User Guide

How To Get The Most Out Of Your Subscription
Thank you for subscribing!

As chief options strategist of *Cabot Options Institute Income Trader*, I want to welcome you on board!

Whether you are just getting started with options or have traded them for years, it’s my goal to teach you my statistically driven, mechanical approach to trading options so that you can create a steady, consistent stream of income.

Simply stated, I’m a quantitative trader. I use math to make all my trading decisions. Probabilities are a key factor in each and every trading decision, not just with earnings trades, but with all my options trades. And my hope is that by learning my statistical approach to options trading, you will have the ability to use the strategies learned to take advantage of the wide variety of options opportunities the market has to offer.

For *Cabot Options Institute Income Trader* subscribers, this guide will provide both beginning and advanced traders the step-by-step guidance for making the most of the advisory’s abundance of resources.

I hope that through weekly webinars, alerts and updates you will quickly learn from my 25 years of professionally trading options.

At any time, if you have questions or comments, please do not hesitate to email me at Andy@CabotWealth.com.

Once again, it’s great to have you on board. And I hope you find the service helpful in all your trading endeavors. I look forward to a long and profitable relationship.

Kindest,

Andy Crowder
Chief Analyst
*Cabot Options Institute Income Trader*
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Issue
Every Monday I will publish a weekly issue that discusses our open trades and how we plan to proceed going forward. Each weekly issue will include the companies that I plan to focus on plus several other trade ideas for those that wish to trade a bit more often on their own. Every month, on the Wednesday before the third Friday of the month (options expiration), we will get together for a live webinar. In each webinar we will discuss not only open trades, but potential trades as well. I will also answer any pertinent questions you may have regarding past trades, future trades or just anything options. Each webinar will be recorded and archived just in case you are not able to attend the live webinar.

Alerts
You will receive email alerts when market or trade conditions warrant it; during each expiration cycle I will issue between 3-8 alerts using our risk-defined strategies.

Special Reports
Our catalog of Special Reports provides further options analysis that provides a deeper dive into trading strategies and tactics. Here you will find all of my step-by-step strategy guides for the strategies we use most frequently, plus the statistical approach I use around each and every income trade.

24/7 Archives
Your subscription gives you access to our vast online library of analysis, including past weekly updates, reports, related webinars, and other educational content published by Cabot Wealth Network.

Direct Contact
Outside of our live webinars where you can ask as many questions as you would like, whenever you have an investment-related question, you can also email me directly at Andy@CabotWealth.com. You can also call our Cabot Investor Services desk at 800-326-8826 anytime during business hours to speak with someone about your subscription. Or you can email our subscription support staff at Support@CabotWealth.com.
In *Cabot Options Institute Income Trader*, I use four different options strategies with the intent of producing steady, consistent income from one expiration cycle to the next.

The four strategies are as follows:

1. Selling Puts
2. Income Wheel Strategy
3. Covered Strangle
4. Jade Lizards

In this section I will go over my approach to each options strategy and what a typical trade will look like within the service.

### Selling Puts

Selling puts is an integral part of the service. Now I know some of you may have reservations selling puts as a strategy, but I think after a little education on how I approach the strategy, your thoughts on the strategy will certainly change. There is a reason why so many professional options traders sell puts as their bread-and-butter income strategy.

For starters, most investors think of selling a naked put as an aggressive, advanced options strategy. Nothing could be further from the truth, if the strategy is used appropriately.

Synthetically speaking, selling a put carries the same risk as a covered call. The difference is when selling a put I have the ability to not only choose my own probability of success, but the capital outlay is also far less.

But again, the approach must be sound. I only sell puts on stocks that I am willing to own. That being said, I rarely buy a stock or ETF at its current price. Why would I? Selling puts is a much better alternative.

If I'm truly interested in buying a security, I typically have a price target below the current price of the stock. Most investors just set a buy limit at their price target and hope they get shares at their chosen price. But that approach is short-sighted and, well, uninformed.

Because again, there is a much better alternative.

Selling puts allow investors to collect premium (income) while waiting for the stock to hit their price. That's right, let me say it again, investors can essentially produce income while waiting for a stock to hit their chosen price. And the premium produced can be used as a potential source of income or to simply lower the cost basis of the stock they want to buy.

But the thing is, you don’t have to purchase stock when selling puts, unless you really want to own the shares. In most cases, I simply buy back the puts prior to expiration and continue to sell more puts in the same underlying or simply move on to another opportunity. Either way, my goal is to continually produce income through the use of selling puts.

But there will be times when I actually want to own shares, which I'll talk about further in the Wheel Options Strategy section below. But before we get there, let's go over the basics of how I approach the strategy of selling puts for income.
The first step is choosing a well-known, mostly low-beta stock, that has a highly liquid options chain ... and that I don’t mind holding shares of, if needed.

For instance, let’s say you are interested in selling puts on Walmart (WMT) and you would be willing to buy shares, if needed.

In this example, the stock is currently trading for 156.86.

![Walmart Stock Chart](image)

You prefer to sell puts at the 148 strike and potentially own the underlying security at both a future date and a more favorable price, in this case 148.

Now, most investors, would simply set a buy limit at 148 and move on, right? But that approach is archaic. Because you can sell one put for every 100 shares of WMT and essentially create your own return on capital (depending on the strike you choose).

Some say, it’s like creating your own dividend and in a way, I kind of agree.

Inherently, a short put, or selling puts, is a bullish options strategy with undefined risk and limited profit potential. Again, short puts have the same risk and reward as a covered call. Shorting or selling a put means you are promising to buy a stock at the put strike of your choice. In our example, that’s the 148 strike.

If you look at the options chains for WMT below you will quickly notice that for every 100 WMT shares we want to purchase at 148, we are able to bring in roughly $2.15 or $215 per put contract sold, every 40 days.
The trade itself is simple: **Sell to open June 3, 2022, WMT 148 puts for a limit price of $2.15.**

**Quick note: when selling options, set your limit price just under the mid-price of the bid-ask spread. In the example above the bid-ask price of the 148 strike is 1.95 to 2.40. The mid-price is between 2.15 and 2.20, so selling the 148 puts for $2.15 seems reasonable. By not selling at the bid, we are saving $0.25. Doesn’t seem like a lot, but when you start to add up $0.25 for each trade you place, well, it doesn’t take long to realize the impact over the long term. So, the lesson here is **never sell at the market price.** Always, use a limit price. Again, using this approach will create significant returns over the long term that you would otherwise forfeit. Trade intelligently!**

So, by selling the 148 put options in June you can, again, bring in $215 per put contract, for a return of 1.4% on a cash-secured basis over 40 days. That’s $1,935 or 12.6% annually. Again, you can use the premium collected from selling the 148 puts either as a source of income or to lower your cost basis.

Just think about that for a second.

You would like to buy shares of WMT at 148 or possibly just sell WMT puts as a source to produce steady income. The stock is currently trading for 156.86.

If choosing the former, by selling puts at the 148 strike you can lower your cost basis to 154.71. That’s 1.4% below where the stock is currently trading. And you can continue to sell puts over and over, lowering your cost basis even further, until your price target is hit.

As for the latter, you could simply sell puts for a consistent source of income, knowing that if you are put the stock, it’s okay. It was a stock you did not mind owning from the onset.

Or, like most investors, you could just sit idly by and wait for WMT to hit your target price of 148. Losing out on all that opportunity.

In review, by selling puts at the 148 strike we receive $215 in cash, immediately. It’s ours to keep, to do with what we choose. The maximum reward is the $215 per put contract sold. The maximum risk is that the short 148 put is assigned and you have to buy the stock for 148 per share. But, you still get to keep $215 collected at the start of the trade, so the actual cost basis of the WMT position is 148 – $2.15 = $145.85 per share. The $145.85 is our breakeven point. A move below that level and the position would begin to take a loss.

But remember, most investors would have purchased the stock at its current price, unaware there was a better way to buy a security. We rarely take that approach. We know better. We understand we can purchase stocks at our own stated price and collect cash until our price target is hit or simply just use the low-beta stock as a consistent source of income. It’s a no-brainer.

### Income Wheel Strategy

The income wheel strategy is an inherently bullish, mechanical, options income strategy known by various names. The covered call wheel strategy, the income cycle, and the options wheel strategy are just a few of the many names that investors use. But one thing is certain, the systematic approach remains the same.

More and more investors are choosing to use the income wheel strategy over a buy and hold approach because of the ability to create a steady stream of income on stocks you want to or already own.

The mechanics are simple.
• Sell Cash-Secured Puts on a stock until you are assigned shares (100 shares for every put sold)
• Sell Covered Calls on the assigned stock until the shares are called away
• Repeat the Process!

Basically, find a highly liquid stock that you are bullish on and have no problem holding over the long term. Once you find a stock that you’re comfortable holding, sell out-of-the-money puts at the price where you don’t mind owning the stock.

Keep selling puts, collecting even more premium, until eventually you are assigned shares of the stock, again, at the strike price of your choice. Once you have shares of the stock in your possession begin the process of selling calls against your newly issued shares. Basically, you are just following a covered call strategy, collecting more and more premium, until the stock pushes above your call strike at expiration. Once that occurs, your stock will be called away, thereby, locking in any capital gains, plus the credit you’ve collected.

Let’s go through an example to show you exactly how the wheel options strategy works.

Like when selling puts, my preference is to look for low-beta high-quality stocks, household names, that I feel comfortable holding over the long term. I’ve found that dividend aristocrat stocks work well with the wheel options strategy because they have a history of stability, strength and a proven ability to weather market turbulence.

Walmart (WMT)

Wheel Options Strategy – Step One

The retail behemoth is currently trading for 156.86.

Let’s say we decide to go with the 148 put strike.
We can sell to open the 148 puts for roughly $2.15, or $215 per put sold.

<table>
<thead>
<tr>
<th>Stripes: ALL</th>
<th>Strike</th>
<th>Bid X</th>
<th>Ask X</th>
<th>Delta</th>
<th>Prob.OTM</th>
<th>Prob.Touch</th>
</tr>
</thead>
<tbody>
<tr>
<td>3 JUN 22</td>
<td>130</td>
<td>.19 C</td>
<td>.54 C</td>
<td>-.05</td>
<td>94.06%</td>
<td>26.74%</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>135</td>
<td>.52 A</td>
<td>.66 X</td>
<td>-.08</td>
<td>90.84%</td>
<td>17.79%</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>140</td>
<td>.87 A</td>
<td>1.03 X</td>
<td>-.12</td>
<td>85.98%</td>
<td>27.19%</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>145</td>
<td>1.47 A</td>
<td>1.75 Z</td>
<td>-.19</td>
<td>78.20%</td>
<td>42.17%</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>148</td>
<td>1.95 C</td>
<td>2.40 X</td>
<td>-.25</td>
<td>72.14%</td>
<td>53.80%</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>149</td>
<td>2.21 C</td>
<td>2.65 X</td>
<td>-.27</td>
<td>69.72%</td>
<td>58.43%</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>150</td>
<td>2.48 C</td>
<td>2.91 C</td>
<td>-.30</td>
<td>67.24%</td>
<td>63.16%</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>155</td>
<td>4.25 X</td>
<td>4.60 Z</td>
<td>-.43</td>
<td>53.21%</td>
<td>89.74%</td>
</tr>
</tbody>
</table>

By selling the 148 puts for $2.15 our return is 1.4% cash-secured, or 9.5% on margin over 40 days.

If WMT stays above our 148 put strike at expiration we begin the process of selling puts again, thereby creating more premium to use as income or to lower the cost basis of our position. So, if we bring in a conservative 1.4% every 40 days, and we can sell puts roughly 9 times over the course of a year (if the stock stays above our chosen short put strike) our annual return is 12.6% on a cash-secured basis ... or 85.5% on margin. Again, it bears repeating, we can use that capital to either produce a steady stream of income or to lower the cost basis of our position.

But what if WMT closes below our short put strike?

No biggie. We are issued or assigned shares at the price where we wanted to buy the stock. Think about it for a sec. We collect a premium as a source of income to wait for a stock to hit our chosen price.

**Wheel Options Strategy – Step Two**

So, let's say WMT closes below our 148 put strike at expiration. If so, we are issued 100 shares at $148 for every put contract we've sold.

Once we have shares in our possession, we begin the process of selling out-of-the-money calls against our shares, which begins the covered call portion of the wheel options strategy on WMT.

Now the question is which strike to choose. Again, ultimately it just comes down to preference. My preference is focusing on call strikes that have a probability of success ranging from 68% to 85%.

<table>
<thead>
<tr>
<th>Calls</th>
<th>Delta</th>
<th>Prob.OTM</th>
<th>Prob.Touch</th>
<th>Bid X</th>
<th>Ask X</th>
</tr>
</thead>
<tbody>
<tr>
<td>3 JUN 22</td>
<td>.41</td>
<td>62.29%</td>
<td>78.53%</td>
<td>3.25 X</td>
<td>3.65 A</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>.26</td>
<td>75.99%</td>
<td>49.68%</td>
<td>1.73 X</td>
<td>2.08 A</td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>.15</td>
<td>86.35%</td>
<td>28.10%</td>
<td>.84 C</td>
<td>1.05 A</td>
</tr>
</tbody>
</table>

Let's say, for example, we decide on the selling the 165 calls against our newly issued WMT shares for roughly $1.85 per call contract. Our probability of success on the 165 calls stands at 75.99%.

Our static return or return on capital is 1.3% over 40 days.

If WMT stays below our 165 call strike at expiration we begin the process of selling calls again, thereby creating more premium to use as income or to lower the cost basis of our position. So, if we bring in a conservative 1.3% every 40 days, and we can sell calls roughly 9 times over the course of a year (if the stock
stays below our chosen short call strike) our annual return is 11.7%. Again, it bears repeating, we can use that capital to either produce a steady stream of income or to lower the cost basis of our position.

But what if WMT closes above our short call strike?

Again, no big deal. Our shares are called away, so of course, we keep our $185 per call contract, plus we are able to reap any capital gains from our stock. In this case, we would keep the $185 plus an additional $17 per share or $1,700 per 100 shares for a 11.5% gain.

Once our shares are called away, the wheel options strategy cycle ends, and the decision has to be made whether or not to continue using the strategy with the same stock.

The wheel options strategy is a wonderful strategy for those wanting to generate steady income, with lower risk compared to most options strategies. It also gives the investor an opportunity to lower the overall cost basis of a position.

The strategy isn’t a get rich quick strategy, rather a methodical, systematic approach to trading options that generates consistent returns, month after month, on stocks that you want to hold in your portfolio over the long term.

**Covered Strangle**

A covered strangle is simply a covered call strategy coupled with a short put—or just buying a stock and wrapping a short strangle (sell out-of-the-money put and sell out-of-the-money call) around it. Either way, it’s a covered strangle.

Investors want to use a covered strangle when they wish to enhance the returns on a long position (stock or ETF) by two to four times, while also having the opportunity to buy even more shares at a price of their choosing. It’s a great income strategy to use on stocks you already own or wish to acquire.

But, let’s go through an example to really get down to the nitty-gritty of how a covered strangle works.

**Apple (AAPL) – Covered Strangle**

I’m going to keep it simple by using tech behemoth Apple (AAPL) for our covered strangle example.

With AAPL trading for 161.79, we are going to buy 100 shares for $16,179.
Once we've purchased at least 100 shares we then will sell a delta-neutral short strangle around the shares. Since AAPL is trading for roughly 162, we will look to sell a short strangle that has a delta of roughly 0.10 to 0.30 for both the call and put. Moreover, I will look to go out 20 to 50 days. My preference is to go with a shorter duration for my short strangle, but the amount of premium I can bring in will define my choice of expiration cycle.

Here are our choices for expiration cycles. I'm going to use the June 3, 2022, expiration cycle with 40 days left until expiration.

<table>
<thead>
<tr>
<th>Date</th>
<th>Strike</th>
<th>Days Left</th>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>20 MAY 22</td>
<td>100</td>
<td>26</td>
<td></td>
</tr>
<tr>
<td>27 MAY 22</td>
<td>100</td>
<td>33 (Weekly)</td>
<td></td>
</tr>
<tr>
<td>3 JUN 22</td>
<td>100</td>
<td>40 (Weekly)</td>
<td></td>
</tr>
<tr>
<td>17 JUN 22</td>
<td>100</td>
<td>54</td>
<td></td>
</tr>
</tbody>
</table>

Once I've chosen my expiration cycle, I then must decide which strikes I wish to use for my short strangle. In most cases, I want to sell a short strangle that has an 80%+ probability of success, or a delta of roughly 0.20 or less.

On the call side:

<table>
<thead>
<tr>
<th>Strike</th>
<th>Delta</th>
<th>Prob. OTM</th>
<th>Prob. Touch</th>
<th>Bid</th>
<th>Ask</th>
</tr>
</thead>
<tbody>
<tr>
<td>3 JUN 22 180 Call</td>
<td>.45</td>
<td>59.48%</td>
<td>85.00%</td>
<td>6.00 N</td>
<td>6.50 H</td>
</tr>
<tr>
<td>3 JUN 22 35 Call</td>
<td>.35</td>
<td>69.52%</td>
<td>63.44%</td>
<td>3.50 Q</td>
<td>4.50 X</td>
</tr>
<tr>
<td>3 JUN 22 25 Call</td>
<td>.25</td>
<td>78.51%</td>
<td>44.47%</td>
<td>2.21 Q</td>
<td>2.75 P</td>
</tr>
</tbody>
</table>

We can sell the 180 call strike for roughly $1.50. The 180 call strike has a probability of success of 85.45%, and a delta of 0.17.

On the put side:

<table>
<thead>
<tr>
<th>Strike</th>
<th>Delta</th>
<th>Prob. OTM</th>
<th>Prob. Touch</th>
<th>Bid</th>
<th>Ask</th>
</tr>
</thead>
<tbody>
<tr>
<td>3 JUN 22 135 Put</td>
<td>.10</td>
<td>91.30%</td>
<td>17.85%</td>
<td>.47 X</td>
<td>1.14 Z</td>
</tr>
<tr>
<td>3 JUN 22 130 Put</td>
<td>.17</td>
<td>85.45%</td>
<td>29.99%</td>
<td>1.27 X</td>
<td>1.80 N</td>
</tr>
</tbody>
</table>

We can sell the 135 put strike for roughly $1.50. The 135 put strike has a probability of success of 85.21%, and a delta of 0.11.
The Trade

Simultaneously:

- Sell out-of-the-money call
- Sell out-of-the-money put

Sell to open AAPL June 3, 2022, 180 call
Sell to open AAPL June 3, 2022, 135 call for a total credit of $3.00

Premium Return: $3.00 ($1.50 for the call + $1.50 for the put)

A Few Possible Outcomes

Stock Pushes Above Short Call Strike

If Apple pushes above the 180 short call strike, no worries, we get to keep the put premium of $1.50, the call premium of $1.50 and we make roughly $18 on the stock. Overall, our gain would be $2,100, or 12.98% over 40 days.

Stock Stays Within the Range of 135 to 180

If Apple stays between our short put and short call, we get to keep the entire premium of $3.00, or 1.85% over 40 days. We can use the covered strangle strategy roughly 9 more times over the course of the year for a total annual return (just premium) of approximately 16.7%.

Stock Pushes Below our Short Put Strike

If Apple pushes below our short put strike of 135, we still get to keep our overall premium of $3.00. But we would be issued 100 shares of stock for every put sold. Our breakeven on the newly issued shares would be $132.00, a discount to where the stock is currently trading of 18.4%.

To sum up a covered strangle options strategy, if you wish to enhance a stock position, like AAPL, consider this often overlooked but highly flexible covered strangle. You start with the same exposure as a long stock and have protection if the stock moves above or below the stock price. And again, if the stock stays between the short put and short call, you will be rewarded with significantly more premium than with a standard covered call.

Jade Lizard

Weird name, I know, but it seems almost all options strategies have strange names.

Nonetheless, the jade lizard is an incredible, defined-risk strategy that offers investors the opportunity to take advantage of high implied volatility environments.

In fact, when used correctly, the strategy offers no risk to the upside … that's right, absolutely no risk to the upside. But before we get to that aspect, let's go over the basics of the strategy.

A jade lizard consists of a short put and a short call vertical spread (bear call spread) with limited maximum profit potential, and no risk to the upside. The strategy has a neutral to bullish market assumption but can also make money on slightly lower markets as well.
The credit that is created is higher than the width of the bear call spread.

The trade setup for a jade lizard options strategy is as follows:

- Sell an out-of-the-money put
- Sell an out-of-the-money bear call spread (short call vertical spread)

However, the above doesn’t get into the necessary details. The key is to create a credit from the short put and bear call spread that is greater than the overall width of our bear call spread.

For this to occur, in most cases, my goal is to bring in roughly 70% of the overall credit from my short put, which means 30% of my credit must come from the bear call spread. Now, of course, the percentages are approximations, but remember, the goal is to bring in an overall credit that is greater than the strike width of our bear call spread. By doing so, we **eliminate all risk to the upside**.

**Jade Lizard Strategy – Step-By-Step**

*Remember, this is neutral to bullish strategy, so that should be our leaning going into the trade.*

The first item is to look for an underlying stock that has a high IV rank and IV percentile. Implied volatility (IV) is one of the key components to any options pricing model, so when IV is high, we have the opportunity to bring in more premium.

After doing a quick screen (I’ll show you how to set up a similar screen in a follow up video) on stocks with a mid-to-high IV rank, I found a decent candidate, **Intel (INTC)**. Just remember, we are simply going through the mechanics of a jade lizard, so if the trade doesn’t meet your expectations, no worries, at least you will know how to implement the trade when an opportunity arises.

The next step is to take a look at the expected move of the expiration cycles ranging from 30 to 60 days.

Below is the August 20, 2021, expiration cycle with 32 days until expiration. It’s an older example, but the focus should be on the mechanics of the trade, not the dates. As you can see from the vertical bar highlighted in yellow, the expected range or move is from roughly 50 to 58.50.

Ideally, we want to place our jade lizard outside of the range. But the most important aspect is to keep our probabilities as high as we can while making sure the amount of credit we bring in exceeds the width of our bear call spread.
Let’s start by taking a look at the put side of things.

I plan on going with a 2-strike-wide bear call spread, so we need to look for a put that totals roughly 70% of the $2.00, or roughly $1.40.

So, taking that into account, we can choose either the 52 strike or 52.5 strike.

Let’s go with the 52.5 strike. We can bring in roughly $1.56, which covers 78% of our 2-strike-wide bear call spread.

In this example, the probability of success on the downside is 60.81%. My preference is to be closer to one standard deviation out, or approximately 68%.

Quick note: If I’m not pleased with my probabilities, at any time I can move on to another potential trade, possibly looking for an underlying stock that has a higher implied volatility.

Now that we know we can bring in $1.56 worth of premium from selling the 52.5 put, we can look towards the bear call spread to bring in the remaining premium, or $0.44. Again, this will meet our requirement of...
bringing in enough premium to cover our 2-strike-wide bear call spread.

<table>
<thead>
<tr>
<th>Calls</th>
<th>Strike</th>
<th>Expiration</th>
<th>Delta</th>
<th>Bid</th>
<th>Ask</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prob.OTM 68.10%</td>
<td>20 AUG 21</td>
<td>57</td>
<td>0.26</td>
<td>1.30 N</td>
<td>1.32 D</td>
</tr>
<tr>
<td>Prob.OTM 71.07%</td>
<td>20 AUG 21</td>
<td>57.5</td>
<td>0.33</td>
<td>1.14 D</td>
<td>1.16 Z</td>
</tr>
<tr>
<td>Prob.OTM 73.77%</td>
<td>20 AUG 21</td>
<td>58</td>
<td>0.30</td>
<td>1.00 A</td>
<td>1.04 H</td>
</tr>
<tr>
<td>Prob.OTM 76.47%</td>
<td>20 AUG 21</td>
<td>58.5</td>
<td>0.27</td>
<td>0.87 C</td>
<td>0.90 D</td>
</tr>
<tr>
<td>Prob.OTM 78.89%</td>
<td>20 AUG 21</td>
<td>59</td>
<td>0.24</td>
<td>0.76 C</td>
<td>0.79 Z</td>
</tr>
<tr>
<td>Prob.OTM 81.09%</td>
<td>20 AUG 21</td>
<td>59.5</td>
<td>0.22</td>
<td>0.67 D</td>
<td>0.69 Z</td>
</tr>
</tbody>
</table>

If we look at the 57.5/59.5 bear call spread, we can bring in roughly $0.45 worth of premium. Our probability of success on the upside is 60.74%, but remember, in total, between selling the put and bear call spread we are able to bring in $2.01 ($1.56 + $0.45). So, our upside has no risk, whatsoever. INTC can move $20 higher, and we will not experience any risk.

How to Manage Risk When Using a Jade Lizard Options Strategy

If INTC does move higher and through our bear call spread, even though we have no risk to the upside, we can roll up our put strike and bring in additional premium, thereby giving us a greater return on the trade.

If INTC pushes lower, we can roll down the bear call spread to bring in more premium.

Worst case, scenario is that we can allow ourselves to be put INTC stock, in this case for 52.5, or simply close out the trade. Just remember, we have brought in $2.01 worth of premium, so our downside risk is 50.49 (52.5 put strike – $2.01 premium).

I manage winning trades by taking off the trade when I can take off 50% to 75% of the premium that I brought in. In our example that would be $1.00 to $1.50.

Trade Summary for Intel (INTC)

Directional Assumption is neutral to bullish.

- Trade Setup: Sell OTM put
- Sell OTM bear call spread (short call vertical)
- Trade: Sell to open 52.5 put for $1.56
  - Sell to open 57.5/59.5 bear call spread for $0.45
- Total credit or premium = $2.01
- Max Profit: Credit received from trade or $201. Max profit occurs when the stock, in this case INTC, closes between the short put strike and short call strike at options expiration.
- Breakeven: strike price of short put – premium or credit received (52.5 – $2.01) = 50.49
- No risk to the upside.

The jade lizard is a great alternative to an iron condor, or if you’ve sold puts and would like to add a risk-defined strategy to create more income on your current position. It’s certainly a worthwhile strategy to add to your options strategy toolbelt.
Frequently Asked Questions

Can you recommend options brokers?

I use Tastyworks and ThinkorSwim, although you will find that there is a plethora of good brokers out there that offer excellent platforms, I have found these to be the best in the business. That said, I have no additional relationship with them, nor is this an endorsement. Whatever broker you choose, make sure you are paying a competitive rate on commissions. You also want a broker that offers a good trading platform and the ability to speak with someone on the trading desk. All of this will be helpful in your future trading endeavors.

How much capital should I start with?

The beautiful thing about options is it doesn't take much capital to gain large market leverage. You certainly don't need more than $500 to put on many of the trades I suggest, though many of my readers trade much higher amounts.

I missed your recommended price. Should I trade at the current price?

With each trade recommendation, I lay out my strategy of choice and the mechanics behind it. It’s then up to you to decide if it’s a good enough idea for you to make the trade. And if you like the trade, you need to decide how much capital to allocate to the trade, and at what price, based on your feel for the market and your investment goals.

As always, there will be trades where you get a better price and some where the price isn't as good as stated in the alert. That is the nature of trading. Ultimately, it is up to you to decide what price you are willing to take. This is something that we will go over each month in our live webinar.

How much should I allocate to each trade?

This is an incredibly important question and one that I must take some time to answer. Please don’t take position size lightly if you plan on being a successful trader over the long term.

It doesn't matter if you are just starting or have an advanced grasp of all things options, if you don’t think of yourself as a risk manager first, you will fail, it's just a matter of time.

Proper risk management is what separates those that succeed from those that continually struggle or simply just give up.

What people continue to struggle with is trying to find the latest and greatest strategy, constantly hopping from one strategy to the next. Strategy is far less important than proper risk management.

Placing trades, well, it's the easiest part of the trading process. Anyone can place a trade. It's how you handle the trade that allows you to be profitable over the long term.

Which is why you MUST think of yourself as a risk manager first, especially if you are taking a truly quant-based approach. The law of large numbers is your foundation but managing sequence risk is the obstacle that most traders just can’t overcome.

Sequence risk is the inherent risk that a trader could suffer multiple losses in a row. The best way to combat sequence risk is through proper position sizing. Position sizing mitigates the impact of consecutive losses. The lower the capital risked per trade, the lower the probability that a sequence of losing trades will cause a significant drawdown.
The table below shows how sequence risk can impact your overall account and why it is imperative that you use proper position size when investing/trading.

<table>
<thead>
<tr>
<th>Probability of Success</th>
<th>Consecutive Losses</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>50%</td>
<td>1:2</td>
<td>1:4</td>
<td>1:32</td>
<td>1:1024</td>
<td>1:10.4M</td>
<td></td>
</tr>
<tr>
<td>60%</td>
<td>1:3</td>
<td>1:7</td>
<td>1:98</td>
<td>1:9537</td>
<td>90.9M</td>
<td></td>
</tr>
<tr>
<td>70%</td>
<td>1:4</td>
<td>1:11</td>
<td>1:412</td>
<td>1:169350</td>
<td>1:28T</td>
<td></td>
</tr>
<tr>
<td>80%</td>
<td>1:5</td>
<td>1:25</td>
<td>1:3125</td>
<td>1:9.7M</td>
<td>1:100T</td>
<td></td>
</tr>
<tr>
<td>90%</td>
<td>1:10</td>
<td>1:100</td>
<td>1:10000</td>
<td>1:10T</td>
<td>T X T</td>
<td></td>
</tr>
</tbody>
</table>

Again, we know losing trades are going to occur. It’s a hard fact that we must accept. So, trades must be managed appropriately. And the first step is proper position size.

The most important decision you will make as a successful options trader is how much to allocate per trade. From a risk-management standpoint, maintaining a consistent position size among your trades is of the utmost importance. We want to limit the havoc that one trade could have on our portfolio.

For simplicity’s sake, let’s say our trading account stands at $10,000 in this example.

In one case, we have allocated 50% per trade. In the other, we have allocated 5% per trade.

**$10,000 Account (50% allocated per trade):**

One position, equally weighted at $5,000. So, with each trade, a 10% drop will cause a 5% drop in our overall portfolio. A 20% drop will cause a 10% drop, 30% would be 15% . . . you get the picture.

Just knowing this gives every options trader the insight necessary to shape a position size and stop-loss strategy for maximum effectiveness.

Let’s say with each trade we set our stop-loss order at 50% of our allocated amount. For example, with 50% allocated to each trade, our stop loss would be set at $2,500.

This would only allow us to diversify among two positions with 50% of our overall portfolio value at risk.
$10,000 Account (5% allocated per trade):

One position, equally weighted at $500. So, with each trade, a 10% drop will cause a 0.5% drop in our overall portfolio. A 20% drop will cause a 1% drop, 30% would be 1.5% . . . again, you get the picture.

Our stop-loss with 5% allocated per trade is $250.

For example, if we had four iron condor trades open simultaneously, we would have $2,000 in play with only $1,000 or 10% of our overall portfolio at risk.

**Worst-Case Scenario**

If we assume our position size of $500 per trade and had four trades going at one time, our maximum loss is 10% or $1,000 of our overall portfolio (barring a catastrophic gap up or down that bypasses stop-loss levels).

A 10% loss in the portfolio would need an 11.11% overall gain to make up for the loss.

**Summary**

I realize the prior exercise is fairly simplistic. Again, it only begins the important discussion of risk management. Without some form of risk management, emotions take over.

And emotions are the enemy. Hindsight never exists in the present. We must realize that we will be wrong on occasion.

Being privy to this allows us to prepare accordingly. We know over the long term that having a defined stop-loss will only serve to benefit the performance of our respective portfolios. More importantly, we always know when to sell. Of course, all of the above assumes that we prefer the straight percentage stop-loss.

If you want to be a successful trader/investor over the long term, then taking the time to figure out an appropriate position-sizing plan is imperative. Please, please, please do not overlook this important concept.

You will not regret it.
Options jargon and terminology can sometimes sound like a foreign language. Here are a few terms that are commonly used in the investment methods discussed in *Cabot Options Institute Income Trader*.

**Call Option**

A call option gives its holder the right to buy 100 shares of the underlying security at the strike price, any time prior to the option’s expiration date. The seller of the option has the obligation to sell the shares.

**Exercise**

Exercise is the process by which an option holder invokes the terms of the option contract. If exercising a call, the holder will buy the underlying stock, while the put owner will sell the stock under the terms set by the option contract. All option contracts that are in-the-money by at least one cent at expiration will be automatically exercised.

**Expected Move or Expected Range**

The expected move, otherwise known as the expected range, is the amount a stock is predicted to advance or decline from its current share price, based on the security’s current level of implied volatility and days to expiration. Additionally, the expected move fluctuates, in real time, based on changes in a security’s price and its implied volatility.

Simply stated, the expected move shows us the future expected range of a security over a specific time frame.

**Expiration Date**

The expiration date is the last day an option exists. Monthly options cease trading on the third Friday of each month and expire the next day. Weekly options cease trading on the Friday of the week they are due to expire.

**IV Percentile**

IV Percentile tells us the percentage of days that implied volatility (IV) has been below the current level of IV over the past 12 months. IV percentile is a ranking system from 0-100. For example, if a stock has a current IV percentile of 80%, it simply means that the current level of IV is higher than 80% of all IV readings over the past 12 months.

**IV Rank**

IV Rank tells us if current implied volatility (IV) is considered high or low on an underlying security in comparison to all other IV readings over the past 12 months. IV rank is calculated by taking the highest IV reading and lowest IV reading over the past 12 months.

**Law of Large Numbers**

The foundation of all quantitative or statistically-based options traders rests on one statistical law – The Law of Large Numbers. The Law of Large Numbers states that as you increase your sample size, in our case number of trades, our expected value or probability of success will come to fruition. This is because the Central Limit Theorem shows us that actual values will converge on expected values. But, in order for the Central Limit Theorem to work, we need a large enough sample size or number of observations—in our case, trades. This is where the Law of Large Numbers comes in.
Option

An option is a contract that conveys to its holder the right, but not the obligation, to buy (in the case of a call) or sell (in the case of a put) shares of the underlying security at a specified price (the strike price) on or before a given date (expiration day). After this given date, the option ceases to exist. Equity option contracts usually represent 100 shares of the underlying stock.

Options Premium

An options price is called the “premium.” The potential loss for the holder of an option is limited to the initial premium paid for the contract. On the other hand, the seller of the option has unlimited potential loss that is somewhat offset by the initial premium received for the contract.

Put Option

A put option gives its holder the right to sell 100 shares of the underlying security at the strike price, at any time prior to the option's expiration date. The seller of the option has the obligation to buy the shares.

Strike Prices

Strike Prices (or exercise prices) are the stated price per share for which the underlying security may be purchased (in the case of a call) or sold (in the case of a put) by the option holder upon exercise of the option contract.

Time Decay

All options are a wasting asset whose time value erodes to zero by expiration. This erosion is known as time decay. Generally, the longer the time remaining until an option's expiration, the higher the premium will be. This is because the longer an option's lifetime, the greater the possibility that the underlying share price might move so as to make the option in-the-money. This time decay increases rapidly in the last several weeks of an option's life as the likelihood of it finishing in the money declines.
Andy Crowder is a professional options trader, researcher and chief options strategist of Cabot Options Institute Income Trader. Formerly with Oppenheimer & Co. in New York, Andy has leveraged his investment experience to develop his statistically based options trading strategy which applies probability theory to option valuations in order to execute risk-controlled trades.

His proprietary strategies have been refined through two decades of research and real-world experience and has been featured in the Wall Street Journal, Seeking Alpha, and numerous other financial publications.

As a professional options trader, Andy has helped thousands of option traders learn and implement his meticulous rules-driven options trading strategies through highly attended conferences, one-on-one coaching, webinars, and his work as a financial columnist.

He currently resides in Bolton Valley, Vermont and when he’s not trading, teaching and writing about options, he enjoys spending time with his wife and two daughters, backcountry skiing, biking, running and enjoying all things outdoors.
About Cabot Wealth Network

Cabot Wealth Network, established in 1970, is a trusted independent source of advice for individuals striving to take control of their investments and find the best stocks. Its investment advisory services deliver high-quality advice to more than 200,000 individual investors and investment professionals in 141 countries. Headquartered in historic Salem, Mass., Cabot Wealth employees take great pride in providing intelligent investment advice and timely, personal service without the hype and fabricated claims. Cabot is a member of the American Association of Individual Investors, Better Business Bureau, Specialized Information Publishers Association, and the Salem Chamber of Commerce.