

Stock Investor Pro SIG

Baskets of Stocks, ETFs, and
Options
July 21, 2009

Agenda for 7/21/09

- Baskets of stocks
- ETF screen
- Market Leaders screen
- What are options
- Why use options

Baskets of Stocks

- Baskets of stocks are collections of stocks grouped for a purpose
- Common types of groupings:
 - Size – e.g., S&P 500, 400 and 600
 - Exchange based – e.g., NASDAQ 100
 - Sector/Industry based – e.g., Financials
- Exchange Traded Funds (ETFs) are financial instruments that represent baskets of stocks
- Investors can use ETFs to buy a basket of stocks

SI Pro screen for ETFs

- In SI Pro, ETFs are identified as members of the Misc Financial Services industry
- In the screen editor, create a new screen where Industry – Equals – Misc Financial Services
- The database uses the Standard Industrial Classification (SIC). ETFs belong to 6799.
- The results include more than ETFs
- Save screen as ETFs

Market Leaders

- A basket of stocks created by James P. O'Shaughnessy in "What Works on Wall Street"
- Outperforms All Stock and Large Cap "baskets" over time
- Screen is created in SI Pro from the O'Shaughnessy Value screen by eliminating the Yield requirement.
- Save screen as Market Leaders

What are options

- An option is a contract giving the buyer the right, but not the obligation, to buy (call) or sell (put) an underlying asset.
- An option is a security, just like a stock or bond, and constitutes a binding contract with strictly defined terms and properties.
- For online tutorials see The Options Institute by the Chicago Board Options Exchange at <http://www.cboe.com/LearnCenter/Tutorials.aspx>

Why Use Options

- Buy options (puts) to decrease the risk of stock ownership much like an insurance policy.
- Sell options (puts or calls) to enhance portfolio income
- Buy options to control a large block of stock without having to own it.
 - Buy calls rather than go long
 - Buy puts rather than go short

Option Gotchas

- Only the risk portion of the trade should be applied to options
- Being naked can be embarrassing financially
- Without liquidity, buy/sell spreads can eliminate gains. Liquidity matters.
- Understand the time value of the contract
- Remember you will need to be “more” right

Additional option info

- Online brokers have educational material – particularly if they encourage option trading (e.g., Options Express)
- Standard and Poors publishes an “Options Report” for many of the stocks it follows. Check with your broker.
- Option tables are available at online stock charting sites (e.g., stockcharts.com, bigcharts.com)
- Options websites (e.g., ShaeffersResearch)
- “google” to find some sites

Example: Buy an ETF call

- Add an "optionable" filter to the ETF screen as well as a liquidity filter.
- Pick a candidate – e.g., QQQQ
- Go online and check closing price and near-the-money August 21 calls
- Evaluate possible scenarios (assume bullish on QQQQ in near term)
- Discussion

Example: Sell a covered call

- Add an "optionable" filter to the Market Leader screen as well as a liquidity filter.
- Pick a candidate – e.g., AA
- Go online and check closing price and near-the-money August 21 calls
- Evaluate possible scenarios including being called away. Include dividend.
- Discussion

Questions & Comments
