliance:** Working with a reputable and regulated broker ensures alignment with legal requirements and provides additional oversight and protection.
- **Continuous Education:** Staying informed about regulatory changes and updates is part of ongoing compliance and responsible trading.

##### Ethical Considerations

- **Avoiding Manipulative Practices:** Engaging in practices like front-running, wash trading, or other manipulative or deceptive tactics is strictly prohibited.
- **Adhering to Best Practices:** Following industry best practices and ethical guidelines promotes integrity, transparency, and trust in trading activities, including The Loop Strategy.
- **Transparency with Clients:** If managing funds for clients, clear communication, disclosure, and alignment with client objectives and risk tolerance are essential ethical considerations.
- **Responsible Risk Management:** Implementing The Loop Strategy responsibly, with a clear understanding of risks and alignment with overall investment goals, reflects ethical trading behavior.

**Conclusion:** Legal and regulatory considerations are foundational to the responsible and successful implementation of The Loop Strategy. By understanding the regulatory landscape, ensuring compliance, and emphasizing ethical trading practices, an investor can navigate the complexities of options trading with confidence and integrity. These considerations reinforce the robustness and credibility of The Loop Strategy, aligning it with legal requirements and ethical standards.



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#### V. Advanced Strategies with The Loop

##### A. Optimizing Income Generation with The Loop

###### Strategy Enhancement

- **Selecting Specific Underlying Assets:** Choosing underlying assets with stable price movements, attractive premiums, and alignment with market outlook can enhance income generation within The Loop.
- **Timing Strategies:** Implementing timing strategies, such as selling cash-secured puts during periods of increased volatility, can capture higher premiums and contribute to optimal income.
- **Utilizing Advanced Option Techniques:** Techniques like rolling options, managing expiration dates, and employing spreads can further refine The Loop for income optimization.
- **Diversification:** Diversifying across sectors, asset classes, or expiration dates can reduce risk and create multiple income streams within The Loop.

###### Portfolio Integration

- **Alignment with Portfolio Goals:** Integrating The Loop into a broader investment portfolio requires alignment with overall income goals, risk tolerance, and investment horizon.
- **Balancing Risk and Reward:** The Loop can be balanced with other investment strategies, such as dividend investing or bond holdings, to create a diversified and consistent income stream.
- **Leveraging Portfolio Synergies:** Utilizing The Loop with complementary strategies can enhance overall portfolio performance, providing both income and potential capital appreciation.

###### Performance Metrics

- **Return on Capital (ROC):** Evaluating the return on capital invested in The Loop, including premiums collected and potential asset acquisition costs.
- **Win/Loss Ratio:** Analyzing the ratio of successful trades to losses within The Loop to gauge consistency and effectiveness.
- **Sharpe Ratio:** Assessing the risk-adjusted returns of The Loop, considering both income generation and associated volatility.
- **Benchmark Comparison:** Comparing The Loop's performance to relevant benchmarks or indices to understand relative performance and market alignment.
- **Ongoing Monitoring and Review:** Regularly reviewing performance metrics, adapting strategies, and making necessary adjustments to ensure continued alignment with income optimization goals.

##### B. Using Technical and Fundamental Analysis within The Loop

###### Technical Analysis

- **Trend Lines:** Utilizing trend lines to identify prevailing market trends and potential reversal points, aiding in the timing of cash-secured put sales within The Loop.
- **Moving Averages:** Employing moving averages to smooth out price fluctuations and identify underlying trends, providing insights into entry and exit points.



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- **Indicators:** Using indicators like the Relative Strength Index (RSI), Moving Average Convergence Divergence (MACD), and Bollinger Bands to gauge momentum, trend strength, and potential overbought or oversold conditions.
- **Chart Patterns:** Recognizing chart patterns such as head and shoulders, double tops, or flags to anticipate potential price movements and align The Loop's strategy accordingly.
- **Volume Analysis:** Analyzing trading volume to confirm trends and identify potential reversals, enhancing decision-making within The Loop.

#### Fundamental Analysis

- **Earnings Reports:** Evaluating company earnings reports to assess financial health, growth prospects, and potential impact on option premiums within The Loop.
- **Economic Indicators:** Monitoring key economic indicators like GDP growth, inflation, and interest rates to understand macroeconomic trends that may influence underlying assets.
- **Industry Analysis:** Assessing industry trends, competitive landscape, and regulatory changes to inform asset selection and strategy within The Loop.
- **Dividend Considerations:** Considering dividend payments and ex-dividend dates, as they may influence option premiums and underlying asset behavior within The Loop.

#### Combining Analyses

- **Holistic Approach:** Combining technical and fundamental analysis provides a more comprehensive view of market conditions, asset behavior, and potential opportunities within The Loop.
- **Informed Decision Making:** Integrating both analyses allows for more nuanced and informed decisions, balancing short-term price movements with long-term fundamentals.
- **Risk Management:** Utilizing a combination of analyses enhances risk management by providing multiple perspectives and validation points within The Loop.
- **Adaptation to Market Conditions:** The flexibility to employ both technical and fundamental analysis enables adaptation to various market conditions, enhancing the resilience and effectiveness of The Loop Strategy.

#### C. Combining The Loop with Other Options and Investment Strategies

##### Complementary Strategies

- **Hedging Strategies:** Combining The Loop with hedging strategies like protective puts or collars can provide downside protection, balancing income generation with risk mitigation.
- **Diversification:** Integrating The Loop across various asset classes, sectors, or geographic regions can enhance diversification, reducing concentration risk.
- **Income Strategies:** Pairing The Loop with other income-generating strategies like dividend investing or bond laddering can create a comprehensive income portfolio.
- **Leveraging Other Options Strategies:** Utilizing strategies like iron condors, butterflies, or straddles in conjunction with The Loop can provide additional opportunities and flexibility.

##### Synergistic Effects

- **Enhanced Returns:** Combining The Loop with complementary strategies can create opportunities for enhanced returns through multiple income streams or capital appreciation.
- **Risk Reduction:** Synergistic combinations can reduce specific risks, such as market, sector, or asset-specific risks, through diversification and hedging.



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- **Adaptability:** The ability to integrate and adapt various strategies within The Loop allows for responsiveness to changing market conditions and investment objectives.
- **Efficiency:** Combining strategies can lead to more efficient capital utilization and alignment with broader financial goals.

#### Example 3: Integrating The Loop with Your Technical Trading Strategies

##### Overview:

You're an active trader looking to enhance the timing and execution of The Loop Strategy by integrating it with your technical trading strategies. You're specifically focusing on trend-following or momentum strategies. This combination leverages the strengths of both technical analysis and options trading, providing opportunities for enhanced returns and strategic trading.

##### Strategy Components:

1. **Technical Analysis Integration:** You employ technical analysis tools such as moving averages, trend lines, momentum indicators (e.g., Bulls 'n Bars, Advantage Lines), and chart patterns to identify trends and momentum in underlying assets.
2. **Implementation of The Loop:** You use The Loop Strategy, selling covered calls and then cash-secured puts if the calls are exercised, aligning the execution with identified trends and momentum signals.
3. **Trend-Following Approach:** You focus on identifying and trading with prevailing trends, using The Loop to capitalize on sustained upward or downward movements.
4. **Momentum Approach:** Alternatively, you focus on momentum signals, using The Loop to capitalize on short-term price movements and volatility.
5. **Risk Management:** You employ stop-loss orders, position sizing, and other risk management techniques to control potential losses and align with your risk tolerance.
6. **Continuous Monitoring:** Ongoing monitoring of technical indicators and market conditions is essential for timely adjustments and execution within The Loop.

##### Benefits:

- **Enhanced Timing:** Integrating technical analysis allows for more precise timing in executing The Loop, potentially enhancing returns.
- **Strategic Trading:** The combination offers a strategic approach to trading, allowing for alignment with market trends or momentum.
- **Risk Control:** Technical signals can provide additional risk control, offering exit signals or warning signs of potential trend reversals.
- **Versatility:** The strategy can be adapted to various time frames, market conditions, and underlying assets, providing flexibility for you as an active trader.

##### Considerations:

- **Technical Skill Requirements:** Successful integration requires a solid understanding of technical analysis and the ability to interpret and act on technical signals.
- **Potential for Overtrading:** The active nature of this approach may lead to overtrading, increasing transaction costs and potential risks.
- **See my other books on Amazon where I teach the art of Technical Analysis with an eye toward trading the Loop using Fibonacci Projections & The Wycoff Accumulation model.**



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#### B. Resources and Further Reading

##### Recommended Books

1. "Stock Market PlayBook of Strategies" by Lan Turner: The Fibonacci Effect: How to gain discipline and courage through knowledge and strategy. (Technical Analysis)
2. "Trading Commodity Options" by Carley Garner: When, why, and how to develop strategies to improve the odds in any market environment and risk-reward profile.
3. "Options as a Strategic Investment" by Lawrence G. McMillan: A comprehensive guide to options trading, suitable for both beginners and advanced traders.
4. "Trading Options For Dummies" by Joe Duarte: A beginner-friendly introduction to options trading, including basic strategies and risk management.

##### Online Resources

1. Investing 401, Intro to trading options. (Multimedia video course) online at: [www.LanTurner.com](http://www.LanTurner.com) Understanding options and how to begin trading them.
2. [CommodityTradingSchool.com](http://CommodityTradingSchool.com) Learn to trade The Loop on futures, where there are no pattern day trading rules, and you can open your account with as little as \$2,500.
3. [TradeMentors.com](http://TradeMentors.com) Just in case you need a helping hand.

##### Tools and Software

1. Brokerage: [www.GeckoFS.com](http://www.GeckoFS.com) my brokerage firm, a boutique firm who caters to small to mid-sized traders who need someone to call and ask questions to, just to make sure you're getting it done correctly.
2. [www.Tools4Traders.ORG](http://www.Tools4Traders.ORG) This is where we curate all the best tools, education, trading software and platforms for market analysis and trading.
3. [www.TracknTrade.com](http://www.TracknTrade.com) My software trading platform. Winner of Stocks & Commodities Annual Reader's Choice Award Seven Years.

**Conclusion:** The journey of mastering The Loop Strategy doesn't end with this book. Continuous learning, engagement with trading communities, and utilization of advanced tools and software will further enhance understanding and execution of The Loop. The resources listed above provide a starting point for further exploration, offering insights, practical guidance, and community support. By leveraging these resources, readers can deepen their knowledge, refine their skills, and stay abreast of the ever-evolving world of options trading.



## Questions and Answers: The Loop Strategy

**Question 1: What is a covered call?**

**Answer: Definition and Basics of Covered Calls:**

**A.** A covered call is an options trading strategy where an investor holds a long position in an underlying asset, typically shares of stock, and simultaneously sells (writes) call options on the same asset. The call options are sold with a specific strike price and expiration date. By selling these call options, the investor collects a premium from the buyer, which provides additional income.

The term "covered" in covered calls refers to the fact that the investor already owns the underlying asset, which covers or backs the obligation of selling the asset at the strike price if the call options are exercised by the buyer. This coverage limits the potential risk involved in selling call options and defines the strategy's maximum profit potential.

**B. How Covered Calls Work:**

When an investor sells covered calls, they agree to sell their shares of the underlying asset to the call option buyer at the specified strike price, but only if the option buyer decides to exercise the call option before or on the expiration date. The investor retains the premium received from selling the call options, regardless of whether the call options are exercised or expire worthless.



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The covered call strategy is often used by investors who have a neutral to slightly bullish outlook on the underlying asset. It allows them to generate additional income while potentially benefiting from modest price appreciation in the asset.

#### C. Benefits of Selling Covered Calls:

**Income Generation:** Selling covered calls enables investors to receive upfront premium income from the sale of call options, providing a steady stream of additional cash flow.

**Risk Reduction:** By holding a long position in the underlying asset, the investor has some downside protection. The premium received from selling calls partially offsets potential losses if the stock price declines.

**Enhanced Returns:** If the stock price remains below the strike price of the sold call options, the investor keeps both the premium received and the underlying asset, leading to enhanced total returns.

**Flexibility:** Investors can tailor the covered call strategy based on their market outlook and risk tolerance. They can choose different strike prices and expiration dates to optimize their income potential.

**Passive Income Strategy:** Covered calls are popular among income-oriented investors seeking regular cash flow from their investments without actively trading.

It's important to note that while covered calls offer many advantages, they also have some limitations and risks. Understanding these aspects and learning to manage them is crucial for successful implementation of the covered call strategy.

Question 2: How do I select the right stock for covered calls?

Answer:

#### A. Criteria for Choosing a Suitable Stock:

Selecting the right stock is a critical step in executing a successful covered call strategy. Several key criteria can help investors identify suitable stocks for this options trading approach:

**Liquidity:** Choose stocks that have high trading volumes and ample liquidity in the options market. Higher liquidity ensures that you can easily enter and exit positions without facing significant price discrepancies.

**Blue-Chip or Large-Cap Stocks:** Consider established and well-known companies with a history of stable performance. Blue-chip or large-cap stocks often have lower volatility and are less prone to sudden price swings.

**Strong Fundamentals:** Analyze the company's financial health, earnings growth, and overall stability. Stocks of companies with solid fundamentals are more likely to withstand market fluctuations.



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**Covered Call Candidates:** Look for stocks that have a history of consistent price movements or are currently trading in a range-bound pattern. These stocks can provide more predictable outcomes for covered call strategies.

#### B. Evaluating Dividend-Paying Stocks:

Dividend-paying stocks can be particularly attractive for covered call strategies. Dividends provide additional income on top of the call premium, further enhancing the strategy's overall returns. When evaluating dividend-paying stocks, consider the following:

**Dividend Yield:** Assess the dividend yield, which is the annual dividend payment as a percentage of the stock price. Higher dividend yields can lead to more substantial total returns when combined with call option premiums.

**Dividend Growth:** Look for companies with a history of increasing their dividends over time. Steady dividend growth may indicate a financially healthy and shareholder-friendly company.

**Ex-Dividend Dates:** Be mindful of ex-dividend dates when selling covered calls. If the call options are exercised before the ex-dividend date, you may miss out on the upcoming dividend payment.

#### C. Analyzing Stock Price Stability:

Stability is a crucial factor when selecting stocks for covered calls, as significant price swings can lead to unexpected outcomes. To analyze stock price stability:

**Historical Price Behavior:** Review the stock's historical price movements over different time frames. Stocks with smoother and less volatile price trends may be more suitable for covered calls.

**Support and Resistance Levels:** Identify key support and resistance levels on the stock's price chart. Stocks that often respect these levels may be more predictable for covered call strategies.

**Implied Volatility:** Check the implied volatility of the stock's options. Stocks with lower implied volatility may have more predictable option pricing, making it easier to strategize covered calls.

**Question 3:** What is the best strike price to use when selling covered calls?

**Answer:**

#### A. Understanding Strike Price Selection:

The strike price of a covered call is a crucial element that determines the potential outcomes of the strategy. It represents the price at which the call option can be exercised, allowing the underlying stock to be sold. When selecting the best strike price for selling covered calls, consider the following factors:



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**Current Stock Price:** The current stock price serves as a reference point for choosing the strike price. It helps determine whether the option will be in-the-money (ITM), at-the-money (ATM), or out-of-the-money (OTM).

**Market Outlook:** Assess your outlook on the underlying stock. If you are bullish and expect the stock to rise, an OTM strike may be more appropriate. For a neutral or slightly bullish outlook, an ATM strike could be considered. If you are more cautious or bearish, an ITM strike might be preferred.

**Risk Tolerance:** Different strike prices come with varying levels of risk and potential reward. Consider your risk tolerance and how comfortable you are with the potential outcomes at different strike prices.

#### B. Pros and Cons of In-the-Money (ITM), At-the-Money (ATM), and Out-of-the-Money (OTM) Strikes:

Each type of strike price offers distinct advantages and disadvantages for covered call sellers:

**In-the-Money (ITM) Strikes:** ITM strikes have a higher premium due to their intrinsic value. They provide a greater downside protection against potential stock declines. However, they offer limited upside potential as the stock must appreciate significantly to profit from both the premium and the stock's appreciation.

**At-the-Money (ATM) Strikes:** ATM strikes often offer a balanced trade-off between premium income and potential stock appreciation. They are closest to the current stock price and may provide a higher return if the stock price remains relatively stable.

**Out-of-the-Money (OTM) Strikes:** OTM strikes have lower premiums but provide more significant upside potential. If the stock price rises significantly, you can profit from both the premium received and the stock's appreciation. However, they offer less downside protection, and if the stock price declines, the option may expire worthless.

#### C. Tailoring Strike Price to Your Risk Tolerance and Market Outlook:

The choice of strike price ultimately depends on your individual risk tolerance and market outlook. If you are conservative and seek more downside protection, ITM or ATM strikes may be preferred. If you are optimistic about the stock's potential upside, OTM strikes could be more attractive.

Additionally, consider your profit targets and desired returns when selecting the strike price. Remember that covered calls are a versatile strategy, and you can adjust your strike price selection based on changing market conditions and your long-term investment goals.

By understanding the nuances of strike price selection and tailoring it to your risk profile and market expectations, you can optimize the potential outcomes of your covered call strategy and achieve your financial objectives.

**Question 4:** How do I determine the appropriate expiration date for covered calls?

**Answer:**



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#### A. Importance of Expiration Date in Covered Call Strategy:

The expiration date of a covered call option is a critical aspect of the strategy. It defines the period during which the option can be exercised, allowing the underlying stock to be sold at the strike price. Selecting the appropriate expiration date is essential in optimizing the potential returns and managing risk.

#### B. Short-Term vs. Long-Term Expirations:

When selling covered calls, you have the option to choose between short-term and long-term expirations. Short-term expirations typically range from a few days to a few weeks, while long-term expirations extend several months or even a year.

Short-term expirations offer the advantage of more frequent opportunities to generate income from the strategy. It allows you to capitalize on shorter market movements and reevaluate your covered call positions more frequently.

On the other hand, long-term expirations provide more extended timeframes for the stock to appreciate, potentially leading to higher capital gains if the stock price rises significantly. However, they offer fewer chances to adjust your strategy and may require more patience as you wait for the option to expire.

#### C. Selecting Expiration Date Based on Market Conditions:

The choice of expiration date should also consider current market conditions and your outlook on the underlying stock. If you anticipate significant price movement or volatility in the short term, shorter expirations may be more suitable. Short-term expirations also provide the flexibility to reassess and adapt your strategy in response to market events.

Alternatively, if you have a more extended bullish outlook on the stock and believe it will appreciate gradually over time, longer expirations could be considered. Long-term expirations allow you to capture potential stock appreciation while earning premium income.

Moreover, it is essential to align the expiration date with your overall investment goals and risk tolerance. If you prefer to generate consistent income through frequent covered call writing, short-term expirations may align better with your objectives. Conversely, if you seek to enhance capital appreciation while earning premium income, long-term expirations may align more effectively.

Ultimately, the choice of expiration date should be based on a combination of market analysis, individual preferences, and investment objectives. Regularly reviewing your covered call positions and adjusting the expiration date as needed can help you optimize your strategy and achieve successful outcomes in the options market.

Question 5: What happens if the stock price exceeds the strike price of my covered call?

Answer:

#### A. Understanding Assignment and Call Option Exercise:

When the stock price exceeds the strike price of your covered call, the option is said to be "in-the-money" (ITM). In this scenario, the buyer of the call option has the right to exercise the option and buy the stock from you at the strike price, which is lower than the current market



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price. The process of the buyer exercising the option and you, as the seller, delivering the stock is known as "assignment."

#### B. Consequences of Covered Call Assignment:

If your covered call gets assigned, you will be obligated to sell your shares of the underlying stock at the strike price, regardless of its current market value. While this may seem disadvantageous if the stock price has significantly increased, it is essential to remember that you still retain the premium received when selling the covered call. This premium helps reduce the effective selling price of the stock and provides additional income.

#### C. Strategies to Manage Assignment Risk:

To manage assignment risk, several strategies can be employed:

**Rolling the Option:** If the stock price has surpassed the strike price, you may consider "rolling" the covered call position. This involves buying back the current covered call and simultaneously selling a new covered call with a higher strike price and/or a later expiration date. Rolling allows you to capture additional premium income while keeping the stock position.

**Buying Back the Option:** If you want to retain ownership of the stock and avoid assignment, you can choose to buy back the call option before it gets exercised. This involves paying a premium to close out the position, and you can then decide whether to sell another covered call or hold onto the stock.

**Allowing Assignment:** If you are willing to part with the stock and realize profits at the strike price, you can allow the covered call to be assigned. In this case, you will sell the shares at the strike price, and the premium received from selling the call will enhance your overall returns.

**Taking No Action:** If your objective is to sell the stock at the strike price and you have a bullish view on the stock's long-term prospects, you can let the assignment happen without making any adjustments.

The appropriate strategy depends on your market outlook, risk tolerance, and investment goals. It's crucial to be proactive in managing covered call positions, especially when the stock price approaches or exceeds the strike price. By evaluating your options and employing the right strategy, you can effectively navigate the potential outcomes of covered call assignments and optimize your overall portfolio performance.

Answer:

#### A. Assessing Suitability for Covered Calls:

Selling covered calls can be a valuable strategy, but it may not be suitable for all stocks in your portfolio. Before deciding to sell covered calls on a particular stock, consider the stock's characteristics, your investment goals, and your risk tolerance. Suitable stocks for covered calls are typically those with relatively stable prices, moderate to low volatility, and a history of dividend payments. Additionally, it's essential to understand the fundamentals of the company and its future growth prospects.

#### B. Diversification and Risk Management:



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Diversification is a key principle in investing, and it's crucial to have a well-balanced portfolio that includes various asset classes and investment strategies. While covered calls can provide additional income and mitigate downside risk to some extent, relying solely on this strategy for all your stocks may expose you to undiversified risk. Consider having a mix of covered call positions and other investments to spread risk and enhance overall portfolio stability.

#### C. Balancing Income Generation with Stock Appreciation Potential:

Selling covered calls generates income through option premiums, which can be attractive, especially in sideways or slightly bullish markets. However, it's essential to weigh this income against the potential for stock appreciation. By selling covered calls, you limit your upside potential if the stock's price surges significantly. As a result, you may miss out on substantial gains if the stock experiences substantial price increases. Therefore, strike a balance between generating income with covered calls and participating in the long-term growth potential of your stocks.

In summary, selling covered calls can be a useful strategy for generating additional income and managing risk, especially in certain market conditions. However, it's crucial to assess each stock's suitability for covered calls, maintain a diversified portfolio, and strike a balance between income generation and potential stock appreciation. By doing so, you can optimize the use of covered calls in your overall investment approach and work towards achieving your financial objectives.

Question 7: How do I adjust my covered call strategy in a bearish or volatile market?

Answer:

#### A. Adapting Covered Call Strategy to Different Market Conditions:

In a bearish or highly volatile market, the standard covered call strategy may require adjustments to mitigate potential losses and manage risk effectively. While covered calls can still generate income during such market conditions, additional precautions may be necessary to protect your portfolio.

#### B. Rolling Options and Adjusting Strike Prices:

One way to adjust your covered call strategy in a bearish or volatile market is by rolling options. This involves buying back your current short call option and simultaneously selling a new call option with a later expiration date and/or different strike price. By rolling the options, you can extend the time frame for potential stock appreciation or choose a more conservative strike price to reduce downside risk.

#### C. Using Protective Puts as a Risk Management Tool:

Another adjustment is to implement protective puts. A protective put involves buying put options for the same number of shares you hold, essentially providing insurance against significant stock price declines. If the stock price drops below the put option's strike price, the value of the put option increases, offsetting losses in the stock's value. This strategy can act as a hedge in a bearish market, limiting potential downside risk.

It's important to note that adjustments to your covered call strategy should be based on thorough analysis of market conditions, your portfolio's specific needs, and your risk tolerance.



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Consider consulting with a financial advisor or experienced options trader to help you tailor the strategy to your individual circumstances.

By adapting your covered call strategy in bearish or volatile markets, you can enhance risk management, potentially limit losses, and continue to use the strategy effectively even in challenging market environments. Remember that flexibility and proactive adjustments are essential elements in navigating the ups and downs of the financial markets while pursuing your investment goals.

**Question 8: What are the tax implications of covered call trading?**

**Answer:**

#### **A. Tax Treatment of Covered Call Premiums:**

The premiums received from selling covered calls are generally treated as short-term capital gains and are taxable as ordinary income in the year they are received. As such, they are subject to your ordinary income tax rate. It's essential to keep track of the premiums earned throughout the year for accurate reporting on your tax return.

#### **B. Tax Implications of Stock Assignment:**

If your covered call option is assigned (exercised) and the stock is called away, you may realize a capital gain or loss on the underlying stock. The capital gain or loss is calculated as the difference between the stock's selling price (strike price) and its original cost basis (the price at which you acquired the stock). The gain or loss may be short-term or long-term, depending on the holding period of the stock.

#### **C. Consulting a Tax Professional for Guidance:**

Tax regulations can be complex, and the implications of covered call trading may vary based on individual circumstances, such as your overall tax situation, investment objectives, and tax jurisdiction. Therefore, it's crucial to consult a qualified tax professional or advisor who can provide personalized guidance tailored to your specific situation.

A tax professional can help you navigate the intricacies of covered call taxation, advise you on reporting requirements, and assist in optimizing your tax position. Additionally, they can help you understand any tax deductions or credits that may apply to your covered call trading activities.

By seeking guidance from a tax expert, you can ensure compliance with tax laws and make informed decisions to help minimize tax liabilities while maximizing the benefits of your covered call trading strategy. Remember that tax planning is an essential aspect of successful investing, and professional advice can be a valuable resource in this regard.

**Question 9: Can I use covered calls in retirement accounts like IRAs?**

**Answer:**

#### **A. Covered Call Trading in Retirement Accounts:**



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Yes, covered call trading is allowed in retirement accounts like Individual Retirement Accounts (IRAs). IRAs offer a tax-advantaged way to invest for retirement, and covered calls can be an effective strategy to generate income while potentially reducing risk.

#### B. Complying with IRA Regulations:

While covered call trading is permissible in IRAs, there are some rules and restrictions that investors must follow to ensure compliance with IRA regulations. For example, the IRS prohibits certain types of transactions that could be considered self-dealing or prohibited transactions within the IRA.

Investors must also be mindful of the "unrelated business taxable income" (UBTI) rules, which apply to tax-exempt entities like IRAs. If an IRA generates income from a trade or business that is unrelated to its tax-exempt purpose, such as active trading in options, it may be subject to UBTI tax.

#### C. Benefits and Considerations of Covered Calls in IRAs:

Using covered calls in IRAs can provide several benefits. First, it allows investors to potentially generate income from their retirement accounts without triggering immediate tax liabilities. The premium received from selling covered calls can help supplement retirement income and grow the IRA's value over time.

Moreover, covered calls can be a risk management tool in IRAs. By selling calls against existing stock positions, investors can partially hedge their portfolio against potential downside moves in the market. This hedging aspect can be particularly beneficial in volatile market conditions.

However, there are also considerations to keep in mind when using covered calls in IRAs. As mentioned earlier, investors must adhere to IRA regulations and avoid any prohibited transactions. Additionally, the potential for call assignment and stock sell-off could impact the diversification of the IRA's holdings, so careful position sizing and stock selection are essential.

Overall, covered calls can be a valuable addition to retirement accounts, offering the potential for income generation and risk management. Before implementing covered call strategies in an IRA, it is advisable to consult with a financial advisor or tax professional to ensure compliance with IRA regulations and to determine the suitability of the strategy for individual retirement goals and risk tolerance.

Question 10: How do I calculate my potential return on a covered call trade?

Answer:

#### A. Understanding Potential Return if Unexercised:

The potential return if unexercised, also known as the maximum return, refers to the profit that an investor could make from a covered call trade if the option is not exercised by the expiration date. To calculate the potential return if unexercised, use the following formula:

$$\text{Potential Return if Unexercised (\%)} = (\text{Option Premium} / \text{Stock Price}) * 100$$

In this formula, the option premium is the amount received from selling the covered call, and the stock price is the current price of the underlying stock.



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### B. Calculating Return if Exercised:

The return if exercised, also known as the realized return, represents the profit or loss that an investor would incur if the covered call option is exercised, and the stock is called away at the strike price. To calculate the return if exercised, use the following formula:

$$\text{Return if Exercised (\%)} = [(\text{Option Premium} + (\text{Strike Price} - \text{Stock Price})) / \text{Stock Price}] * 100$$

In this formula, the option premium is the amount received from selling the covered call, the strike price is the price at which the stock will be sold if exercised, and the stock price is the current price of the underlying stock.

### C. Evaluating the Overall Profitability of Covered Call Trades:

When evaluating the overall profitability of covered call trades, it is essential to consider both the potential return if unexercised and the return if exercised. These two metrics provide insights into different scenarios:

If the potential return if unexercised is relatively high, it indicates that the investor can generate a significant return without having the stock called away. This might be preferable if the investor is bullish on the stock's potential and wants to retain ownership.

On the other hand, if the return if exercised is attractive, it implies that the investor is willing to part with the stock at the strike price and realizes a profit from the call option's sale. This might be suitable if the investor is content with the stock's current performance and seeks additional income from the covered call premium.



# Questions and Answers: Selling Cash-Secured Puts

**Question 1: What is a cash-secured put?**

**Answer:**

**A. Definition and Basics of Cash-Secured Puts:**

A cash-secured put is an options trading strategy in which an investor sells put options while setting aside enough cash to cover the potential purchase of the underlying asset if the option is exercised. The term "cash-secured" indicates that the investor has sufficient funds on hand to fulfill the obligation of buying the stock at the predetermined price, known as the strike price.

**B. How Selling Puts Works:**

When an investor sells a cash-secured put, they are entering into a contract to potentially buy the underlying stock at the strike price if the put option buyer decides to exercise the option. In return for taking on this obligation, the investor receives a premium from the sale of the put option. The premium represents immediate income for the investor and is theirs to keep, regardless of whether the put option is exercised or not.

**C. Benefits of Selling Cash-Secured Puts:**

**Income Generation:** Selling cash-secured puts allows investors to generate income upfront through the premium received from the put option sale. This income can serve as a source of additional returns, especially in sideways or mildly bullish markets.

**Buying Opportunities:** If the stock price falls below the strike price and the put option is exercised, the investor can purchase the stock at a discounted price. This can be advantageous for investors who are interested in owning the stock at a lower cost or have a bullish outlook on the underlying asset.



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**Risk Management:** By setting aside cash to cover the potential stock purchase, the investor limits the risk involved in selling puts. They are fully prepared to buy the stock if the option is exercised, reducing the likelihood of significant losses.

**Versatility:** Cash-secured puts offer versatility in adjusting the strike price and expiration date to suit the investor's risk tolerance and market outlook. Investors can tailor their cash-secured put strategy based on their expectations for the stock's price movement.

Overall, selling cash-secured puts can be an effective strategy for generating income, entering the market at a discounted price, and managing risk. As with any options trading strategy, it is crucial for investors to thoroughly understand the mechanics and risks involved in cash-secured puts, conduct proper due diligence, and align the strategy with their financial goals and risk tolerance. Consulting with a financial advisor or options trading professional can provide valuable insights and guidance when implementing cash-secured puts in a portfolio.

**Question 2:** How do I select the right stock for selling cash-secured puts?

**Answer:**

#### A. Criteria for Choosing Stocks to Sell Puts On:

Selecting the right stocks for selling cash-secured puts is a crucial step in implementing a successful strategy. Consider the following criteria to identify suitable stocks:

**Strong Fundamentals:** Look for companies with solid financials, strong earnings growth, and a history of profitability. Fundamental analysis helps assess the overall health and stability of the underlying company.

**Dividend-Paying Stocks:** Dividend-paying stocks can provide an additional source of income for the investor, even if the put option is exercised. Companies with a history of consistent dividend payments are often preferred.

**Blue-Chip Stocks:** Blue-chip stocks are shares of well-established and reputable companies with a history of market stability. They are generally less volatile and carry lower risk compared to smaller or speculative stocks.

#### B. Evaluating Stocks for Potential Purchase:

Since the goal of selling cash-secured puts is to potentially acquire the underlying stock at the strike price, it's essential to evaluate the stocks as if you were planning to buy them outright. Conduct thorough research on the company's business model, competitive advantage, growth prospects, and overall industry conditions.

#### C. Analyzing Stock Price Trends and Support Levels:

Technical analysis can provide valuable insights into the stock's price trends and potential support levels. Identify key support areas where the stock has historically found buying interest and bounced back from previous declines. This analysis can help determine suitable strike prices for selling cash-secured puts.



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Overall, choosing the right stocks for selling cash-secured puts requires a balanced approach of fundamental and technical analysis. The combination of strong fundamentals, dividend-paying status, and careful evaluation of stock price trends can enhance the chances of success in generating income and potentially acquiring desirable stocks at favorable prices. As with any investment strategy, it is essential to consider individual risk tolerance, perform due diligence, and seek professional advice if needed.

Question 3: What is the best strike price to use when selling cash-secured puts?

Answer:

#### A. Understanding Strike Price Selection for Put Selling:

Selecting the appropriate strike price when selling cash-secured puts is a critical aspect of the strategy. The strike price determines the price at which the put option buyer has the right to sell the underlying stock. Consider the following factors when deciding on the best strike price:

**Personal Investment Goals:** Your investment goals and risk tolerance play a significant role in strike price selection. If you are more conservative, you may prefer lower strike prices to increase the likelihood of assignment and acquire the stock at a discount. If you seek higher potential returns, you may opt for higher strike prices but accept a lower chance of assignment.

**Market Outlook:** Assess the current market conditions and your outlook for the underlying stock. If you believe the stock's price will rise or remain relatively stable, you may consider out-of-the-money (OTM) puts with strike prices below the current stock price. For a more neutral or bearish view, in-the-money (ITM) or at-the-money (ATM) puts might be preferred.

#### B. Evaluating In-the-Money (ITM), At-the-Money (ATM), and Out-of-the-Money (OTM) Puts:

The three types of put options have different strike price relationships to the current stock price:

**In-the-Money (ITM) Puts:** These have strike prices above the current stock price. Selling ITM puts means you are willing to buy the stock at a higher price than the current market value, but you will receive a higher premium as compensation.

**At-the-Money (ATM) Puts:** These have strike prices equal to the current stock price. ATM puts offer a balance between premium income and the likelihood of assignment.

**Out-of-the-Money (OTM) Puts:** These have strike prices below the current stock price. Selling OTM puts means you are willing to buy the stock at a lower price than the current market value, but the premium income will be lower.

#### C. Tailoring Strike Price to Your Risk Tolerance and Market Outlook:

The choice of strike price depends on your risk tolerance, market outlook, and desired return. A conservative investor seeking more safety might choose ITM or ATM puts, while a more aggressive investor might prefer OTM puts for higher returns and potential capital appreciation.



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Ultimately, the best strike price for selling cash-secured puts varies based on individual preferences and market conditions. Balancing risk and reward, and aligning the strike price with your investment goals and outlook, will help optimize the effectiveness of your cash-secured put selling strategy. As always, careful consideration and analysis are essential, and consulting with a financial advisor can provide valuable guidance tailored to your specific financial situation and objectives.

**Question 4: How do I determine the appropriate expiration date for selling cash-secured puts?**

**Answer:**

#### **A. Importance of Expiration Date in Put Selling Strategy:**

The expiration date of a put option is a crucial factor in selling cash-secured puts. It determines the timeframe during which the put option buyer can exercise their right to sell the underlying stock to you. As an options seller, you want to strike a balance between generating premium income and managing the time risk associated with put selling.

#### **B. Short-Term vs. Long-Term Put Expirations:**

**Short-Term Expirations:** Selling puts with short-term expirations, typically 30 to 45 days, can be appealing for investors seeking quicker premium income. Short-term options offer a faster turnover, allowing you to redeploy your capital and sell new puts more frequently.

**Long-Term Expirations:** On the other hand, selling puts with longer expirations, such as six months or more, provides more time for potential stock price movement in your favor. Longer expirations may also offer higher premium income due to increased time value.

#### **C. Selecting Expiration Date Based on Market Conditions:**

When choosing the appropriate expiration date for selling cash-secured puts, consider the prevailing market conditions and your market outlook:

**Bullish Outlook:** If you have a bullish outlook on the underlying stock, you may lean towards short-term expirations. This allows you to capture premium income more frequently as you expect the stock's price to rise or remain stable.

**Neutral to Bearish Outlook:** If you are neutral or bearish on the stock, longer-term expirations might be preferred. Longer expirations provide more time for the stock to potentially decline to your desired entry point if assigned.

**Market Volatility:** In highly volatile markets, shorter-term expirations may be more appropriate as the stock price can experience significant fluctuations within a short timeframe.

Remember, as the expiration date approaches, the time value of the put option decreases, impacting the premium you can collect. Additionally, the premium will be influenced by the stock's implied volatility and the distance between the strike price and the current stock price.

Ultimately, the choice of expiration date depends on your risk tolerance, market outlook, and desired frequency of put selling. It's essential to align the expiration date with your overall investment strategy and be prepared to adjust your approach based on changing market



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conditions. Regularly reassessing your put selling strategy will help ensure it remains effective and aligned with your financial goals. As always, seeking guidance from a financial advisor can provide valuable insights tailored to your individual circumstances.

Question 5: What happens if the stock price drops below the put's strike price?

Answer:

#### A. Understanding Assignment and Put Option Exercise:

If the stock price drops below the put option's strike price, the put option buyer has the right to sell the underlying stock to you at the strike price. This process is known as "assignment," and it means you become obligated to buy the stock from the put option buyer.

#### B. Consequences of Put Assignment and Obligation to Buy the Stock:

When your put option is assigned, you must fulfill your obligation to purchase the stock at the predetermined strike price, even if the current market price is lower. This can lead to an unfavorable purchase of the stock, as you are buying it at a higher price than the current market value.

#### C. Strategies to Manage Put Assignment Risk:

To manage the risk of put assignment and potential losses, consider the following strategies:

**Adequate Cash Reserves:** Selling cash-secured puts means you have enough cash to purchase the stock if assigned. Maintaining sufficient cash reserves in your account is essential to fulfilling this obligation without causing financial strain.

**Strike Price Selection:** Choose a strike price that aligns with your desired entry point for the stock. If you are comfortable buying the stock at a specific price, select a strike price close to that level. Avoid overly aggressive strike prices that may expose you to significant losses if the stock drops sharply.

**Diversification:** Diversifying your put selling across multiple stocks and industries can help mitigate the impact of put assignment on your overall portfolio. By spreading the risk, potential losses from individual stock assignments can be balanced out by gains in other positions.

**Rolling Options:** If the stock price drops close to the strike price, you might consider rolling the put option to a later expiration or a different strike price. Rolling involves buying back the current put option and simultaneously selling a new one with a later expiration or a more favorable strike price. This allows you to extend the time for potential stock recovery or adjust the position based on market conditions.

**Using Protective Puts:** Purchasing protective put options on the same stock can act as insurance against significant price declines. A protective put allows you to sell the stock at the strike price of the put option, limiting potential losses in case of a stock market downturn.

**Monitoring and Adjusting:** Keep a close eye on your put positions and the underlying stock's performance. Be prepared to adjust your strategy if the market conditions change or your outlook on the stock shifts.



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Remember, selling cash-secured puts carries the risk of put assignment, but it also presents an opportunity to acquire stocks at attractive prices. By managing your risk effectively and employing sound strategies, you can enhance the potential for success when selling cash-secured puts as part of your overall investment approach. Always seek professional advice if needed to tailor your put selling strategy to your unique financial situation and objectives.

Question 6: Should I sell cash-secured puts on all the stocks I want to own?

Answer:

### A. Assessing Suitability for Selling Puts:

Selling cash-secured puts can be an effective strategy to acquire stocks at favorable prices, but it may not be suitable for all investors. Before selling puts on all the stocks you want to own, consider the following factors:

**Market Outlook:** Evaluate your outlook on the overall market and individual stocks. Selling puts is a bullish strategy that benefits from rising stock prices. If you have a positive long-term view on the market and the specific stocks, put selling might align with your investment goals.

**Risk Tolerance:** Selling puts involves assuming the obligation to buy the stock if assigned. This exposes you to potential losses if the stock price declines significantly. Assess your risk tolerance and ensure that you are comfortable with the potential risks and rewards of put selling.

**Financial Situation:** Selling cash-secured puts requires having enough cash reserves to cover the stock purchase if assigned. Ensure that you have adequate funds set aside for this purpose without affecting your overall financial stability.

### B. Diversification and Risk Management with Put Selling:

Rather than selling puts on all the stocks you want to own, consider diversifying your put selling across multiple stocks and industries. Diversification can help spread the risk and reduce the impact of potential losses from individual stock assignments.

Put selling can be a valuable tool for income generation and acquiring desired stocks at discounted prices. However, it is essential to use this strategy judiciously and not concentrate too much risk in a single position.

### C. Using Put Selling to Build a Position in Desired Stocks:

One effective way to use put selling is to target stocks that you want to own at lower prices. Instead of buying the stock outright, selling cash-secured puts allows you to potentially acquire the stock at a discount. If the stock price remains above the strike price until expiration, you keep the premium as income. If the stock price drops below the strike price, you can acquire the stock at the predetermined price, effectively building a position in the stock.

Remember that selling puts on all the stocks you want to own may not always be the best approach. It is crucial to consider your investment objectives, risk tolerance, and market outlook when incorporating put selling into your portfolio. Additionally, be prepared to monitor your positions regularly and adjust your strategy as market conditions change.



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Seeking guidance from a financial advisor can provide valuable insights tailored to your specific financial goals and circumstances.

**Question 7: How do I adjust my cash-secured put strategy in a bullish or volatile market?**

**Answer:**

**A. Adapting Put Selling Strategy to Different Market Conditions:**

In a bullish or volatile market, it is essential to adjust your cash-secured put strategy to align with the changing market conditions. Put selling is a versatile strategy that can be adapted to take advantage of different market scenarios.

**B. Rolling Puts and Adjusting Strike Prices:**

One way to adjust your cash-secured put strategy in a bullish or volatile market is through rolling puts and adjusting strike prices. If the underlying stock price rises significantly, and you still want to maintain exposure to potential further gains, you can "roll up" your put options by buying back the original puts and selling new puts at a higher strike price. This allows you to capture additional premium while positioning yourself for potential stock assignment at a more favorable price.

Conversely, in a volatile market where the stock price experiences significant swings, you can "roll out" your puts by buying back the near-term puts and selling new puts with a later expiration date. This gives you more time for the stock price to stabilize or move in your favor before potential assignment.

**C. Using Protective Calls as a Risk Management Tool:**

In a bullish or volatile market, you can also consider using protective calls as a risk management tool in conjunction with your cash-secured put strategy. By buying call options as a hedge, you protect your short put positions from excessive losses if the stock price experiences a sudden and significant decline.

If the stock price drops below the strike price of your puts, the protective calls can help mitigate potential losses, providing you with added downside protection. This approach allows you to participate in the upside potential while limiting your exposure to downside risk.

As with any trading strategy, it is crucial to monitor the market closely and stay informed about changing market conditions. Adapting your cash-secured put strategy in a bullish or volatile market requires a thorough understanding of the risks and rewards involved. Remember to assess your risk tolerance and investment objectives to ensure that the adjustments align with your overall financial goals.

It is also advisable to seek guidance from a qualified financial advisor, especially if you are new to options trading or need personalized advice tailored to your individual financial situation. By staying flexible and proactive, you can navigate a bullish or volatile market effectively with your cash-secured put strategy.

**Question 8: What are the tax implications of selling cash-secured puts?**

**Answer:**



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#### A. Tax Treatment of Put Premiums Received:

When selling cash-secured puts, the premiums you receive from selling the puts are generally treated as short-term capital gains. This means that the income generated from selling puts is taxable in the year you receive it at your ordinary income tax rate.

It's essential to keep accurate records of your options trades, including the premiums received, dates of transactions, and any associated expenses or commissions. This information will be crucial for accurate tax reporting at the end of the tax year.

#### B. Tax Implications of Stock Purchase Through Put Assignment:

If the stock price drops below the strike price of your cash-secured put, and you are assigned to buy the stock, you will acquire the shares at the strike price, regardless of the current market value.

The tax implications of this stock purchase depend on what you choose to do with the stock afterward. If you hold the stock for more than one year before selling it, any gains from the eventual sale will be treated as long-term capital gains, which typically have a more favorable tax rate than short-term capital gains.

On the other hand, if you decide to sell the stock within one year of purchasing it through put assignment, any gains will be considered short-term capital gains and will be taxed at your ordinary income tax rate.

#### C. Consulting a Tax Professional for Guidance:

As tax regulations can be complex and vary based on individual circumstances, it's essential to consult a qualified tax professional to understand the specific tax implications of your cash-secured put trades and any subsequent stock purchases or sales.

A tax advisor can help you navigate the tax rules and regulations, identify potential tax-saving strategies, and ensure that you are in compliance with all tax laws. By seeking professional advice, you can make informed decisions and optimize your tax outcomes when selling cash-secured puts.

Keep in mind that tax laws are subject to change, so staying informed about current tax rules and regulations is essential for managing your tax liabilities effectively. Regularly reviewing your trading activity with a tax advisor can help you proactively plan and minimize any potential tax burdens associated with your cash-secured put strategy.

Question 9: Can I use cash-secured puts in retirement accounts like IRAs?

Answer:

#### A. Selling Puts in Retirement Accounts:

Yes, you can use cash-secured puts in retirement accounts like IRAs (Individual Retirement Accounts). However, not all brokerages may allow certain options trading strategies, so it's essential to verify with your IRA custodian whether put selling is permitted in your specific retirement account.



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#### B. Complying with IRA Regulations for Put Selling:

If your IRA allows options trading, including selling cash-secured puts, you must ensure that your put selling activities comply with IRS (Internal Revenue Service) regulations and the rules set by your IRA custodian. It's important to understand any restrictions or limitations imposed by your IRA custodian to avoid potential penalties or account restrictions.

One critical consideration when selling puts in an IRA is that you must have enough cash or cash equivalents in your account to cover the cost of purchasing the underlying stock if you are assigned to buy it. This requirement is to ensure that your IRA remains in compliance with IRA regulations and avoids prohibited transactions.

#### C. Benefits and Considerations of Selling Cash-Secured Puts in IRAs:

Selling cash-secured puts in an IRA can be an attractive strategy for generating income and potentially acquiring stocks at a discount. By selling puts, you collect premium income upfront, which can enhance the overall return of your retirement account. If the puts expire without being assigned, you keep the premium as profit.

Moreover, using cash-secured puts in an IRA can provide a way to build a position in stocks you desire to hold long-term. If you are assigned to buy the stock at the strike price, you effectively acquire the shares at a lower cost basis than the current market price, allowing you to potentially benefit from stock appreciation over time.

However, it's important to recognize the risks associated with selling puts in an IRA. If the stock price declines significantly below the strike price, and you are assigned to buy the stock, your IRA may be exposed to potential losses on the stock position. Therefore, careful stock selection and risk management are crucial when using cash-secured puts in a retirement account.

Overall, selling cash-secured puts in an IRA can be a valuable strategy for income generation and potentially adding high-quality stocks to your retirement portfolio at favorable prices. Always consult with a financial advisor or tax professional to understand the implications of using this strategy in your specific retirement account and to ensure it aligns with your overall investment goals and risk tolerance.

Question 10: How do I calculate my potential return on a cash-secured put trade?

Answer:

#### A. Understanding Potential Return if Not Assigned:

When selling cash-secured puts, the potential return if not assigned refers to the profit made from selling the put option without being obligated to purchase the underlying stock. The return in this scenario is the premium received from selling the put option. To calculate this potential return, divide the premium by the cash secured in the trade (which is typically the strike price multiplied by the number of contracts).

Potential Return if Not Assigned (%) = (Premium Received / Cash Secured) \* 100

#### B. Calculating Return if Assigned and Required to Purchase the Stock:

In the event that the put option is assigned, and you are required to purchase the underlying stock at the strike price, the return calculation becomes slightly different. To calculate the



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return if assigned, subtract the cash secured (strike price multiplied by the number of contracts) from the total cost of purchasing the stock (strike price multiplied by the number of contracts) and add the premium received.

Return if Assigned (%) =  $[(\text{Premium Received} + (\text{Strike Price} * \text{Number of Contracts})) - (\text{Strike Price} * \text{Number of Contracts})] / (\text{Strike Price} * \text{Number of Contracts}) * 100$

#### C. Evaluating the Overall Profitability of Put Selling Trades:

To evaluate the overall profitability of selling cash-secured puts, you need to consider both potential scenarios: not being assigned and retaining the premium as profit, and being assigned and purchasing the stock at the strike price. Compare the two potential returns to assess the attractiveness of the trade.

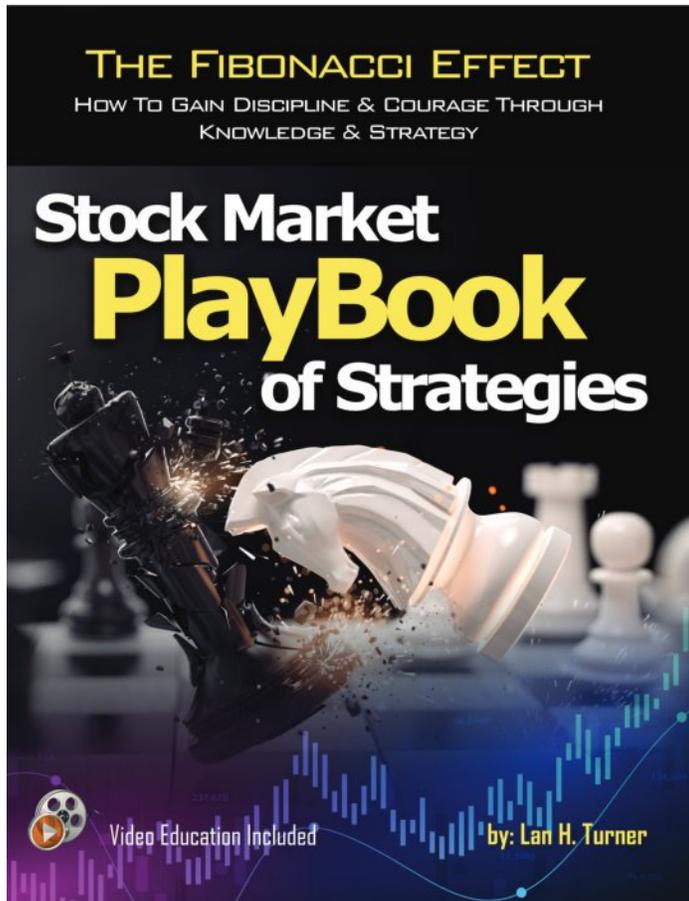
Keep in mind that selling cash-secured puts involves the obligation to buy the stock if the option is exercised, which could result in capital allocation for stock purchase. Therefore, it's essential to evaluate the potential return if assigned and ensure it aligns with your investment goals and risk tolerance.

Additionally, consider the time frame and frequency of put selling trades to determine their overall impact on your investment portfolio. Regularly selling puts can provide a steady income stream, but it also means you may acquire stocks at different times and prices, affecting your portfolio's overall performance.

As with any investment strategy, risk management and prudent decision-making are crucial when selling cash-secured puts. Be mindful of the risks associated with this strategy, and consider consulting with a financial advisor or professional options trader to optimize your put selling approach and enhance your overall portfolio returns.



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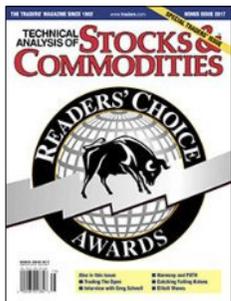
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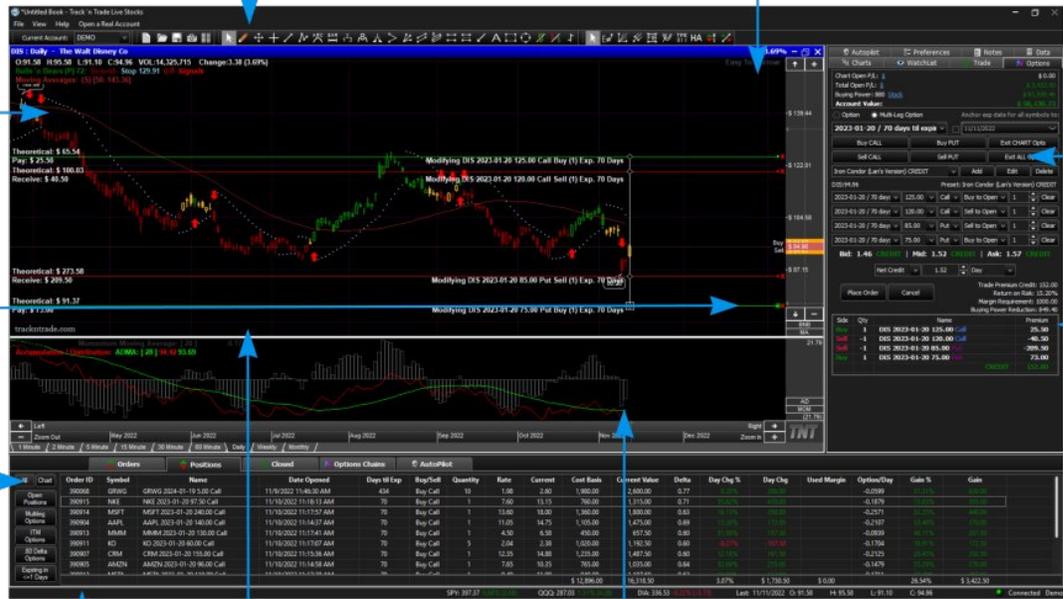
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Slide to hide!

**Mini-Account:**  
Running account balances, totals, at risk, profits, and margins.

**Trade Buttons:**  
Extremely fast, one-click trade buttons, drag 'n drop multiple orders, on-screen, simultaneously.

**Options P&L Calculator**  
Calculate % Return on gain, margin and buying power.

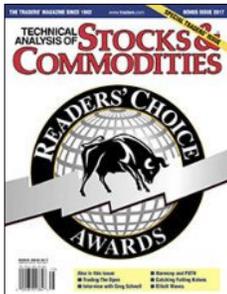


**Multi-Chart View:**  
View multiple charts simultaneously, or view one chart at a time for maximum price action monitoring capabilities.

**Full Featured Accounting Window:**  
Track your real-money trades, as the world turns, manage your trades all in one central location, easy to manage.

**Chart Time Frame Controls:**  
Access multiple, user definable, chart times from a single button bar click, which allowing multi-chart screen views to share multiple times, 5min, 10min, 15min, etc... (Any 1 minute increment.) Plus, Range & Volume bars!

**Indicator Windows:**  
Includes dozens & dozens of the best proven technical indicators with highly accurate, customizable, buy/sell signals, for better decision making.



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## TradeMiner Market Data Miner

Scans and Finds Historically Repeating Market Cycles & Trends

### Tabbed Control Panel:

By following through, from one tab to the next, TradeMiner takes you through a simple step-by-step process of analyzing the markets for the highest probability trading opportunities coming during the upcoming month.\*

### Neural Network (Portfolio) Tab:

Discover the probabilities of a market repeating its historical pattern again this year.

### Paragraph Style User Inputs:

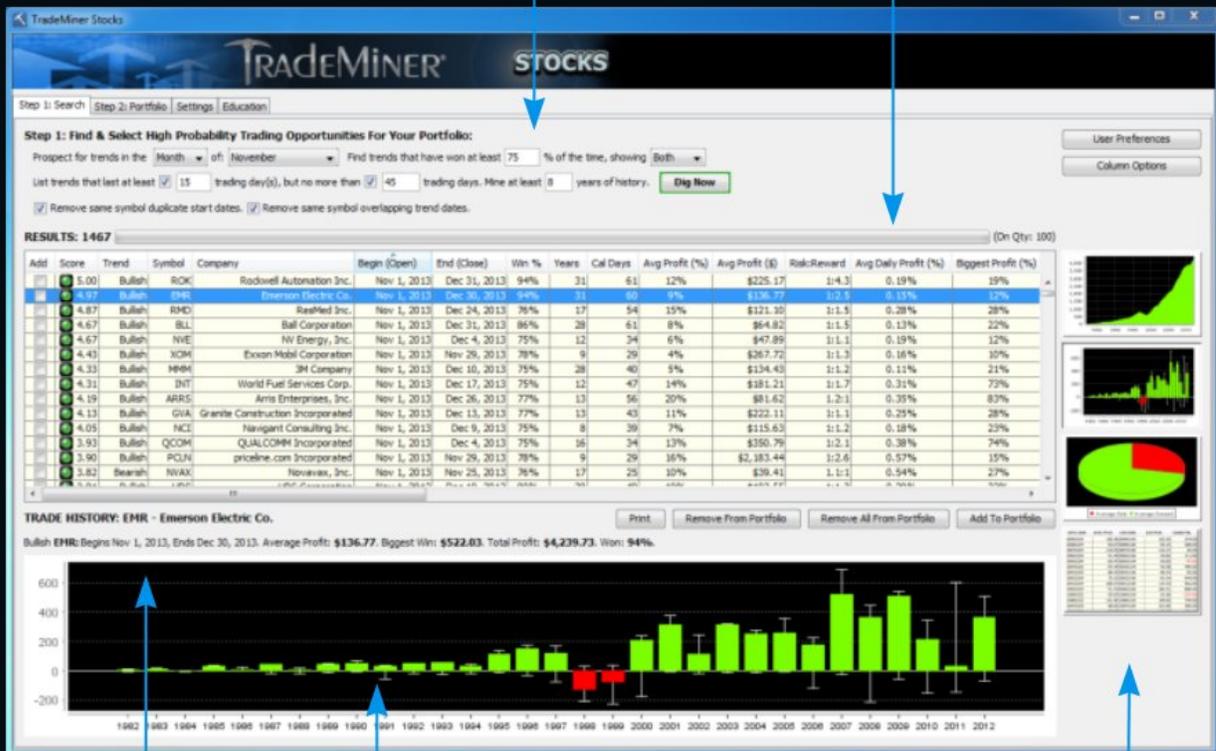
By using a simple question answering paragraph, TradeMiner guides you through the process of picking the right stock, futures contract, or Forex pair to trade this month.\*

### Results Table, and Reports:

TradeMiner provides every single statistical report imaginable about each individual trading signal and opportunity.\*

**Score:**  
Each opportunity receives a score, ranking it from 0-5, Red, Yellow & Green.

Simply trade the highest scoring opportunities.\*



### Chart Window:

Provides a graphical view of the historical yearly results for any chosen trade.

### Chart Selection Buttons:

Click and select the different graphical statistical views. Each chart will show up in the lower Chart Window view once clicked.\*

### Trade Summary:

Each trading opportunity is summarized above the chart window, for easy navigation and statistical accessibility.\*

**History Continually Repeats Itself, Over & Over & Over.  
The KEY is Knowing When That Might Happen Again!**

[www.TradeMinerPro.com](http://www.TradeMinerPro.com)