8. Option Strategies.

Today we will be discussing option strategies which are nothing but the simultaneous, and often mixed, buying or selling of one or more options that differ in one or more of the options' variables such as moneyness, expiration and strike price. This is often done to gain exposure to a specific type of opportunity or risk while eliminating other risks as part of a trading strategy. A very straight forward strategy might simply be the buying or selling of a single option, however option strategies often refer to a combination of simultaneous buying and or selling of options. Options strategies allow to profit from movements in the underlying that are bullish, bearish or neutral. The option positions used can be long or short positions in calls and Puts.

1. Bullish strategies:

Bullish options strategies are employed when the options trader expects the underlying stock price to move upwards. The trader can also just assess how high the stock price can go and the time frame in which the rally will occur in order to select the optimum trading strategy for just buying a bullish option.

The most bullish of options trading strategies is the simply buying a call option used by most options traders. There is limited risk when trading options when using the appropriate strategy. While maximum profit is capped for some of these strategies, they usually cost less to employ for a given nominal amount of exposure. There are options that have unlimited potential to the up or down side with limited risk if done correctly. The bull call spread and the bull put spread are common examples of moderately bullish strategies which we will discuss in coming chapters.

2. Bearish strategies:

Bearish options strategies are employed when the options trader expects the underlying stock price to move downwards. It is necessary to assess how low the stock price can go and the time frame in which the decline will happen in order to select the optimum trading strategy. The most bearish of options trading strategies is the simple put buying or selling strategy utilized by most options traders.

Stock can make steep downward moves. Moderately bearish options traders usually set a target price for the expected decline and utilize bear spreads to reduce cost. This strategy can have unlimited amount of profit and limited risk when down correctly.

3. Neutral strategies:

Neutral strategies in options trading are employed when the options trader does not know whether the underlying stock price will rise or fall. Also known as non-directional strategies, they are so named because the potential to profit does not depend on whether the underlying stock price will go upwards. Rather, the correct neutral strategy to employ depends on the expected volatility of the underlying stock price.

Option Strategy Profit or Loss Chart:

A typical option strategy involves the purchase selling of at least 2-3 different options with different strikes and or time to expiry and the value of such portfolio may change in a very complex way. Therefore to analyze and understand the behavior of a certain option strategy is by drawing its Profit or Loss graph.

In upcoming chapters we will be discussing these strategies in more details. For any queries related in today topic kindly contact us on knowledge@grovalue.in