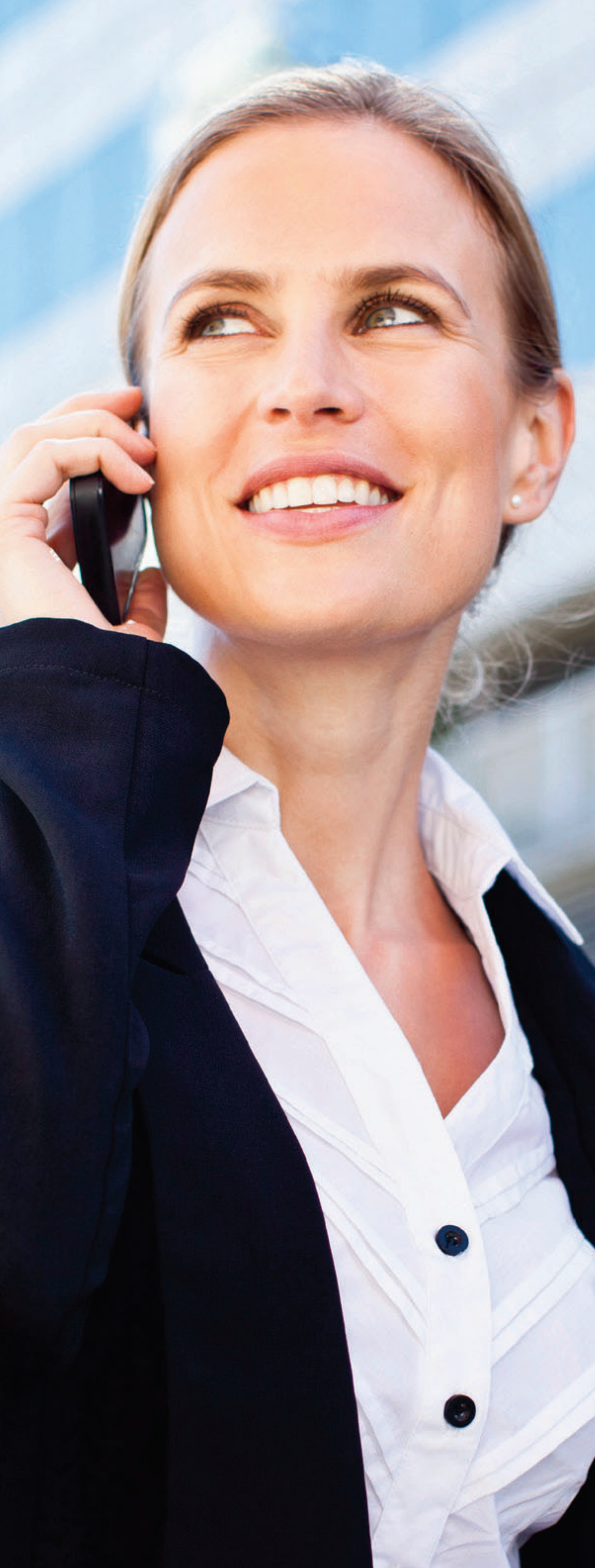


OBJECTIVE: ACQUIRING STOCK BELOW TODAY'S MARKET VALUE BY SELLING A SECURED PUT OPTION

# How one investor received a premium while willingly obligating herself to acquire stock at a lower price than current market value at a future date.

Michelle was interested in buying stock in a company that, according to the research she received from her financial advisor, could dip in value in the near future but had the potential to increase longer-term. Because the current stock price was higher than Michelle had hoped to pay, she decided to explore options as a way to potentially acquire stock at a discount to today's current price.

Her advisor told her about a stock alternative options strategy called a secured put. Rather than buying the stock at its full market value today, selling a secured put option would allow Michelle to receive a premium while she waited for the stock to potentially fall to a more attractive price level.

So Michelle sold a put with an expiration approximately two months in the future at a strike price a few dollars below the stock's current price. She received a premium and set aside adequate funds in her brokerage account to fulfill her obligation to buy the stock at the strike price if the put were to be assigned on or before expiration. On the other hand, if the stock remained at or above its current value, the contract would expire worthless and Michelle would keep the premium and would not be obligated to buy any shares. If the value of the stock did fall, she would be obligated to buy stock at the strike price using the funds set aside when she originally secured the contract, including the premium she received. In either case, Michelle would keep the premium she received from taking on the obligation to acquire stock. If Michelle's put were assigned and her outlook for the stock held true, she would have been able to receive a premium and buy a stock that she was already interested in purchasing for a lower price than where it was trading when she initiated the contract.

> "In this example, Michelle's patience paid off when the stock's value dipped, triggering her obligation to purchase stock at the desired price along with receiving the premium associated with selling the put.*"

*This is a hypothetical illustration and is not intended to reflect any actual outcome. Please review the "How it Works" section of this brochure for other possible outcomes when using this strategy.

RAYMOND JAMES

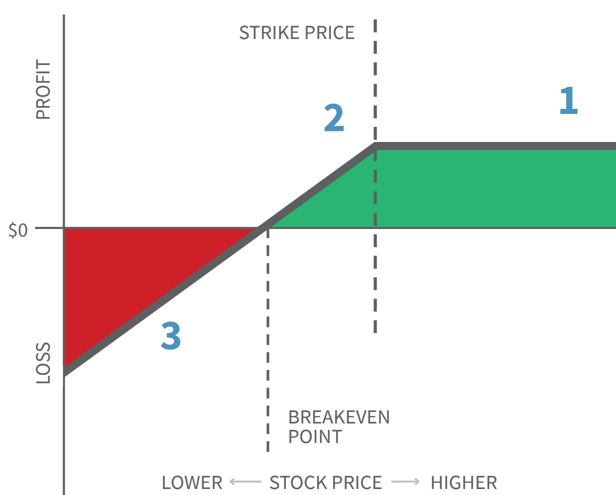
# Obligating yourself to potentially acquire stock at a reduced price while receiving a premium

Selling a secured put option gives you the ability to receive a premium and potentially take advantage of a stock's decline by purchasing shares at a future date at a cost lower than the current market price.

This option contract gives the holder (buyer) the right – but not the obligation – to sell underlying stock to the writer (seller) at a designated strike price any time between the date of sale and expiration date of a put contract. This moderately bullish strategy is best for investors who are price-sensitive and have a positive long-term outlook on a specific stock.

The transaction begins when an investor sells to open a put contract, or writes a put, and receives a premium. At the same time, the investor sets aside adequate funds to purchase the equivalent amount of stock at the strike price for a later date. If the stock price falls below the strike price and the written put contract is assigned, the effective purchase price would amount to the strike price minus the premium received from originally selling the put. For example, if a stock is currently trading at $52.00 and a put writer sells one (1) $50 strike put contract for $1.00, the put writer would collect $100.00 today. Simultaneously, he or she would be taking on an obligation to buy 100 shares at the strike price of $50.00. The options put writer would secure the put by setting aside $5,000.00 in his or her brokerage account. If the price of the stock dips below the strike price and the option put holder exercises his or her right to sell, the put writer is obligated to buy at the strike price. In this example, instead of buying a stock today at $52.00, why not receive $1.00 in premium and be a willing buyer of stock at $50.00 between now and expiration? After receiving $1.00, the net cost, if assigned, would actually be $49.00.

PROFIT AND LOSS FOR SELLING A SECURED PUT




NOTE: Commissions, fees and taxes have not been included in this example. These costs will impact the outcome of all stock and options transactions and must be considered prior to entering into any transactions.

Not approved for rollover solicitations. Not all products and types of accounts are appropriate for all investors. Please discuss your individual situation and goals with your financial professional.

We recommend selling secured puts in an attempt to potentially benefit from the downward movement of an underlying stock. An investor will want to sell a contract at a strike price that is "out of the money," meaning below the current stock price. Selling a secured put includes limited (or defined) risk as a stock's value could always plummet to zero, but an investor understands this defined risk and believes the reward of buying at an affordable price outweighs that risk.

## HOW IT WORKS

With a secured put option, there are three potential outcomes:

**1** The stock stays above the strike price. In this scenario, the holder of the put would not exercise his or her right and would let the option contract expire worthless. If the put is not assigned, the writer of the put would keep the premium received and would not be obligated to purchase stock.

**2** The stock falls below the strike price. In this case, a put holder would typically exercise the put, and the put writer would be obligated to purchase stock at the strike price minus the premium previously received.

**3** The stock falls to zero. A put writer should be comfortable with the strike price as an acceptable long-term acquisition price. If a stock were to plummet, a put writer could buy to close the short option position, realizing – but potentially limiting – his or her losses. Remember, if the put writer takes no action, the option position is assigned, obligating the purchase of stock at the strike price. Therefore, if the worst-case scenario were to transpire, the maximum loss would occur when the put writer is assigned, obligating the purchase of a worthless stock at the strike price.

## Talk to your advisor about secured put options

Selling a secured put option is a way to potentially acquire stock below current market value with the benefit of receiving a premium. Talk to your Raymond James advisor today to see whether your portfolio could potentially benefit from this stock alternative options strategy.

## IMPORTANT SECURED PUT OPTION DEFINITIONS

**Ask** – The disseminated price at which exchanges indicate options can be bought.

**American-style** – An option that can be exercised/assigned at any point before expiration. Equity options are American-style.

**Assignment** – Writers of American-style put options can be assigned at any time. Upon assignment they deliver cash to the option holder and must receive the underlying securities.

**Bid** – The disseminated price at which exchanges indicate options can be sold.

**Breakeven point** – The put strike price minus the premium collected from selling the equity option.

**Decay** – A term used to describe how the theoretical value of an option erodes or declines with the passage of time. Time decay is specifically quantified by theta.

**Delta** – A measure of the rate of change in an option's theoretical value for a one-unit change in the price of the underlying stock.

**Exercise** – To invoke the rights granted to the owner of an option contract. In the case of a long put, the option owner sells the underlying stock.

**Holder** – Any person who has made an opening put purchase transaction and has a long position in their brokerage account.

**In the money / In-the-money option** – A term used to describe an option with intrinsic value. For standard options, a put option is in the money if the stock price is below the strike price.

**Intrinsic value** – The in-the-money portion of an option's premium.

**Options contract** – One options contract typically represents 100 shares of stock.

**Premium** – The price you pay if you're an option buyer, or the amount you receive if you're an option writer.

**Put option** – An option contract that gives the owner the right but not the obligation to sell the underlying security at a specified price (its strike price) for a certain, fixed period (until its expiration). For the writer of a put option, the contract represents an obligation to buy the underlying product if the option is assigned.

**Secured put** – An option strategy in which a put option is written against a sufficient reserve to purchase stock if the short option is assigned.

**Short put option position** – The position of an option seller (writer) that represents the obligation to buy stock (in the case of a put) at a specified price (strike price) at or before some date in the future (the expiration date). This position results from an opening sell transaction (short put).

**Strike** – The price at which stock is traded upon exercise/assignment of an option contract. Some options have multiple underlying stocks. In these cases, the strike times the multiplier is the total price paid for all of the option's underlying securities.

**Theta** – A measure of the rate of change in an option's theoretical value for a one-unit change in time to the option's expiration date.

**Time decay** – The decline in value of your option as the expiration date approaches.

**Time value** – The perceived and often changing value of the time left until an option's expiration.

**Underlying** – The cash or securities that are delivered upon exercising an option. Most options deliver 100 shares of a single stock.

**Writer** – Any person who has made an opening put sell transaction and has a short position in their brokerage account.

**Options involve unique risks, tax consequences and commission charges and are not suitable for all investors. When appropriate, options should comprise a modest portion of an investor's portfolio.** No statement within this document should be construed as a recommendation to buy or sell a security or to provide investment advice. Prior to making any options transactions, investors must receive a copy of the Options Disclosure Document which may be obtained from your financial advisor. Supporting documentation will be supplied upon request.

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