

Options Trading



8 Important Tips for Successfully Trading Options

DON'T DO THIS

It sounds simple and you've certainly heard it before but, "Do not trade stocks or options with money that's needed for other necessities or you cannot afford to lose." It's not my rule, but it does make a lot of sense. There is more than enough pressure in options trading without making it harder on yourself. It reduces your chances of trading successfully and clouds your judgment. Although I tend to be more of a risk taker than most of our Options Newsletter Subscribers, in every possible way, be sure to follow this rule.

As the saying goes, "The market hurts as many people as it can, as often as it can."

PROTECT YOUR WEALTH

"Insure your positions from loss." Buying put options on stocks that you already own or stocks in the same sector provides your portfolio with very inexpensive insurance while maintaining your upside potential. Buying cheap "out-of-the-money" puts gives you a safety net for a very nominal price (and you'll sleep like a baby). You'll find that, more times than not, both positions eventually become profitable. In institutional circles it's called "hedging."

EXERCISE YOUR RIGHTS

Buy call options to initiate a long position. By buying "near-the-money" calls on stocks you believe are undervalued, you can participate in the upside movement of the stock price. You can also sell the option contract at any time for a profit. Options give you the ability to apply "leverage" to your investing while completely limiting any possible loss to the amount paid for the option itself. If the stock price drops, the most you can lose is the amount you paid for option, nothing more.

DO IT THE RIGHT WAY

Choose options that are undervalued, underpriced and trading "close-to-the-money" (the stock price is trading close to the options strike price).

Look for as much time as possible (determined by the option pricing) before option expiration date in buying both puts and calls.

TESTING THE LIMITS

A limit order requires that you get the exact price you want to pay or the trade won't be made. Initially, when buying options with "limit orders" it might take a few tries getting an order filled at the price you want to pay, but it is worth it. Try setting a limit order at a price between the "bid" and the "ask" price. Knowing that most stock prices fluctuate even during the course of a day, this will help you get filled at a better price, get filled more often and save you a good amount of money over time.

LAST EXIT BEFORE TOLL

Sometimes it makes sense to exit a trade that's not going your way. Setting "sell stops" is a personal decision and it's one that every trader wrestles with. There have been volumes written on sound money management and in the next section I will be covering the subject in much more depth. Most traders set between 10% & 50% down in value as a loss limit. The reasoning is that once a trade has lost 50% of it's value, rarely will you see it make a full recovery, much less become profitable... better to cut you loss and look for a spot to get the strength out of your money. Options are a cash business (yes it's a business) and you have a limited amount of time to either win or lose. The more a trade goes against you the less money you have in your account that's available for the next trading opportunity.

WHAT'S MY OPTIONS?

You need to know where to find stock/option buying opportunities with a 3-1 risk/reward potential. This is a quite normal risk to profit ratio to look for when trading options. To do this, it's advisable to find one or two good stock/options advisory newsletters with a good track record such as our "Hyland Option Traders" service. In doing this you can take advantage of extensive stock research and concentrate on managing your trades and your money properly. It is not necessary or advised that you spend every spare minute researching individual stocks in the hopes of uncovering a

gem when when you can have a professional lead you in the right direction. I'm assuming you became interested in options trading to make more money so you can have more free time... not to take on another 20-30 hour a week part time job researching potential trades. It can be very time consuming.

TAKE THE LEAP

"Leaps" options is one of the most important tools that can tilt the odds of winning in your favor. Leaps stand for "Long-Term Equity Appreciation Securities". When you combine undervalued stocks with Leaps options your chances for profit are greatly increased. The value of this tool is that their option expiration dates are 1-2 years in length with all the leverage of regular option contracts. Leaps are such a valuable weapon in the options trader's arsenal that I am including an entire section on their use in the coming Option Trader's Classes.