

>: Recapture Lost Profits With This Easy Options Strategy

Tuesday, April 14, 2009 / Chris Rowe

You can't be afraid of what you don't know, if you ever want to change your current situation. And most people's situation right now is one in which they fell into an investing pigeon hole that they have to claw their way back out of.

This puts us in the classic situation that we have all found ourselves in at one point or another: "I took (what, in hindsight, was) a silly risk and lost a huge amount of money. So, the only way to make that money back is to INCREASE that risk. But, deep inside, I know that's the wrong thing to do."

(Even though people know taking an even-bigger risk at this point is absolutely the wrong thing to do, they do it anyway. You know how that would probably end.)

So, if you find yourself in this situation, what do you do? Quit while you still can?

Of course, the real answers -- the answers nobody in that situation wants to hear -- are: "You should not be in this situation in the first place. You shouldn't have taken so much risk. You should have paid more attention to *learning and understanding what it is that you were doing with your money in the first place*. You should have accepted a lower-risk-with-lower-reward strategy."

It's too late for an investor whose portfolio is down to hear any of those painful answers. So, we look for the more-responsible answers, because all hope isn't lost.

But the answer is NOT: "*Reduce* your potential reward by *reducing* your incurred risk."

And the answer CERTAINLY is NOT: "*Increase* your potential reward, thereby taking on *MORE* risk in order to make your money back."

It doesn't have to be one or the other. **You CAN have both.** You CAN increase your potential reward while at the same time reducing your risk.

Portfolio Out-of-the-Money? Time to Go 'In-the-Money'

So, how can you get the maximum-possible leverage out of the money in your portfolio while putting the least amount of money on the table for each trade? The answer is "trade high-delta options" (aka, in-the-money options) that have far-out expiration months. (Although all options come with an expiration date, you can buy as much as 2 1/2 years' worth of time to let the trade work in your favor. If you trade stocks, this may be the same amount of time, or longer, that you hold shares in your account.)

I know, I know, this might sound intimidating to those option novices. But the fact is, it's not as complicated as one would think.

The answer to your dilemma of having a down portfolio that you want to get back to even on is not a question of adjusting your approach to higher risk or lower reward. The answer is: Spend just a little bit of time learning a simple strategy. That's it. If you spend a couple of hours learning this options strategy, then when you start to replace your stock positions with the options positions I'm describing, you'll lose a fraction of what you would have lost on the stock trade (when you're wrong) and you'll make more than you would have made on the stock trade (when you're right)!

HYPOTHETICAL EXAMPLE:

XYZ stock trades 20 points in either direction

STOCK OWNER (of 1,000 shares)

Up 20 points: STOCK TRADER MAKES \$20,000

Down 20 points: STOCK TRADER LOSES \$20,000

STOCK OPTIONS OWNER (of 13 of the right options contracts)

Up 20 points: OPTION TRADER MAKES \$21,684

Down 20 points: OPTION TRADER LOSES \$17,420

NOTE: Notice the option trader makes more on the upside than he/she loses on the downside.

How much is that worth? Well, let's look at it this way: How much schooling (formal or informal) did you go to through to learn whatever skill you have that puts food on your table? Months? Years?

Can you think of a profession that would have a similar situation where the person that would have a higher potential to make more money would have spent more time in school than the person that would have a lower potential to make more money?

100% false. Ignoring the fact that you are taking too much risk RIGHT NOW might be what caused the losses you may have already incurred.

I'm not saying this in a condescending way. If you are down on your investment portfolio, BELIEVE me you aren't alone. But I'm trying to tell you that you can start taking steps NOW to protect your money and to generate far more over time.

There is a way out of it without taking more risk, and instead taking LESS risk. And this is the way you should trade for the rest of your life. The past is the past.

So, why did I title this article, "Recapture Lost Profits With This Easy Options Strategy"?

It's easy because anyone can learn options enough to successfully reduce risk while increasing profits at the same time. There is no shortage of profits to go around in the options market -- there is enough for anyone who makes smart, savvy trades. The options market isn't some exclusive club only open to Wall Street types -- any one of us can learn how to trade options and be paid handsomely for trading them *well*.

I can't cover all the necessary information that goes into making good options trades in one article, but I will give you the basics below.

The Power of High Delta (In-the-Money) Options

What if you thought Research In Motion (RIMM) was going to trade higher? (I have no opinion on Research In Motion; this is just a hypothetical example.)

Assuming Research In Motion stock trades at \$64:

- * The stock trader might buy 1,000 shares of RIMM at \$64.
- * The option trader might buy 13 in-the-money call options. (This example uses the RIMM January (2010) 50 Calls trading at \$22, instead.)

NOTE: The calls in the example above give you the right to buy shares of RIMM at \$50 until those options expire on the third Friday of January 2010. Because options are priced on a per-share basis but option contracts represent 100 shares of the underlying, you would spend \$22 x 100 (\$2,200) per contract. Multiply that by 13 contracts, and your cash outlay would be \$28,600 to control 1,300 shares of RIMM until January 2010. The calls at the \$50 strike are high-delta because, with the stock trading at \$64, the options are deep in-the-money.

So, back to our example:

- * Stock trader commits to the position (invests) \$64,000 in RIMM stock (1,000 shares at \$64).
- * Option trader also commits to the position (invests) \$64,000 -- \$28,600 into the call options, and leaves the remaining \$35,400 in cash. The cash is considered to be part of the position. (\$28,600 + \$35,400 = \$64,000 total position size.)

SIDE NOTE: The options trader's maximum risk is the dollar amount invested in the stock option (\$28,600) and that is the extreme scenario where there is a disaster and the stock loses *most* of its value. But that's not why we have a much higher reward-to-risk ratio. Let me explain. ...

Here's a quick comparison to what will happen to each position given three different possible scenarios:

Scenario 1: The stock moves 10 points in either direction today

Up 10 points: OPTION TRADER MAKES ~~\$~~**10,550**

Down 10 points: OPTION TRADER LOSES ~~\$~~**9,360**

(MAX RISK \$28,600)

NOTE: Notice the option trader makes more on the upside than he/she loses on the downside.

Up 10 points: STOCK TRADER MAKES ~~\$~~**10,000**

Down 10 points: STOCK TRADER LOSES ~~\$~~**10,000**

(MAX RISK \$64,000)

NOTE: Option trader makes more than, or loses less than, the stock trader. At the same time, the stock trader's max risk is more than two times the option trader's max risk.

Scenario 2: The stock moves 20 points in either direction

trader's max risk.

Scenario 3: The stock moves 50 points in either direction today

Up 50 points: OPTION TRADER MAKES ~~\$~~57,746

Down 50 points: OPTION TRADER LOSES \$28,548

(MAX RISK \$28,600)

NOTE: Notice the option trader makes A HECK OF A LOT more on the upside than he/she loses on the downside.

Up 50 points: STOCK TRADER MAKES ~~\$~~50,000

Down 50 points: STOCK TRADER LOSES \$50,000

(MAX RISK \$64,000)

NOTE: Option trader makes more than, or loses less than, the stock trader. At the same time, the stock trader's max risk is more than two times the option trader's max risk.

I think we're beginning to see a pattern here!

There is a whole lesson behind this, and it makes sense to use several different examples using both call options (to profit from stock advances) and put options (to profit from declines)!

I can't give you all of that here. I can, however, invite you to participate in the webinar I'll be doing for Sector Hunter members. This is not meant to be a "tease" to get you to sign up for something. I'm saying this because it would be irresponsible of me to try to pack a ton of instruction into a short article.

So, I'm inviting you to the webinar I'm holding LIVE in a few weeks, which you can attend by signing up with [Sector Hunter](#).

We offer a 30-day money back guarantee, so you can test-drive the service and attend the webinar risk-free during that period. Like I said, Sector Hunter has automatically issued 30 trade alerts since we launched it in March, 27 of which were profitable. So, while you are signing up to check out the webinar in order to give you a profit-making strategy to use for the rest of your life, you also gain access to an automated trading system that will actually give you trading ideas to try this strategy out on!

I already held one options-trading webinar for Sector Hunter members (last week). It's recorded, and posted on the Web site for those who missed it to have access to this powerful information and for those who were in attendance to go back and review it to ensure that they truly "know their stuff" before making an options trade.

Last week's webinar was a bit "off the cuff," and Sector Hunter members were able to watch me go to a few Web sites to give a few examples. However, the next webinar will address options trading more in-depth, which you can attend as a Sector Hunter member. Plus, after signing up, you get two bonus reports explaining the options strategy I'm talking about, and you will immediately gain access to last week's webinar on the very same topic.

Plus, you will get a much better and higher-quality online seminar in a few weeks where you can ask me questions. This is so much more helpful, since you'll be able to go over the strategy long before the webinar is held. By then, you should be able to start your journey back to profitability by taking LESS RISK with a higher potential reward.

I hope to see you there!

[Visit this link to check it out.](#)

?Profit from the Trend?



Chris Rowe

Chief Investment Officer

≥