

The 10-Step **OPTIONS TRADING CHECKLIST** EVERY TRADER NEEDS

OPTIONS

TRADING

1.

2.

3.

JAY SOLOFF

Options Trading Checklist

- ✓ **1.) TRADING PLAN:** First and foremost, you must have a trading plan. Know when you want to exit your trade based on gains, losses, underlying asset targets, timeframe, etc. For instance, is your goal to make 30% returns on a trade? Or, are you waiting for the underlying stock to hit a certain level?

Jay's Commentary: Despite seeming to be a very basic concept, the trading plan is probably the most important part of trading options (or trading any asset for that matter). Too many times traders lose money because they enter a trade without a plan. I'm guilty of this as well. Your trading plan isn't always going to maximize your returns, but done properly, it will reduce risk. Remember, the most important thing is being able to trade another day. There are plenty of resources out there to help you develop a trading plan and I highly recommend you check them out before you start trading regularly.

- ✓ **2.) NEWS:** Check the underlying asset for any news. You don't want to get into a new options trade just to realize the fundamentals have shifted. It's okay if there's something minor which comes out. However, if the company preannounces worse than expected earnings, you definitely want to reconsider.

Time	Title (Click for story)
13:45:51	S&P, Nasdaq Close at Record Highs, Boosted by Strong Earnings Reports
13:00:00	U.S. Day Ahead: How grounding of Boeing's 737 MAX jets is affecting company
10:38:21	Toronto Dominion Bank, Microsoft Strike Digital Transformation Deal
10:08:23	Clouds Part: Amazon And Microsoft Cloud Businesses In Focus Ahead Of Earnings
09:14:00	*MW Microsoft's stock surges 1.0% toward record close, and 8th gain in 9 sessions
08:37:00	MW Melinda Gates: Being married to Bill Gates is 'incredibly hard' sometimes
07:30:00	UK Day Ahead: FTSE hits 6-month high; Sterling drops as Brexit pressure builds on May
06:02:24	Sector Update: Most Top Tech Stocks Advance Pre-Market Tuesday

Jay's Commentary: You don't necessarily have to go through every headline in a given day with a fine-toothed comb. However, you should definitely make sure your trade thesis is still intact. If there's a big news item, at least take the time to scan it for anything which may change your mind on the trade.

- ✓ **3.) SANITY CHECK:** Before pulling the trigger, make sure you are comfortable with the trade. Will you be able to sleep at night knowing the trade is on? If your answer is no, you need to rethink the trade. You'll only succeed as a trader in the long-term if you enjoy what you're doing – and that requires a certain comfort level with all your trades.

Jay's Commentary: Every trader has a different DNA. Some traders are only comfortable buying options. Other traders may prefer to only trade covered calls. There are many ways to trade and many paths to success. The key is finding out what kind of trader you are and what you are comfortable doing over the long-run.

- ✓ **4.) EXPIRATION:** Decide how long you want to give this trade. In other words, pick your option expiration month – will it be weeks or months until it expires? Options with longer expirations will cost more money but will give your trade thesis more time to work out. You need to decide if you're willing to pay more for more time.

Expiration ?

Apr 18 '19

- Apr 18 '19
- May 17 '19
- Aug 16 '19
- Nov 15 '19

Jay's Commentary: This is one of the hardest decisions for an options trader to make. How much time do you want to purchase if you're buying options? Often times the answer depends on your trade thesis. Is this trade a play on earnings? In that case you may just stick to the period that covers the earnings release. Is the timing of your trade thesis uncertain? In that situation, it's probably worth it to pay up for time.

- ✓ **5.) CALL OR PUT:** With any options trade, you must choose your option type. Is it a call (makes money if the underlying asset goes up) or put (makes money if the underlying asset goes down)? Sometimes call and put prices can be similar so make sure you are picking the right one!

CALLS			JUN 21 '19							PUTS		
Open Interest	Volume	Net Change	Last	Bid	Ask	Strike Price	Bid	Ask	Last	Net Change	Volume	Open Interest
88,475	6,621	1.61	7.61	7.59	7.66	290.00	3.92	3.94	3.98	-0.97	14,852	30,207
24,618	5,878	1.61	6.86	6.85	6.94	291.00	4.21	4.24	4.27	-1.08	2,629	5,851
25,188	5,365	1.52	6.16	6.17	6.21	292.00	4.55	4.58	4.60	-1.16	4,585	9,199
23,956	7,974	1.35	5.41	5.50	5.53	293.00	4.92	4.95	5.00	-1.28	8,638	1,625
16,503	2,214	1.05	4.68	4.86	4.91	294.00	5.33	5.36	5.35	-1.44	3,020	2,715
49,890	14,699	1.13	4.27	4.28	4.32	295.00	5.78	5.81	5.85	-1.47	1,180	4,117
13,152	1,512	0.99	3.61	3.73	3.76	296.00	6.25	6.33	6.32	-1.82	1,353	751

Jay's Commentary: One interesting thing about calls and puts is they typically aren't priced equally based on how far they are from the current stock price. For instance, a call that's 5% higher than the stock price is almost always going to be cheaper than a put that's 5% lower. Why? It's because puts are used for hedging (protecting) stock positions so are in demand more than calls. This is particularly true in index (or ETF) options. It's such a common situation in options chains (the list of options by strike, which you see in the screenshot) that we have a name for it – options skew.

- ✓ **6.) BUY OR SELL:** Once you pick call or put, you have to decide if you're buying or selling. Most new traders will be focused on buying options to start. You'll only be selling to close the position. Make sure to double-check buy versus sell before you send your order in! Keep in mind, when you buy an option, the only risk you have is the money you spend on purchasing your call or put.

Jay's Commentary: When you buy options you're making a debit trade. Selling options results in a credit trade. Credit trades are generally for more experienced traders as they require a margin account to trade. As a general rule of thumb, debit trades are low probability trades with high returns, while credit trades have a high probability of success but low returns. I always recommend buying options to start with, as it's a really good way to learn how options work without taking big risks. For those interested in trading options for credit, the best way to start is with covered calls, as it is also a very low risk strategy (but requires a fair amount of trading capital).

- ✓ **7.) STRIKE:** The next step is to pick the strike price. If the strike is the same or very close to the underlying asset price, it's considered at-the-money. A call strike that's higher than the asset price or a put strike that's lower than the price are both considered out-of-the-money. You'll mostly likely be trading at-the-money or out-of-the-money options in most circumstances.

Calls		↑	Puts	
Bid	Ask		Bid	Ask
3.40 x35	3.45 x7	114.00	0.34 x82	0.36 x326
2.58 x65	2.62 x5	115.00	0.52 x16	0.54 x89
1.84 x126	1.89 x25	116.00	0.78 x95	0.80 x42
1.23 x394	1.27 x25	117.00	1.16 x134	1.20 x55
0.76 x455	0.80 x189	118.00	1.68 x149	1.73 x39
0.44 x171	0.47 x96	119.00	2.35 x78	2.41 x43

Jay's Commentary: Think of the strike price as a probability scenario. The closer the strike is to the current stock price, the higher probability it will end up in-the-money, but the more you'll pay for the option. There isn't a right way to pick a strike. It completely depends on how much you are willing to spend and how far you think a stock is going to move. One tip that I give every new options trader: don't buy options too far out-of-the-money.

If you are purchasing an option for 5 or 10 cents then the strike price is too far away and you are essentially wasting money. In most cases you want to be looking for at least \$0.25-\$0.50 options for the strike to be worthwhile.

Note: This may not be true for very high priced or very volatile stocks. In that case you usually have to pay up for any reasonable strike. For new traders, try to avoid these types of stocks to start with.

- ✓ **8.) QUANTITY:** Next, pick the number of contracts (options) you want to trade. Be sure you don't have extra zeros on your quantity! It's generally a good idea to start small (1 contract) if you are new to options trading. Remember, you'll be multiplying quantity by price to figure out how much you'll spending when buying options.

Action: Buy Open | Quantity: 3 | Expiration: Apr 18 '19 | Strike: 100 | Type: Call

Jay's Commentary: I can't tell you how many times someone has told me they accidentally traded 10 contacts instead of 1, or even 100 contracts instead of 10. It's much easier than you may suspect to hit that extra zero when entering quantity. I've done it myself. Also, don't try to do too many contacts to begin with as a new options trader. Start small and slowly raise your volume up over time. To this day, I rarely trade more than a 5-lot on any trade I make - unless I really like the trade.

- ✓ **9.) PREMIUM:** Pick your premium (price). I recommend starting at the midpoint between the bid and ask and moving up (or down) from there. And don't forget to use a limit order – just like with stocks, market orders with options can result in undesirable results. With options, one cent is equal to \$1, so a \$0.50 option will cost you \$50 for each contract you purchase.

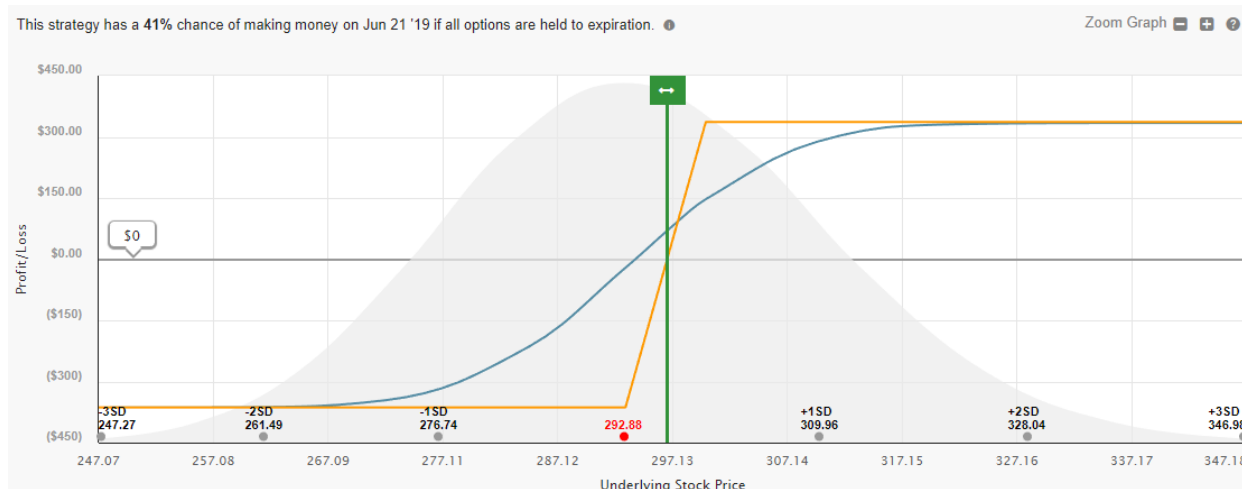
Action: Buy Open | Quantity: 3 | Expiration: Apr 18 '19 | Strike: 120 | Type: Call | Bid x Size: 1.30 x 24 | Ask x Size: 1.33 x 97 | Last: 1.30

Price Type: Limit | Limit Price: 1.32

Jay's Commentary: I usually don't spend more than \$2.00 per option (\$200 in dollar terms) when buying options. More often than not, that number is closer to \$1.00. As I mentioned in the strike price commentary above, I don't go below \$0.25 - \$0.50 for an option in the vast majority of circumstances.

If an option is not in-the-money, the premium will diminish over time in a process options traders call time decay. Keep that in mind when buying options. If you are purchasing an out-of-the-money options for \$200 per option, that's a lot of time decay. Try to keep your costs low whenever possible, but at the same time, don't go overly cheap either.

- ✓ **10.) REVIEW:** After you get your fill confirmed, double-check everything to make sure you got your option type, quantity, strike, and price the way you expected it to be. If there's a mistake, you want to catch it right away so you can reverse out of it and get back into the proper trade. It's always a good idea to be as accurate as possible when trading options.



Jay's Commentary: The graph above is an example of a Profit/Loss graph. Just about any options broker should provide this feature on their trading platform. Make sure you understand your profit/loss potential before making a trade. And then, before you hit "send", look at the P/L graph and make sure the trade is offering what you think it should be offering in terms of risk versus reward.