

THE INTELLIGENT F&O TRADER

30+ Strategies with Hedging & Adjustments

VOLUME II

AMIT R CHARAN

All content in this book is entirely original and self-composed. No part of it has been generated by artificial intelligence. The material is the result of extensive personal learning, research and reflection.



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About the Author



Amit is a distinguished corporate lawyer with almost two decades of experience specializing in Banking & Finance, honed at India's top-tier law firms. He has studied Law, Business Administration and software programming.

His professional journey, marked by advising domestic and international financial institutions and private equity firms on complex debt and equity transactions, has provided him with an unparalleled understanding of various aspects of finance including capital markets. This extensive legal and financial expertise, combined with a deep-seated passion for independent research and a keen analytical mind, fuelled his in-depth study of financial instruments, trading styles, and investment concepts. It is this unique blend of a corporate lawyer's precision and a researcher's curiosity that has culminated in his authorship of this comprehensive book on Futures & Options trading, designed to bridge the gap between academic theory and practical application.

A prolific writer, Amit has also authored numerous articles on law and finance for various journals and has authored a book on Letters of Credit and

this current series of THE INTELLIGENT F&O TRADER wrapped in 3 Volumes. Beyond his legal career, Amit has embraced his entrepreneurial spirit.

As a visionary entrepreneur, Amit has founded a startup called **Aineura** where he is driving the development of a unique Generative AI-powered multilingual platform called **FnKnowBot** designed to democratize personal finance knowledge for all people globally.

FnKnowBot is accessible at <https://fnknowbot.in> and it serves as a powerful tool for learning everything about all money matters, offering a full spectrum of financial guidance of practical application in real life—from investing and trading, F&O & crypto, fundamental & technical analysis to budgeting, debt management, succession planning and financial report & chart analysis etc. Through this venture, Amit continues his mission to empower individuals with the knowledge and tools needed for financial success including and beyond capital markets.

DEDICATION

This book is lovingly dedicated to my family, whose sacrificial love and unwavering support have carried me through my every endeavour.

To my beloved wife, Sharon, and my precious daughter, Jessica—my treasures and my daily joy—your love fills my life with meaning and strength.

To my dearest mother, Elizabeth Charan, whose prayers and nurturing spirit have been my foundation, and to my late father, K. B Charan, who fought a good fight of faith and was promoted to glory to be with the Lord.

To my sister, Tehnaz, my brother-in law, Ankur and my nephew Aaron, for their love and encouragement.

Each of you is God's special gift to me, and this work is as much yours as it is mine.

This work is born from the grace of the Almighty and the cherished prayers of loved ones who have stood beside me in all seasons.

ACKNOWLEDGMENT

I extend my heartfelt thanks and deep gratitude to Mr. Nitish Kumar Singh of NK Stock Talk, from whom I have drawn valuable inspiration and profound insights into the practical aspects of F&O trading.

His rich experience of over 25 years as a successful trader and investor has illuminated significant dimensions of Futures and Options.

His vast knowledge and generous guidance to the retail trading community have been instrumental in inspiring me to author this book as a comprehensive knowledge resource for all F&O traders and enthusiasts.

DISCLAIMER

This Book on F&O Trading (the “Book”) is intended for informational and educational purposes only. The information, concepts, strategies, techniques, trading plans, graphs, charts, data, and risk management advice presented in the Book are based on the author’s personal learnings, studies, research, experiments and market experience up until a few months prior to the publishing of this Book. The author makes no representation or warranties with respect to the profitability through F&O trading basis the contents of this book. Therefore, if you wish to apply ideas and contents contained in this Book, you are taking full responsibility for your actions. You must consult with a financial advisor before making any investment / trading decisions based on the contents of the Book.

Trading in Futures and Options involves substantial risk of loss and is not suitable for all investors/ traders. Past performance is not indicative of future results. The author do not guarantee any specific outcome or profit from the use of the information contained in the Book. You should carefully consider whether F&O trading is suitable for you in light of your financial condition, risk appetite and investment / trading objectives.

The Book has been composed basis applicable market norms in F&O segment of Indian capital markets, as per the relevant date of writing the book or part of it. The specific information, data including lot sizes, expiry series, instruments etc. presented in the Book may undergo change per the actions taken by the regulator and may be applicable with relevant changes thereto. Readers are advised to seek updated information from authentic sources / stock exchanges.

The author shall in no event be held liable to any party for any direct, indirect, punitive, special, incidental or other consequential damages or indemnities arising directly or indirectly from any use of the material & contents contained in the Book, which is provided “as is”, and without warranties.

ABOUT THE BOOK

This Book on **F&O Trading** has been written with the vision of enabling F&O traders to learn the practical aspects of F&O trading in simple easy-to-understand language. The Book has been composed basis extensive learnings, research carried out and real-life F&O trade experiences of the Author.

Objective of the Book is to help shorten the learning curve of the F&O traders, which in turn would contribute in minimizing their trading losses to a great extent. We, sincerely, believe that with the learnings contained in separate Volumes, when practiced over a period of time with discipline and risk management, many serious learners would eventually evolve as a successful trader.

The Book has been divided into separate Volumes, for the sake of brevity and precision.

Volume-I:

This Volume-I caters to explain about all the basic features concerning Futures and Options as derivative instruments, from trading perspective. Volume-I also expounds on the varied behavioural aspects of Options, which is the backbone of trading in Options. Most of the learning material generally available only confines itself to the academic understanding of Greeks and other Options influencing factors, but we have endeavoured to take special care to bring forth the practical understanding about these factors and its significance with respect to its usage from trading perspective. Volume-I covers unique concepts pertaining to behavioural aspects of Options. This volume also provides detailed guidance on the procedural aspect of F&O trading by explaining different order types, which would enable the trader to effectively initiate and manage trading positions by employing relevant order types basis the action required in trading. We have also provided in Volume-I, a detailed Chapter dedicated on trading rules (*which we are calling as 'Golden Rules of Trading'*) which will be kind of a guide for the beginners to set their preparations & expectations right and also a guidance note for the practicing traders to ensure proper checks & balances while

trading F&O, and to prepare traders in advance to be mindful of possible situations, risks and temptations pertaining to trading and a guidance note to effectively handle such scenarios through proper risk management.

A brief summary of the key topics covered in Volume-I are outlined below:

- Introduction to Futures & Options, their meaning and usage in trading
- Key features of F&O like Expiry series and Lot size etc for different underlying like Indices, Stocks, Commodities & Currency etc.
- Important concepts pertaining to both Futures & Options like LTP, Open Interest, liquidity, volume, bid & ask price and bid & ask quantity. Long & Short buildup and Unwinding etc.
- Important concepts pertaining to Options like Options Chain, ITM-ATM-OTM, calculation of Intrinsic Value & Time Value, Greeks, PCR, Maxpain, Max Concentration of OI etc.
- Long & Short in Futures
- Long & Short in CE & PE, calculation of Breakeven to determine profit & loss area
- Differences between Long Options & Short Options positions
- Options Behaviour (impact of Expiry, momentum & volatility on Options and other behavioural aspects of Options)
- Tradability of premium & discount between Futures & Spot
- Tradability of discount in ITMs
- Calculation of future price of Options during their lifetime
- Procedural aspects of initiating and managing trading positions
- Golden rules of trading (Do's & Don'ts)

Thus, Volume-I contains a full comprehensive learning on all essential features of F&O from trading perspective, which every trader must know, so as to be able to trade equipped with thorough knowledge on various factors which makes an impact on Futures & Options.

Volume-II:

In Volume-II, we have focussed on creation of hedge and construct of F&O Strategies, employing different behavioural aspects of Options in order to play a particular market trend/dynamics. We have also expounded about different Adjustment techniques that can be considered by traders in the event of trend reversal adversely impacting their running trades. The Volume-II provides detailed explanations of about +30 Conventional Strategies (*like Straddle, Strangle, Bull CE Spread, Bear Put Spread etc.*) so as to give an insight into the construct & logic behind these Strategies and possible adjustments which can be considered for these Strategies.

A brief summary of the key topics covered in the Volume-II are outlined below:

- Introduction to the concept of hedging and creation of simple hedge designs & trading Strategies
- Adjustment Concept & different adjustment techniques
- Detailed explanation on +30 Conventional Strategies along with study on Options behaviour and possible adjustments

Volume III:

Besides Volume I & II, the Volume-III specifically deals with detailed discussions on about +20 Advanced Customised Strategies and about 10 unique Expiry Day Strategies, which can be used profitably to play different market situations.

A brief summary of the key topics covered in Volume III are broadly outlined below:

- Discussing construction of different customised Strategies to play different market conditions
- Customised naked & hedged Strategies – positional & intraday trading with risk adjustments
- Detailed explanation on +20 Advanced Customised Strategies along with study on Options behaviour with possible adjustments, to play different market conditions

- Detailed explanation on about unique 10 Expiry Day Strategies, for intraday play on Expiry Day

Complete Knowledge Pack, useful for all traders across the Globe

All Volumes together make it a comprehensive learning kit on F&O trading. A beginner obviously must begin with Volume-I and those who are well acquainted with various aspects of F&O (*as briefly outlined for Volume-I above*) may explore to armour themselves with the various hedge designs, adjustment techniques, various Strategies & trading rules, all encapsuled under subsequent Volumes.

While this Book makes reference of Indian Indices and F&O instruments, however, the fact of the matter is that all the learnings, concepts, techniques and Strategies discussed in the Book can be adopted and implemented by a F&O trader anywhere in the Globe wherever European Options are traded. Thus, this Book can very well be used by traders across the Globe for their learning purposes and enhancing their knowledge base.

Must have Knowledge Pack by every trader:

We sincerely believe that this learning kit with all 3 Volumes must be available with every trader, **not just for their learning needs but also as a reference material for referring to varied concepts.** The Book has been composed basis applicable market norms, in F&O segment of Indian capital markets, few months before the publication of this volume.

We hope you will enjoy & cherish the learnings contained in the Book, and that it will contribute to shorten the learning curve and help you to build a successful trading career.

Wishing you success,

With Best Wishes & Compliments,

Amit

Happy Learning !

Case For F&O Trading: Why F&O Trading?

In the context of F&O trading, the most basic and utmost significant questions which need to be addressed is: **why should someone consider F&O trading?** Entertaining the thought of considering F&O trading as a career option, appears to be even more dreadful, especially because the success rate in F&O trading in India (from profitability perspective) is less than 10%. Therefore, such hard facts about F&O trading, would obviously make someone ponder, if exploring F&O trading is worth giving it the time, money & attention it demands ?

Most of us are aware that F&O trading is a very risky proposition, a zero sum game ! However, before it is discarded outrightly (on the aforesaid ground), I strongly feel that it merits outlining the undisputed advantages it contains, which are obviously the points of attractions for retail traders (causing many to flock towards it without putting the checks & balances in place before taking plunge into F&O trading).

Advantages of F&O Trading:

To talk about the merits of F&O trading, the following brief pointers, would suffice in order to appreciate the advantages it offers as one of the straight-forward clean ways in which **BIG MONEY** can be made:

- F&O trading (unlike investing, which is dependent on bull market) can help a trader to make money in all kinds of market situations, whether bull, bear or sideways. So, a F&O trader is never out of market.
- Investment portfolios can take a huge hit due to several adverse market conditions, *viz geopolitics, wars, inflation & recession, domestic issues, scams, non-compliances & irregularities and so on and on*. However, F&O trading is not deeply or permanently impacted on account of such situations, infact such opportunities offers a great deal

of opportunities to smart traders to make killing profits (sometimes even with very low capital).

- F&O trading can be done with a bare minimum requirement of a computer, and a reasonable capital amount, which can be done from anywhere (with internet access) anytime. However, all other business ventures or employment opportunities needs adherence to a time schedule or a fixed place of operation and most of the business ventures would require huge expenses (both one-time and recurring expenses on various factors *viz manpower, machinery, office space etc*) and cash reserves for operations until breakeven. Thus, F&O trading offers an opportunity to start-off with reasonably okay capital, least of infra requirement with anytime-anywhere operational flexibility.
- Most of the employment and business opportunities remain subject to various out-of-control factors (*viz. pandemic, recession, wars, geopolitics, health issues, demand & supply factors, dearth of material, pricing issues, change of technology or style, job loss, competition etc*). However, F&O trading is an ongoing thing in most of the situations, as markets apparently seems to be the last of the things to close down (*ofcourse, in case of extreme situations like war etc.*) and keeps offering opportunities to a trader to keep making money in ever-changing/ evolving situations.
- No formal education is needed to start-off with trading. A drop-out or somebody not inclined towards academics or somebody with below average resources can also take up F&O trading as an option for regular income or wealth creation.
- The stock market offers to all retail F&O traders equal opportunities; there is no discrimination (on any ground whatsoever amongst the retailers), politics, groupism, favouritism, bossing-over, peer pressure, exploitation, unreasonable target pressure, performance pressure, unfair compensation package etc, which an employee may have to face during the course of his career pursuit at some time or the other, are completely absent in this method of money making.
- F&O trading, probably, is one of the few ways which offers clean opportunities to make BIG Money in quickest time even with low

capital. While, on the other hand, in most of the employment-oriented careers, the compensation structure is barely able to provide even saving opportunities (post taxation & inflation); thus, financial freedom or wealth creation is certainly impossible through most of the employment-oriented careers.

- Money making through F&O trading has no retirement age. Even people who are differently abled or those who are unable to pursue otherwise lucrative career options due to any kind of ailments (even if bed-ridden), can also opt for this method of income generation, not just for earning their livelihood but for wealth creation.
- Starting a business venture or embarking on an entrepreneurial journey itself may be a risky proposition, requiring lot of hard work, R&D, investing good amount of time & money. In spite of having a good idea, the success of a business plan may still be dependent on a lot of factors (which may or may not be within the control of a person). However, success in F&O trading seems achievable with proper learning, knowledge, skill development, practice, discipline and risk management. Thus, success in F&O trading is dependent on self-evolution & learning !

Today, owing to the fact that information is readily available, we know of few names who have made huge money from trading F&O, and are regularly making BIG Money consistently through F&O trading. Cherry-on-the-cake is that these names have made fortune for themselves through trading in F&O, in spite of starting from a very humble background or even with low capital or without pursuing any formal studies in finance / capital markets. These success stories offers a great deal of confidence that the much-longed for financial freedom by the mid-income group and the desire to live-their-dream by the retailers can certainly be fulfilled through F&O trading !

Success mantra in F&O Trading:

The aforesaid base case, clearly establishes that F&O trading has huge advantages over conventional employment-based careers or business pursuits, and also seems to offer great opportunity for wealth creation and can therefore be considered as a full-time career. Having said this, we must remember that the

success rate in India is less than 10% in the space of F&O trading. So **how can an average person achieve his financial goal through F&O trading ?**

The answer for the said question can be derived by evaluating the success stories of F&O traders who have made for themselves a fortune from F&O trading. The commonalities in most of these success stories boils down to the fact that: undoubtedly, F&O trading is a complex subject, but silver lining is that it can be learnt by any average person (even by those who do not have any finance or maths background). **Acquiring relevant knowledge about F&O concepts & trading, which is practically required, is the first step towards exploring F&O trading as a source of income or financial freedom.**

This learning about practically relevant aspects of F&O trading, unfortunately, is not very widely available. Most of the learning materials on F&O are academic knowledge driven – which is a big drawback, as the practically relevant matters relating to F&O trading gets lost like a needle in a hay stack. Moreover, such materials are presented in a manner as if only the finance wizards are suitable for learning F&O concepts and no one else. Thus, learners find it extremely difficult to be able to start making sense of what is being explained in such materials.

The speciality of this Book:

It is our sincere endeavour to present to the keen learners, a learning material which is comprehensive, in easy-to-understand simple language, and focussing only on practically relevant aspects of F&O trading, explaining them with real case studies and examples. **With this vision, this book on F&O Trading has been composed, split in more than one Volume, for the sake of brevity and precision.**

While, learning about practically relevant aspects of F&O trading is certainly the first step; but to evolve as a successful F&O trader is a process which will require besides acquiring knowledge (both about F&O & Technical Analysis), skill development which comes with practice, developing trading psychology, inculcating discipline & following risk management. Knowledge can be acquired but all other aspects which are required to eventually evolve as a successful trader, will have to be developed by a learner by own self by keen observation, evaluation, discipline, patience & exercising restraint.

No short-cut to Success:

To be successful in any discipline of life, one needs to persevere, devote time, attention and resource; and the same applies to F&O trading as well.

In the present times, with advent and advancement in AI (*artificial intelligence*), people misunderstand that through AI or algorithm trading, one can by-pass the need for learning relevant aspects and concepts relating to F&O trading. This is absolutely incorrect and the truth is that one can neither randomly employ any AI tool for their learnings (even Chat-GPT gives wrong responses in relation to F&O trading related queries), nor can someone safely rely on algo set-ups for all their trading needs. It is therefore an absolute requirement to walk that extra mile for learning F&O concepts & trading in a structured manner by devoting time and being patient, than to opt for dangerously unreliable short-cuts.

Infact, **appropriate knowledge about F&O concepts, techniques and Strategies can even help a trader to build their own algorithms using AI tools for coding algos; rather than considering AI trading tools or algos as a substitute for learning.** Ultimately, success in the trading career lies in the time-tested approach of taking small steps of learning, one at a time, and making gradual progression in this trading career and evolving as a knowledgeable self-reliant trader; and definitely not through random hit & try approach.

While, the journey of becoming a successful F&O trader may not be very easy, but we know that it is not invincible, it can be learnt by people from all walks of life, has undisputed advantages over conventional employment-oriented career or business ventures and last but not the least - the reward in F&O trading, if done properly, has no limits (as can be deduced from genuine success stories) !

Powerful Knowledge Pack:

This **book on F&O Trading** (with its other Volumes) is an attempt to help retail traders to shorten their learning curve in knowing about F&O concepts as one ought to know, in order to eventually evolve as a successful trader. Concepts about F&O, which are practically relevant from trading perspective, and various unique concepts, techniques and Strategies pertaining to F&O trading, have been carefully crafted and incorporated in separate Volumes.

We sincerely hope and desire that the learnings that this Book contains will be instrumental in shaping your trading career and fast-forward you towards achieving your financial goals.

A brief summary of what all is covered in the Book, is already discussed earlier.

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Chapter – 1

F&O Trading

Construction of Hedge & Strategies

In Volume – I, we have covered in detail the most important basic aspects of F&O trading, which are: (i) Basic features of the Futures and Options; (ii) Calculations pertaining to FNO trading positions; (iii) Options behaviour; (iv) Significance of Long & Short in Options; (v) procedural aspects of initiating different order types as per the trading requirements; and (vi) Golden rules of trading, as a guidance note on risk management procedures, etc.

The basic features of the Futures and Options instruments, various calculations pertaining to FNO trading positions, different behavioural aspects of Options and relevance of Long & Short in F&O instruments, forms the backbone of all the hedges and F&O trades that we will discuss in this and subsequent Chapters in this Volume II of the Book. **Various important aspects pertaining to F&O instruments and F&O trading, covered in Volume I, will be used as the building blocks for designing and decoding various Strategies and Adjustment techniques relevant for trading F&O instruments, discussed in this Volume II.**

We now kick-off discussions on Volume II, with this Chapter. This first Chapter of Volume II, is focussed on the parameters and approach to be factored in order to play different market dynamics through F&O instruments. Here, we will also understand about the various factors which play a very important role in constructing a particular hedge design / Strategy employing F&O. A sound understanding of the basic building block, to design a Strategy, will help us appreciate many Conventional Strategies which are still very useful and will also be able to put our own thoughts to carve out a suitable Customised hedge design in order to play a particular market dynamic.

Let us begin !

STEPS INVOLVED IN F&O TRADING

Trading in F&O, requires beforehand planning and identification of the following factors:

- 1) Trend / view on the underlying
- 2) Decision to execute a Hedged trade or a naked trade
- 3) Implementation of most suitable Strategy to play the Trend
- 4) Adjustment of the trade, if view goes wrong

These four factors must be thoroughly analysed and planned by a smart trader. If a trader understands how F&O instruments play out and various factors concerning them, then he will be able to deploy right instrument or mix of instruments and design a suitable Strategy to play out his view on the underlying and would also know how to wriggle his way out if the trade does not go as per plan by making suitable adjustments to his trade.

Our discussion on these important aspects in this Chapter, narrates the thought process which will help in selection / designing of a suitable Strategy and the next Chapter is focussed on making suitable adjustments to curtail the potential loss that arise on the trade (if the view goes wrong). These factors basically empower a trader to plan what he should play, how he should play and how best he can mitigate the loss.

TREND IDENTIFICATION / VIEW ON THE UNDERLYING

Let us discuss about each of the first three important factors in this Chapter; and we will focus on the fourth factor on Adjustments in the next Chapter.

Before, we decide on whether to Long or Short an Option or which particular Strategy to deploy, we need to be clear about our view on the underlying. Therefore, basis the technical analysis, generally speaking, we may have any of the following views on the underlying we wish to play out by trading in Options/ FNO instrument pertaining to that underlying:

- Bullish
- Mildly Bullish
- Bearish
- Mildly Bearish
- Rangebound / sideways (with narrow range)
- Rangebound / sideways (with wide range)
- Non-directional (may either breakout or breakdown from the range)

DECISION TO INITIATE NAKED OR HEDGED TRADES

Here we are not expounding about the technical analysis to determine the trend. A trader must have proper understanding about determining the trend, as this is the first step of trading.

After first step of identification of the trend is done, the next logical step will be whether we should play out the trend with a naked position or a hedged position/Strategy. The concept of a naked position or a hedged position, is discussed below.

Naked Positions in F&O:

When basis our view on the underlying, we may consider to initiate our single position to play out the view/ trend. When a trend is played out through Long or Short position by employing single F&O instruments or instruments favouring the direction of the trend, then such positions are referred to as **naked positions/ Strategies**.

For example, the aforementioned trends can be played out by initiating Long or Short in single F&O instruments or through instruments favouring the direction of the trend, in the following manner:

Sl. No.	Trend / view on the underlying	Naked F&O position(s)
1	Bullish	CE Long; or Futures Long
2	Mildly Bullish	PE Short; or Futures Long
3	Bearish	PE Long; or Futures Short
4	Mildly Bearish	CE Short; or Futures Short
5	Rangebound / sideways	CE Short & PE Short
6	Non-directional (may either breakout or breakdown from the range)	CE Long & PE Long

Construction of Hedged Strategies:

When a trader decides to play cautiously and initiates a position to play his view on the underlying as the main position through F&O instruments favouring the direction of the trend (referred to as the **primary leg**), but also adds to this naked primary leg position a counter position with a opposite view to the primary leg (i.e. through F&O instruments in the opposite direction of the trend), then this counter position is referred to as the **hedged leg**. This counter position or hedged leg is added to the primary leg, with an understanding that if the technical analysis about the trend goes wrong or there occurs some unplanned developments which goes against / opposite to the trend being played out through primary leg, then the hedged leg will help mitigate the losses that might occur on the primary leg. Thus, the significance of hedged leg is to cover for losses to some extent, that may occur on the primary leg when the main position (initiated to follow the trend / view on the underlying) goes wrong.

Therefore, generally, when a particular view on the underlying is played out through a primary leg and also another leg is also simultaneously initiated to

counter the primary leg in order to mitigate the potential losses on the primary leg, then such trades are referred to as **hedged positions/ Strategies**. In a hedged trade/ Strategy, the hedged leg is added to the primary leg with a conscious understanding that if the primary leg goes as per plan i.e. as expected per technical analysis, then the hedged position (being opposite to the primary leg) would yield loss and therefore would cut some profit from the primary leg. But inspite of this loss of profit in the primary leg caused by the hedged leg in the event of a successful trade, it is advisable to initiate a trade as a **hedged trade** and not a **naked trade**, because from trading perspective it is better to make some profit than to book a loss, as these small-small profits make a compounding effect in overall profitability. Moreover, the hedged trade, besides covering for risk, also helps to reduce the margin on the main position thereby enabling the trader to increase their trading volume.

In the above example of naked positions, these can be converted to a hedged position by simultaneously executing a counter position as a hedged leg, such as:

Sl. No.	Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
1	Bullish	CE Long	CE Short
		Futures Long	PE Long
2	Mildly Bullish	PE Short	PE Long
		Futures Long	CE Short
3	Bearish	PE Long	PE Short
		Futures Short	CE Long
4	Mildly Bearish	CE Short	CE Long
		Futures Short	PE Short
5	Rangebound / sideways	CE Short	PE Short
		CE Short & PE Short	CE Long & PE Long
6	Non-directional (may either breakout or breakdown from the range)	CE Long	PE Long
		CE Long & PE Long	CE Short & PE Short

Further, in certain kind of market situations, such hedged Strategies may also be designed or employed, which may be targeted to yield profit on both the primary leg (due to successful trend identification) as well as on the hedged leg. Thus, in these Strategies, depending on specific market conditions, the hedged leg is simultaneously initiated (or sometimes added later upon further confirmation of the trend) in order to not only mitigate the loss that may arise on the primary leg if the trend does not go as expected, but also to yield profit even if the primary leg does not yield any loss and plays out the trend as expected.

Thus, the hedged leg is primarily initiated / added to the naked position, to mitigate the loss (if the trend does not play out as expected). But sometimes, depending on the view on the underlying, the hedged leg is initiated / added to the naked position also because the trend may appear to be such that: not only when the primary leg would yield loss that the hedged leg would yield profit, but even if the trend is played out well by the primary naked leg generating profit, the hedged leg may also likely yield profit. For example: a mild bullish view through Call Ratio Spread. We will discuss different Strategies in details in subsequent Chapters.

It can be concluded that the hedged positions/ Strategies are safer from the perspective of overall loss and also require less capital for implementation i.e. lower margin requirement.

Now, let us also understand how profit & loss situation gets balanced out in a hedged position/ Strategy.

Profit & Loss Scenario in Hedged Strategies:

As mentioned above, the primary leg is initiated as our main position basis our view / technical analysis. Hedged leg is added to the primary leg mainly in order to cover for losses that may occur in the primary leg if our view concerning our main position goes wrong. Thus, if our main position goes as per our view, then the primary leg generates profit but the hedged leg generates loss. But if our main position does not go as per our view, then the primary leg generates loss but the hedged leg generates profit.

Thus, in any hedged position / Strategy, the basic intention is that the following balance is maintained between the primary leg and hedged leg of a given hedged Strategy:

- when the main position goes as per plan, then the primary leg generates more profit than the loss generated in the hedged leg, thereby the hedged strategy/position generates net profit; and
- when the main position does not go as per plan, then the primary leg generates a loss but the hedged leg should generate some reasonable profit such that the net loss in the hedged strategy/position is reasonably contained.

Therefore, the hedged leg must be such that it should not eat the profit generated by the primary leg, yet at the same time must be able to generate suitable profit to reasonably absorb the loss in the primary leg.

This aforesaid **balance between the primary leg and the hedged leg of a hedged position/ Strategy is primarily maintained in case of Options, through selection of Options pertaining to: relevant Strike level(s) and of a given closer or farther Expiry series.** The relevance of the Strike selection of a specific Expiry series of Options, in case of hedged Strategies/ positions involving Options, is explained below.

Strike Selection for Options Strategies:

Strike level of Options, are most important, for the purpose of designing a suitable hedged Strategy/ position in order to maintain pre-calculated suitable profit & loss balance in the Strategy. This is because each Strike level in the Options Chain offer two most critical piece of information, basis which a hedged position/ Strategy must be planned. These are:

- (a) Delta values of Strike levels
- (b) Premium / LTP of the Options at different Strike levels and Expiry series

These two important factors, which has a direct relevance for deciding the primary leg and/or the hedged leg for any given Options Strategy, are discussed below.

Delta Values in Options Strategies:

The Options Chain, provided by the stock brokers on their trading terminal¹, gives the Delta values for each of the CE & PE Options (for single Lot basis). A good understanding about Delta values and their interplay helps a trader to plan a better trading position or design a robust Strategy. Few most important factors regarding the Delta value of Options, which every trader must borne in mind while designing a hedged Options Strategy, are mentioned below:

- On CE & PE sides: deep OTMs to ATM, Delta value progressively increases from 0 to 0.5. Further, from ATM towards deep ITMs, the Delta value progressively increases from 0.5 at ATM to 1. Delta value of both CE & PE ATM Strike is 0.5.
- In the Options Chain, for the CE side: the Delta values are +ve as it denotes proportional relationship of rise/fall in the LTP of CE Options with the movement of the underlying, i.e. if the underlying moves up, the CE Options' LTP moves up; and if the underlying moves down, the CE Options' LTP moves down. On the contrary, in the Options Chain, for the PE side: the Delta values are -ve as it denotes inversely proportional relationship of rise/fall in the LTP of PE Options with the movement of the underlying, i.e. if the underlying moves up, the PE Options' LTP moves down; and if the underlying moves down, the PE Options' LTP moves up.
- On CE & PE OTM sides: Both Delta value and Theta value progressively decreases from ATM towards deep OTM.

¹ May be for some subscription charges. Greek values for various Options are also provided by certain Options analytical softwares.

- On CE & PE ITM sides: Delta values progressively increases from ATM towards deep ITM; whereas Theta value progressively decreases from ATM towards deep ITM.
- Delta values of CE OTMs somewhat matches with those of the PE OTMs. Also, Delta values of CE ITMs somewhat matches with those of the PE ITMs.
- On CE side, lower Strike has more Delta value and more Premium; and higher strike has lower Delta and lower Premium. On the contrary, for the PE side, higher Strike has more Delta value and more Premium; and lower strike has lower Delta and lower Premium.
- A given CE OTM having similar Delta value as that of any PE OTM, are likely to have somewhat similar LTPs (or vice-versa). Also, any given CE ITM having similar Delta value as that of any PE ITM, are likely to have somewhat similar LTPs (or vice-versa).
- Futures have a Delta of 1.
- Deep ITM Options (both CE & PE) have almost 100% Intrinsic Value has a Delta value close to 1, and thus behaves like Futures.
- Each Strike has a CE and a PE Option, and their aggregate Delta value is always 1. Therefore, if at same Strike one side Option is on Long and another side Option on Short, then such position will have a Delta value of 1, and thus behaves like Futures.
- For ITM Options (both CE & PE), the Delta value of same strike ITMs decreases as we move from closer Expiry series towards farther Expiry series. On the contrary, for OTM Options (both CE & PE), the Delta value of same Strike OTMs increases as we move from closer Expiry series towards farther Expiry series.
- Delta effect on a Strategy/ hedged position depends upon the aggregate Delta value in the primary leg and the hedged leg. Delta values gets added up depending upon the number of Lots used to create a position, i.e. for example: if in a hedged Strategy, the primary leg has 3 Lots Options of a given Strike and the hedged leg is initiated

with 6 Lots of Options on a different Strike, then the final Delta effect on this Strategy, will be determined basis the aggregate Delta value on the primary leg (i.e. Delta value for 1 Lot x 3) and the aggregate Delta value in the hedged leg (i.e. Delta value for 1 Lot x 6).

- CE Long and PE Short has a +ve Delta which denotes that if the underlying moves up, the CE Long and PE Short yields profit. While, CE Short and PE Long has a -ve Delta which denotes that if the underlying moves down, the CE Short and PE Long yields profit. Thus, in a hedged Strategy, if the net Delta value (i.e. aggregate Delta value of primary leg – aggregate Delta value of hedged leg) is +ve then the Strategy is tilted towards bullish side and will generate profit if the underlying moves higher; and if the net Delta value of the Strategy is -ve then the Strategy will yield profit if the underlying will slide down.
- Accordingly, a bullish Strategy can be designed with more aggregate +ve Delta on the Strategy than the aggregate -ve Delta. Likewise, a bearish Strategy can be designed with more aggregate -ve Delta than the aggregate +ve Delta. And a neutral strategy would involve Options with same / similar Delta values.
- When the Options position keep advancing in the money, the effect of climbing higher Delta ladder causes rise in the Premium up in a compounding manner as the position keeps moving deeper in the money drifting from higher Delta levels to even higher Delta levels. In such case, the Premium of the Options position increases at a higher rate with every move to a higher Delta level than the previous rate (due to current higher Delta value than that of the previous lower level). However, when the Options position keep advancing out of the money, the effect of coming down from the Delta ladder (i.e. from higher Delta level to lower level) causes lesser and lesser fall in the Premium as the position keeps moving deeper out of the money drifting from higher Delta levels to lower and then even lower Delta levels. In such case, the Premium of the Options position decreases at a reduced rate with every move to a lower Delta level than the

previous rate (due to current lower Delta value than that of the previous higher level to next lower level).

- On Expiry day, all Options lose the Time Value comprised in the Premium. Accordingly, on Expiry day, Delta values of all OTMs start to exceedingly reduce to become zero by the end of the Expiry (from deep OTMs towards ATM); and the Delta values of all ITMs tend to become 1 by the close of the Expiry (from deep ITMs towards ATM). Thus, by mid-day on Expiry, even very near ITMs get on to the Delta value of 1 and thereby start behaving like Futures.

Options behaviour, such as above, helps a trader to design a suitable hedged position depending upon his view on the underlying. The aforesaid information can be used to maintain a specific distance / tilt on the bullish side or the bearish side in a given Strategy at the time of initiating the positions; or to maintain a non-directional neutral Strategy by having Options of same Delta values for the primary leg and the hedged leg of the Strategy. The Delta values would help ensure the change in the Premium values of the Options at the primary leg and the hedged leg, in response to both, the favourable and unfavourable movement in the underlying. Thus, the bullish/ bearish tilt or neutrality in the Strategy is ensured by choosing appropriate Strike levels with the requisite Delta values and maintaining a proper difference in the Delta values between the primary leg and the hedged leg of the Strategy at the time of initiating the positions/ Strategy.

Now let us discuss and understand the importance of Strike levels for a suitable hedge design, from the perspective of their Premium.

Premium of Options in different Strikes & Expiry:

The Options Chain provides the LTP/ premium value of each of the CE and PE Options at each Strike level on almost real time basis. Certain important aspects pertaining to the Premium of Options, which must be borne in mind, while designing a Strategy are summarised below:

- On CE & PE sides: the Premium progressively increases from deep OTMs towards deep ITMs.

- On CE side: lower Strike has more Premium and more Delta value; and higher strike has lower Premium and lower Delta.
- On the PE side, higher Strike has more Premium more and Delta value; and the lower strike has lower Premium and lower Delta.
- Premium of CE OTMs somewhat matches with those of the PE OTMs. Also, Premium of CE ITMs somewhat matches with those of the PE ITMs.
- A given CE OTM having similar Premium value as that of any PE OTM, are likely to have somewhat similar Delta value (or vice-versa). Also, any given CE ITM having similar Premium value as that of any PE ITM, are likely to have somewhat similar Delta value (or vice-versa).
- All OTMs and ATMs (both CEs & PEs) only have Time Value in their Premium/ LTP.
- Only ITMs (both CEs & PEs) have Intrinsic Value in their Premium/ LTP. For both CEs & PEs, from ATM towards deep ITM, the Intrinsic Value component in the Premium/LTP of ITMs keeps increasing and the Time Value keeps decreasing. Deepest ITMs have only Intrinsic Value and no Time Value. Such deepest ITMs have a Delta value of 1 and behave like Futures.
- Options' Premium follows the Futures' LTP of the relevant underlying until Expiry and on the Expiry day the Options starts following the Spot value of the underlying.
- With each passing day towards the Expiry of the Options, the Time Value of all the Options undergo decay on account of time decay/ Theta effect.
- On Expiry of the relevant Options, Time Value in all the Options become zero. Consequently, on Expiry, both ATMs and all OTMs expire worthless as their Premium has 100% Time Value; while the ITMs are left with the final LTP equal to their Intrinsic Value.

- On Expiry, the ITMs would have final Premium left equal to their Intrinsic Value. Since, on Expiry day, Intrinsic value of ITMs is the difference between the Spot value of the underlying (*or the ATM Strike on Expiry*) and the Strike value of the relevant ITM, therefore, in effect the Premium of each of the ITM Options would be the distance between the ITM Strike and the ATM. For example: the Premium of an ITM which is 7th Strike from ATM of BankNifty Options would be 700 (*because distance between each Strike in the BankNifty Options Chain is in multiples of 100*); and the Premium of an ITM which is 7th Strike from ATM of Nifty Options would be 350 (*because distance between each Strike in the Nifty Options Chain is in multiples of 50*). However, the final Premium value of ITMs, sometimes, may not exactly be the same as the distance between their Strike and the ATM, due to final effects of rise / drop in Volatility thereby closing marginally higher or lower than the actual difference between the ITM Strike and the ATM.
- Time decay which erodes the Time Value of Options, becomes fast and Theta value increases as the Expiry draws near.
- On Expiry day, the Premium value of all OTMs starts to exceedingly reduce to become zero by the end of the Expiry from deep OTMs towards ATM; and the Premium value of all ITMs tend to get reduced to their Intrinsic Value from deep ITMs towards ATM. Thus, by mid-day on Expiry, even very near ITMs have their Premium value almost close to their Intrinsic Value (which starts behaving like Futures, as such ITMs have their Delta value of 1).
- Premium of same Strike Options, from closer to farther Expiry series, increases. Theta value is higher in closer Expiry series than farther Expiry series.
- Long Options (buying CE or PE) involves payment of Premium, thus it is a debit position. Short Options (selling CE or PE) involves receiving credit of Premium, thus it is a credit position.

- Long Options should be preferably initiated on farther Expiry series (with lower Theta value) for a long holding period; and Short Options should be initiated on closer Expiry series (with higher Theta value) for a shorter holding period.
- When the underlying moves higher, Premium of CE Options rises; and that of the PE Options fall. However, when the underlying moves lower, Premium of CE Options falls; and that of the PE Options rises. Higher the momentum in the underlying upwardly, higher the CE Options' Premium may rise (like 300% or 400% etc.), but the Premium of the PEs can fall as much as 100%. Likewise, higher the momentum in the underlying downwardly, higher the PE Options' Premium may rise (like 300% or 400% etc.), but the Premium of the CEs can fall as much as 100%.
- Long Options may have unlimited reward if the trend is favourable and with momentum; but would have a maximum loss limited to the extent of Premium paid on them. While, Short Options may have unlimited risk potential if the trend is unfavourable with momentum; but would have a maximum profit limited to the extent of Premium credit received on them.
- Rise in Volatility causes rise in the Premium or keeps the Premium value from falling much. This is because the rise in Volatility causes expansion in the Time Value comprised in the Premium. Fall in Volatility causes drop in the Premium or keeps the Premium value from rising much. This is because the fall in Volatility causes contraction in the Time Value comprised in the Premium.
- Impact of momentum and volatility is felt in the Most Impacted Radius Zone in the Options Chain, which is mainly concentrated upto a few Strikes around ATM particularly towards OTM. Options at the Strike levels outside the Most Impacted Radius Zone may not get much or negligibly impacted with the momentum / Volatility.
- During low Volatility periods, for Short Options positions, closer Expiry series may not offer suitable Premium credit. Therefore, in

such cases, subject to market condition, farther Expiry series Strike levels may be considered for Shorting to play movement in the underlying (which may not be necessarily suitable to play Theta decay, as Theta value would be lower in farther Expiry).

- Since Long Options are debit positions, from Expiry perspective, the underlying must cross-over the Breakeven Strike of the Long Options. Breakeven Strike of CE Long position is: $\text{CE Strike} + \text{Premium paid}$. Breakeven Strike of PE Long position is: $\text{PE Strike} - \text{Premium paid}$. If by Expiry, the underlying does not cross the Breakeven Strike then the entire Premium paid is a loss. Thus, in Long Options, from Expiry perspective, profit begins after crossing the Breakeven Strike.
- Since Short Options are credit positions, from Expiry perspective, the underlying must not cross-over the Breakeven Strike of the Short Options. Breakeven Strike of CE Short position is: $\text{CE Strike} + \text{Premium credit}$. Breakeven Strike of PE Short position is: $\text{PE Strike} - \text{Premium credit}$. If by Expiry, the underlying does not cross the Breakeven Strike then the Short Options position yields profit. However, if by Expiry, the Short Options position crosses beyond the Breakeven Strike then the Short Options position may suffer unlimited loss.
- In Long Options, the Premium rises (thus generating profit) as the Long Strike keeps moving in the money (in which case it moves up the Delta ladder). In Short Options, the Premium falls (thus generating profit) as the Short Strike keeps moving out of the money (in which case it moves down the Delta ladder).
- When the Options position keep advancing in the money, the Premium of the Options rises up in a compounding manner i.e. the Premium of the Options position increases at a higher rate with every move in to the money (due to the Strike getting drifted in to the money from current higher Delta value than that of the previous level). However, when the Options position keep advancing out of the money, the Premium of the Options falls at a reduced rate than the previous rate with every move out of the money (due to the Strike

getting drifted further out of the money from current lower Delta value to even lower next Delta level).

Using the aforesaid information, a trader can plan to design his Strategy by selecting appropriate Strike levels at which primary legs and hedged legs may be initiated, in order to play out a particular market condition by creating a net debit or credit Strategy. Net Debit and Net Credit hedged positions are discussed below.

Net Debit Hedged Strategies:

If a trader plans to play a strong momentous move in the underlying, he may opt to play such momentum through a net debit Strategy by having Long Options with higher aggregate Premium and Short Options with lesser aggregate Premium. Higher aggregate Premium can be achieved:

- by having higher number of Long Options than Short Options, such that the aggregate Premium of Long Options leg is higher than the aggregate Premium on Short Options leg; or
- by initiating equal number Long Option at higher Premium Strike (i.e. lower Strike for CEs and higher Strike for PEs) and equal number of Short Options initiated at lower Premium Strike (i.e. higher Strike for CEs and lower Strike for PEs); or
- by initiating equal number Long Option at farther Expiry series Options (which have higher Premium value for same Strike Options) and equal number of Short Options initiated at closer Expiry series (which have lower Premium value for same Strike Options)

In the Net Debit hedged positions, a trader can pre-calculate the Breakeven Strike, risk & reward in the Strategy and plan his positions accordingly.

Net Credit Hedged Strategies:

If a trader wishes to play a mild directional move or a sideways movement of the underlying, then he may opt to design a suitable credit Strategy by having Short

Options with higher aggregate Premium and Long Options with lesser aggregate Premium. Higher aggregate Premium can be achieved:

- by having higher number of Short Options than Long Options, such that the aggregate Premium of Short Options leg is higher than the aggregate Premium on Long Options leg; or
- by initiating equal number Short Option at higher Premium Strike (i.e. lower Strike for CEs and higher Strike for PEs) and equal number of Long Options initiated at lower Premium Strike (i.e. higher Strike for CEs and lower Strike for PEs); or
- by initiating equal number Short Option at farther Expiry series Options (which have higher Premium value for same Strike Options) and equal number of Long Options initiated at closer Expiry series (which have lower Premium value for same Strike Options).

In the Net Credit hedged positions, a trader can pre-calculate the Breakeven Strike upto which the Strategy is safe and accordingly select suitable Strikes for the primary and the hedged leg.

Thus, the aforesaid Options behavioural aspects which have an impact on the Options' Premium value, helps a trader to design a suitable hedged position with pre-calculated profit & loss areas and risk to reward ratio and taking into account the favourable and unfavourable factors prevalent at the time of initiating the hedged debit/ credit Strategy and during the lifetime of the Strategy. Ultimately, it is about the Premium of the Options that we trade for. Hence, these factors must be considered for selecting suitable Strikes in order to design a particular Strategy to play out the trend / movement of the underlying.

Basis the aforesaid discussions on the relevance of Strike levels from the perspective of the Delta value and the Premium at those Strike levels, suitable Strategies can be designed for the different market situations / trend in the underlying by identification of appropriate Strikes for the primary leg and the hedged leg. Strike levels at which the primary leg and the hedged leg can possibly be initiated to play out the trend would constitute a hedged Strategy. A few hedged Strategies are briefly discussed below in view of the possible trend in the underlying.

SELECTION OF SUITABLE STRATEGY TO PLAY THE TREND

Once, the trend is identified as the first step, and then suitable Strike levels are analysed (*keeping in mind their Premium, Theta value, Delta value, Expiry etc.*) to play out the trend though initiating Long or Short positions for the primary leg and hedged leg, then a most suitable hedged positions/ Strategy can be planned and implemented.

Examples of Hedged Strategies

The Table below broadly outlines the Strategy that can be implemented to play out the possible trend scenarios as highlighted in this Chapter, namely: Bullish, Mild Bullish, Bearish, Mild Bearish, Rangebound (*non-directional*), Breakout/ Breakdown (*non-directional*).

(i) Bullish Trend:

Strategy 1 for Bullish Trend		
Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Bullish	CE Long	CE Short

Strategy / Hedge Design with explanation:

- Long lower Strike CE having higher Delta (*primary leg*)
- Short higher Strike CE with lower Delta (*hedged leg*)

Bullish trend is planned to be played through Long CE. A CE Short counter position is also executed to mitigate for any loss on the primary leg if the bullish trend reverses. CE Long is to be initiated on higher Delta thus lower Strike CE, and CE Short is initiated on lower Delta thus higher CE Strike, so that if bullish trend continues then primary leg yields higher profit than the loss on the hedged leg; and if the trend reverses then the hedged leg is not too low on Delta than that of the primary leg so as to be able to reasonably mitigate the loss on the primary leg through the profit generated on the hedged leg.

Further, since lower CE Strike is the Long leg therefore Long leg requires more Premium payment than the Premium credit received on the hedged leg, thus making

it a net debit strategy. Both the primary and hedged leg can be initiated on the same Expiry if Expiry is still far to avoid time decay on the Long leg. Moreover, the Long leg should be within the Most Impacted Radius Zone in order to get benefited most from the expected bullish momentum. This Strategy is called **Bull CE Debit Spread**

Strategy 2 for Bullish Trend

Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Bullish	Futures Long	PE Long

Strategy / Hedge Design with explanation:

- Long Futures with Delta of 1 (*primary leg*)
- Long ITM Strike PE with Delta of around 0.6 or higher (*hedged leg*)

Bullish trend is planned to be played through Long Futures. The primary leg is hedged with a Long PE so that if the trend reverses to a downward momentum then PE Long is able to set-off the losses on Futures position. Futures have a Delta of 1, therefore, PE Long must not be having greater difference in the Delta values with the Futures position, so that in case of reversal towards downward momentum PE generates decent profit and can reasonably set-off losses on Futures.

However, in case of reversal towards slow downward trend, this position should be held only upto a time before Theta starts overpowering profits on the PE Long. But if the bullish momentum continues as originally envisaged, then Futures being on a higher Delta would yield more profit than the loss incurred on PE Long. Also, in case of bullish momentum, the maximum loss that can be incurred on the PE hedged leg is to the limited extent of the Premium paid on PE.

(ii) Mildly Bullish Trend:

Strategy 1 for Mild Bullish Trend

Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Mildly Bullish	PE Short	PE Long

Strategy / Hedge Design with explanation:

- Short PE at higher Strike with higher Delta (*primary leg*)

- Long PE at lower Strike with lower Delta (*hedged leg*)

Mild bullish trend is planned to be played through PE Short. A PE Long counter position is also executed to mitigate for any loss on the primary leg if the mild bullish trend reverses on the downside. PE Short is to be initiated on higher Delta thus higher Strike PE, and PE Long is initiated on lower Delta thus lower PE Strike, so that if mild bullish trend continues then primary leg yields higher profit than the loss on the hedged leg; and if the trend reverses then the hedged leg is not too low on Delta than that of the primary leg so as to be able to reasonably mitigate the loss on the primary leg through the profit generated on the hedged leg.

Further, since higher PE Strike is the Short leg therefore Short leg received more Premium credit than the Premium paid on the lower PE Strike Long leg, thus making it a net credit strategy. Both the primary and hedged leg can be initiated on the same Expiry. The net Premium credit received in this strategy needs to be protected and the net credit of premium received shall be the maximum profit in this strategy. The Short leg should be such which must be at Far OTM Strike so that it expires as OTM on Expiry. This Strategy is called **Bull PE Credit Spread**.

Strategy 2 for Mild Bullish Trend

Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Mildly Bullish	Futures Long	CE Short

Strategy / Hedge Design with explanation:

- Long Futures with Delta of 1 (*primary leg*)
- Short OTM Strike CE (*hedged leg*)

Mild bullish trend is planned to be played through Long Futures. The primary leg is hedged with a Short CE so that if the trend reverses to a downward momentum then CE short is able to set-off the losses on Futures position. Further, in order to benefit from Theta the CE Short leg should be such which must be at Far OTM Strike so that it expires as OTM on Expiry. If CE Short leg expires as OTM then the hedged leg position yields profit. Futures have a Delta of 1, therefore, if the mild bullish trend reverses to a steep downward momentum, then the CE short leg would not be able to

absorb the loss on the Futures Long leg more than the Premium credit received on the CE short leg (the maximum profit of the hedged leg).

Moreover, since CE Short leg is initiated on Far OTM Strike, the Delta value of Short leg will be too less as compared to that of the Futures Long leg, therefore, the loss incurred on account of steep reversal on the downside would be phenomenally higher. Thus, instead of Far OTM CE, near OTM CE or ATM CE even near ITM CE can be Shorted for the hedged leg. This Strategy is called **Covered Call**.

(iii) **Bearish Trend:**

Strategy 1 for Bearish Trend		
Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Bearish	PE Long	PE Short
Strategy / Hedge Design with explanation: • Long higher Strike PE having higher Delta (<i>primary leg</i>) • Short lower Strike PE lower Delta (<i>hedged leg</i>) Bearish trend is planned to be played through Long PE. A PE Short counter position is also executed to mitigate for any loss on the primary leg if the bearish trend reverses. PE Long is to be initiated on higher Delta thus higher Strike PE, and PE Short is initiated on lower Delta thus lower PE Strike, so that if bearish trend continues then primary leg yields higher profit than the loss on the hedged leg; and if the trend reverses then the hedged leg is not too low on Delta than that of the primary leg so as to be able to reasonably mitigate the loss on the primary leg through the profit generated on the hedged leg. Further, since higher PE Strike is the Long leg therefore Long leg requires more Premium payment than the Premium credit received on the hedged leg, thus making it a net debit strategy. Both the primary and hedged leg can be initiated on the same Expiry if Expiry is still far to avoid time decay on the Long leg. Moreover, the Long leg should be within the Most Impacted Radius Zone in order to get benefited most from the expected bearish momentum. This Strategy is called Bear PE Spread.		

Strategy 2 for Bearish Trend		
Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Bearish	Futures Short	CE Long
Strategy / Hedge Design with explanation: • Short Futures with Delta of 1 (<i>primary leg</i>) • Long ITM Strike CE with Delta of around 0.6 or higher (<i>hedged leg</i>) Bearish trend is planned to be played through Short Futures. This primary leg is hedged with a Long CE so that if the trend reverses to an upward momentum then CE Long is able to set-off the losses on Futures position. Futures have a Delta of 1, therefore, CE Long must not be having greater difference in the Delta value with the Futures position, so that in case of reversal towards upward momentum CE generates decent profit and can reasonably set-off losses on Futures. However, in case of reversal towards slow upward trend, this position should be held only upto a time before Theta starts overpowering profits on the CE Long. But if the bearish momentum continues as originally envisaged, then Futures being on a higher Delta would yield more profit than the loss incurred on CE Long. Also, in case of bearish momentum, the maximum loss that can be incurred on the PE hedged leg is to the limited extent of the Premium paid on CE.		

(iv) **Mildly Bearish Trend:**

Strategy 1 for Mild Bearish Trend		
Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Mildly Bearish	CE Short	CE Long
Strategy / Hedge Design with explanation: • Short CE at lower Strike with higher Delta (<i>primary leg</i>) • Long CE at higher Strike with lower Delta (<i>hedged leg</i>)		

Mild bearish trend is planned to be played through CE Short. A CE Long counter position is also executed to mitigate for any loss on the primary leg if the mild bearish trend reverses on the upside. CE Short is to be initiated on higher Delta thus lower Strike CE, and CE Long is initiated on lower Delta thus higher CE Strike, so that if mild bearish trend continues then primary leg yields higher profit than the loss on the hedged leg; and if the trend reverses then the hedged leg is not too low on Delta than that of the primary leg so as to be able to reasonably mitigate the loss on the primary leg through the profit generated on the hedged leg.

Further, since lower CE Strike is the Short leg therefore Short leg received more Premium credit than the Premium paid on the higher CE Strike Long leg, thus making it a net credit strategy. Both the primary and hedged leg can be initiated on the same Expiry. The net Premium credit received in this strategy needs to be protected and the net credit of premium received shall be the maximum profit in this strategy. The Short leg should be such which must be at Far OTM Strike so that it expires as OTM on Expiry. This Strategy is called **Bear CE Credit Spread**.

Strategy 2 for Mild Bearish Trend

Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Mildly Bearish	Futures Short	PE Short

Strategy / Hedge Design with explanation:

- Short Futures with Delta of 1 (*primary leg*)
- Short OTM Strike PE (*hedged leg*)

Mild bearish trend is planned to be played through Short Futures. This primary leg is hedged with a Short PE so that if the trend reverses to an upward momentum then PE short is able to set-off the losses on Futures position. Further, in order to benefit from Theta the PE Short leg should be such which must be at Far OTM Strike so that it expires as OTM on Expiry. If PE Short leg expires as OTM then the hedged leg position yields profit. Futures have a Delta of 1, therefore, if the mild bearish trend reverses to a steep upward momentum, then the PE short leg would not be able to absorb the loss on the Futures Short leg more than the Premium credit received on the PE short leg (the maximum profit of the hedged leg).

Moreover, since PE Short leg is initiated on Far OTM Strike, the Delta value of Short leg will be too less as compared to that of the Futures Short leg, therefore, the loss incurred on account of steep reversal on the upside would be phenomenally higher. Thus, instead of Far OTM PE, near OTM PE or ATM PE or even near ITM PE can be Shorted for the hedged leg. This Strategy is called **Covered Put**.

(v) **Rangebound/ Sideways (*non-directional*) Trend:**

Strategy 1 for Rangebound Trend		
Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Rangebound / sideways	CE Short	PE Short
Strategy / Hedge Design with explanation: • Short ATM CE (<i>primary leg</i>); and • Short ATM PE (<i>primary leg</i>). When underlying is expected to remain within a very tight range from its current level and Expiry is expected almost close to the current price level, then ATM CE & PE can be shorted to benefit from the rangebound up & down move of the underlying which causes erosion of the Time Value in the Shorted Options; and also to benefit from Theta decay: as by Expiry both or one of the Short leg would Expire worth less yielding entire Premium credit on that leg as profit and the other leg may also face some decay of the Time Value even if it expires as an ITM very close to ATM. The ATM Strike commands a very good Premium with highest Theta value and 100% Time Value in the Premium. However, this Strategy comprises of naked Short positions, which may yield potentially unlimited loss if the underlying breaks-out in either direction. However, so long the underlying hovers up & down within the tight range, the two Short legs in this strategy being ATM Strikes have same Delta values and therefore have a neutral or balanced Delta effect (i.e. when one leg profits other loses in almost same proportion). The strategy has an aggregate Premium credit, which needs to be retained for deriving profit. This Strategy is called Short Straddle.		

Strategy 2 for Rangebound Trend		
Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Rangebound / sideways	CE Short	PE Short
Strategy / Hedge Design with explanation: - Short OTM CE with similar Delta value as that of PE leg (<i>primary leg</i>); and - Short OTM PE with similar Delta value as that of CE leg (<i>primary leg</i>). When the underlying is expected to remain within a wide range and Expiry is expected somewhere between the anticipated wide range from the current price level, then OTM CE & PE can be shorted to benefit from the rangebound up & down move of the underlying which causes erosion of the Time Value in the Shorted Options; and also to benefit from Theta decay: as by Expiry at best both of the Short leg would Expire worthless yielding entire Premium credit on both the legs as profit. The OTM Strike has relatively less Premium but has 100% Time Value in the Premium. However, this Strategy comprises of naked Short positions, which may yield potentially unlimited loss if the underlying breaks-out in either direction and one of the Short leg ends up as an ITM by Expiry. The two OTM strikes which are selected must be having similar Delta values (and almost same Premium values), so that so long the underlying hovers up & down within the wide defined range, the two Short legs would have a neutral or balanced Delta effect (i.e. when one leg profits other loses in almost same proportion). The strategy has an aggregate Premium credit, which needs to be retained for being profitable. This Strategy is called Short Strangle.		
Strategy 3 for Rangebound Trend		
Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Rangebound / sideways	CE Short & PE Short	CE Long & PE Long
Strategy / Hedge Design with explanation: Short ATM CE with higher Delta (<i>primary leg</i>) and Long OTM CE at higher Strike with lower Delta (<i>hedged leg</i>); and		

- Short ATM PE with higher Delta (*primary leg*) and Long OTM PE at lower Strike with lower Delta (*hedged leg*)

When underlying is expected to remain within a very tight range from its current level and Expiry is expected almost close to the current price level, then ATM CE & PE can be shorted for the reasons explained in case of Short Straddle Strategy. However, in this strategy, both the naked Short positions are hedged by simultaneously initiating Long counter position to mitigate for any loss on the primary Short leg if the underlying breakouts the narrow range and starts trending in one direction. Both CE Long and PE Long hedged legs are initiated on lower Delta thus OTM CE & PE Strike. Consequently, Short legs receives more Premium credit than the premium paid for the Long legs.

Thus, this strategy is a net premium credit strategy, which needs to be retain for being profitable in this strategy. If the underlying by Expiry remains within the narrow range then the primary Short leg yields higher profit than the loss on the hedged leg; and if the underlying breaks out of the narrow range in either direction, then the hedged leg must not be too low on Delta than that of the primary leg, so as to be able to reasonably mitigate the loss on the primary leg through the profit generated on the hedged leg. Both the primary and hedged leg can be initiated on the same Expiry. The net Premium credit received in this strategy shall be the maximum profit in this strategy. This strategy is therefore hedged Short Straddle, referred to as **Iron Fly or Iron Butterfly**.

Strategy 4 for Rangebound Trend

Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Rangebound / sideways	CE Short & PE Short	CE Long & PE Long

Strategy / Hedge Design with explanation:

- Short OTM CE at lower Strike with higher Delta (*primary leg*) and Long CE at higher Strike with lower Delta (*hedged leg*); and
- Short OTM PE at higher Strike with higher Delta (*primary leg*) and Long PE at lower Strike with lower Delta (*hedged leg*)

When the underlying is expected to remain within a wide range and Expiry is expected somewhere between the anticipated wide range from the current price level, then OTM CE & PE can be shorted for the reasons explained in case of Short Strangle

Strategy. However, in this strategy, both the naked Short positions are hedged by simultaneously initiating Long counter position to mitigate for any loss on the primary Short leg if the underlying breakouts the defined range and starts trending in one direction. Both CE Long and PE Long hedged legs are initiated on lower Delta thus even Far OTM CE & PE Strikes. Consequently, Short legs receives more Premium credit than the premium paid for the Long legs.

Thus, this strategy is a net premium credit strategy, which needs to be retained for being profitable in this strategy. If the underlying by Expiry remains within the defined range then the primary Short leg yields higher profit than the loss on the hedged leg; and if the underlying breaks out of the defined range in either direction, then the hedged leg must not be too low on Delta than that of the primary leg, so as to be able to reasonably mitigate the loss on the primary leg through the profit generated on the hedged leg. Both the primary and hedged leg can be initiated on the same Expiry. The net Premium credit received in this strategy shall be the maximum profit in this strategy. This strategy is therefore hedged Short Strangle, referred to as **Iron Condor**.

(vi) **Rangebound/ Sideways (non-directional) Trend:**

Strategy 1 for Rangebound Trend – Expecting Breakout / Breakdown		
Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Non-directional (may either breakout or breakdown from the range)	CE Long	PE Long
Strategy / Hedge Design with explanation: • Long ATM CE (<i>primary leg</i>); and • Long ATM PE (<i>primary leg</i>). When underlying is expected to take a sudden strong momentous move shortly in any one direction from its current level (owing to some news, event or results etc.), about which there is no certainty as to in which direction the momentum would arrive, then such expected momentous move can be played out by initiating a neutral		

position through Long ATM CE & ATM PE. However, in this strategy, the requirement is that momentum should be strong and must arrive soon before Theta starts eroding the Premium. Both the positions are naked Long positions initiated at ATM thereby maintaining a neutral Delta position on the strategy.

Moreover, since both the positions are Long positions therefore this strategy is an aggregate Premium debit strategy, which needs to be first set-off from the profits so as to be net profitable in this strategy. Both the positions can be initiated on the same Expiry. If the momentum fails to arrive soon or is feeble then the maximum loss that may occur in this strategy shall be limited to the extent of the aggregate premium paid on this strategy. This strategy is referred to as **Long Straddle**.

Strategy 2 for Rangebound Trend – Expecting Breakout / Breakdown

Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Non-directional (may either breakout or breakdown from the range)	CE Long	PE Long

Strategy / Hedge Design with explanation:

- Long OTM CE with similar Delta value as that of PE leg (*primary leg*); and
- Long OTM PE with similar Delta value as that of CE leg (*primary leg*)

When underlying is expected to take a sudden strong momentous move shortly in any one direction from its current level and keep trending in that direction (owing to some news, event or results etc.), about which there is no certainty as to in which direction the momentum would arrive, then such expected momentous move can be played out by initiating a neutral position through Long OTM CE & OTM PE. However, in this strategy, the requirement is that momentum should be strong and must arrive soon before Theta starts eroding the Premium on both OTM legs. Both the positions are naked Long positions initiated at OTM Strikes having similar Delta values (and similar Premium values), thereby maintaining a neutral Delta position on the strategy.

Moreover, since both the positions are Long positions therefore this strategy is an aggregate Premium debit strategy, which needs to be first set-off from the profits so

as to be net profitable in this strategy. Both the positions can be initiated on the same Expiry, provided, the Theta value is still less and favourable (i.e. there is reasonable time for Expiry). However, if the momentum fails to arrive soon or is feeble, then the maximum loss that may occur in this strategy shall be limited to the extent of the aggregate premium paid on this strategy. This strategy is referred to as **Long Strangle**.

Strategy 3 for Rangebound Trend – Expecting Breakout / Breakdown

Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Non-directional (may either breakout or breakdown from the range)	CE Long & PE Long	CE Short & PE Short

Strategy / Hedge Design with explanation:

- Long ATM CE having higher Delta (*primary leg*) and Short higher Strike OTM CE with lower Delta (*hedged leg*)
- Long ATM PE having higher Delta (*primary leg*) and Short lower Strike PE with lower Delta (*hedged leg*)

When underlying is expected to breakout / take a strong momentous move in any one direction from its current level, then Long position on ATM CE & PE can be initiated for the reasons explained in case of Long Straddle Strategy. However, in this strategy, both the naked Long positions are hedged by simultaneously initiating Short counter positions on OTM Strikes to mitigate for any loss on the primary Long leg(s) if the underlying fails to breakout and take a strong momentous move in any one direction shortly, because then the rangebound underlying will eat away the premium on the Long legs and Theta will further erode their premium value. In such situation, the Short legs will also face erosion in their premium value and therefore will generate some profit which will mitigate the losses on the Long legs(s). Both CE Long and PE Long hedged legs are initiated on higher Delta as they are ATM Strikes, while the Short legs initiated on OTM Strikes are on lower Delta. Consequently, Long legs pays more Premium than the premium credit received on the Short legs.

Thus, this strategy is a net premium debit strategy, which needs to be first recovered in order for this strategy to be profitable, for which the underlying must soon take a momentous move in any one direction such that the net profit will be much higher

than the aggregate net premium paid on the strategy. If the underlying by Expiry remains within a range or momentum is slow and weak, then this strategy may suffer loss to the maximum extent of the aggregate net premium paid on this strategy. Both the primary and hedged leg can be initiated on the same Expiry. This strategy is, therefore, hedged Long Straddle, and is called **Reverse Iron Butterfly or Reverse Iron Fly**.

Strategy 4

Trend / view on the underlying	Primary Leg (Naked F&O position)	Hedged Leg (Counter positions)
Non-directional (may either breakout or breakdown from the range)	CE Long & PE Long	CE Short & PE Short

Strategy / Hedge Design with explanation:

- Long OTM CE at lower Strike having higher Delta (*primary leg*) and Short higher Strike OTM CE with lower Delta (*hedged leg*)
- Long OTM PE at higher Strike having higher Delta (*primary leg*) and Short lower Strike PE with lower Delta (*hedged leg*)

When underlying is expected to breakout / take a strong momentous move in any one direction from its current level and to trend in that direction until around Expiry, then Long position on OTM CE & PE can be initiated for the reasons explained above in case of Long Strangle Strategy. However, in this strategy, both the naked Long positions are hedged by simultaneously initiating Short counter positions on even far OTM Strikes on both CE & PE sides, to mitigate for any loss on the primary Long leg(s) if the underlying fails to breakout and take a strong momentous move in any one direction shortly, because then the rangebound underlying will eat away the premium on the Long legs and Theta will further erode their premium value. To cater to such situation, the Short legs will also face erosion in their premium value and therefore will generate some profit which will mitigate the losses on the Long legs(s). Both CE Long and PE Long hedged legs are initiated on higher Delta i.e. CE Long on lower Strike and PE Long on higher Strike, than their respective hedged legs comprising of even farther OTM Strikes (i.e. CE Short on higher Strike and PE Short

on lower Strike). Consequently, Long legs pays more Premium than the premium credit received on the Short legs.

Thus, this strategy is a net premium debit strategy, which needs to be first recovered in order for this strategy to be profitable, for which the underlying must soon take a momentous move in any one direction such that the net profit will be much higher than the aggregate net premium paid on the strategy. If the underlying by Expiry remains within a range or momentum is slow and weak, then this strategy may suffer loss to the maximum extent of the aggregate net premium paid on this strategy. Both the primary and hedged leg can be initiated on the same Expiry. This strategy is, therefore, hedged Long Strangle, and is called **Reverse Iron Condor**.

Thus, suitable hedged strategies can be planned and executed to play a specific market trend with good understanding of the Options behaviour as summarised and discussed above in this Chapter and as explained in depth in Volume 1. The Strategies mentioned in the above table briefly gives the reasoning behind its design, and these Strategies along with a few other Strategies are discussed in detail in subsequent Chapters in this Volume II.

Now, we have seen thus far in this Chapter, as to how we arrive at a decision regarding which particular Strategy would be most suitable to play out a particular trend, we also need to now understand as to what are we going to do if the trend basis which a Strategy was designed and executed, did not turn out as expected. Then in such situation the whole objective should be to save the capital which may potentially be lost on the Strategy which is not going so well. This objective to further mitigate the potential loss in a hedged Strategy can be achieved by taking fresh Long and/or Short positions. This process of initiating fresh Long and/or Short positions in F&O instruments to mitigate the potential loss in the executed hedged Strategy, which is not going as originally envisaged, is generally referred to as **Adjustment of trade**.

Let us therefore now proceed to understand the process of Adjustment of trade and different Adjustment Techniques which can be employed to adjust existing trading positions in order to mitigate loss, discussed in the next Chapter.

Chapter – 2

Adjustment Techniques

Mitigating Losses

We have discussed in detail in the previous Chapter, about the steps that need to be followed and the know-how that is required, in order to plan and execute a trade through F&O instruments. As discussed, we must first identify the trend and then accordingly plan the trade and execute the trade through designing a suitable Strategy to play the trend.

But trading is a game of probability, in which a trader analyses the market information and plans a trade basis his knowledge & skill, for an outcome which seems relatively more probable to him. Having said this, the truth of the matter is, that the market may surprise a trader more than often. There are various factors which are not within the control of a trader after he has initiated his trade. There can be sudden events & announcements, which cannot be factored by any trader howsoever well informed and abreast with information relevant to the markets. There is always an overnight risk on positional trades from any untoward developments. There can also be sudden change in the price governing factors such as demand & supply, volatility, interest rates, besides many other factors which can cause disruptions and throw challenges on to a running trade, and may cause loss on such trading positions, which would obviously lead to capital depletion.

It is therefore imperative for every trader to understand the possible ways by which a trader can bring down his losses and protect his trading capital, if the analysis basis which he initiated trading positions, goes wrong. At what point, a trader can conclude, that now his trading position is not going as he planned, is a matter of technical analysis, which is not the point of focus for us in this Chapter. But once, it has been concluded that the trend has reversed and the running positions are / will not go as envisaged, then the trader must plan to mitigate the potential losses in the running trade positions. Mitigation of loss in

the running F&O positions, is done by initiating suitable Long and/or Short positions in same or other F&O instruments, in the direction of reversal or basis the then prevailing market situation. Thus, initiating fresh positions in suitable F&O instruments in order to mitigate or outrun the losses in the running trading positions is generally referred to as the **Adjustments to trade**.

Options are a dynamic instrument. Besides using them for riding a trend or hedging a trading position, the Options can also be employed to make suitable adjustments to the losing positions originally initiated whether through Futures or through Options or both.

In this Chapter, we will be focussing on the thought process basis which we can consider making appropriate adjustments to trade, keeping in mind the then prevailing market conditions, broadly, through initiating suitable Long and/or Short positions in Options, with the sole objective of mitigating the losses on the running F&O trading positions. Obviously, since, adjustments to trade requires executing fresh Long and/ or Short positions in Options, it requires extra capital deployment by the trader in addition to what is already deployed in the running trading positions. A trader must therefore spare reasonable amount from his capital to make these adjustments, should the need arise. Ideally, at any given point in time, a trader must not deploy more than 40% of his capital unless he is seasoned trader and has sufficient backup capital.

Let us now begin traversing through the thought process involved in carrying out the adjustments to losing F&O positions. The objective here is to learn about the various factors which a trader must bear in mind while deciding to carry out Adjustments to trade; and not necessarily to follow exactly the same methodologies which are discussed in this Chapter to handle a particular situation. Let us therefore focus on the various factors being discussed here in the context of Adjustments to trade under different market situations and trend reversal.

ADJUSTMENTS TO TRADE

Reversal of trend requiring Adjustments:

As discussed earlier, the first step before any particular trading position is initiated or a Strategy is executed, is to identify the trend. If the position or Strategy executed to play out the identified trend goes right, then the Strategy would obviously yield profit and a trader may consider booking the profits generated on the Strategy before Expiry of the F&O instruments involved in the trading positions. However, the problem would arise if the trend basis which the F&O trading positions were executed goes wrong. In such situation there may be a need to make adjustments to the running positions to mitigate the losses.

The following table outlines broadly the situation, when the trend as originally envisaged is no longer applicable/ sustaining and thereby meriting adjustments to the running F&O positions:

Sl. No.	Trend as originally envisaged at the time of initiating trading positions	Reversal/Trend which requires adjustments to be made to the original trading positions
1	Bullish	When original bullish trend turns mild bullish or bearish
2	Mildly Bullish	When original mild bullish trend turns bearish
3	Bearish	When original bearish trend turns mild bearish or bullish
4	Mildly Bearish	When original mild bearish trend turns bullish
5	Rangebound / sideways	When the underlying breaks out from the range and starts trending in either direction
6	Non-directional	When the underlying fails to break out / break down and gets trapped in range

	(may either breakout or breakdown from the range)	
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Thus, when the original trend is confirmed to have reversed as per the technical analysis, then the situation would require making adjustments to the running F&O positions. Let us now discuss the possible ways in which adjustments to the running positions can be made.

Objective of Adjustments:

The basic premise in an Adjustment to trade is to mitigate the potential loss after reversal of the main trend (basis which the original Strategy was initiated). The original Strategy are usually either a Debit Strategy or a Credit Strategy, from expiry perspective. The objective to carry out adjustments to these original Debit Strategy or Credit Strategy are as follows:

- In a Debit Strategy, adjustments are primarily targeted to recover the potential limited loss of Premium paid on the Strategy, in the unlikely event of the underlying not being able to cross-over the Breakeven Strike level of the Debit Strategy; and
- In a Credit Strategy, adjustments are primarily targeted to mitigate the unlimited loss situation that may arise if the underlying starts trending beyond the Breakeven Strike of the Credit Strategy.

TYPE OF ADJUSTMENTS TO TRADE

This is the primary objective in adjustments to trade depending on whether the Strategy deployed is a Debit or a Credit Strategy.

Broadly, there can be two ways by which adjustments to a losing position can be considered. These are as follows:

1. Adjustment through F&O instruments pertaining to different underlying

2. Adjustment through F&O instruments pertaining to same underlying

Both these aforesaid types of adjustments to running trading positions are discussed below.

Adjustments through F&O of different Underlying:

This type of adjustment is done by employing F&O instruments of an underlying which moves in directly inverse correlation to the underlying pertaining to which F&O positions are currently running in losses. For example: *Nifty may have an inverse relationship with Gold. Thus, if bullish positions/ Strategy was initiated on Nifty through F&O instruments pertaining to Nifty, and the Nifty trend reverses on the bearish side then a bullish position(s) may be initiated on Gold through its F&O instruments. Idea here is to absorb the losses on the bullish positions initiated on Nifty, by initiating fresh bullish positions on Gold F&O instruments (either naked or hedged, depending upon our view on the movement in Gold prices).*

Thus, in the above example, adjustments involved initiating fresh positions on Gold F&O instruments on the bullish side, in order to curtail / outrun the losses on the bullish Strategy initiated on Nifty originally. The bullish position on Gold F&O instruments, may need to be initiated on atleast double the quantity than the Nifty bullish trading positions (as originally initiated) so as to suitably outrun / absorb the losses in the Nifty positions.

However, the drawback of employing this kind of Strategy are two folds: (i) the other second underlying may not necessarily go in inverse direction of the first underlying on which original trading positions were initiated, due to changed market dynamics, geopolitical and economical tussle; and (ii) the second underlying (which is being contemplated for initiating positions as adjustments) may not give a sound technical go-ahead to play out the trend in the opposite direction to the first underlying on which original positions were initiated. Thus, such adjustments may have to be carefully weighed before putting into effect merely on the reasoning that the underlyings have historically demonstrated trends in opposite directions.

Let us now explore adjustments initiated on the same underlying on which the original trading positions were initiated.

Adjustments through F&O of same Underlying:

This type of adjustment mode is pretty straightforward in terms of choice of the underlying F&O instruments, for employing them as adjustments to the running trading positions. That is: if the original trading positions were initiated employing Nifty's F&O instruments to play out a bullish trend on Nifty index, and subsequently if there is a reversal of the trend in Nifty on the bearish side, then we would contemplate making adjustments to the running bullish trading positions/ Strategy on Nifty, by employing F&O instruments pertaining to Nifty (and not any other underlying), in order to play out the new trend of Nifty, with the objective to mitigate the losses arising on the running bullish positions on Nifty F&O instruments (originally initiated).

Now, whenever there arises the need to make adjustments to the running F&O trading positions, the possible adjustments broadly speaking which may be made, can be categorised into the following two categories:

- A. Adjustments through countering the original trading position;
and
- B. Adjustments through pyramiding.

These two categories of adjustments are discussed below.

ADJUSTMENTS THROUGH COUNTERING

This simply means initiating trading positions in more quantity (than the original trading quantity) of suitable F&O instruments, with higher Delta value (than the Delta value of the original trading Strategy), in the direction of the reversed trend (which is in opposite direction of the original trend basis which running F&O positions/ Strategy was executed originally). That is: if the original trend in Nifty was bullish and the trend was being played out by initiating some bullish trading positions / Strategy by employing F&O instruments of Nifty, then in order to make counter adjustments upon reversal of the bullish trend

towards bearish side, we would contemplate initiating fresh Nifty F&O positions/ Strategy with more quantity and higher delta on the bearish side (than the delta value of the bullish position). Thus, initiating positions on the opposite side of the original trend is called **Counter Adjustments** or **Adjustment through Countering** the original position.

This adjustment may be done only by deploying naked Options positions or hedged Strategies to play out the trend reversal.

Counter Adjustments through Long or Short Options:

However, the most important aspect in Counter Adjustment is to consider if the trend reversal needs to be played through favourable Long Options or favourable Short Options. That is: if the original trend of Nifty has reversed from bullish to bearish, then the Counter Adjustments need to be planned basis whether we must play the bearish reversal through Long PE or Short CE. Likewise, if the original trend of Nifty has reversed from bearish to bullish, then the Counter Adjustments need to be planned basis whether we must play the bullish reversal through Long CE or Short PE. The answer to this is as follows:

- If the reversal seems to be with momentum, which is expected to sustain and the trend to continue, then we must make counter Adjustment positions by employing Long Options in the direction of the current trend upon reversal. For example, bearish reversal can be played through PE Long and bullish reversal through CE Long.
- If the reversal seems to be slow (not with momentum) or likely to remain rangebound or the reversal is with momentum but does not seem last, then we must make counter Adjustment positions by employing Short Options in the direction of the current trend upon reversal. For example, bearish/mild bearish reversal can be played through CE Short and bullish/mild bullish reversal through PE Short.

Thus, whether or not there seems to be a sustaining momentum basis technical analysis, is the key factor for determining if the counter Adjustments should be initiated with Long Option positions or Short Option positions.

However, initiating Short Options positions would require more capital and may also have to meet the MTM requirements.

The significance of Counter Adjustments is that it can be used for both mild and super reversals. Mild reversals are played through Short Options and super reversal having momentum are played through Long Options.

Counter Adjustments through Delta positions:

Higher Delta on positions in Counter Adjustments:

Second most important factor, after determining whether the trend reversal should be played out through Long Option positions or Short Option positions, is the aggregate Delta value of the positions initiated as part of Counter Adjustments.

The positions on the Counter Adjustments must have an aggregate higher Delta (than the aggregate Delta on the original position) in the direction of the current trend after reversal. This higher Delta requirement on the Counter Adjustment positions can be met by, either selecting higher Delta Strike or increasing quantity on lower Delta Strike (thereby achieving higher Delta than the original position):

Thus, if the original bullish trend reverses on the bearish side, then such bearish reversal can be played through few PE Long on such higher Strike, which can on aggregate basis make up for higher Delta for the counter position (than the aggregate Delta on the original position); or through more quantity of PE Long on lower Strike, which can on aggregate basis make up for higher Delta for the bearish counter position (than the aggregate Delta on the original position). However, bearish reversal through CE Short must be preferably played through Far OTMs. This is because, if the trend again reverses on the bullish side, then the PE Long counter positions may suffer limited loss (to the extent of Premium paid), but CE Short may suffer unlimited loss if it is near ATM Strike as it will go in the money should there arrives a bullish trend again.

Likewise, if the original bearish trend reverses on the bullish side, then such bullish reversal can be played through few CE Long on such lower Strike, which

can on aggregate basis make up for higher Delta for the counter position (than the aggregate Delta on the original position); or through more quantity of CE Long on higher Strike, which can on aggregate basis make up for higher Delta for the bullish counter position (than the aggregate Delta on the original position). However, bullish reversal through PE Short must be preferably played through Far OTMs. This is because, if the trend again reverses on the bearish side, then the CE Long counter positions may suffer limited loss (to the extent of Premium paid), but PE Short may suffer unlimited loss if it is near ATM Strike as it will go in the money should there arrives a bearish trend again.

Delta shifting in Counter Adjustments:

When Counter Adjustments are planned through overall higher Delta on the adjustment positions (than the original trading position), then the same may be implemented and played through Delta shifting mechanism. Therefore:

- if the original bullish trend reverses on the bearish side, then such bearish reversal can be played through Delta shifting mechanism by buying PEs as Near OTMs / slightly Far OTMs (i.e. those PEs having Delta values per Lot basis, ranging from 0.3 to 0.45). Once these Near OTM PEs / slightly Far OTM PEs becomes an ITM, then these PEs can be booked and if the bearish reversal seems to continue, then again fresh set of Near OTM PEs / slightly Far OTM PEs (i.e. those PEs having Delta values per Lot basis, ranging from 0.3 to 0.45) can be bought, in order to continue to ride the bearish reversal as an Counter Adjustment to the original bullish side trading positions. This process of initiating fresh lower Deltas (and booking them at profit), time and again to ride the bearish momentum is **PE side Delta shifting (through Long Options) based Counter Adjustment to play the bearish side reversal**. In this Delta shifting based Counter Adjustment, it is ensured that if the trend reversal fails upon initiating the Counter Adjustment trading positions, then the loss on these positions will be relatively less (as they are on lower Delta), as compared to the Counter Adjustment trading positions initiated on per Lot higher Delta PEs (like ITMs / deeper ITMs).

This bearish reversal can also be played through **CE side Delta shifting (through Short Options) Counter Adjustment**. In this case, the bearish reversal can be targeted through Delta shifting by initiating Counter Adjustments on Far OTM CEs having Delta value around the range of 0.3 to 0.20 per Lot sorts. This position is booked when the profit is generated on these Short CEs, when the CE Strike becomes even Far OTM due to bearish move in the underlying and the Ce Strikes moves to even lower Delta value like 0.15 or less. If the bearish move in the underlying appears to continue, then again a fresh Short CE is initiated at a relatively higher Delta value like 0.3 to 0.2 per Lot, on which profit is booked again as this Strike too becomes an even farther OTM due to bearish move in the underlying.

- if the original bearish trend reverses on the bullish side, then such bullish reversal can be played through Delta shifting mechanism by buying CEs as Near OTMs / slightly Far OTMs (i.e. those CEs having Delta values per Lot basis, ranging from 0.3 to 0.45). Once these Near OTM CEs / slightly Far OTM CEs becomes an ITM, then these CEs can be booked and if the bullish reversal seems to continue, then again fresh set of Near OTM CEs / slightly Far OTM CEs (i.e. those CEs having Delta values per Lot basis, ranging from 0.3 to 0.45) can be bought, in order to continue to ride the bullish reversal as an Counter Adjustment to the original bearish side trading positions. This process of initiating fresh lower Deltas (and booking them at profit), time and again to ride the bullish momentum is **CE side Delta shifting based Counter Adjustment to play the bullish side reversal**. In this Delta shifting based Counter Adjustment, it is ensured that if the trend reversal fails upon initiating the Counter Adjustment trading positions, then the loss on these positions will be relatively less (as they are on lower Delta), as compared to the Counter Adjustment trading positions initiated on per Lot higher Delta CEs (like ITMs / deeper ITMs).

This bullish reversal can also be played through **PE side Delta shifting (through Short Options) Counter Adjustment**. In this case, the bullish

reversal can be targeted through Delta shifting by initiating Counter Adjustments on Far OTM PEs having Delta value around the range of 0.3 to 0.20 per Lot sorts. This position is booked when the profit is generated on these Short PEs, when the PE Strike becomes even Far OTM due to bullish move in the underlying and the PE Strike moves to even lower Delta value like 0.15 or less. If the bullish move in the underlying appears to continue, then again a fresh Short PE is initiated at a relatively higher Delta value like 0.3 to 0.2 per Lot, on which profit is booked again as this Strike too becomes an even farther OTM due to bullish move in the underlying.

The decision whether or not to buy a lower Delta Options for the purpose of Counter Adjustments through Delta shifting, will depend on the expected momentum in the trend reversal. This Delta shifting for Counter Adjustment, through Long Options positions, must only be implemented when the trend reversal is expected to be strong and last, else Delta shifting based Counter Adjustment through Short Options position can be explored.

Counter Adjustments to Net Premium Credit - Debit:

Every original Options positions/ Strategies, which is initiated to play out a trend, is effectively, either:

- (i) a Debit position (*i.e. where Premiums are paid on Long legs; or more Premiums are paid on Long legs than the Premium credit received on Short legs*); or
- (ii) a Credit position (*i.e. where Premium credits are received on Short legs; or more Premiums credits are received on Short legs than the Premium paid on the Long legs*).

Therefore, when the original Options positions/ strategies goes wrong, on account of trend reversal or otherwise, then the Counter Adjustments need to also factor in the following considerations:

- (i) If the original Options position/ Strategy is a Premium Debit positions/Strategy, then the Counter Adjustments must be targeted to save the loss of the Premium debit incurred on the original Strategy. This can be achieved by initiating Short Options

positions in the direction of trend reversal², at far OTM Strikes, with such large quantity so as to have an effective Delta higher than the Delta value of the original Strategy. Here the objective must be to have as much Premium credit on Short Options (contemplated as part of Counter Adjustments) so as to be able to recover the Premium debit incurred on the original Strategy.

However, if the original Strategy involves a Futures leg (or huge Premium debit positions in large quantities) and the trend reversal is with strong momentum, then the Short Options position (contemplated as part of Counter Adjustments) may have the limitation of being able to generate limited profits to the maximum extent of the Premium credits received on the Short Options positions initiated as part of Counter Adjustments, and thus may not be able to sufficiently cover up for the losses incurred on the original Strategy. This limitation can be mitigated by, either:

- a) initiating numerous successive batches of Short Options positions (favourable to the direction of the reversed trend), in large quantities, initiated one after the other i.e. as soon as the one batch of Short Options position is exhausted of its Premium and the momentum in the direction of the trend reversal is still continuing, a successive batch of Short Options positions (favourable to the direction of the reversed trend) can be initiated after booking profit on the earlier batch of Short Options; or
- b) to play such momentum in the direction of reversed trend though initiating Long Options positions, with such large quantity so as to have an effective Delta higher than the Delta value of the original Strategy, as part of Counter Adjustments to the original Strategy. The objective is that these Long Options must yield greater / reasonable profit so as to be able

² i.e. PE Short to play trend reversal towards bullish/ mild bullish; and through CE Shorts to play trend reversal towards bearish/ mild bearish.

to absorb the max loss on the original Debit strategy to the tune of Premium paid, as the reversed trend continues with momentum. as part of Counter Adjustments to the original Strategy. Since, initiating Long Options positions as Counter Adjustments, will create Premium debit positions, therefore, such Long Options positions must only be initiated as part of Counter Adjustment when the strong lasting momentum is expected on the trend reversal.

- (ii) If the original Options position/ Strategy is a Premium Credit positions/Strategy (or involves a Futures leg), then the Counter Adjustments must be targeted to save the max unlimited loss situation that may arise on account of the Short Options position or Futures position in the original Strategy. This can be achieved by initiating Short Options positions in the direction of trend reversal³, at far OTM Strikes, with such large quantity so as to have an effective Delta higher than the Delta value of the original Strategy. Here the objective must be to have as much Premium credit on Short Options (contemplated as part of Counter Adjustments) so as to be able to mitigate the loss likely to be incurred on the original Strategy.

However, if the original Strategy involves huge Premium credit positions in large quantities on account of Short Options positions (or Futures leg) and the trend reversal is with strong momentum, then the Short Options position (contemplated as part of Counter Adjustments) may have the limitation of being able to generate limited profits to the maximum extent of the Premium credits received on the Short Options positions initiated as part of Counter Adjustments, and thus may not be able to sufficiently cover up for the losses incurred on the original Strategy. This limitation can be mitigated by, either:

- a) initiating numerous successive batches of Short Options positions (favourable to the direction of the reversed trend), in

³ i.e. PE Short to play trend reversal towards bullish/ mild bullish; and through CE Shorts to play trend reversal towards bearish/ mild bearish.

large quantities, initiated one after the other i.e. as soon as the one batch of Short Options position is exhausted of its Premium and the momentum in the direction of the trend reversal is still continuing, a successive batch of Short Options positions (favourable to the direction of the reversed trend) can be initiated after booking profit on the earlier batch of Short Options; or

- b) to play such momentum in the direction of reversed trend though initiating Long Options positions, with such large quantity so as to have an effective Delta higher than the Delta value of the original Strategy, as part of Counter Adjustments to the original Strategy. The objective is that these Long Options must yield greater / reasonable profit as compared to the loss being incurred on the original Credit strategy, as the reversed trend continues with momentum. Since, initiating Long Options positions as Counter Adjustments, will create Premium debit positions, therefore, such Long Options positions must only be initiated as part of Counter Adjustment when the strong lasting momentum is expected on the trend reversal.

Strike Selection for Counter Adjustments:

Counter Adjustment positions through Options, are therefore, decided after taking into account all the abovementioned factors, namely:

- i. Counter Adjustment positions to be initiated in the direction of the reversed trend (i.e. in opposite direction of the original trend basis which running F&O positions/ Strategy was executed). Thus, if the original trend has reversed and turned bearish / mild bearish, then adjustments are done initiating Long PEs or Short CEs; and if the trend has reversed and turned bullish / mild bullish, then adjustments are done initiating Long CEs or Short PEs.
- ii. Counter Adjustment positions must be initiated at a higher aggregate Delta value than the Delta value of the original Strategy.

- iii. Counter Adjustment positions should also factor the Options Premium debit/ credit situation in the original Strategy.
- iv. And finally, depending upon whether the trend reversal is in momentum or not, Counter Adjustment positions may employ Long Options or Short Options.

Thus, basis the aforementioned factors, Counter Adjustment positions must be initiated through Options at suitable Strike levels.

Illustrations of Counter Adjustment techniques:

The following table will indicatively explain about the Positions and Strike levels that may be considered for initiating Counter Adjustment positions taking into account all the above mentioned factors discussed above in the context of Counter Adjustments (also refer to the note section in the Tables below):

Original Strategy/ positions(naked / hedged)	Trend Reversal	Selection of Strike levels for Counter Adjustments
Bullish / Mild Bullish	Bearish momentum	Long PE with such quantities on ITM or OTM Strikes so as to have aggregate Delta more than the aggregate Delta on original Strategy. Idea is to play trend reversal on bearish momentum, through higher Delta PE Long counter positions, to cover/mitigate potential loss on the original Strategy; or Short CE with such quantities on far OTM Strikes so as to have aggregate Delta more than the aggregate Delta on original Strategy. Also, idea is to get sufficient Premium credit on Short CEs, so as to cover/mitigate potential loss in original Strategy. In order to do so, successive batches of far OTM CEs may need to be Shorted as and when the previous batch of CE Short have exhausted their Premium value, and

		the bearish momentum is still trending and continuing.
Bullish / Mild Bullish	Mild Bearish	Short CE with such quantities on far OTM Strikes so as to have aggregate Delta more than the aggregate Delta on original Strategy. Also, idea is to get sufficient Premium credit on Short CEs, so as to cover/mitigate potential loss in original Strategy.
Bearish / Mild Bearish	Bullish momentum	Long CE with such quantities on ITM or OTM Strikes so as to have aggregate Delta more than the aggregate Delta on original Strategy. Idea is to play trend reversal on bullish momentum, through higher Delta CE Long counter positions, to cover/mitigate potential loss on the original Strategy; or Short PE with such quantities on far OTM Strikes so as to have aggregate Delta more than the aggregate Delta on original Strategy. Also, idea is to get sufficient Premium credit on Short PEs, so as to cover/mitigate potential loss in original Strategy. In order to do so, successive batches of far OTM PEs may need to be Shorted as and when the previous batch of PE Short have exhausted their Premium value, and the bullish momentum is still trending and continuing.
Bearish / Mild Bearish	Mild Bullish	Short PE with such quantities on far OTM Strikes so as to have aggregate Delta more than the aggregate Delta on original Strategy. Also, idea is to get sufficient Premium credit on Short PEs, so as to cover/mitigate potential loss in original Strategy.
Rangebound	Bullish momentum	Long CE with such quantities on ITM or OTM Strikes so as to have aggregate Delta more than the aggregate Delta on the bearish leg of original

	range Breakout	Strategy (i.e. <i>Futures Short and/or CE Short and/or PE Long, as the case may be</i>). Idea is to play bullish momentum breakout trend, through higher Delta CE Long counter positions, to cover/mitigate potential loss on the original Strategy; or Short PE with such quantities on far OTM Strikes so as to have sufficient Premium credit on Short PEs, in order to cover/mitigate potential loss in original Strategy. In order to do so, successive batches of far OTM PEs may need to be Shorted as and when the previous batch of PE Short have exhausted their Premium value, and the bullish momentum is still trending and continuing.
Rangebound	Mild Bullish range Breakout	Short PE with such quantities on far OTM Strikes so as to have aggregate Delta more than the aggregate Delta on the bearish leg of original Strategy (i.e. <i>Futures Short and/or CE Short and/or PE Long, as the case may be</i>). Also, idea is to get sufficient Premium credit on Short PEs, so as to cover/mitigate potential loss in the original Strategy.
Rangebound	Bearish momentum range Breakdown	Long PE with such quantities on ITM or OTM Strikes so as to have aggregate Delta more than the aggregate Delta on the bullish leg of original Strategy (i.e. <i>Futures Long and/or PE Short and/or CE Long, as the case may be</i>). Idea is to play bearish momentum breakdown trend, through higher Delta PE Long counter positions, to cover/mitigate potential loss on the original Strategy; or Short CE with such quantities on far OTM Strikes so as to have sufficient Premium credit on Short CEs, in order to cover/mitigate potential loss in original Strategy. In order to do

		so, successive batches of far OTM CEs may need to be Shorted as and when the previous batch of CE Short have exhausted their Premium value, and the bearish momentum is still trending and continuing.
Rangebound	Mild Bearish range Breakdown	Short CE with such quantities on far OTM Strikes so as to have aggregate Delta more than the aggregate Delta on the bullish leg of original Strategy (i.e. <i>Futures Long and/or PE Short and/or CE Long, as the case may be</i>). Also, idea is to get sufficient Premium credit on Short CEs, so as to cover/mitigate potential loss in the original Strategy.
Non-directional breakout/ breakdown Strategy	Breakout/ Breakdown with momentum does not arrive or fails (i.e. underlying gets rangebound)	Short CEs and Short PEs with such number of equal quantities on far OTM Strikes (outside the possible range). Idea is to get sufficient Premium credit on Short CEs and Short PEs, collectively, so as to cover/mitigate potential loss in the original Strategy (or to have aggregate Premium credit more than the Premium paid for on the original Strategy).
Non-directional breakout/ breakdown Strategy	Mild Breakout instead of Strong Breakout with momentum	Short PEs with such quantities on far OTM Strikes so as to have sufficient Premium credit on Short PEs, in order to cover/mitigate potential loss in the original Strategy (or to have aggregate Premium credit more than the Premium paid for on the original Strategy).
Non-directional breakout/ breakdown Strategy	Mild Breakdown instead of Strong Breakdown	Short CEs with such quantities on far OTM Strikes so as to have sufficient Premium credit on Short CEs, in order to cover/mitigate potential loss in the original Strategy (or to have

	with momentum	aggregate Premium credit more than the Premium paid for on the original Strategy).
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Note:

- Long Options positions in the aforementioned Counter Adjustments must be of the current Expiry series only if the Expiry is still far, in order to avoid Theta impact. However, if the Expiry is near, then in order to avoid the impact of Theta decay, Long Options of subsequent farther Expiry series may be considered to initiate positions for Counter Adjustments.
- Long Options are being contemplated as part of counter Adjustments, as against Futures position, because the Long Options position will have limited risk to the extent of Premium paid on them (whereas Futures positions would have unlimited risk) if the trend again reverses back to the direction of the original Strategy.
- Short Options positions in the aforementioned Counter Adjustments must be of the current Expiry series, so as to get benefit of the increasing Theta impact due to approaching Expiry. The Short Options for Counter Adjustments must be of the same Expiry series as that of the closer Expiry series in the original Strategy. However, if the Premium in the closer Expiry series is less (due to low volatility or otherwise), then large quantities at smaller available Premium values may be considered (*i.e. more decay on large Short quantities*); or else even large quantities on subsequent farther Expiry series may also be considered to get benefitted from lower decay on much large quantities of Short positions (*i.e. lower decay on even much larger quantities with higher Premium values*).
- Short Options positions, as part of Counter Adjustments, must be initiated at such far OTM Strikes, which are reasonably expected to expire worthless as OTM by Expiry, i.e. CE Shorts must be above the upper resistance level where the underlying is not expected to cross by Expiry and the PE Shorts must be below the lower support level where the underlying is not expected to cross by Expiry.
- Counter Adjustments involving Short Options positions may require huge capital and compliance towards MTM requirements.
- The Counter Adjustments may be implemented through naked Options positions or through relevant hedged Strategies favourable to the direction / type of the trend reversal requiring adjustments to the original trade.

However, hedged strategies will require relatively much larger quantities than the naked positions for implementing relevant adjustments.

- If Volatility is in rising state then Counter Adjustments through Long Options must be considered; and if Volatility is in falling state then Counter Adjustments through Short Options must be considered.

Now, basis the aforesaid understanding about the possible trading positions which can be initiated as part of Counter Adjustment to the existing positions, we can explore different possible Counter Adjustments that may be employed to different types of trading positions, in order to mitigate the losses on such existing positions in case of trend reversal. This is discussed below.

Different Counter Adjustment Techniques:

Let us now look at some situations to understand the logic with which certain Counter Adjustment techniques can be employed, in case of trend reversal. Primarily, the logic to use **these adjustment techniques, are based on Net Premium Debit / Credit situation or bringing in the Delta variance in the overall trading positions/ Strategy**, as already explained above.

Here for the purpose of understanding the core concept of making suitable Counter Adjustments in a trading position, we will discuss the naked positions of FNO. This will help us understand the logic to be applied to Counter Adjust the leg which may cause the overall trading positions/ Strategy into loss.

Let us explore a few situations, and possible Counter Adjustment options that may be employed upon occurrence of trend reversal, depending on varied market dynamics.

We have used below the nomenclature of certain Strategies. Please do not feel uncomfortable with these nomenclatures. For now, just focus on the possible Counter Adjustment measures that may be employed to adjust a loss causing leg. A detailed study on all the Strategies referred to here, is given on subsequent Chapters. You may consider to refer to the relevant Strategies in the subsequent Chapters, should you wish to understand about those Strategies in detail.

(i) **Adjustment of a Naked CE Long position:**

Original Position: CE Long (<i>bullish view</i>)
Trend Reversal: Bearish / Mild Bearish
Logic of the Adjustments: To set-off the possible loss on the Premium paid for the CE Long due to reversal on the Bearish / Mild Bearish side, through collecting Premium Credit by Shorting relevant CEs. The adjustments discussed below are all Counter Adjustment measures.
Adjustment-1: Converting naked CE into CE Ratio Credit Spread. Short Far OTM CEs (<i>i.e. CEs of much higher Strike than CE Long leg</i>) in more quantity than the CEs on Long leg. This will convert naked CE into CE Ratio Credit Spread. Ensure that Premium Credit received on CE Short is more than the Premium paid on the CE Long leg (by selling more quantity of Far OTM CE). Logic for Adjustment-1: Premium paid on CE Long leg, can be set-off by the Premium Credit received on the CE Short leg initiated towards adjustment as part of CE Ratio Spread, if the trend remains towards bearish / mild bearish side (thus, CEs shorted expire worthless as OTMs on Expiry thereby generating profit higher than the loss generated by the CE Long leg). However, if the trend again reverses on the bullish side, such that it appears that the underlying may breach the CE Short Strike by Expiry of the CE Long leg, then these CE Shorts must be adjusted by taking more CE Long of same or preferably higher Expiry series (than that of the CE Short leg) as explained below in relation to Adjustment for naked CE Shorts.
Adjustment-2: Converting naked CE into Bear CE Credit Spread. In the event, reversal towards bearish side is strong and confirmed, then Short CEs of lower Strike than CE Long leg. This will convert naked CE into Bear CE Credit Spread. • <i>In Bear CE Credit Spread, CE Short shall be of the same quantity as that of the CE Long leg. The net Premium credit (i.e. Premium received on CE Short leg</i>

minus Premium paid on CE Long leg), shall be the max profit in this Strategy, from Expiry perspective.

- *Ensure that Premium Credit received on CE Short is more than the Premium paid on the CE Long leg (by Shorting CEs of such lower Strike which offers decent Premium Credit).*
- *However, if upon bearish reversal, naked CE Long position is adjusted subsequently by Shorting CEs of any given lower Strike than CE Long leg Strike, then there may be a possibility that the Premium credit received on the CE Short leg would be less than the Premium already paid on the Long leg. Thus, in this scenario, there will be a net Premium debit situation on the Bear CE Credit Spread; and the net Premium debit shall be the max loss in this Strategy. This net Premium debit, may be attempted to be recovered by shorting some extra Far OTM CEs aggregating to atleast net Premium debit or more.*

Logic for Adjustment-2: Premium paid on CE Long leg, will be lower than the Premium Credit received on the CE Short leg initiated towards adjustment as part of Bear CE Credit Spread. The Net Premium Credit on the Spread will be the expected profit from Expiry perspective. Further, strong bearish move will favour the Delta move on this Bear CE Credit Spread to set-off potential loss on CE Long leg.

Adjustment-3: Converting naked CE into Futures Hedge (Bearish side).

In the event, reversal towards bearish side is strong and confirmed, then Short Futures. This will convert naked CE into **Futures Hedge (Bearish side)**.

Futures Short shall be of the same quantity and Expiry series as that of the CE Long.

Logic for Adjustment-3: Futures will have a Delta of 1 (per Lot basis), and will be higher than the Delta on the CE Long leg (per Lot basis). Therefore, effectively, the net Delta of Futures Hedge (Bearish side) shall favour the bearish move in the underlying. Thus, as the downtrend continues, Futures Short leg would generate more profit than the loss incurred on the CE Long leg. Further, the max loss on the CE Long leg due to continued downtrend will be limited to the amount of Premium paid; while the potential profit on the Futures Short leg due to continued downward move in the underlying would be unlimited.

Thus, in the event of confirmed reversal on the bearish side, this Futures Hedge (Bearish side) Strategy may be implemented, to take advantage of the Delta move of Futures Short leg.

Further, there will not be any Theta impact on the Futures leg and hence this position can be held close to Expiry to take full advantage of the unlimited profit potential on a continued downward move of the underlying. Also, there will not be any adverse impact of rise or fall in volatility / VIX on this Futures Hedge (Bearish side) Strategy, and thus can be held with conviction so long the underlying is in a downtrend.

Adjustment-4: Converting naked CE into Bull CE Debit Spread.

In the event reversal towards bearish side is unsure, or if the CE Long leg does not seem to generate desired profit, then potential loss on CE Long leg may be set-off to some extent by Shorting Far OTM CEs of higher Strike than CE Long leg. This will convert naked CE into **Bull CE Debit Spread**.

- *In Bull CE Debit Spread, Far OTM CE Short shall be of the same quantity as that of the CE Long leg. The net Premium debit (i.e. Premium paid on CE Long minus Premium credit received on CE Short leg), shall be the max loss in this Strategy, from Expiry perspective. This net Premium debit, may be attempted to be recovered by Shorting some extra Far OTM CEs aggregating to atleast net Premium debit or more. If more quantity of Far OTM CE is shorted than those on CE Long leg, such that the aggregate Premium Credit on CE Short leg is more than the Premium debit on the CE Long leg, then the Strategy will not be Bull CE Debit Spread but CE Ratio Spread (already discussed above as Adjustment 1).*
- *Ensure that Premium Credit received on Far OTM CE Short is not too low than the Premium paid on the CE Long leg.*

Logic for Adjustment-4: Premium paid on CE Long leg, will be higher than the Premium Credit received on the CE Short leg initiated towards adjustment as part of Bull CE Debit Spread. The Net Premium Debit on the Spread will be the max loss from Expiry perspective. The idea in this adjustment is that the potential loss in the CE Long leg, due to bearish/ mild bearish trend reversal, will be largely set-off from the premium credit received on the CE short leg. Further, if the trend again changes on the bullish side, then CE Long will generate more profit than the loss generated by the CE Short leg, hence, this Strategy (both Long & Short legs) can be continued if the trend again changes towards bullish side.

Important points in relation to aforesaid Counter Adjustments:

The logic in all the aforesaid Counter Adjustments is that upon reversal of trend on the bearish or mild bearish side, the potential loss on the CE Long leg must be

attempted to be recovered by collecting Premiums through Shorting CEs or Shorting Futures.

Since, these Counter Adjustments require initiating CE Short / Futures Short positions therefore more capital would be needed in order to sell CEs or Short Futures. However, since, there are already CE Long against which CE Shorts / Futures Short are initiated therefore initiating these CE Shorts/ Futures Short will effectively require lower margins as compared to the capital required for initiating naked Short Options / Futures.

Further, in order to consider an appropriate Adjustment technique, one must also consider the: (i) state of volatility VIX; and (ii) strength of trend reversal on bearish side. Accordingly, if the volatility / VIX is in rising state and bearish trend is in strong momentum, then it may be advisable to initiate Counter Adjustments using Futures Short (instead of using CE Short). However, if the volatility / VIX is stable or in falling state, and bearish trend is not in strong momentum, then it may be advisable to initiate Counter Adjustments using CE Short (instead of using Futures Short).

Lastly, in order to look for Shorting CEs, following key factors must be borne in mind:

- Do not exit the CE Long leg, instead try to recover losing Premium on Long leg by Shorting Far OTM CEs in higher quantities.
- Try to get Premium credit of an amount closer or more than the Premium paid for the CE Long leg.
- Try to get Premium credit by Shorting Far OTM CEs (*avoid Shorting CEs of Strike lower than the CE Long leg, unless strong bearish trend is confirmed, as mentioned above*). Idea here is to ensure that the Far OTM CEs must be of those Strikes which are not expected to be breached by the underlying on the upside by the Expiry. This is important so as to ensure that there is no risk even if the bearish side again reverses and gets mild bullish;
- It is better to add more quantity of CE Shorts to get the desired Premium Credit, rather than compromising on the Strike and choosing a lower CE OTM Strike closer to ATM (in order to get higher Premium Credit with fewer quantity of CEs) than higher CE Strike Far OTM for CE Short leg. This will save the Adjustment made in case of any subsequent reversal on the mild bullish side.
- If there is safe opportunity then it is advisable to keep booking profit on CE Short leg, and re-create the CE Short position (if needed, by moving CE

Short positions at lower Strikes with relatively more Premium) in same or farther Expiry series. Idea is to take benefit of favourable Delta move on CE Short leg during continuation of bearish trend.

- Try to get Premium credit on the same or closer Expiry series than the Expiry series of the CE Long leg. This will help get the Theta to work on the CEs Shorted in order to generate quick profit even if the bearish trend is not swift.
- In case there isn't enough Premium credit available on Far OTM CEs of the same or closer Expiry series, then Far OTM CEs of immediately next higher Expiry series may also be considered. However, in this case, the trend must either be bearish or mildly bearish; then only the CE short initiated at this next Expiry series will benefit to recover loss on the CE Long leg. But if the trend ceases to remain bearish/ mild bearish, and again reverses on the bullish side, then these CE Shorts initiated at next Expiry series will not work (as both Theta and Delta will not be favourable); in which case these CE Shorts must either be immediately exited at minor loss or these CE Shorts must be adjusted by taking more CE Longs of same or preferably higher Expiry series (than that of the CE short leg) as explained below in relation to Adjustment for naked CE Shorts.

(ii) Adjustment of a Naked PE Long position

Original Position: PE Long (*bearish view*)

Trend Reversal: Bullish / Mild Bullish

Logic of the Adjustments: To set-off the possible loss on the Premium paid for the PE Long due to reversal on the Bullish / Mild Bullish side, through collecting Premium Credit by Shorting relevant PEs. The adjustments discussed below are all Counter Adjustment measures.

Adjustment-1: Converting naked PE into PE Ratio Credit Spread.

Short Far OTM PEs (*i.e. PEs of much lower Strike than PE Long leg*) in more quantity than the PEs on Long leg. This will convert naked PE into **PE Ratio Credit Spread**.

Ensure that Premium Credit received on PE Short is more than the Premium paid on the PE Long leg (by selling more quantity of Far OTM PEs).

Logic for Adjustment-1: Premium paid on PE Long leg, can be set-off by the Premium Credit received on the PE Short leg initiated towards adjustment as part of PE Ratio Spread, if the trend remains towards bullish / mild bullish side (thus, PEs shorted expire worthless as OTMs on Expiry thereby generating profit higher than the loss generated by the PE Long leg). However, if the trend again reverses on the bearish side, such that it appears that the underlying may breach the PE Short Strike by Expiry of the PE Long leg, then

these PE Shorts must be adjusted by taking more PE Long of same or preferably higher Expiry series (than that of the PE Short leg) as explained below in relation to Adjustment for naked PE Shorts.

Adjustment-2: Converting naked PE into Bull PE Credit Spread.

In the event, reversal towards bullish side is strong and confirmed, then Short PEs of higher Strike than PE Long leg. This will convert naked PE into **Bull PE Credit Spread**.

- *In Bull PE Credit Spread, PE Short shall be of the same quantity as that of the PE Long leg. The net Premium credit (i.e. Premium received on PE Short leg minus Premium paid on PE Long leg), shall be the max profit in this Strategy, from Expiry perspective.*
- *Ensure that Premium Credit received on PE Short is more than the Premium paid on the PE Long leg (by Shorting PEs of such higher Strike which offers decent Premium Credit).*
- *However, if upon bullish reversal, naked PE Long position is adjusted subsequently by Shorting PEs of any given higher Strike than PE Long leg Strike, then there may be a possibility that the Premium credit received on the PE Short leg would be less than the Premium already paid on the Long leg. Thus, in this scenario, there will be a net Premium debit situation on the Bull PE Credit Spread; and the net Premium debit shall be the max loss in this Strategy. This net Premium debit, may be attempted to be recovered by shorting some extra Far OTM PEs aggregating to atleast net Premium debit or more.*

Logic for Adjustment-2: Premium paid on PE Long leg, will be lower than the Premium Credit received on the PE Short leg initiated towards adjustment as part of Bull PE Credit Spread. The Net Premium Credit on the Spread will be the expected profit from Expiry perspective. Further, strong bullish move will favour the Delta move on this Bull PE Credit Spread to set-off potential loss on PE Long leg.

Adjustment-3: Converting naked PE into Futures Hedge (Bullish side).

In the event, reversal towards bullish side is strong and confirmed, then Long Futures. This will convert naked CE into **Futures Hedge (Bullish side)**.

Futures Long shall be of the same quantity and Expiry series as that of the PE Long.

Logic for Adjustment-3: Futures will have a Delta of 1 (per Lot basis), and will be higher than the Delta on the PE Long leg (per Lot basis). Therefore, effectively, the net Delta of Futures Hedge (Bullish side) shall favour the bullish move in the underlying. Thus, as the uptrend continues, Futures Long leg would generate more profit than the loss incurred on the PE Long leg. Further, the max loss on the PE Long leg due to continued uptrend will be limited to the amount of Premium paid; while the potential profit on the Futures Long leg due to continued upward move in the underlying would be unlimited.

Thus, in the event of confirmed reversal on the bullish side, this Futures Hedge (Bullish side) Strategy may be implemented, to take advantage of the Delta move of Futures Long leg.

Further, there will not be any Theta impact on the Futures leg and hence this position can be held close to Expiry to take full advantage of the unlimited profit potential on a continued upward move of the underlying. Also, there will not be any adverse impact of rise or fall in volatility / VIX on this Futures Hedge (Bullish side) Strategy and thus can be held with conviction so long the underlying is in an uptrend.

Adjustment-4: Converting naked PE into Bear PE Debit Spread.

In the event reversal towards bullish side is unsure, or if the PE Long leg does not seem to generate desired profit, then potential loss on PE Long leg may be set-off to some extent by Shorting Far OTM PEs of lower Strike than PE Long leg. This will convert naked PE into **Bear PE Debit Spread**.

- *In Bear PE Debit Spread, Far OTM PE Short shall be of the same quantity as that of the PE Long leg. The net Premium debit (i.e. Premium paid on PE Long minus Premium credit received on PE Short leg), shall be the max loss in this Strategy, from Expiry perspective. This net Premium debit, may be attempted to be recovered by Shorting some extra Far OTM PEs aggregating to atleast net Premium debit or more. If more quantity of Far OTM PE is shorted than those on PE Long leg, such that the aggregate Premium Credit on PE Short leg is more than the Premium debit on the PE Long leg, then the Strategy will not be Bear*

PE Debit Spread but PE Ratio Spread (already discussed above as Adjustment 1).

- *Ensure that Premium Credit received on Far OTM PE Short is not too low than the Premium paid on the PE Long leg.*

Logic for Adjustment-4: Premium paid on PE Long leg, will be higher than the Premium Credit received on the PE Short leg initiated towards adjustment as part of Bear PE Debit Spread. The Net Premium Debit on the Spread will be the max loss from Expiry perspective. The idea in this adjustment is that the potential loss in the PE Long leg, due to bullish/ mild bullish trend reversal, will be largely set-off from the premium credit received on the PE short leg. Further, if the trend again changes on the bearish side, then PE Long will generate more profit than the loss generated by the PE Short leg, hence, this Strategy (both Long & Short legs) can be continued if the trend again changes towards bearish side.

Important points in relation to aforesaid Counter Adjustments:

The logic in all the aforesaid Counter Adjustments is that upon reversal of trend on the bullish or mild bullish side, the potential loss on the PE Long leg must be attempted to be recovered by collecting Premiums through Shorting PEs.

Since, these Counter Adjustments require initiating PE Short / Futures Long positions therefore more capital would be needed in order to sell PEs or buy Futures. However, since, there are already PE Long against which PE Shorts / Futures Long are initiated therefore initiating these PE Shorts / Futures Long will require lower margins as compared to the capital required for initiating naked Short Options or Futures Long.

Further, in order to consider an appropriate Adjustment technique, one must also consider the: (i) state of volatility / VIX; and (ii) strength of trend reversal on bullish side. Accordingly, if the volatility / VIX is in rising state and bullish trend is in strong momentum, then it may be advisable to initiate Counter Adjustments using Futures Long (instead of using PE Short). However, if the volatility / VIX is stable or in falling state, and bullish trend is not in strong momentum, then it may be advisable to initiate Counter Adjustments using PE Short (instead of using Futures Long).

Lastly, in order to look for Shorting PEs, following key factors must be borne in mind:

- Do not exit the PE Long leg, instead try to recover losing Premium on Long leg by Shorting Far OTM PEs in higher quantities.

- Try to get Premium credit of an amount closer or more than the Premium paid for the PE Long leg.
- Try to get Premium credit by Shorting Far OTM PEs (*avoid Shorting PEs of Strike higher than the PE Long leg, unless strong bullish trend is confirmed, as mentioned above*). Idea here is to ensure that the Far OTM PEs must be of those Strikes which are not expected to be breached by the underlying on the downside by the Expiry. This is important so as to ensure that there is no risk even if the bullish side again reverses and gets mild bearish.
- It is better to add more quantity of PE Shorts to get the desired Premium Credit, rather than compromising on the Strike and choosing a higher PE OTM Strike closer to ATM (in order to get higher Premium Credit with fewer quantity of PEs) than lower PE Strike Far OTM for PE Short leg. This will save the Adjustment made in case of any subsequent reversal on the mild bearish side.
- If there is safe opportunity then it is advisable to keep booking profit on PE Short leg, and re-create the PE Short position (if needed, by moving PE Short positions at higher Strikes with relatively more Premium) in same or farther Expiry series. Idea is to take benefit of favourable Delta move on PE Short leg during continuation of bullish trend.
- Try to get Premium credit on the same or closer Expiry series than the Expiry series of the PE Long leg. This will help get the Theta to work on the PEs Shorted in order to generate quick profit even if the bullish trend is not swift.
- In case there isn't enough Premium credit available on Far OTM PEs of the same or closer Expiry series, then Far OTM PEs of immediately next higher Expiry series may also be considered. However, in this case, the trend must either be bullish or mildly bullish; then only the PE short initiated at this next Expiry series will benefit to recover loss on the PE Long leg. But if the trend ceases to remain bullish/ mild bullish, and again reverses on the bearish side, then these PE Shorts initiated at next Expiry series will not work (as both Theta and Delta will not be favourable); in which case these PE Shorts must either be immediately exited at minor loss or these PE Shorts must be adjusted by taking more PE Longs of same or preferably higher Expiry series (than that of the PE short leg) as explained below in relation to Adjustment for naked PE Shorts.

(iii) **Adjustment of a Naked Futures Long position**

Original Position: Futures Long (<i>bullish view</i>)
Trend Reversal: Bearish and Mild Bearish
Logic of the Adjustments: In case of mild bearish trend reversal, potential loss caused on Futures Long leg may be set-off, through collecting Premium Credit by Shorting Far OTM CEs. In case of strong bearish trend reversal, potential loss caused on Futures Long leg may be set-off, by playing the strong bearish momentum of the trend through Long PEs or Shorting large quantities of Far OTM CEs. Both these adjustments are Counter Adjustments.
Adjustment-1: Converting naked Futures Long into Covered Call Strategy. Short Far OTM CEs of the same Expiry series as that of the Futures leg. This will convert naked Futures Long leg into Covered Call Strategy. Ensure that there is sufficient Premium Credit received on CE Short (by selling more quantity of Far OTM CEs). Aggregate amount of Credit collected through CE Shorting, will be the max amount upto which Futures loss shall be mitigated. Logic for Adjustment-1: Premium credit received on the CE Short leg will help absorb the loss incurred on Futures Long leg, if the trend remains towards bearish / mild bearish side. Idea is to ensure that the underlying does not breaches the CE Strike Shorted on the upside by Expiry (thus, CEs Shorted expire worthless as OTMs on Expiry thereby generating profit, which will absorb the loss incurred on the Futures Long leg). Delta value of a Futures is 1 (per Lot), accordingly, suitable quantity of Far OTM CE Shorts need to be ensured, so that the net Delta position on this Strategy is favourable for the bearish trend (and accordingly movement of the underlying on the bearish side causing loss on the Futures Long leg is sufficiently absorbed by the CE Shorts).
Adjustment-2: Converting naked Futures Long into Futures Hedge. In the event reversal towards bearish side is sure and strong, then potential loss on Futures Long leg can be limited to large extent by initiating ITM PE Long of same

or farther Expiry series as that of the Futures leg. This will convert naked Futures Long into **Futures Hedge (PE side)**.

- *In Futures Hedge, ITM PE Long shall be of the same quantity as that of the Futures Long leg. ITM PE must have atleast around 75% Intrinsic Value.*
- *This Strategy helps confine the potential unlimited loss on Futures Long leg due to trend reversal on the bearish side to the max extent of Time Value comprised in the ITM PE leg (per Lot basis).*
- *If the trend again reverses on the bullish side then addition of PE Long leg does not limit the upside profit potential for the Futures Long, thereby making this Strategy an unlimited reward and limited loss Strategy. Therefore, if the trend again reverses on the bullish side after initiating PE Long leg, then no further adjustments would be required and the Futures Hedge Strategy can be continued as such to play the bullish move in the underlying.*
- *The max loss that may be caused due to continued bearish trend, to the maximum extent of Time Value of the PE Long leg (per Lot basis), can be attempted to be recovered by Shorting some Far OTM CEs (in addition to Futures Hedge comprising of Futures Long & PE Long only) aggregating to atleast max loss amount or more.*
- *Also, if the continuation of strong downtrend momentum is confirmed to sustain, then even more PE Longs in higher quantity than the existing Futures Long quantity can be initiated, in order to make the net Delta on this Futures Hedge Strategy favouring bearish side. This way, the max loss on this Futures Hedge Strategy can be mitigated and even profit can be generated out of the strong downtrend.*

Logic for Adjustment-2: Strong bearish momentum will cause Futures Long leg to bleed profusely as its Delta is 1. This can be best mitigated by initiating a Long PE leg with around 80% or more Intrinsic Value, which will have around 0.7 Delta value or more (per Lot basis), thus effectively controlling the loss caused on Futures leg. Further, the downside risk in this Strategy gets limited to pre-defined max loss, which can be easily set-off by Shorting some Far OTM CEs; while the upside profit remains unlimited and does not require any further adjustments.

Important points in relation to aforesaid Counter Adjustments:

The logic in all the aforesaid Counter Adjustments is that upon reversal of trend on the bearish or mild bearish side, the potential loss on the Futures Long leg must be

attempted to be either recovered by collecting Premiums through Shorting CEs or by limiting potential loss by initiating ITM Long PEs (*even more PE Long can be initiated than Futures Long quantity, in order to make the net Delta on Futures Hedge Strategy favouring bearish side*).

Further, in order to consider an appropriate Adjustment technique, one must also consider the: (i) state of volatility / VIX; and (ii) strength of trend reversal on bearish side. Accordingly, if the volatility / VIX is in rising state and bearish trend is in strong momentum, then it may be advisable to initiate Counter Adjustments using more quantity of Long PE (instead of using CE Short). However, if the volatility / VIX is stable or in falling state, and bearish trend is not in strong momentum, then it may be advisable to initiate Counter Adjustments using CE Short (instead of using Long PE).

In relation to the above Adjustments, following key factors must be borne in mind:

- Since, there are already Futures Long against which PE Long are initiated therefore these PE Long will lower the overall margin requirement as compared to the capital required for initiating naked Long Futures.
- These Counter Adjustments may require initiating CE Short positions therefore more capital would be needed in order to sell CEs.
- Do not exit the Futures Long leg, instead try to mitigate loss incurred on Futures Long leg by initiating suitable Counter Adjustments as explained above.
- Try to get Premium credit by Shorting Far OTM CEs. Idea here is to ensure that the Far OTM CEs must be of those Strikes which are not expected to be breached by the underlying on the upside by the Expiry. This is important so as to ensure that there is no risk even if the bearish side again reverses and gets mild bullish.
- It is better to add more quantity of CE Shorts to get the desired Premium Credit, rather than compromising on the Strike and choosing a lower CE OTM Strike closer to ATM (in order to get higher Premium Credit with fewer quantity of CEs) than higher CE Strike Far OTM for CE Short leg. This will save the Adjustment made in case of any subsequent reversal on the mild bullish side.
- If there is safe opportunity then it is advisable to keep booking profit on CE Short leg, and re-create the CE Short position (if needed, by moving CE Short positions at lower Strikes with relatively more Premium) in same

or farther Expiry series. Idea is to take benefit of favourable Delta move on CE Short leg during continuation of bearish trend.

- Try to get Premium credit when plan to Short CEs, on the same or closer Expiry series than the Expiry series of the Futures Long leg. This will help get the Theta to work on the CEs Shorted in order to generate quick profit even if the bearish trend is not swift.
- In case there isn't enough Premium credit available on Far OTM CEs of the same or closer Expiry series, then Far OTM CEs of immediately next higher Expiry series may also be considered. However, in this case, the trend must either be bearish or mildly bearish; then only the CE Short initiated at this next Expiry series will benefit to recover loss on the Futures Long leg. But if the trend ceases to remain bearish/ mild bearish, and again reverses on the bullish side, then these CE Shorts initiated at next Expiry series will not work (as both Theta and Delta will not be favourable); in which case these CE Shorts must either be immediately exited at minor loss or these CE Shorts must be adjusted by taking more Futures Long or CE Longs (of same or preferably higher Expiry series than that of the CE Short leg) as explained below in relation to Adjustment for naked CE Shorts.

(iv) **Adjustment of a Naked Futures Short position**

Original Position: Futures Short (*bearish view*)

Trend Reversal: Bullish and Mild Bullish

Logic of the Adjustments:

In case of mild bullish trend reversal, potential loss caused on Futures Short leg may be set-off, through collecting Premium Credit by Shorting Far OTM PEs.

In case of strong bullish trend reversal, potential loss caused on Futures Short leg may be set-off, by playing the strong bullish momentum of the trend through Long CEs or Shorting large quantities of Far OTM PEs.

Both these adjustments are Counter Adjustments.

Adjustment-1: Converting naked Futures Short into Covered Put Strategy.

Short Far OTM PEs of the same Expiry series as that of the Futures leg. This will convert naked Futures Short leg into **Covered Put Strategy**.

Ensure that there is sufficient Premium Credit received on PE Short (by selling more quantity of Far OTM PEs). Aggregate amount of Credit collected through PE Shorting, will be the max amount upto which Futures loss shall be mitigated.

Logic for Adjustment-1: Premium credit received on the PE Short leg will help absorb the loss incurred on Futures Short leg, if the trend remains towards bullish / mild bullish side.

Idea is to ensure that the underlying does not breaches the PE Strike Shorted on the downside by Expiry (thus, PEs Shorted expire worthless as OTMs on Expiry thereby generating profit, which will absorb the loss incurred on the Futures Short leg).

Delta value of a Futures is 1 (per Lot), accordingly, suitable quantity of Far OTM PE Shorts need to be ensured, so that the net Delta position on this Strategy is favourable for the bullish trend (and accordingly movement of the underlying on the bullish side causing loss on the Futures Short leg is sufficiently absorbed by the PE Shorts).

Adjustment-2: Converting naked Futures Short into Futures Hedge.

In the event reversal towards bullish side is sure and strong, then potential loss on Futures Short leg can be limited to large extent by initiating ITM CE Long of same or farther Expiry series as that of the Futures leg. This will convert naked Futures Short into **Futures Hedge (CE side)**.

- *In Futures Hedge, ITM CE Long shall be of the same quantity as that of the Futures Short leg. ITM CE must have atleast around 75% Intrinsic Value.*
- *This Strategy helps confine the potential unlimited loss on Futures Short leg due to trend reversal on the bullish side to the max extent of Time Value comprised in the ITM CE leg (per Lot basis).*
- *If the trend again reverses on the bearish side then addition of CE Long leg does not limit the downside profit potential for the Futures Short, thereby making this Strategy an unlimited reward and limited loss Strategy. Therefore, if the trend again reverses on the bearish side after initiating CE Long leg, then no further adjustments would be required and the Futures Hedge Strategy can be continued as such to play the bearish move in the underlying.*

- *The max loss that may be caused due to continued bullish trend, to the maximum extent of Time Value of the CE Long leg (per Lot basis), can be attempted to be recovered by Shorting some Far OTM PEs (in addition to Futures Hedge comprising of Futures Short & CE Long only) aggregating to atleast max loss amount or more.*
- *Also, if the continuation of strong uptrend momentum is confirmed to sustain, then even more CE Longs in higher quantity than the existing Futures Short quantity can be initiated, in order to make the net Delta on this Futures Hedge Strategy favouring bullish side. This way, the max loss on this Futures Hedge Strategy can be mitigated and even profit can be generated out of the strong uptrend.*

Logic for Adjustment-2: Strong bullish momentum will cause Futures Short leg to bleed profusely as its Delta is 1. This can be best mitigated by initiating a Long CE leg with around 80% or more Intrinsic Value, which will have around 0.7 Delta value or more (per Lot basis), thus effectively controlling the loss caused on Futures leg. Further, the upside risk in this Strategy gets limited to pre-defined max loss, which can be easily set-off by Shorting some Far OTM PEs; while the downside profit remains unlimited and does not require any further adjustments.

Important points in relation to aforesaid Counter Adjustments:

The logic in all the aforesaid Counter Adjustments is that upon reversal of trend on the bullish or mild bullish side, the potential loss on the Futures Short leg must be attempted to be either recovered by collecting Premiums through Shorting PEs or by limiting potential loss by initiating ITM Long CEs (*even more CE Long can be initiated than Futures Short quantity, in order to make the net Delta on Futures Hedge Strategy favouring bullish side*).

Further, in order to consider an appropriate Adjustment technique, one must also consider the: (i) state of volatility / VIX; and (ii) strength of trend reversal on bullish side. Accordingly, if the volatility / VIX is in rising state and bullish trend is in strong momentum, then it may be advisable to initiate Counter Adjustments using more quantity of Long CE (instead of using PE Short). However, if the volatility / VIX is stable or in falling state, and bullish trend is not in strong momentum, then it may be advisable to initiate Counter Adjustments using PE Short (instead of using Long CE).

In relation to the above Adjustments, following key factors must be borne in mind:

- Since, there are already Futures Short against which CE Long are initiated therefore these CE Long will lower the overall margin requirement as compared to the capital required for initiating naked Futures Short.
- These Counter Adjustments may require initiating PE Short positions therefore more capital would be needed in order to sell PEs.
- Do not exit the Futures Short leg, instead try to mitigate loss incurred on Futures Short leg by initiating suitable Counter Adjustments as explained above.
- Try to get Premium credit by Shorting Far OTM PEs. Idea here is to ensure that the Far OTM PEs must be of those Strikes which are not expected to be breached by the underlying on the downside by the Expiry. This is important so as to ensure that there is no risk even if the bullish trend again reverses and gets mild bearish.
- It is better to add more quantity of PE Shorts to get the desired Premium Credit, rather than compromising on the Strike and choosing a higher PE OTM Strike closer to ATM (in order to get higher Premium Credit with fewer quantity of PEs) than lower PE Strike Far OTM for PE Short leg. This will save the Adjustment made in case of any subsequent reversal on the mild bearish side.
- If there is safe opportunity then it is advisable to keep booking profit on PE Short leg, and re-create the PE Short position (if needed, by moving CE Short positions at higher Strikes with relatively more Premium) in same or farther Expiry series. Idea is to take benefit of favourable Delta move on PE Short leg during continuation of bullish trend.
- Try to get Premium credit when plan to Short PEs, on the same or closer Expiry series than the Expiry series of the Futures Short leg. This will help get the Theta to work on the PEs Shorted in order to generate quick profit even if the bullish trend is not swift.
- In case there isn't enough Premium credit available on Far OTM PEs of the same or closer Expiry series, then Far OTM PEs of immediately next higher Expiry series may also be considered. However, in this case, the trend must either be bullish or mildly bullish; then only the PE Short initiated at this next Expiry series will benefit to recover loss on the Futures Short leg. But if the trend ceases to remain bearish/ mild bearish, and again reverses on the bearish side, then these PE Shorts initiated at next Expiry series will

not work (as both Theta and Delta will not be favourable); in which case these PE Shorts must either be immediately exited at minor loss or these PE Shorts must be adjusted by taking more Futures Short or PE Longs (of same or preferably higher Expiry series than that of the PE Short leg) as explained below in relation to Adjustment for naked PE Shorts.

(v) **Adjustment of a Naked CE Short position**

Original Position: CE Short (*bearish view*)

Trend Reversal: Bullish (*such that the underlying price is likely to breach the CE Short Strike, on the upside, by Expiry*)

Logic of the Adjustments:

In case of bullish trend reversal, potential loss caused on CE Short leg may be unlimited. Thus, unlimited loss situation can be set-off, by initiating positions to play the bullish trend and outwit the potential loss on the CE Short leg.

Accordingly, in case of strong bullish trend reversal, potential loss caused on CE Short leg may be set-off, by playing the strong bullish momentum of the trend through Long Futures or Long CEs.

Both these adjustments are Counter Adjustments.

Adjustment-1: Converting naked CE Short into Covered Call Strategy.

As soon as the trend reversal on the bullish side is confirmed and strong (*and CE Short Strike is expected to become an ATM or near ITM*), add Long Futures position of the same Expiry series as that of the CE Short leg. This will convert naked CE Short leg into **Covered Call Strategy**.

Ensure to add same quantity of Futures as those on CE Short leg.

Logic for Adjustment-1: Futures Delta is 1 (per Lot basis), which is higher than the Delta value of CE (per Lot basis). Thus, as the strong uptrend continues, the loss generated on the CE Short leg would get set-off with relatively more profit generated on the Futures Long leg.

Further, there will not be any Theta impact on the Futures leg and hence this position can be held close to Expiry to take full advantage of the unlimited profit potential on a continued upward move of the underlying. Also, there will not be any adverse

impact of rise or fall in volatility / VIX on the Futures leg, and thus can be held with conviction so long the underlying is in an uptrend.

In the event the trend again reverses on the bearish side, after initiating Futures Long leg, then this Covered Call Strategy would be able to absorb any bearish move upto the Futures Long Buy Price *minus* Premium Credit collected on CE Short leg. Any downward move below this Strike, would require adjustments with the logic as applicable on naked Futures Long leg (discussed above).

Adjustment-2: Converting naked CE Short into Bull CE Spread.

In the event reversal towards bullish side appears indecisive (i.e. whether it would sustain or reverse back), then such type of reversal on the bullish side may be adjusted by initiating Long CE. This will convert naked CE Short into **Bull CE Spread**.

- *In Bull CE Spread, Long CE (on same Expiry series as that of the CE Short leg, if 50% or more time period is remaining to Expiry) can be initiated on lower Strike than CE Short leg; so as to bring the Delta variance between the CE Long and CE Short leg (i.e. CE Long on higher Delta than the CE short leg). Further, the CE Long strike must have such Premium value, so as to ensure that the net Premium debit (if any) on this Spread Strategy is reasonably less. The net Premium debit on this Vertical Spread will be the max loss on this Strategy from Expiry perspective. This net Premium debit, may be attempted to be recovered after a clear view on the underlying is established.*
- *If 50% or more time period to Expiry for the CE Short leg has already lapsed, the CE Long leg must be initiated on next / farther Expiry Series (making it a Calendar Spread), in order to avoid the Theta impact on this CE Long leg. However, the net Premium debit factor must still be ensured to keep the max loss situation reasonably low. Also, Delta variance must be ensured such that CE Long is at higher Delta than CE Short leg.*

Logic for Adjustment-2: By initiating CE Long on higher Delta than CE Short leg, it can be ensured that if the bullish move continues then from the time the adjustment is implemented, CE Long will set-off the losses incurred on CE short leg. Further, the net Premium debit is ensured to be low, so that the max loss on the Spread from Expiry perspective (for the CE Short leg), is kept low. This max loss situation can be mitigated upon confirmation of the bullish trend by Shorting Far OTM PEs with an aggregate Premium Credit sufficient to set-off the max loss situation on the Spread.

In the event the trend again reverses on the bearish side, after initiating CE Long leg, then this Spread Strategy may generate max loss situation from Expiry perspective. In such event, suitable adjustments may have to be made with the logic as applicable on naked CE Long leg (discussed above). In such case, converting the Spread into CE Ratio Spread may be explored.

Important points in relation to aforesaid Counter Adjustments:

The logic in the aforesaid Counter Adjustments is that upon reversal of trend on the bullish side, the potential unlimited loss on the CE Short leg must be attempted to be either recovered by initiating Futures Long (*to take Delta advantage*) or by limiting the loss by converting into Bull CE Spread thereby limiting potential loss on CE Short leg.

Since, Adjustment-1 requires initiating Futures Long positions therefore more capital would be needed in order to buy Futures. Moreover, Futures Long are initiated against naked CE Short which itself requires higher margin. Therefore, conversion into Covered Call Strategy would entail requirement of more capital to fulfil margin & MTM requirements.

Further, Adjustment-2 requiring conversion into Bull CE Spread, would entail lesser margin requirements as it involves buying CE against existing CE Shorts. However, in order to cover the max loss on the Spread, PE Short may be required to be initiated, which would entail requirement of more capital to fulfil margin & MTM requirements.

Additionally, in order to consider an appropriate Adjustment technique, one must also consider the: (i) state of volatility / VIX; and (ii) time period for Expiry of the CE Short leg. Accordingly, if the volatility / VIX is in falling state, or the Expiry of the CE Short leg has already lapsed by 50% or more, then it may be advisable to initiate Counter Adjustments using Futures Long (instead of using CE Long). But if volatility / VIX is in rising state, and the Expiry of the CE Short leg has not already lapsed by 50% or more, and the bullish momentum is not very sure, then it may be advisable to initiate Counter Adjustments using CE Long (instead of using Futures Long).

It is not advisable to exit the CE Short leg, instead try to mitigate loss on CE Short leg by initiating suitable Counter Adjustments as explained above.

(vi) **Adjustment of a Naked PE Short position**

Original Position: PE Short (<i>bullish view</i>)
Trend Reversal: Bearish (<i>such that the underlying price is likely to breach the PE Short Strike, on the downside, by Expiry</i>)
Logic of the Adjustments: In case of trend reversal on the bearish side, potential loss caused on PE Short leg may be unlimited. Thus, unlimited loss situation can be set-off, by initiating positions to play the bearish trend and outwit the potential loss on the PE Short leg. Accordingly, in case of strong bearish trend reversal, potential loss caused on PE Short leg may be set-off, by playing the strong bearish momentum of the trend through Short Futures or Long PEs. Both these adjustments are Counter Adjustments.
Adjustment-1: Converting naked PE Short into Covered Put Strategy. As soon as the trend reversal on the bearish side is confirmed and strong (<i>and PE Short Strike is expected to become an ATM or near ITM</i>), add Futures Short position of the same Expiry series as that of the PE Short leg. This will convert naked PE Short leg into Covered Put Strategy. Ensure to add same quantity of Futures as those on PE Short leg. Logic for Adjustment-1: Futures Delta is 1 (per Lot basis), which is higher than the Delta value of PE (per Lot basis). Thus, as the strong downtrend continues, the loss generated on the PE Short leg would get set-off with relatively more profit generated on the Futures Short leg. Further, there will not be any Theta impact on the Futures leg and hence this position can be held close to Expiry to take full advantage of the unlimited profit potential on a continued downward move of the underlying. Also, there will not be any adverse impact of rise or fall in volatility / VIX on the Futures leg, and thus can be held with conviction so long the underlying is in a downtrend. In the event the trend again reverses on the bullish side, after initiating Futures Short leg, then this Covered Put Strategy would be able to absorb any bullish move upto the Futures Short Sell Price <i>plus</i> Premium Credit collected on PE Short leg. Any

upward move above this Strike, would require adjustments with the logic as applicable on naked Futures Short leg (discussed above).

Adjustment-2: Converting naked PE Short into Bear PE Spread.

In the event reversal towards bearish side appears indecisive (i.e. whether it would sustain or reverse back), then such type of reversal on the bearish side may be adjusted by initiating Long PE. This will convert naked PE Short into **Bear PE Spread**.

- *In Bear PE Spread, Long PE (on same Expiry series as that of the PE Short leg, if 50% or more time period is remaining to Expiry) can be initiated on higher Strike than PE Short leg; so as to bring the Delta variance between the PE Long and PE Short leg (i.e. PE Long on higher Delta than the PE short leg). Further, the PE Long strike must have such Premium value, so as to ensure that the net Premium debit (if any) on this Spread Strategy is reasonably less. The net Premium debit on this Vertical Spread will be the max loss on this Strategy from Expiry perspective. This net Premium debit, may be attempted to be recovered after a clear view on the underlying is established.*
- *If 50% or more time period to Expiry for the PE Short leg has already lapsed, the PE Long leg must be initiated on next / farther Expiry Series (making it a Calendar Spread), in order to avoid the Theta impact on this PE Long leg. However, the net Premium debit factor must still be ensured to keep the max loss situation reasonably low. Also, Delta variance must be ensured such that PE Long is at higher Delta than PE Short leg.*

Logic for Adjustment-2: By initiating PE Long on higher Delta than PE Short leg, it can be ensured that if the bearish move continues then from the time the adjustment is implemented, PE Long will set-off the losses incurred on PE Short leg. Further, the net Premium debit is ensured to be low, so that the max loss on the Spread from Expiry perspective (for the PE Short leg), is kept low. This max loss situation can be mitigated upon confirmation of the bearish trend by Shorting Far OTM CEs with an aggregate Premium Credit sufficient to set-off the max loss situation on the Spread.

In the event the trend again reverses on the bullish side, after initiating PE Long leg, then this Spread Strategy may generate max loss situation from Expiry perspective. In such event, suitable adjustments may have to be made with the logic as applicable on naked PE Long leg (discussed above). In such case, converting the Spread into PE Ratio Spread may be explored.

Important points in relation to aforesaid Counter Adjustments:

The logic in the aforesaid Counter Adjustments is that upon reversal of trend on the bearish side, the potential unlimited loss on the PE Short leg must be attempted to be either recovered by initiating Futures Short (*to take Delta advantage*) or by limiting the loss by converting into Bear PE Spread thereby limiting potential loss on PE Short leg.

Since, Adjustment-1 requires initiating Futures Short positions therefore more capital would be needed in order to sell Futures. Moreover, Futures Short are initiated against naked PE Short which itself requires higher margin. Therefore, conversion into Covered Put Strategy would entail requirement of more capital to fulfil margin & MTM requirements.

Further, Adjustment-2 requiring conversion into Bear PE Spread, would entail lesser margin requirements as it involves buying PE against existing PE Shorts. However, in order to cover the max loss on the Spread, CE Short may be required to be initiated, which would entail requirement of more capital to fulfil margin & MTM requirements.

Additionally, in order to consider an appropriate Adjustment technique, one must also consider the: (i) state of volatility / VIX; and (ii) time period for Expiry of the PE Short leg. Accordingly, if the volatility / VIX is in falling state, or the Expiry of the PE Short leg has already lapsed by 50% or more, then it may be advisable to initiate Counter Adjustments using Futures Short (instead of using PE Long). But if volatility / VIX is in rising state, and the Expiry of the CE Short leg has not already lapsed by 50% or more, and the bearish momentum is not very sure, then it may be advisable to initiate Counter Adjustments using PE Long (instead of using Futures Short).

It is not advisable to exit the PE Short leg, instead try to mitigate loss on PE Short leg by initiating suitable Counter Adjustments as explained above.

Adjustments, as explained above in the context of naked Futures and Options (Long & Short) positions, would form the basic tenet basis which even the hedged Strategies can also be adjusted.

Adjustments applicable towards specific Strategies (*viz. Bull CE Debit Spread, Bear CE Credit Spread, Bear PE Debit spread, Bull PE Credit Spread, Covered Call, Short Strangle, Straddle etc*) are explained in the subsequent Chapters as part of comprehensive discussions on those Strategies. You may

consider exploring those Strategies as referred to above, in the subsequent Chapters.

ADJUSTMENTS THROUGH PYRAMIDING

Now, let us discuss about the Adjustments through Pyramiding.

Contrary to Counter Adjustments discussed above, adjustments through pyramiding are done by initiating positions in the direction of the original trend (i.e. *not following the trend reversal*). However, this type of adjustment is only deployed when:

- (i) the reversal is a trending one but upto a limited extent (i.e. would maximum last upto a strong resistance level on the upside or to a strong support level on the downside); and
- (ii) Expiry is not far.

The idea / objective behind this type of adjustment is to capture high Premium Far OTM Options (which gets benefited from the trend reversal) for shorting, and eventually deriving profit from their decay due to approaching/ not-so-far Expiry. **This adjustment may be done only by deploying naked Short Options positions (*preferably*) or Credit hedged Strategies (*in large quantities*).**

Thus, this type of adjustments can be deployed in case of following situations:

- (iii) **Mild-Bearish Trending Reversal:** When a bullish / mild bullish trend was being played out through a Strategy, and there arrives a mild-bearish reversal, which is expected to not trend below a strong support level as per the technical analysis by the approaching Expiry of the F&O instruments involved in the original Strategy.
- (iv) **Mild-Bullish Trending Reversal:** When a bearish / mild bearish trend was being played out through a Strategy, and there arrives a mild-bullish reversal, which is expected to not trend above a strong resistance level as per the technical analysis by the approaching Expiry of the F&O instruments involved in the original Strategy.

Let us understand in detail about 'Adjustments through Pyramiding' in case of the aforesaid two trending reversal situations.

Pyramiding in Mild-Bearish Trend Reversal:

If an original position / Strategy was initiated to play bullish trend but the trend has reversed to mild-bearish which is expected to remain mild-bearish only upto a strong support level on the downside, then adjustments through pyramiding would be done by shorting Far OTM PEs below the strong support level, as it gets a higher Premium value from the reversal on the bearish side. Further, in this adjustment, more quantity is shorted on even lower Strikes as the mild-bearish reversal keeps approaching towards the support level.

For example: if Nifty ATM is at 17000 and a Bull CE Debit Spread Strategy was initiated expecting Nifty to trend higher; but the Nifty reverses and becomes mild-bearish and starts trending downward (*causing PE Premiums to rise and CE Premiums to fall, thereby causing loss in the original Strategy*) and there seems to be a strong support level at 16000 PE below which the Nifty is not expected to slip by Expiry (which is not too far from the time of trend reversal), then we can consider shorting PE Options as they get benefited with higher Premium as the underlying starts approaching 16000 support level. Thus, we can consider shorting:

- Far OTM 15800 PE 2 Lots at Rs. 100 per Lot (when its Premium rises from Rs. 50 to Rs 100) as Nifty starts its downward move below 17000; and
- thereafter, can short 3 or 4 lots of 15600 PE at Rs. 85 per Lot (when its Premium rises from 45 Rs. to Rs. 85) as Nifty slides below 16500; and
- thereafter, can short 5 or 6 lots of 15400 PE at Rs. 65 per Lot (when its Premium rises from 25 Rs. to Rs. 65) as Nifty slides below 16200 towards the support level of 16000.

Idea here is that the Nifty will respect the strong support level of 16000 and will not slip below that level by approaching Expiry, which is close-by. Approach in this adjustment is to keep shorting more quantity of PEs at lower

Strikes below the support level of 16000, when they get benefited with relatively higher Premium (than these Strikes had earlier). If our technical view is correct, then the Nifty will respect the strong support level of 16000 and the rise in Premium values of PE will not happen once Nifty slides down to 16000 level and sustains. Infact, as the Nifty sustains at 16000 level and remains there or closes higher at Expiry, these PE Shorts initiated as part of adjustments through pyramiding, will start showing profit due to cessation of downward momentum and Theta effect of approaching Expiry. Thus, all these PEs which were shorted (taking benefit of higher Premiums due to mild-bearish trend reversal) will expire worthless as OTM by Expiry, thereby yielding profit to the extent of Premium credit received on these Short PEs. This profit on Premium credit from PE Shorts are targeted to mitigate the potential loss on the original Bull CE Spread Strategy.

The benefit of this adjustment is: (a) to be able to take benefit of collecting higher Premium due to the momentum; (b) shorts are targeted at Far OTM Strikes below strong support levels; (c) since these adjustments collects Premium at lower Strike levels, it helps to increase the Breakeven Strike much below the support level; (d) to get benefited from Theta decay due to close-by Expiry.

However, having said above, there is a potent risk in this type of adjustment. The risk is: if the downward momentum does not stop at the support level and slides down breaching the Breakeven Strikes of all these PE Shorts taken collectively. Since, the adjustments involves shorting Options or credit strategy, therefore, in case the momentum breaks the support level on the downside and also breaches the Breakeven Strike levels, then it may lead to an unlimited loss situation on these adjustments, besides loss on the original Strategy. This unlimited loss situation can be contained by deploying equal number of PE Long at even lower Strike than the PE Short Strike (*thus, converting naked PE Shorts into PE Credit Spread*). While, these hedged positions may contain the unlimited loss to some extent, but this should be initiated when the bearish momentum appears to be not very strong. However, if the bearish trend appears to be continuing and strong then instead of initiating PE Long at lower Strikes than PE Short, it will be prudent to initiate PE Long on higher Strike than PE Shorts in equal quantity (*thus, converting naked PE Shorts in to Bear PE Spread*). Since, the original Strategy was towards bullish side, therefore

large quantities for Bear PE Spread may need to be deployed as part of these adjustments in order to sufficiently mitigate the loss on the original Strategy due to trend reversal on the bearish side.

Therefore, this adjustment, to play out the bearish trending reversal so as to curtail/mitigate the loss on the original bullish/mild bullish Strategy, should be considered only if there is a strong conviction on the support level on the downside to remain intact by Expiry.

Pyramiding in Mild-Bullish Trend Reversal:

If an original position / Strategy was initiated to play bearish trend but the trend has reversed to mild-bullish side which is expected to remain mild-bullish only upto a strong resistance level on the upside, then adjustments through pyramiding would be done by shorting Far OTM CE above the strong resistance level, as it gets a higher Premium value from the reversal on the bullish side. Further, in this adjustment, more quantity is shorted on even higher Strikes as the mild-bullish reversal keeps approaching towards the resistance level.

For example: if Nifty ATM is at 17000 and a Bear PE Debit Spread Strategy was initiated expecting Nifty to trend lower; but the Nifty reverses and becomes bullish and starts trending upward (*causing CE Premiums to rise and PE Premiums to fall, thereby causing loss in the original Strategy*) and there seems to be a strong resistance level at 18000 CE, above which the Nifty is not expected to rise further up by Expiry (which is not too far from the time of trend reversal), then we can consider shorting CE Options as they get benefited with higher Premium as the underlying starts approaching 18000 resistance level. Thus, we can consider shorting:

- Far OTM 18200 CE 2 Lots at Rs. 120 per Lot (when its Premium rises from Rs. 95 to Rs 120) as Nifty starts its upward move from 17000; and
- thereafter, can short 3 or 4 lots of 18300 CE at Rs. 100 per Lot (when its Premium rises from 75 Rs. to Rs. 100) as Nifty rises above 17600; and

- thereafter, can short 5 or 6 lots of 18500 CE at Rs. 75 per Lot (when its Premium rises from 50 Rs. to Rs. 75) as Nifty further rises above 17800 towards 18000 resistance level.

Idea here is that the Nifty will respect the strong resistance level of 18000 and will not rise above that level by approaching Expiry, which is close-by. Approach in this adjustment is to keep shorting more quantity of CEs at higher Strikes above the resistance level of 18000, when they get benefited with relatively higher Premium (than these Strikes had earlier). If our technical view is correct, then the Nifty will respect the strong resistance level of 18000 and the rise in Premium values of CE will not happen once Nifty reaches upto 18000 level and sustains. Infact, as the Nifty sustains at 18000 level and remains there or closes lower at Expiry, these CE Shorts initiated as part of adjustments through pyramiding, will start showing profit due to cessation of upward momentum and Theta effect of approaching Expiry. Thus, all these CEs which were shorted (taking benefit of higher Premiums due to mild-bullish trend reversal) will expire worthless as OTM by Expiry, thereby yielding profit to the extent of Premium credit received on these Short CEs. This profit on Premium credit from CE Shorts are targeted to mitigate the potential loss on the original Bear PE Spread Strategy.

The benefit of this adjustment is: (a) to be able to take benefit of collecting higher Premium due to the momentum; (b) shorts are targeted at Far OTM Strikes above strong resistance levels; (c) since these adjustments collect Premium at higher Strike levels, it helps to increase the Breakeven Strike much above the resistance level; (d) to get benefited from Theta decay due to close-by Expiry.

However, having said above, there is a potent risk in this type of adjustment. The risk is: if the upward momentum does not stop at the resistance level and rises up even higher breaching the Breakeven Strikes of all these CE Shorts taken collectively. Since, the adjustments involves shorting Options or credit strategy, therefore, in case the momentum breaches the resistance level and the Breakeven Strike levels, then it may lead to an unlimited loss situation on these adjustments, besides loss on the original Strategy. This unlimited loss situation can be contained by deploying equal number of CE Long at even

higher Strike than the CE Short Strike (*thus, converting naked CE Shorts into CE Credit Spread*). While, these hedged positions may contain the unlimited loss to some extent, but this should be initiated when the bullish momentum appears to be not very strong. However, if the bullish trend appears to be continuing and strong then instead of initiating CE Long at higher Strikes than CE Short, it will be prudent to initiate CE Long on lower Strike than CE Shorts in equal quantity (*thus, converting naked CE Shorts in to Bull CE Spread*). Since, the original Strategy was towards bearish side, therefore large quantities for Bull CE Spread may need to be deployed as part of these adjustments in order to sufficiently mitigate the loss on the original Strategy due to trend reversal on the bullish side.

Therefore, this adjustment, to play out the mild-bullish trending reversal so as to curtail/mitigate the loss on the original bearish/mild bearish Strategy, should be considered only if there is a strong conviction on the resistance level on the upside to remain intact by Expiry.

Thus, the significance of Adjustments through pyramiding is that it can be used only for trending reversals which can be reasonably expected to trend to limited extent and not beyond.

Further, this kind of Adjustment would be best suited for:

- original Strategies/positions which are exposed to a defined / limited loss; or
- for original Strategies/ positions which are exposed to unlimited loss and the trend reversal is almost absolutely confirmed to be of a limited extent (i.e. would not breach the relevant resistance/ support level, as the case may be) and for a temporary time.

Also, this Adjustment must be considered, when Volatility is not in a rising state; and Expiry is quite near.

Illustrations of Adjustment through Pyramiding:

Basis the aforementioned factors, the following table will indicatively explain the Adjustments through Pyramiding in different trend reversal situations (also refer to the note section below the Tables):

Original Strategy/ positions: (naked / hedged)	Bullish / Mild Bullish
Trend Reversal:	Mild-Bearish momentum
Selection of Strike levels for Adjustments through Pyramiding: Idea is to benefit by Shorting the Option whose Premium would be on rise due to trend reversal. In this case of trend reversal toward bearish momentum, we will target Shorting PEs below the support level (below which we do not expect the underlying to fall by the approaching relevant Expiry of the instruments in the original Strategy). We will keep adding larger quantity of Short PEs at lower Strikes (below the support level and at Strikes even lower than the Strike at which PE Shorts were initiated previously as part of adjustments through pyramiding), as their Premium rises due to trending reversal toward bearish momentum. Thus: • few quantities of PE Short at Strike below the support level; • then, more quantities of PE Short below support level and at even lower Strikes than the previous PE Short Strike • then, even more quantities of PE Short below support level and at even lower Strikes than the previous two PE Short Strikes; and so on.	
Original Strategy/ positions: (naked / hedged)	Bearish / Mild Bearish
Trend Reversal:	Mild-Bullish momentum
Selection of Strike levels for Adjustments through Pyramiding: Idea is to benefit by Shorting the Option whose Premium would be on rise due to trend reversal. In this case of trend reversal toward bullish momentum, we will target Shorting CEs above the resistance level (above which we do not expect the underlying to rise by the approaching relevant Expiry of the instruments in the original Strategy). We will keep adding larger quantity of Short CEs at higher Strikes (above the resistance level and at even higher Strikes than the Strike at which CE Shorts were initiated previously as part of adjustments through pyramiding), as their Premium rises due to trending reversal toward bullish momentum. Thus: • few quantities of CE Short at Strike above the resistance level; • then, more quantities of CE Short above the resistance level and at even higher Strikes than the previous CE Short Strike	

- then, even more quantities of CE Short above the resistance level and at even higher Strikes than the previous two CE Short Strikes; and so on.

Original Strategy/ positions: (naked / hedged)	Rangebound
Trend Reversal:	Mild-Bullish momentum with range Breakout
Selection of Strike levels for Adjustments through Pyramiding: Through CE Shorts as explained above.	

Original Strategy/ positions: (naked / hedged)	Rangebound
Trend Reversal:	Mild-Bearish momentum with range Breakdown
Selection of Strike levels for Adjustments through Pyramiding: Through PE Shorts as explained above.	

Additional Notes on Adjustments through Pyramiding:

- Short Options positions in the aforementioned Adjustments must be of the current Expiry series, so as to get benefit of the increasing Theta impact due to approaching Expiry. The Short Options for these Adjustments must be of the same Expiry series as that of the closer Expiry series in the original Strategy.
- Short Options positions, as part of these Adjustments, must be initiated at such far OTM Strikes, which are reasonably expected to expire worthless as OTM by Expiry, i.e. CE Shorts must be above the upper resistance level where the underlying is not expected to cross by Expiry and the PE Shorts must be below the lower support level where the underlying is not expected to cross by Expiry.
- These Adjustments involving Short Options positions may require huge capital and compliance towards MTM requirements.

- These Adjustments may be implemented through naked Short Options positions or through relevant hedged credit Strategies. However, hedged credit strategies will require relatively much larger quantities than the naked Short positions, to collect good amount of Premium Credit through Pyramiding.
- Ensure that Volatility is not in rising state.

BOOKING LOSS VS ADJUSTMENTS

Adjustments must be initiated as soon as the trend reversal is identified, but also only when trend reversal is absolutely confirmed; because it is extremely difficult to further adjust the positions initiated as part of Adjustments (if the trend reversal, as understood, goes wrong).

Sometimes, it would be more prudent to take a minor loss than to consider initiating Adjustments. It may be better to take a minor loss and wait for a convincing trend reversal confirmation; and then initiate a fresh trade/ Strategy in the direction of the new trend / trend reversal.

SUMMARY ON ADJUSTMENT TECHNIQUES

Thus, basis the foregoing discussions, following conclusions concerning adjustments to trade, can be drawn:

- Adjustments may be required in the original positions/ Strategy, once the original trend has reversed or is no more valid.
- Adjustments to the original trade, can be done broadly in two ways: (i) Counter Adjustments (ii) Adjustments through Pyramiding.
- Counter Adjustment positions are initiated in the direction of the new trend/ reversed trend, by employing Long Options or Short Options. Main objective in this type of Adjustment is to mitigate losses in the original trade positions, through Delta play (*by initiating higher Delta positions on the Counter Adjustments than the original trade/Strategy*), i.e. by countering the losses in original trade by playing the direction of the new / reversed trend with Delta advantageous positions initiated on Counter Adjustment positions over Delta position on

original Strategy/ trade. Theta impact on Premium credits collected on Short Options positions initiated as Counter Adjustments are also harnessed to mitigate loss on the original Strategy/trade positions.

- Position in Adjustments through Pyramiding are initiated in the direction of the original trend, by employing Short Options. Main objective in this type of Adjustment is to mitigate losses in the original trade positions, through collecting Premium credits by initiating Short positions on those Options which are getting Premium appreciation due to trending underlying (i.e. *CE Short when underlying is rising; and PE Short when underlying is falling*), and to eventually get benefited on account of Theta impact on Premium credits collected on such Short Options positions initiated in pyramidal fashion.
- Adjustments through Pyramiding are relatively riskier than Counter Adjustments, as the former is in opposite direction of the new/reversed trend. Therefore, Adjustments through Pyramiding must be initiated only when the intensity of momentum and level of resistance/ support convincingly meets the criterion of Adjustments through Pyramiding discussed above. Also, Adjustments through Pyramiding must be implemented only when the Expiry is near and the relevant Resistance / Support zone is strong to not let the underlying breach the relevant Resistance/ Support zone, as the case may be.
- These Adjustments can be implemented through naked Options positions or by implementing suitable hedged Strategies. However, much larger quantities would be needed for Adjustments through hedged positions rather than naked positions.
- If Volatility is in rising state then Adjustments involving Long Options must be considered; and if Volatility is in falling state then Adjustments through Short Options may be considered.
- Adjustments employing Short positions (especially naked Shorts) would require higher capital, and may have MTM consequences.

After having learnt about the approach for initiating a trade and constructing a hedged Strategy in the previous Chapter and the logic behind

making Adjustments (if the original Strategy seems to have failed) in this Chapter, we are now prepared to dive into understanding the merits and applicability of various Conventional and Customised Strategies, which are discussed in details in the subsequent Chapters starting with Chapter 3.

Chapter – 3

F&O Strategies

Conventional Strategies

It needs to be understood that in order to design / play a particular Strategy, it is very important to have a sound understanding about the following concepts regarding FNO, broadly segregated below:

- i. The basic features about the Futures and Options, behavioural aspects of Options under different market dynamics and the understanding & significance of Long Options and Short Options positions; and
- ii. Factors to be considered for initiating / designing a trading position / Strategy (*viz., trend, Premium debit/credit, , effects of Options Greeks etc.*) and Trade Adjustments that may be considered if the original trade position goes wrong.

These aforesaid aspects are extremely crucial and forms the backbone of all the F&O trades. Of these two broadly categorised concepts, topics mentioned as (i) above are explained in Volume-I of the Book and those mentioned as (ii) above have been explained in the previous Chapters in this Volume-II itself. Make sure that you have a sound understanding of these important concepts, as it will help you to plan, identify, execute, ride manage and adjust a trading position, basis the dynamic market conditions.

Now, it's time that we explore the structure, inter-play and significant factors basis which certain Conventional Strategies/ trading positions are designed and may be considered for taking a trading position for a given market situation.

Let us begin !

CONVENTIONAL STRATEGIES

In this Chapter, we will learn and focus on some of the most common and important Conventional Strategies involving Futures and/or Options.

In the context of these Conventional Strategies, we would be discussing here in-depth about various important parameters of each of Strategies, viz. its objective, merits & demerits, Breakeven levels, Profit & loss scenario, Payoff charts, Risk & Reward, Options behaviour and inter-play of Greeks, selection of Strikes, the logic behind the design of a Strategy and possible adjustments should the Strategy seems to fail its expectation. We have tried to cover as many aspects as are practically relevant to be learnt about these Strategies; and have thus provided comprehensive coverage to each heads and subheads under each Strategy, to bring ultra-clarity and sound understanding on their various facets, even if it is at the cost of repetition.

Word of Caution:

Before we start discussions on various Strategies, we would like to again upfront highlight as a **caution that: one must avoid to trade in FNO instruments of such asset class / underlying (like FNO stocks), where there is a requirement to comply with physical delivery.** Because if the FNO instruments of such underlying / assets (*which is subject of physical delivery requirements*) expires as an ITM, then even though any given Strategy may be overall profitable, but such situation may warrant the trader to unnecessarily comply with the physical delivery requirements. Hence, if any Strategy is executed deploying FNO instruments in relation to such assets/ underlying (*which are subject to physical delivery requirements*), then it is advisable to not hold the trading positions in such instruments till Expiry (or even near to Expiry). Instead, it is advisable to play any trading Strategy(ies) on positional basis, only on Indices/ assets, where there is no requirements toward physical delivery viz. *Nifty F&O / BankNifty F&O / FinNifty F&O etc.*, so as completely avoid unwarranted situation which may fall upon due to any factor beyond one's control.

Also, it must be clearly understood that knowing Strategies alone is not sufficient to be profitable in a trade, as the market can be unexpectedly very

volatility (especially on Expiry Days) and there can be numerous factors beyond the knowledge and control of a trader which may influence the trade plan or outcome of a Strategy. Therefore, every trader must first acquire the relevant knowledge and then devote time to develop his trading skill by testing different Strategies in different market conditions, by practicing first on some virtual trading platform and then starting with real trades in just one or two Lots. We have discussed about this aspect of learning and skill development in detail in our **Chapter: Golden Rules ('Dos' & Don'ts in Trading')** contained in Volume I. Please go through that Chapter, before you decide to start initiating real trades.

Different Conventional Strategies:

Having said above, we are going to now explore in this Chapter, about 24 different Conventional Strategies, both hedged & naked, which are commonly employed to play specific market trends. The Strategies which will be discussed in this Chapter, are outlined in the Table below:

Sl. No.	Strategy	To play the Trend
1.	Covered Call	Bullish to sideways
2.	Covered Put	Bearish to sideways
3.	Big Boy's Covered Call and Poor Man's Covered Call	Bullish to sideways
4.	Poor Man's Covered Put	Bearish to sideways
5.	Collar Strategy for Covered Call	Bearish
6.	Collar Strategy for Covered Put	Bullish
7.	Covered Call (<i>Stock</i>)	

8.	Married Put or Protective Put (<i>Stock</i>)	Bearish
9.	Bull Call Debit Spread	Bullish
10.	Bear Put Debit Spread	Bearish
11.	Bull Put Credit Spread	Bullish to sideways
12.	Bear Call Credit Spread	Bearish to sideways
13.	Call Ratio Spread	Bullish to sideways
14.	Put Ratio Spread	Bearish to sideways
15.	Call Calendar Spread	Bullish to sideways
16.	Put Calendar Spread	Bearish to sideways
17.	Short Strangle (<i>naked</i>)	Neutral (<i>underlying to expire within a range</i>)
18.	Iron Condor (<i>hedged Short Strangle</i>)	Neutral (<i>underlying to expire within a range</i>)
19.	Short Straddle (<i>naked</i>)	Neutral (<i>underlying to be in a tight range</i>)
20.	Iron Fly (<i>hedged Short Straddle</i>)	Neutral (<i>underlying to be in a tight range</i>)
21.	Long Strangle (<i>naked</i>)	Neutral (<i>underlying to be in move with momentum in either direction outside a wide the range</i>)
22.	Reverse Iron Condor (<i>hedged Long Straddle</i>)	Neutral (<i>underlying to be in move with momentum in either direction outside a wide range</i>)

23.	Long Straddle (<i>naked</i>)	Neutral (<i>underlying to be in move with momentum in either direction outside a narrow range</i>)
24.	Reverse Iron Fly (<i>hedged Long Straddle</i>)	Neutral (<i>underlying to be in move with momentum in either direction outside a narrow range</i>)

Besides the fact that the aforesaid Strategies pertain to play out different market conditions; these Conventional Strategies is a mixed bag of Strategies, involving: naked & hedged Strategies, Premium Debit & Credit Strategies, Long Options & Short Options, Vertical & Horizontal Spreads, Calendar & Ratio Spreads etc., thus providing analysis on Strategies of varied spectrum.

Further, as mentioned above, for the purpose of practical trading, it is important to understand the various facets of these Strategies to get a comprehensive understanding. The idea behind these in-depth discussions on these Strategies in this Chapter, is to be able to instil a logical thinking to appreciate the construct of these Strategies, which are devised to play a particular market condition; and to help understand the possible ways by which a trade position may be adjusted if it appears to be not going as initially expected.

This understanding will not only help a trader to be able to dissect a Strategy, but will also help to evolve as an informed trader who would know what to deploy when and how to construct and adjust a trade as the situation merits. Also, this analysis about each of these Strategies can also be used as a reference, from time to time, as may be relevant in the context of planning or managing a trading position.

So let us fasten our seat belt to start exploring each of the aforesaid Conventional Strategies.

COVERED CALL & COVERED PUT STRATEGY

If there is a main position with mild bullish view, either in cash Stocks or Long in Futures (the **primary leg**), then this primary leg can be hedged by introducing a hedged leg with a bearish view by employing Options (the **hedged leg**). This hedged leg can be created by selling CE (i.e. Call Short). This hedged position/ strategy where a bullish primary leg is hedged with Call Short position – it is called a **Covered Call Strategy**.

Likewise, if there is a main position with mild bearish view, either in cash Stocks or Short in Futures (the **primary leg**), then this primary leg can be hedged by introducing a hedged leg with a bullish view by employing Options (the **hedged leg**). This hedged leg can be created by selling PE (i.e. Put Short). This hedged position/ strategy where a bearish primary leg is hedged with Put Short position – it is called a **Covered Put Strategy**.

With this background, now let delve into discussing the Covered Call Strategy and Covered Put Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Covered Call Strategy	Covered Put Strategy
Trade legs: - Long Futures (<i>primary leg</i>) - Short CE (<i>hedged leg</i>) or - Stocks bought (<i>primary leg</i>)⁴ - Short CE (<i>hedged leg</i>)	Trade legs: - Short Futures (<i>primary leg</i>) - Short PE (<i>hedged leg</i>)
Objective:	Objective:

⁴ This Strategy wherein Cash segment investments are hedged by Shorting CE, is called Big Boy's Covered Call. Here, the investments on the primary leg must be in the multiples of the Lot size in F&O of that particular Stock, in order to play Covered Call Strategy through Shorting CEs of equivalent number of Lots (*depending on the quantity of stocks held as investments, in the multiples of Lot size in F&O segment of that scrip*).

Objective is to generate limited pre-determined profit from the rangebound-to-mild bullish move in the underlying; and to mitigate the risk / loss that may arise if the primary leg with bullish view gets reversed. Then upon such reversal the loss in the primary leg will get covered to some extent (i.e. <i>to the extent of Premium received on CE Short</i>) by the hedged leg initiated to cover the downside risk. Covered Call can also be played through Synthetic Futures i.e. deep ITM CE with almost 100% Intrinsic Value (<i>instead of Futures Long position</i>) for the primary leg. The hedged leg would as usual be played through CE Short positions. Such Covered Call is called Poor Man's Covered Call. Covered Call can also be played as a Big Boy's Covered Call for the investments held in the Cash segment / other instruments.	Objective is to generate limited pre-determined profit from the rangebound-to-mild bearish move in the underlying; and to mitigate the risk / loss that may arise if the primary leg with bearish view gets reversed. Then upon such reversal the loss in the primary leg will get covered to some extent (i.e. <i>to the extent of Premium received on PE Short</i>) by the hedged leg initiated to cover the upside risk. Covered Put can also be played through Synthetic Futures i.e. deep ITM PE with almost 100% Intrinsic Value (<i>instead of Futures Short position</i>) for the primary leg. The hedged leg would be played through PE Short positions. Such Covered Put is called Poor Man's Covered Put.
<u>Examples of Covered Call:</u> • <i>Nifty Futures 4 Lot Long @ 17108;</i> • <i>Nifty ATM 4 Lot CE 17000 Short at Rs. 200 Premium</i> Or <u>Poor Man's Covered Call:</u> • <i>Nifty Deep ITM 16000 CE Long (Synthetic Futures with 100% Intrinsic Value) 4 Lot at Rs. 1400 Premium per Lot;</i> • <i>Nifty ATM CE 17000 Short 4 Lot at Rs. 200 Premium per Lot</i>	<u>Examples of Covered Put:</u> • <i>Nifty Futures 4 Lot Short @ 17104;</i> • <i>Nifty ATM 4 Lot PE 17000 Short at Rs. 200 Premium</i> Or <u>Poor Man's Covered Put:</u> • <i>Nifty Deep ITM 18000 PE Long (Synthetic Futures with 100% Intrinsic Value) 4 Lot at Rs. 1500 Premium per Lot;</i> • <i>Nifty ATM PE 17000 Short 4 Lot at Rs. 200 Premium per Lot</i>

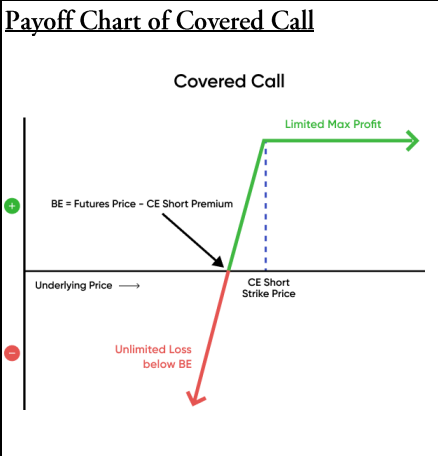
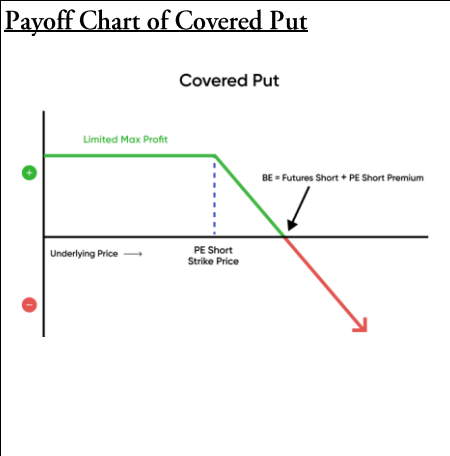
Or <u><i>Big Boy's Covered Call:</i></u> • Investments in Shares (<i>eg: Tata Steel, SBIN etc</i>) equivalent to 1 Lot equivalent in FNO segment of such Shares • Short ATM CE of such FNO Stock (<i>eg: Tata Steel, SBIN etc</i>) 1 Lot	
<u>Demerits:</u> • Max reward / profit is limited and max loss situation is unlimited. • Buying Futures and Shorting Options, both require huge margin and MTM issues. • While, Covered Call Strategy can also be played as Poor Man's Covered Call, in which Futures' Long primary leg is replaced with Synthetic Futures i.e. ITM CE with almost 100% Intrinsic Value, however, such deep ITM CE may not be liquid (especially in case of Stock Options). • Low Volatility may not offer good premium for Shorting CEs for the hedged leg, thereby reducing the loss area/ Breakeven Strike upon reversal besides low Premium as profit from Theta decay. • Sometimes, it may be prudent to Short ITM CE for the hedged leg, to have larger Breakeven room on the downside on this Strategy. But this Strategy may pose risk in instruments (<i>like FNO stocks</i>)	<u>Demerits:</u> • Max reward / profit is limited and max loss situation is unlimited. • Shorting Futures and Shorting Options, both require huge margin and MTM issues. • While, Covered Put Strategy can also be played as Poor Man's Covered Put, in which Futures' Short primary leg is replaced with Synthetic Futures i.e. ITM PE with almost 100% Intrinsic Value, however, such deep ITM PE may not be liquid (especially in case of Stock Options). • Low Volatility may not offer good premium for Shorting PEs for the hedged leg, thereby reducing the loss area/ Breakeven Strike upon reversal besides low Premium as profit from Theta decay. • Sometimes, it may be prudent to Short ITM PE for the hedged leg, to have larger Breakeven room on the upside on this Strategy. But this Strategy may pose risk in instruments (<i>like FNO stocks</i>) where there is a requirement to comply with physical

where there is a requirement to comply with physical delivery obligations. Because if the primary leg and/or Short leg comprising of FNO instruments expires as an ITM of such underlying / assets (which is subject of physical delivery obligations), then even though the Strategy may be overall profitable, but the trader would have to unnecessarily comply with the physical delivery obligations. Hence, even if such assets/ underlying are chosen to play Covered Call (even, Big Boy's Covered Call), then it is advisable to not hold the positions in Futures or Options till Expiry (or even near to Expiry). Instead, it is advisable to play this Strategy on Indices/ assets, where there is no requirements toward physical delivery <i>viz. Nifty F&O / BankNifty F&O etc.</i>	delivery obligations. Because if the primary leg and/or Short leg comprising of FNO instruments expires as an ITM of such underlying / assets (which is subject of physical delivery obligations), then even though the Strategy may be overall profitable, but the trader would have to unnecessarily comply with the physical delivery obligations. Hence, even if such assets/ underlying are chosen to play Covered Call (even, Big Boy's Covered Call), then it is advisable to not hold the positions in Futures or Options till Expiry (or even near to Expiry). Instead, it is advisable to play this Strategy on Indices/ assets, where there is no requirements toward physical delivery <i>viz. Nifty F&O / BankNifty F&O etc.</i>
<u>Benefits of Covered Call:</u> • Futures' Long primary leg can be replaced with Synthetic Futures i.e. Long ITM CE with almost 100% Intrinsic Value (called, Poor Man's Covered Call) to avoid huge margin and MTM requirements applicable on Futures. Further, such Synthetic Futures restricts the loss to maximum extent of the net premium debit incurred on the Strategy (<i>i.e. premium debit incurred on buying Synthetic Futures (deep ITM CE) minus premium credit collected on CE Short leg</i>).	<u>Benefits of Covered Put:</u> • Futures' Short primary leg can be replaced with Synthetic Futures i.e. Long ITM PE with almost 100% Intrinsic Value (called, Poor Man's Covered Put) to avoid huge margin and MTM requirements applicable on Futures. Further, such Synthetic Futures restricts the loss to maximum extent of the premium debit incurred on the Strategy (<i>i.e. premium debit incurred on buying Synthetic Futures (deep ITM PE) minus premium credit collected on PE Short leg</i>).

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| <ul style="list-style-type: none"> • This Covered Call Strategy can also be used to hedge investments made in Stocks/ other segments. This is done by way of initiating CE Short position as a hedged leg, to hedge the already existing position in cash segment i.e. investments (called, Big Boy's Covered Call). While, the hedged leg continues to protect the downside on the already existing investments (in stocks, Nifty Bees, Bank Bees etc.), the hedged leg can help earn regular income by virtue of Theta impact on OTM CE Short leg by its Expiry. This process of introduction of hedged leg can be done regularly to earn rental income on investments until the OTM CE Short leg becomes a deep ITM, requiring the investments held on the primary leg to be liquidated. We have covered this Strategy in detail in the Next Chapter (Customised Strategies). Big Boy's Covered Call on Stocks should not be held until expiry due to physical delivery obligations applicable on F&O Stocks. • This is a very suitable Strategy for a mild bullish to rangebound underlying (as the CE Short hedged leg would generate profit due to Theta impact). • This Strategy is also suitable when the Volatility is relatively high, as CE Shorts for the hedged leg can be initiated at suitable Near OTM Strikes with good Premium. When India VIX is high (<i>like above 20 or so</i>), then good premium credit can | <ul style="list-style-type: none"> • This is a very suitable Strategy for a mild bearish to rangebound underlying (as the PE Short hedged leg would generate profit due to Theta impact). • This Strategy is also suitable when the Volatility is relatively high, as PE Shorts for the hedged leg can be initiated at suitable Near OTM Strikes with good Premium. When India VIX is high (<i>like above 20 or so</i>), then good premium credit can be targeted on Near ITM / ATM / Near OTM PE Strikes for the Short leg, and profit margin in such cases increases phenomenally. |
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be targeted on Near ITM / ATM / Near OTM CE Strikes for the Short leg, and profit margin in such cases increases phenomenally.	
<u>Breakeven Strike from Expiry perspective:</u> So long the underlying keeps moving higher this Strategy would be in profit. Further, if the underlying closes by Expiry, between the CE Short Strike and the Breakeven Strike of this Strategy, then this Strategy would yield profit. Therefore, there is no upside risk on this Strategy. However, if the underlying starts falling, then Futures Long primary leg would start generating loss and CE Short leg would start generating profit. The CE Short leg can generate profit to the maximum extent of Premium credit received. Therefore, from Expiry perspective, if the underlying starts falling, then Futures' Long primary leg would start giving unlimited loss; and CE Short hedged leg would be able to cover the losses incurred on Futures Long primary leg to the maximum extent of the Premium Credit received on the CE Short position. Therefore, there is an unlimited downside risk in this Strategy. Thus, we need to understand the Breakeven level below which if the underlying closes on Expiry, then this Strategy would yield loss. <u>BE Strike Level of Strategy:</u> The Breakeven Price level, below which the loss will arise in this Strategy is calculated as:	<u>Breakeven Strike from Expiry perspective:</u> So long the underlying keeps moving lower this Strategy would be in profit. Further, if the underlying closes by Expiry, between the PE Short Strike and the Breakeven Strike of this Strategy, then this Strategy would yield profit. Therefore, there is no downside risk on this Strategy. However, if the underlying starts rising higher, then Futures Short primary leg would start generating loss and PE Short leg would start generating profit. The PE Short leg can generate profit to the maximum extent of Premium credit received. Therefore, from Expiry perspective, if the underlying starts rising higher, then Futures' Short primary leg would start giving unlimited loss; and PE Short hedged leg would be able to cover the losses incurred on Futures Short primary leg to the maximum extent of the Premium Credit received on the PE Short position. Therefore, there is an unlimited upside risk in this Strategy. Thus, we need to understand the Breakeven level above which if the underlying closes on Expiry, then this Strategy would yield loss. <u>BE Strike Level of Strategy:</u> Accordingly, the Breakeven Price level, above which the loss will arise in this Strategy is calculated as: Breakeven Strike: [Futures' Sell Price + Premium Credit received on PE Short].

Breakeven Strike: [Futures Buy Price – Premium Credit received on CE Short]. Below this level, this Strategy would enter into unlimited loss situation. <i>For Example: If Nifty Futures is at 17000 and a Covered Call Strategy is initiated with the following legs:</i> • Nifty Futures Long 17000; and • Nifty ATM CE 17000 Short at Rs. 200 Premium <i>then the Breakeven level would be: 17000 – 200 = 16800.</i> <i>Thus, from Expiry perspective, if the underlying slips below 16800, then this Covered Call Strategy would yield loss. Lower the underlying trends by Expiry below the said Breakeven level, greater the loss incurred on this Strategy.</i> If the underlying closes above the BE Strike, then the Strategy would yield profit. A near ITM CE has more premium than OTM CE Strike, therefore, if for the hedged leg an ITM CE Short Strike is used then the Breakeven gets expanded and more favourable. That is: below this BE Strike if underlying closes by Expiry, then loss situation will arise; and if underlying closes anywhere higher than the BE Strike, the Strategy would yield some profit.	Above this level, this Strategy would enter into unlimited loss situation. <i>For Example: If Nifty Futures is at 17000 and a Covered Put Strategy is initiated with the following legs:</i> • Nifty Futures Sell 17000; and • Nifty ITM PE 17100 Short at Rs. 250 Premium <i>then the Breakeven level would be: 17000 + 250 = 17250.</i> <i>Thus, from Expiry perspective, if the underlying is found trending above 17250 Strike, then this Covered Put Strategy would yield loss. Higher the underlying trends by Expiry above the said Breakeven level, greater the loss incurred on this Strategy.</i> If the underlying closes below the BE Strike, then the Strategy would yield profit. A near ITM PE has more premium than OTM PE Strike, therefore, if for the hedged leg an ITM PE Short Strike is used then the Breakeven gets expanded and more favourable. That is: above this BE Strike if underlying closes by Expiry, then loss situation will arise; and if underlying closes anywhere lower than the BE Strike, the Strategy would yield some profit.
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Payoff Chart of Covered Call  The chart shows the payoff of a Covered Call strategy. The vertical axis represents profit/loss, and the horizontal axis represents the underlying price. A green line shows the payoff, which is flat at a level labeled 'BE = Futures Price - CE Short Premium' until it reaches the 'CE Short Strike Price'. After this point, the line slopes upward, labeled 'Limited Max Profit'. A red line shows the loss, which is flat at a level labeled 'Unlimited Loss below BE' for prices below the breakeven point. A vertical dashed line marks the 'CE Short Strike Price'.	Payoff Chart of Covered Put  The chart shows the payoff of a Covered Put strategy. The vertical axis represents profit/loss, and the horizontal axis represents the underlying price. A green line shows the payoff, which is flat at a level labeled 'BE = Futures Short + PE Short Premium' until it reaches the 'PE Short Strike Price'. After this point, the line slopes downward, labeled 'Unlimited Loss below BE'. A red line shows the loss, which is flat at a level labeled 'Unlimited Loss below BE' for prices below the breakeven point. A vertical dashed line marks the 'PE Short Strike Price'.
Max Loss from Expiry perspective: Below the Breakeven price level, there could be unlimited loss in this Strategy if the underlying keeps slipping down below the Breakeven Strike level of this Strategy. Loss Level: If by Expiry, the underlying closes on the downside, below the Breakeven Strike level of the Strategy, then from this BE level onwards the loss would commence and become unlimited as the underlying keeps falling below the said BE Strike level of the Strategy. <i>For Example: If Nifty Futures is at 17000 and a Covered Call Strategy is initiated with the following legs:</i> • Nifty Futures Long 17000; • Nifty ATM CE 17000 Short at Rs. 200 Premium <i>then if Nifty Futures starts slipping below the Breakeven level of 16800 (i.e. 17000 – 200) then this Strategy would start incurring unlimited loss.</i>	Max Loss from Expiry perspective: Above the Breakeven price level, there could be unlimited loss in this Strategy if the underlying keeps rising higher above the Breakeven Strike level of this Strategy. Loss Level: If by Expiry, the underlying closes on the upside, above the Breakeven Strike level of the Strategy, then from this BE level onwards the loss would commence and become unlimited as the underlying keeps trending higher the said BE Strike level of the Strategy. <i>For Example: If Nifty Futures is at 17000 and a Covered Put Strategy is initiated with the following legs:</i> • Nifty Futures Sell 17000; and • Nifty ITM PE 17100 Short at Rs. 250 Premium <i>then if Nifty Futures starts rising above the Breakeven level of 17250 (i.e. 17000 + 250) then this Strategy would start incurring unlimited loss.</i> Covered Put with Limited Max Loss: If the Covered Put is initiated as a Poor Man's Covered Put (i.e. with deep ITM PE

<u>Covered Call with Limited Max Loss:</u> If the Covered Call is initiated as a Poor Man's Covered Call (<i>i.e. with deep ITM CE having almost 100% Intrinsic Value, instead of Futures Long on the primary leg</i>), then the unlimited max loss situation on a regular Covered Call, would get curtailed to the limited extent of the net premium debit incurred in the Strategy (<i>i.e. premium debit paid on deep ITM CE minus premium credit collected on CE Short hedged leg</i>). This is a big advantage of a Poor Man's Covered Call.	<i>having almost 100% Intrinsic Value, instead of Futures Short on the primary leg</i>), then the unlimited max loss situation on a regular Covered Put, would get curtailed to the limited extent of the net premium debit incurred in the Strategy (<i>i.e. premium debit paid on deep ITM PE minus premium credit collected on PE Short hedged leg</i>). This is a big advantage of a Poor Man's Covered Put.
<u>Max Reward from Expiry perspective:</u> If the underlying moves upwardly, then the Futures' Buy primary leg would be in profit; but if the Futures trends much higher crossing above the CE Short Strike, then the Futures Long leg will generate profit but CE Short hedged leg would start generating loss. However, due to the Delta difference between the Futures' Long primary leg and the CE Short hedged leg, the Strategy would be in net profit and would generate limited max profit even if the underlying expires at or keeps trending higher than the CE Short leg. <u>Max Profit Level:</u> Thus, the maximum limited reward would be generated in this Strategy, if by Expiry the underlying closes at CE Short Strike or at any higher Strike than the CE Short Strike. This max reward, which is however limited, is calculated as: Max profit = [CE Short Strike + premium credit received] – [Futures Buying Price] x Lot qty Thus, this maximum limited reward situation can be targeted on this Strategy	<u>Max Reward from Expiry perspective:</u> If the underlying moves downwardly, then the Futures' Sell primary leg would be in profit; but if the Futures trends much lower crossing below the PE Short Strike, then the Futures Short leg will generate profit but PE Short hedged leg would start generating loss. However, due to the Delta difference between the Futures' Short primary leg and the PE Short hedged leg, the Strategy would be in net profit and would generate limited max profit even if the underlying expires at or keeps trending lower than the PE Short leg. <u>Max Profit Level:</u> Thus, the maximum limited reward would be generated in this Strategy, if by Expiry the underlying closes at PE Short Strike or at any lower Strike than the PE Short Strike. This max reward, which is however limited, and is calculated as: Max profit = [PE Short Strike - premium credit received] – [Futures Selling Price] x Lot qty Thus, this maximum limited reward situation can be targeted on this Strategy

when the view is rangebound to mildly bullish on the underlying. <u>Profit Zone:</u> If by Expiry the underlying closes between the CE Short Strike and the BE Strike of the Strategy, then also this Strategy would generate some profit. However, if the underlying would close by Expiry closer towards the CE Short Strike, then the profit would be relatively higher, but if the underlying closes lower towards the BE Strike of the Strategy then the profit would be less.	when the view is rangebound to mildly bearish on the underlying. <u>Profit Zone:</u> If by Expiry the underlying closes between the PE Short Strike and the BE Strike of the Strategy, then also this Strategy would generate some profit. However, if the underlying would close by Expiry closer towards the PE Short Strike, then the profit would be relatively higher, but if the underlying closes higher towards the BE Strike of the Strategy then the profit would be less.
<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level:</u> [Futures Buying Price - Premium Credit received on CE Short leg] <u>Min Profit Level:</u> If underlying closes by Expiry above the BE Level <u>Max Profit Level:</u> If underlying closes by Expiry at or anywhere higher than the CE Short Strike <u>Profit Zone:</u> If underlying closes by Expiry anywhere higher than the BE Level. If underlying closes at or higher than CE Short Strike, then Max Profit is generated; and if underlying closes towards the BE Level (<i>on the downside</i>) then less profit generated on the Spread. <u>Loss Starting Level:</u> If underlying closes by Expiry below the BE Level. <u>Max Loss Level:</u> If underlying closes by Expiry, below the BE Level, then the unlimited loss area starts; lower the underlying would close below the BE Level, higher will be the loss incurred on the Strategy. Thus, below the BE level,	<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level:</u> [Futures Selling Price + Premium Credit received on PE Short leg] <u>Min Profit Level:</u> If underlying closes by Expiry below the BE Level <u>Max Profit Level:</u> If underlying closes by Expiry at or anywhere lower than the PE Short Strike <u>Profit Zone:</u> If underlying closes by Expiry anywhere lower than the BE Level. If underlying closes at or lower than PE Short Strike, then Max Profit is generated; and if underlying closes towards the BE Level (<i>on the upside</i>) then less profit generated on the Spread. <u>Loss Starting Level:</u> If underlying closes by Expiry above the BE Level. <u>Max Loss Level:</u> If underlying closes by Expiry, above the BE Level, then the unlimited loss area starts; higher the underlying would close above the BE Level, higher will be the loss incurred on the Strategy. Thus, above the BE level, unlimited Max Loss may occur,

unlimited Max Loss may occur, depending on the fall in the underlying below the BE Level by Expiry. <u>Loss Zone:</u> If underlying closes by Expiry anywhere lower than the BE Level, the Strategy enters into unlimited loss area. Lower the underlying will close by Expiry, higher will be the loss incurred on the Strategy.	depending on the rise in the underlying above the BE Level by Expiry. <u>Loss Zone:</u> If underlying closes by Expiry anywhere higher than the BE Level, the Strategy enters into unlimited loss area. Higher the underlying will close by Expiry, higher will be the loss incurred on the Strategy.
<u>Options behaviour:</u> The primary objective in a regular Covered Call is to target profit due to rangebound-to-mild bullish move in the underlying. However, even if the underlying gets bullish such that the underlying closes by Expiry at or higher than the CE Short leg, then the max reward would be reaped on the Strategy. This max reward on the Strategy would be limited, irrespective of how much higher the underlying keeps trending beyond the CE Short Strike level by the Expiry. The Delta difference between the Futures Long (<i>or Synthetic Futures: Deep ITM CE in case of Poor Man's Covered Call Strategy</i>) primary leg and CE Short hedged leg, helps to maintain a balance between the net profit position, in case of extreme bullish move in the underlying. In case the underlying remains rangebound, then there will not be erosion on the Futures Long primary leg, but the CE Short leg will lose its premium (<i>due to expansion & erosion in its Time Value</i>), thereby generating profit on the overall Strategy. Further, in case the underlying remains rangebound, and there is Volatility	<u>Options behaviour:</u> The primary objective in a regular Covered Put is to target profit due to rangebound-to-mild bearish move in the underlying. However, even if the underlying gets bearish such that the underlying closes by Expiry at or lower than the PE Short leg, then the limited max reward would be reaped on the Strategy. The Delta difference between the Futures Short (<i>or Synthetic Futures: Deep ITM PE in case of Poor Man's Covered Put Strategy</i>) on the primary and the PE Short hedged leg, helps to maintain a balance between the net profit position, in case of extreme bearish move in the underlying. The Delta difference in the Futures Short & PE Short leg would help ensuring the limited max profit on this Strategy, in the aforesaid situation, i.e. howsoever low the underlying keeps going below the PE Short Strike and closes by Expiry lower than the PE Short Strike, the max reward would be same. In case the underlying remains rangebound, then there will not be erosion on the Futures Short primary leg, but the PE Short leg will lose its premium (<i>due to expansion & erosion in its Time</i>

crash (*i.e. India VIX crashes from 18 to 12*), then there will not be erosion on the Futures Long primary leg, but the CE Short leg will lose its premium due to erosion in its Time Value due to volatility crash. Thus, the Strategy would generate profit in such situation.

Also, if after a long holding time, the underlying closes around the same level where the Strategy was initiated, then also there will not be much loss on the Futures Long primary leg, but the Theta impact on the CE short leg would generate profit on the Strategy to the extent of erosion in its Time Value.

If the **underlying falls down, but closes on Expiry between the CE Short Strike and the Breakeven Strike** (*i.e. without breaching the BE Strike of the Strategy downwardly*), then too this Strategy would yield some profit, because the loss in the Futures position would not be more than the profit generated on the CE Short leg (*because the CE Short leg in such situation would expire worthless as OTM and entire premium credit would be the profit on the CE Short leg, which would set-off the loss on Futures Long leg*). However, in the aforesaid situation, lower the Futures fall towards the BE Strike level of the Strategy, lower would be the profit generated on the Strategy.

However, if the **underlying falls down and closes on Expiry below the Breakeven Strike** (*i.e. breaching the BE Strike of the Strategy downwardly*), then the Strategy would yield loss, because the entire premium credit on CE Short leg would get exhausted due to the big downfall/ gapdown and the hedged leg therefore will not be able to cover for any

Value), thereby generating profit on the overall Strategy.

Further, in case the **underlying remains rangebound, and there is Volatility crash** (*i.e. India VIX crashes from 18 to 12*), then there will not be erosion on the Futures Short primary leg, but the PE Short leg will lose its premium due to erosion in its Time Value due to volatility crash. Thus, the Strategy would generate profit in such situation.

Also, if after a long holding time, the underlying closes around the same level where the Strategy was initiated, then also there will not be much loss on the Futures Short primary leg, but the Theta impact on the PE short leg would generate profit on the Strategy to the extent of erosion in its Time Value.

If the **underlying surges upwardly, but closes on Expiry between the PE Short Strike and the Breakeven Strike** (*i.e. without breaching the BE Strike of the Strategy upwardly*), then too this Strategy would yield some profit, because the loss in the Futures position would not be more than the profit generated on the PE Short leg (*because the PE Short leg in such situation would expire worthless as OTM and entire premium credit would be the profit on the PE Short leg, which would set-off the loss on Futures Short leg*). However, in the aforesaid situation, higher the Futures rise towards the BE Strike level of the Strategy, lower would be the profit generated on the Strategy.

However, if the **underlying gets trending upwardly and closes on Expiry above the Breakeven Strike** (*i.e. breaching the BE Strike of the Strategy upwardly*), then the

loss below the BE Strike level of the Strategy. In such situation, lower the underlying would fall below the BE Strike of the Strategy, the Futures Long position (<i>having positive Delta of 1, on per Lot basis</i>) would keep generating loss on the Strategy. Further, in such situation, regular Covered Call with Futures Long position on the primary leg, would keep generating unlimited loss as the fall extends in the underlying. However, if the Strategy is played as a Poor Man's Covered Call (<i>with primary leg comprising of Deep ITM CE</i>), then the max loss on the Strategy would be limited to the extent of net premium debit incurred on the Strategy, in the event the underlying keep extending its fall.	Strategy would yield loss, because the entire premium credit on PE Short leg would get exhausted due to the strong upmove/ gapup in the underlying and the hedged leg therefore will not be able to cover for any loss above the BE Strike level of the Strategy. In such situation, higher the underlying rises above the BE Strike of the Strategy, the Futures Short position (<i>having negative Delta of 1, on per Lot basis</i>) would keep generating loss on the Strategy. Further, in such situation, regular Covered Call with Futures Short position on the primary leg, would keep generating unlimited loss as the upward move continues in the underlying. However, if the Strategy is played as a Poor Man's Covered Put (<i>with primary leg comprising of Deep ITM PE</i>), then the max loss on the Strategy would be limited to the extent of net premium debit incurred on the Strategy, in the event the underlying keep extending its uptrend.
<u>Strike / Delta value:</u> • Future has Delta value of 1 • CE Short can be initiated with a Delta value of 0.5 to 0.6 (<i>0.5 Delta is of ATM and 0.6 is of near ITM</i>) Even Synthetic Futures (<i>deep ITM CE</i>) in Poor Man's Covered Call Strategy, would also have a Delta value close to 1. The Delta difference between the primary leg and the hedged leg will help ensure max reward in this Strategy if by Expiry the Futures closes at CE Short Strike or at any higher Strike than the CE Short Strike. For a strong conviction bullish to sideways view, a lower Delta value ATM	<u>Strike / Delta value:</u> • Future has Delta value of 1 • PE Short can be initiated with a Delta value of 0.5 to 0.6 (<i>0.5 Delta is of ATM and 0.6 is of near ITM</i>) Even Synthetic Futures (<i>deep ITM PE</i>) in Poor Man's Covered Put Strategy, would also have a Delta value close to 1. The Delta difference between the primary leg and the hedged leg will help ensure max reward in this Strategy if by Expiry the Futures closes at PE Short Strike or at any lower Strike than the PE Short Strike. For a strong conviction bearish to sideways view, a lower Delta value ATM PE would be suitable; but where the view

CE would be suitable; but where the view is little uncertain and reversal seems a good possibility then it is better to initiate CE Short at Near ITM with higher Delta value (<i>in order to maintain a net lower Delta difference between the primary leg and the hedged leg</i>) and a larger Breakeven room to cover the loss on the downside (<i>also this BE level from which profit would be generated on the Strategy, will be much lower, if ITM CE is shorted instead of an ATM CE. Hence enhancing the profit probability in case of a bullish view</i>). It is pertinent to note that a higher CE Strike (<i>like Near OTM Strike, as against ITM</i>) on the hedged leg, would have higher profit potential, because the max profit is generated if Expiry happens at CE Short leg or higher. Therefore, higher the CE Short Strike, larger the profit potential, if Futures expires at that CE Short Strike or even higher. But at the same time, in case of a higher OTM CE Short Strike, the underlying will have to travel much higher upto the CE Short Strike in order to generate max profit on the Strategy. But a lower CE Strike (<i>like Near ITM Strike, as against OTM</i>) offers higher Delta and larger Breakeven room, to mitigate the loss on the downside. But lower CE Strike would reduce the limited max profit potential on the Strategy. But at the same time, in case of a lower OTM CE Short Strike, the underlying will have to close only little higher (i.e. upto the CE Short Strike) in order to generate max profit on the Strategy.	is little uncertain and reversal seems a good possibility then it is better to initiate PE Short at Near ITM with higher Delta value (<i>in order to maintain a net lower Delta difference between the primary leg and the hedged leg</i>) and a larger Breakeven room to cover the loss on the upside (<i>also this BE level from which profit would be generated on the Strategy, will be much higher, if ITM PE is shorted instead of an ATM PE. Hence enhancing the profit probability in case of a bearish view</i>). It is pertinent to note that a lower PE Strike (<i>like Near OTM Strike, as against ITM</i>) on the hedged leg, would have higher profit potential, because the max profit is generated if Expiry happens at PE Short leg or lower. Therefore, lower the PE Short Strike, larger the profit potential, if Futures expires at that PE Short Strike or even lower. But at the same time, in case of a lower OTM PE Short Strike, the underlying will have to travel much lower upto the PE Short Strike in order to generate max profit on the Strategy. But a higher PE Strike (<i>like Near ITM Strike, as against OTM</i>) offers higher Delta and larger Breakeven room, to mitigate the loss on the upside. But lower CE Strike would reduce the limited max profit potential on the Strategy. But at the same time, in case of a lower OTM PE Short Strike, the underlying will have to close only little lower (i.e. upto the PE Short Strike) in order to generate max profit on the Strategy.
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Selection of Option Strike for hedged leg:

CE Strike for the hedged leg in this Strategy should be such which should have decent Premium value. Next Month or farther Expiry CE may have higher Premium but lower Theta impact.

Further, its Delta value should be such that it does not eat away much profit from the primary leg; and at the same time is able to cover losses reasonably that may occur on the primary leg if the trade does not go as per plan.

Also, the CE Short should be initiated at such Strike, keeping in mind that if the underlying remains sideways then the Theta impact should yield reasonable profit in the hedged leg. Current Month CE will have higher Theta impact.

Also, lower CE Short Strike will have less amount of max profit, but a higher probability to generate max profit in case the underlying by Expiry closes near the CE Short Strike. However, a higher CE Short Strike will have higher amount of max profit, but the underlying will have to close higher i.e. upwardly upto the higher CE Short Strike, in order to generate max reward on the Strategy.

If there is rise in Volatility then CE Short on the hedged leg may be done at good Premium value at Far OTM CE Strikes, to target profit from Theta decay on the CE Short positions, especially if view on the underlying is inclined more on the bullish side.

Basis aforesaid factors, depending on the intended holding time of the trade, a

Selection of Option Strike for hedged leg:

PE Strike for the hedged leg in this Strategy should be such which should have decent Premium value. Next Month or farther Expiry PE may have higher Premium but lower Theta impact.

Further, its Delta value should be such that it does not eat away much profit from the primary leg; and at the same time is able to cover losses reasonably that may occur on the primary leg if the trade does not go as per plan.

Also, the PE Short should be initiated at such Strike, keeping in mind that if the underlying remains sideways then the Theta impact should yield reasonable profit in the hedged leg. Current Month PE will have higher Theta impact.

Also, higher PE Short Strike will have less amount of max profit, but a higher probability to generate max profit in case the underlying by Expiry closes near the PE Short Strike. However, a lower PE Short Strike will have higher amount of max profit, but the underlying will have to close lower i.e. downwardly upto the lower PE Short Strike, in order to generate max reward on the Strategy.

If there is rise in Volatility then PE Short on the hedged leg may be done at good Premium value at Far OTM PE Strikes, to target profit from Theta decay on the PE Short positions, especially if view on the underlying is inclined more on the bearish side.

Basis aforesaid factors, depending on the intended holding time of the trade, a suitable PE Option Strike level of a

suitable CE Option Strike level of a particular Expiry series and Delta value may be selected for the hedged leg.	particular Expiry series and Delta value may be selected for the hedged leg.
<u>If trade goes as per plan:</u> Future goes higher, Future Long primary leg will generate profit. But with Future going higher, the hedged CE Short leg will generate loss (<i>because the LTP of CE Short leg will rise due to underlying going upward</i>). However, the Delta difference between the primary leg and hedged leg will bring the net position in profit. But as the underlying expires at the CE Short Strike or anywhere on any higher Strike, then the Strategy would yield the limited, pre-determined, max profit on the Strategy. In such situation, profit target on this Strategy is achieved and hence profit must be booked. <u>If underlying becomes sideways:</u> If the underlying keeps fluctuating in a range, then the primary leg (being Futures position) will not get impacted with Theta; but the hedged leg would generate profit due to rangebound fluctuations in the underlying as well as due to Theta impact with passage of time. This situation may likely result in profit in both primary and hedged leg, if Futures end up closing even slightly higher than its buying price. <u>If trade does not go as per plan:</u> Future starts falling, and Futures Long primary leg will generate loss. But with Futures falling down, the hedged CE Short leg will generate limited profit to the extent of Premium received on the	<u>If trade goes as per plan:</u> Future goes lower, Future Short primary leg will generate profit. But with Future going lower, the hedged PE Short leg will generate loss (<i>because the LTP of PE Short leg will rise due to underlying going downward</i>). However, the Delta difference between the primary leg and hedged leg will bring the net position in profit. But as the underlying expires at the PE Short Strike or anywhere on any lower Strike, then the Strategy would yield the limited, pre-determined, max profit on the Strategy. In such situation, profit target on this Strategy is achieved and hence profit must be booked. <u>If underlying becomes sideways:</u> If the underlying keeps fluctuating in a range, then the primary leg (being Futures position) will not get impacted with Theta; but the hedged leg would generate profit due to rangebound fluctuations in the underlying as well as due to Theta impact with passage of time. This situation may likely result in profit in both primary and hedged leg, if Futures end up closing even slightly lower from its selling price. <u>If trade does not go as per plan:</u> Future starts rising, and Future Short primary leg will generate loss. But with Futures rising up, the hedged PE Short leg will generate limited profit to the extent of Premium received on the Short position. Thus, the PE Short hedged leg will protect

Short position. Thus, the CE Short hedged leg will protect the loss in Futures Long primary leg to the extent of Premium collected on the CE Short hedged leg. Accordingly, if by Expiry the underlying closes between the CE Short Strike and the BE Strike level of the Strategy, then also due to premium credit collected on CE Short leg, the Strategy would yield some profit. If underlying closes towards the CE Short Strike then profit would be closer to Max Profit, but if the underlying closes by Expiry towards the BE Strike of the Strategy, then the profit will be less. However, if the underlying keeps falling even further breaching the Breakeven Strike of the Strategy downwardly, then beyond this level the premium credit of the CE Short leg would get exhausted and the Futures Long primary leg (<i>which is having a positive Delta of 1, per Lot basis</i>) will start incurring losses; and in such situation the trade need to be adjusted to mitigate potential losses which may be unlimited if the underlying keeps falling.	the loss in Futures Short primary leg to the extent of Premium collected on the PE Short hedged leg. Accordingly, if by Expiry the underlying closes between the PE Short Strike and the BE Strike level of the Strategy, then also due to premium credit collected on PE Short leg, the Strategy would yield some profit. If underlying closes towards the PE Short Strike then profit would be closer to Max Profit, but if the underlying closes by Expiry towards the BE Strike of the Strategy, then the profit will be less. However, if the Futures keeps rising even further breaching the Breakeven Strike of the Strategy upwardly, then beyond this level the premium credit of the PE Short leg would get exhausted and the Futures Short primary leg (<i>which is having a negative Delta of 1, per Lot basis</i>) will start incurring losses; and in such situation the trade need to be adjusted to mitigate potential losses which may be unlimited if the underlying keeps trending upwardly.
<u>Adjustments (if trade does not go as per plan):</u> Since, hedged leg will be able to cover the losses arising in the primary leg to the extent of the Premium received on CE Short, the following adjustments may be considered: (i) Long PE; or (ii) Short CE. These adjustments are discussed below. (i) If there seems to be a trending downtrend, then PEs can be bought (Long PE). Buying OTM	<u>Adjustments (if trade does not go as per plan):</u> Since, hedged leg will be able to cover the losses arising in the primary leg to the extent of the Premium received on PE Short, the following adjustments may be considered: (i) Long CE; or (ii) Short PE. These adjustments are discussed below. (i) If there seems to be a trending uptrend, then CEs can be bought (Long CE). Buying OTM CEs to protect the upside risk in a Covered

PEs to protect the downside risk in a Covered Call with OTM CE Short converts such a Covered Call into **Collar** (i.e. Covered Call with OTM CE Short + Long OTM PE). This additional PE will overcome the limitation of limited downside protection offered by the hedged leg of CE Short; and this PE Long position will take care of unlimited bearish trend if it continues. Buying PEs to protect the downside risk in this Strategy will add a debit position, therefore this PE Long should only be prudent to initiate only if there is strong momentum for the downward direction.

While, the PE Long position will help CE Short to mitigate the loss incurred on the Futures Long/Cash buy in primary leg, but the difference between the Delta value of the Futures Long and PE Long will determine the net loss. Thus, depending upon the momentum in the downtrend, suitable Delta value of PEs can be added at higher Strike levels (ITM PEs would be preferable if downtrend is expected with momentum so as to suitably cover the losses in Futures Long position), so that in case of continuation of strong downtrend, Long PEs should generate more profit and help cover losses in the Futures Long primary leg. Also, depending upon the likely downtrend momentum, suitable number of Long PEs can be considered to be added as an

Put with OTM PE Short converts makes it akin to **Collar** strategy for the Covered Put. This additional CE will overcome the limitation of limited upside protection offered by the hedged leg of PE Short; and this CE Long position will take care of unlimited bullish trend if it continues. Buying CEs to protect the upside risk in this Strategy will add a debit position, therefore this CE Long should only be prudent to initiate only if there is strong momentum for the upward direction.

While, the CE Long position will help PE Short to mitigate the loss incurred on the Futures Short/Cash Short in primary leg, but the difference between the Delta value of the Futures Short and CE Long will determine the net loss. Thus, depending upon the momentum in the upside, suitable Delta value of CEs can be added (ITM CEs would be preferable if uptrend is expected with momentum so as to suitably cover the losses in Futures Short position), so that in case of continuation of strong uptrend, Long CEs should generate more profit and help cover losses in the Futures Short primary leg. Also, depending upon the likely uptrend momentum, suitable number of Long CEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 4 to 8 times more Lot quantity may be required to be added to Long CEs in comparison to the original number of Lots initiated on the hedged leg of

adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 4 to 8 times more Lot quantity may be required to be added to Long PEs in comparison to the original number of Lots initiated on the hedged leg of this Strategy. Such number of PEs must be added, such that the effective overall Delta position of the Strategy becomes negative (thus, favourable for the bearish move in the underlying).

- (ii) If there seems to be a slow downtrend, then an **OTM CEs can be sold (Short CE)**. This additional CE Short will cover further losses that may be incurred in the Futures primary leg as the downtrend continues, to the extent of Premium received by selling this additional CE. **Far OTM CEs can be sold (CE Short)** above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry in case of a reversal towards uptrend. Idea in this adjustment is to pick up suitable Far OTM CEs for Shorting, such that this Far OTM CEs expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This CE Short will help cover the loss generated on the original Strategy (due to Futures Long primary leg). Generally, atleast 4 to 8 times more Lot quantity may be required to be added to Short CE in comparison to the original

this Strategy. Such number of CEs must be added, such that the effective overall Delta position of the Strategy becomes positive (thus, favourable for the bullish move in the underlying).

- (ii) If there seems to be a slow uptrend, then an **OTM PEs can be sold (Short PE)**. This additional PE Short will cover further losses that may be incurred in the Futures primary leg as the uptrend continues, to the extent of Premium received by selling this additional PE. **Far OTM PEs can be sold (PE Short)** below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry in case of a reversal towards downtrend. Idea in this adjustment is to pick up suitable Far OTM PEs for Shorting, such that this Far OTM PEs expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This PE Short will help cover the loss generated on the original Strategy (due to Futures Short primary leg). Generally, atleast 4 to 8 times more Lot quantity may be required to be added to Short PE in comparison to the original number of Lots in the hedged leg initiated on the original Strategy. Such number of Short PEs must be added, such that the effective overall Delta position of the Strategy becomes positive (thus, favourable for the bullish move in the underlying). However, selling additional PEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.

number of Lots in the hedged leg initiated on the original Strategy. Such number of additional Short CEs must be added, such that the effective overall Delta position of the Strategy becomes negative (thus, favourable for the bearish move in the underlying). However, selling additional CEs will require higher margin / capital to Short CEs and MTM requirements will also have to be met.	
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BIG BOY'S COVERED CALL, POOR MAN'S COVERED CALL & POOR MAN'S COVERED PUT AND COLLAR STRATEGY

In the above discussions on Covered Call and Covered Put, we have also discussed about the Big Boy's Covered Call, Poor Man's Covered Call & Put and Collar Strategy. Briefly, these are explained again here:

Big Boy's Covered Call: When a CE Short position is introduced as a hedged leg to an existing investment (in Stocks, ETFs or otherwise), then such Covered Call are referred to as the Big Boy's Covered Call. For example: *Against 1500 shares of SBI on cash holding, 1 Lot Far OTM SBIN CE is sold (1 Lot of SBIN in F&O segment comprise of 1500 shares of SBI).*

Poor Man's Covered Call: When in a Covered Call strategy, Synthetic Futures (i.e. an ITM CE Option with 100% Intrinsic Value having Delta Value of 1) is employed in the primary leg instead of Futures or stocks, in order to optimize the margin requirements/ deploy less capital and to avoid MTM risk by taking main position in Futures, then such Covered Call are referred to as the Poor Man's Covered Call. Besides aforesaid, the max loss situation in a Poor Man's Covered Call gets curtailed to the maximum extent of net premium debit incurred on the Strategy (*i.e. premium paid for the deep ITM CE minus the premium credit received on the CE Short hedged leg*). For example: Long Deep ITM CE & OTM CE Short.

Poor Man's Covered Put: When in a Covered Put strategy, Synthetic Futures (i.e. an ITM PE Option with 100% Intrinsic Value having Delta Value of 1) is employed in the primary leg instead of shorting Futures or stocks, in order to optimize the margin requirements/ deploy less capital and to avoid MTM risk by taking main position in Futures, then such Covered Put are referred to as the Poor Man's Covered Put. Besides aforesaid, the max loss situation in a Poor Man's Covered Put gets curtailed to the maximum extent of net premium debit incurred on the Strategy (*i.e. premium paid for the deep ITM PE minus the premium credit received on the PE Short hedged leg*). For example: Long Deep ITM PE & OTM PE Short.

Collar Strategy: When in a Covered Call strategy, in order to contain a further downside risk (due to trending downward momentum of the underlying), Long OTM PEs position is added, then such Strategy is called a Collar in the context of a Covered Call. For example: [Futures Long + OTM CE Short] + OTM PEs Long.

Also, when a Married Put Strategy [comprising: Stocks bought + OTM PE Long] seems to be not going into a downwardly trending momentum (as was anticipated), but appears to be mildly bearish, then CE Shorts are added to cover for the losses on the Premium paid on the PE Long of Married Put. This addition of Short CEs to Married Put, also makes this Strategy, a Collar Strategy. For example: [Stocks bought + OTM PE Long] + OTM CE Short.

Likewise, when in a Covered Put strategy, in order to contain a further upside risk, a Long OTM CE position is added, then such Strategy is called a Collar in the context of a Covered Put. For example: [Futures Short + OTM PE Short] + OTM CE Long.

A comparative analysis between Covered Call and Married Put, in relation to holding position in Stocks, is separately discussed below.

COVERED CALL VS MARRIED PUT: FOR STOCK POSITIONS

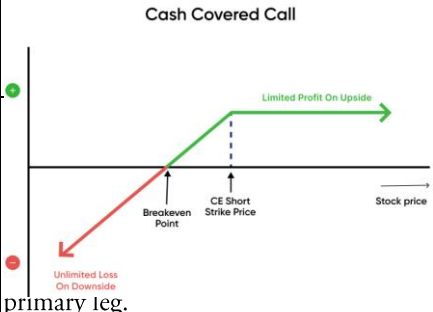
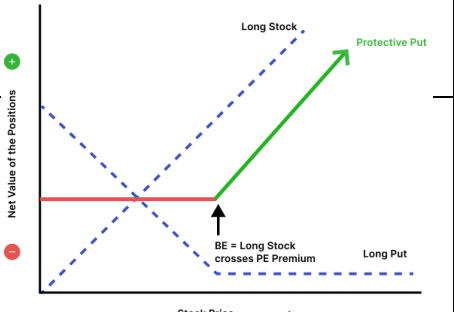
In Covered Call Strategy, existing investments are hedged by Shorting Call in order to cover the downside risk; however, the same can also be achieved by buying Puts instead of Shorting Calls. Thus, when existing investments in stocks etc. are hedged by taking a Long position in Puts of that underlying, then such Strategy is called Married Put.

With this background, now let us delve into discussing the Covered Call Strategy and Married Put Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Covered Call Strategy	Married Put Strategy
<u>Trade Legs:</u> • Stocks bought (<i>primary leg</i>) • Short CE (<i>hedged leg</i>)	<u>Trade Legs:</u> • Stocks bought (<i>primary leg</i>) • Long PE (<i>hedged leg</i>)
<u>Objective:</u> Objective is to mitigate the risk / loss that may arise if the primary leg with mild bullish view on investment gets reversed. Then upon such reversal the loss in the primary leg will get covered to some extent (i.e. <i>to the extent of Premium received on CE Short</i>) by the hedged leg initiated with a bearish view.	<u>Objective:</u> Objective is to mitigate the risk / loss that may arise if the primary leg with bullish view on the investment gets reversed. Then upon such reversal the loss in the primary leg will get covered to an unlimited extent by the PE Long position initiated as the hedged leg with a bearish view.
<u>Demerits:</u> • Shorting Options require huge margin and MTM issues need to be taken care. • Short CE in the hedged leg can cover limited risk in the stock holding position in the primary leg,	<u>Demerits:</u> • PE Long is a Debit position i.e. Premium is paid for this hedged leg, and this Premium will have to be recovered by crossing over the Breakeven Strike from Expiry perspective, else it will generate loss.

i.e. to the extent of Premium received in the CE Short position.	Long PE position in the hedged leg will be subject to time decay and will be suitable only in the event of a strong downtrend reversal on the investments held in the primary leg.
<u>Benefits of Covered Call:</u> - CE Short gives Premium as Credit. - Hedged leg can also be introduced as part of Big Boy's Covered Call Strategy to earn regular rental income therefrom. While, the hedged leg continues to protect the downside on the already existing investments (<i>such as in stocks, NiftyBees, BankNifty Bees etc.</i>), the hedged leg can help earn regular income by virtue of Theta impact on OTM CE Short leg by its Expiry. This process of introduction of hedged leg can be done regularly to earn rental income on investments. This Strategy is covered in detail in our Next Chapter (Customised Strategies). - This is a very suitable Strategy for a mild bullish to rangebound underlying (as the CE Short hedged leg would generate profit due to Theta impact).	<u>Benefits of Married Put:</u> - Buying Put is cheaper than Shorting Call. Further, there is no MTM hassle in being Long in PE. - This is a very suitable Strategy to cover losses incurred on investment position due to strong downtrend; and so long the strong downtrend continues Long PE position will generate unlimited profit.
<u>Selection of Option Strike for hedged leg:</u> For a strong conviction for mild bullish to sideways view, an ATM CE / Near OTM would be suitable; but where the view is little uncertain and reversal seems a good possibility then it is better to	<u>Selection of Option Strike for hedged leg:</u> Where continuation of uptrend in the investments gets highly uncertain and downtrend reversal seems a good possibility then it is better to initiate Married Put to hedge investments.

initiate Married Put instead of Covered Call to hedge investments. CE Strike for the hedged leg in this strategy should be such which should have decent Premium value. Next Month or farther Expiry CE may have higher Premium but lower Theta impact. Further, its Delta value should be such that it does not eat away much profit from the primary leg; and at the same time is able to cover losses reasonably that may occur on the primary leg if the trade does not go as per plan. Further, the CE Short should be initiated at such Strike, keeping in mind that if the underlying remains sideways then the Theta impact should yield reasonable profit in the hedged leg. Current Month CE will have higher Theta impact. Basis aforesaid factors, depending on the intended holding time of the trade, a suitable CE Option Strike level of a particular Expiry series and Delta value may be selected to Short.	PE Strike for the hedged leg in this strategy should be such which should have lower Theta value. Next Month or farther Expiry PE would have lower Theta impact but will be available at higher Premium. Further, depending upon the momentum in the downtrend a suitable Delta value of PE can be selected (an ITM PE would be preferable if uptrend is expected with momentum so as to suitably cover the losses in the investment position). Even Synthetic Futures i.e. deep ITM PE with 100% Intrinsic Value having Delta value of 1 can also be considered to play a sound downtrend momentum, as it will be very effective to mitigate losses in the investment positions. Such Synthetic Futures will have negligible Time Value and therefore will not be impacted with fall in Volatility or Theta impact. Basis aforesaid factors, depending on the intended holding time of the trade, a suitable PE Option of a particular Expiry series and Delta value may be selected to go Long.
<u>Breakeven Strike from Expiry perspective:</u> If the underlying starts falling, then the Breakeven Price level, below which the loss will arise in this Strategy is: [Buying Price – Premium Credit received on CE Short]. Below this level, this Strategy would enter into unlimited loss situation.	<u>Breakeven Strike from Expiry perspective:</u> If the underlying starts falling, then the Breakeven Price level, below which the profit will arise in the hedged leg of PE Long (so as to enable it to mitigate losses on the investments held in the primary leg): [PE Strike – Premium paid for the PE Long hedged leg]. Below this level, the Married Put will cover up the losses

	incurred on the investments held in the primary leg.
<u>Payoff for Cash Covered Call</u> Cash Covered Call  primary leg.	<u>Married Put or Protective Put</u>  holding investment would incur loss, as well as there will be loss in the PE Long hedged leg to the maximum extent of the Premium paid for buying the PEs.
<u>Max Reward from Expiry perspective:</u> Maximum reward would be generated in this Strategy, if the underlying by Expiry of the CE Short leg, closes at the CE Short Strike or at any higher Strike than the CE Short Strike. Thus, this maximum reward situation can be targeted on this strategy when the view is mildly bullish on the underlying.	<u>Max Reward from Expiry perspective:</u> Maximum reward would be generated in this Strategy, if by Expiry the investments held in the primary leg gets profitable due to the upward move of the underlying, and the profit incurred on the investments is much higher than the total Premium paid on the Long PEs in the hedged leg. This situation would arise, if the underlying keeps trending higher and the investments held in the primary leg gets extremely profitable after absorbing the loss on the premium paid for the Protective Puts.
<u>Collar Adjustment:</u> Addition of Married Put to the Covered Call Strategy will make it a Collar Strategy. Married Put will be required to be added to the Covered Call, if the underlying	<u>Collar Adjustment:</u> Addition of CE Short leg to this Married Put Strategy will make it a Collar Strategy. CE Short leg will be required to be added to the Married Put Strategy, if the underlying seems to be not likely to go

reverses and becomes extremely bearish trending with downward momentum. In such situation on bearish reversal, the unlimited loss situation on the Covered Call can be mitigated by adding Far OTM PEs, thereby converting Covered Call into Collar Strategy.

Conversion of Covered Call into Collar can be adopted as an adjustment to Covered Call Strategy, when the underlying does not seem to be trending upwardly with mild bullish trend but is likely to fall downwardly with momentum exhausting the Premium Credit received on the CE Short leg and pushing the Covered Call Strategy into unlimited loss situation. Thus, adding Long PEs will help counter the Collar Strategy makes the overall Strategy a limited profit and limited loss Strategy.

down with momentum and may appear to be bearish to sideways. In such situation of bearish to sideways movement of the underlying, the underlying is not expected to cross-below the Breakeven Strike of the PE Long leg and therefore the entire Premium paid on the PE Long leg would be a loss. Thus, in order to mitigate the loss of Premium paid on the PE Long leg, sufficient quantity of Far OTM CEs can be Sold, with the view that the underlying would not breach the Breakeven Strike of these CE Shorts (i.e. *CE Strike + Premium received on these CE Shorts*) and thereby these CE Shorts would expire as OTM by Expiry and the entire Premium Credit received on these CE Shorts would be the profit on these CE Shorts which will help absorb the loss of Premium on Long Puts. Thus, addition of CE Shorts to this Married Put Strategy, would convert Married Put into Collar Strategy.

Conversion of Married Put into Collar can be adopted as an adjustment to Married Put Strategy, when the underlying does not seem to be falling down with momentum (*which was the original view basis which Married Put was initiated to cover for losses on investments held in the primary leg*). Collar Strategy makes the overall Strategy a limited profit and limited loss Strategy.

BULL CALL DEBIT SPREAD & BEAR PUT DEBIT SPREAD

Bullish and Bearish view can be played through Long Options with hedged positions.

When the view on the underlying is bullish, we can play the uptrend by being Long on CE Options (i.e. buy CE Options) as our main position (the **primary leg**). This primary leg can be hedged by introducing a hedged leg with a bearish view by Shorting Call Options (i.e. sell CE Options), of the same number of Lots as in the primary leg (i.e. in the ratio of 1:1 in terms of Lots/ quantity), on the same underlying with same Expiry series (the **hedged leg**). This hedged position/ strategy where a bullish primary leg initiated with Long CE positions with higher Premium is hedged with a Call Short position with lower Premium, on the same underlying and of same Expiry series – it is called a **Bull Call Spread Strategy or Call Debit Strategy**. It is a Vertical Spread (i.e. involving two same side Options of same Expiry series on different Strikes).

Likewise, when the view on the underlying is bearish, we can play the downtrend by being Long on Put Options (i.e. buy PE Options) as our main position (the **primary leg**). This primary leg can be hedged by introducing a hedged leg with a bullish view by Shorting Put Options (i.e. sell PE Options), of the same number of Lots as in the primary leg (i.e. in the ratio of 1:1 in terms of Lots/ quantity), on the same underlying with same Expiry series (the **hedged leg**). This hedged position/ strategy where a bearish primary leg initiated with Long PE positions having higher Premium, is hedged with a Put Short position having lower Premium, on the same underlying and of same Expiry series – it is called a **Bear Put Spread Strategy or Put Debit Strategy**. It is a Vertical Spread (i.e. involving two same side Options of same Expiry series on different Strikes).

These Strategies have limited profit potential and pre-defined max loss.

With this background, now let us delve into discussing the Bull Call Spread Strategy and Bear Put Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Bull Call Spread Strategy	Bear Put Spread Strategy
Trade Legs: • Long CE of lower Strike with higher Premium (primary leg) • Short CE of higher Strike with lower Premium (hedged leg) Equal number of Lots in primary and hedged leg; and both legs on same Expiry series.	Trade Legs: • Long PE of higher Strike with higher Premium (primary leg) • Short PE of lower Strike with lower Premium (hedged leg) Equal number of Lots in primary and hedged leg; and both legs on same Expiry series.
Example: • Buy 2 Lots Nifty 17600 CE of Current Month Expiry series (at Rs. 75 per Lot) • Sell 2 Lots Nifty 17800 CE of Current Month Expiry series (at Rs. 50 per Lot)	Example: • Buy 3 Lots Nifty 17500 PE of Current Week Expiry series (at Rs. 95 per Lot) • Sell 3 Lots Nifty 17300 PE of Current Week Expiry series (at Rs. 60 per Lot)
Objective: Objective is to play bullish view through buying CEs (as the primary leg); and to mitigate the risk / loss that may arise on the primary leg upon reversal of the trend towards bearish side with a CE Short position (on the hedged leg). If the bullish view continues, overall the Strategy would generate a pre-defined max profit; and if there is reversal of the trend, the loss on the Strategy would also be limited and pre-defined (i.e. <i>to the extent of Net Premium debit incurred on the overall Strategy</i>). Thus, there is a limited profit potential on this Strategy if the bullish view continues, but at the same time a limited max loss scenario on the Strategy (<i>if the bullish view goes wrong</i>).	Objective: Objective is to play bearish view through buying PEs (as the primary leg); and to mitigate the risk / loss that may arise on the primary leg upon reversal of the trend towards bullish side with a PE Short position (on the hedged leg). If the bearish view continues, overall the Strategy would generate a pre-defined max profit; and if there is reversal of the trend, the loss on the Strategy would also be limited and pre-defined (i.e. <i>to the extent of Net Premium debit incurred on the overall Strategy</i>). Thus, there is a limited profit potential on this Strategy if the bearish view continues, but at the same time a limited max loss scenario on the Strategy (<i>if the bearish view goes wrong</i>).

<u>Demerits:</u> • This Strategy has limited profit potential. • This Spread strategy will be suitable for a momentum bullish view. A rangebound or slow uptrend may cause loss in the primary leg due to Theta impact (loss in primary leg would be more than the profit in the hedged leg due to Theta decay). • If the holding period is long, then Synthetic Futures (i.e. ITM CE with almost 100% Intrinsic Value) can be considered for playing the expected bullish move, with less time decay. However, Synthetic Futures (i.e. deep ITM CE) may not be liquid especially in case of Stock Options. • If the holding period is long, then this Spread must be initiated on Next Month / Far Month CE Options, especially if this Spread is being initiated after 15th of a given Current Month with a holding time of 7 days or more. However, Far Month Expiry may have liquidity issues, therefore Next Month Expiry series may be preferred, in such case. Also, Next Month & Far Month Expiry series would require relatively more capital (than the Spread on Current Month Expiry series) as CEs of the same Strike would be on higher premium value on farther Expiry series. • It is a net Premium debit Strategy. Since primary leg comprises of	<u>Demerits:</u> • This Strategy has limited profit potential. • This Spread strategy will be suitable for a momentum bearish view. A rangebound or slow downtrend may cause loss in the primary leg due to Theta impact (loss in primary leg would be more than the profit in the hedged leg due to Theta decay). • If the holding period is long, then Synthetic Futures (i.e. ITM PE with almost 100% Intrinsic Value) for playing the expected bearish move, with less time decay. However, Synthetic Futures (i.e. deep ITM PE) may not be liquid especially in case of Stock Options. • If the holding period is long, then this Spread must be initiated on Next Month / Far Month PE Options, especially if this Spread is being initiated after 15th of a given Current Month with a holding time of 7 days or more. However, Far Month Expiry may have liquidity issues, therefore Next Month Expiry series may be preferred, in such case. Also, Next Month & Far Month Expiry series would require relatively more capital (than the Spread on Current Month Expiry series) as PEs of the same Strike would be on higher premium value on farther Expiry series. • It is a net Premium debit strategy. Since primary leg comprises of buying higher Strike PE, Premium

buying lower Strike CE, Premium at which Long is initiated is the amount of Premium paid. The hedged leg comprises of selling higher Strike CE, therefore the Premium at which CE is sold is the amount of Premium received. Since, primary leg comprises of lower CE Strike and hedged leg of higher CE Strike, the primary leg will have more Premium than the hedged leg. Thus, in this Strategy, Long is initiated at higher Premium and Short at lower Premium, thus making it a Debit Strategy. Accordingly, in this Strategy the Net Debit of Premium need to be recovered in order to come in profit in this Strategy, from Expiry perspective.⁵ • Thus, from Expiry perspective, the bullish move in the underlying must cross above the Breakeven Strike of this Strategy (<i>discussed below here</i>).	at which Long is initiated is the amount of Premium paid. The hedged leg comprises of selling lower Strike PE, therefore the Premium at which PE is sold is the amount of Premium received. Since, primary leg comprises of higher PE Strike and hedged leg of lower PE Strike, the primary leg will have more Premium than the hedged leg. Thus, in this strategy, Long is initiated at higher Premium and Short at lower Premium, thus making it a Debit Strategy. Accordingly, in this Strategy the Net Debit of Premium need to be recovered in order to come in profit in this Strategy, from Expiry perspective.⁶ • Thus, from Expiry perspective, the bearish move in the underlying must cross below the Breakeven Strike of this Strategy (<i>discussed below here</i>). • Fall in Volatility (<i>eg: India VIX is making lower lows</i>), is harmful for
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⁵ Since, this Strategy is a Net Premium Debit Strategy, the cost of the Strategy may sometimes be not so palatable. In such cases, especially when the view is not very bullish, the cost of a Bull Call Spread can be further reduced by adding another Far OTM Short CE leg in order to collect some more Premium Credit for the Strategy. This addition of another CE Short leg to Bull Call Spread, converts it to a **Bull Call Ladder Spread Strategy**. Here, the additional Short Call leg must be at such Far OTM Strike which is reasonably above some major Resistance level (*i.e. upto where the underlying is not expected to trend upwardly & close, by Expiry*), thereby realising the extra Premium Credit collected on these additional Short leg, as profit.

⁶ Since, this Strategy is a Net Premium Debit Strategy, the cost of the Strategy may sometimes be not so palatable. In such cases, especially when the view is not very bearish, the cost of a Bear Put Spread can be further reduced by adding another Far OTM Short PE leg in order to collect some more Premium Credit for the Strategy. This addition of another PE Short leg to Bear Put Spread, converts it to a **Bear Put Ladder Spread Strategy**. Here, the additional Short Put leg must be at such Far OTM Strike which is reasonably below some major Support level (*i.e. upto where the underlying is not expected to trend downwardly & close, by Expiry*), thereby realising the extra Premium Credit collected on these additional Short leg, as profit.

• Fall in Volatility (<i>eg: India VIX is making lower lows</i>), is harmful for the Strategy, as it would become difficult to breakeven the Net Premium debit incurred on this Strategy (<i>as falling volatility would cause erosion in the premium value of all Options</i>) even if underlying makes an upmove. Strong volatility crash may dilute the favourable Delta impact of the upmove in the underlying.	the Strategy, as it would become difficult to breakeven the Net Premium debit incurred on this Strategy (<i>as falling volatility would cause erosion in the premium value of all Options</i>) even if underlying makes bearish move. Strong volatility crash may dilute the favourable Delta impact of a slow fall in the underlying.
<u>Benefits of Bull Call Spread:</u> • This Strategy requires low margin / capital. • This is a very suitable Strategy for a bullish trend. • The risk upon reversal or otherwise is limited to the extent of Net Premium paid, i.e. Max Loss is limited. • Rise in Volatility (<i>eg: India VIX is making higher highs</i>), is suitable for the Strategy.	<u>Benefits of Bear Put Spread:</u> • This Strategy requires low margin / capital. • This is a very suitable Strategy for a bearish trend. • The risk upon reversal or otherwise is limited to the extent of Net Premium paid, i.e. Max Loss is limited. • Rise in Volatility (<i>eg: India VIX is making higher highs</i>), is suitable for the Strategy.
<u>Breakeven Strike of this Strategy from Expiry perspective:</u> Net Premium paid on the Strategy (<i>i.e. the difference between the premium paid on the primary leg and the premium credit received on the hedged leg</i>), must be crossed upwardly by the underlying above the Strike at which CE Long primary leg is initiated, by Expiry, in order that this Spread be profitable by Expiry. Thus, we need to determine the Breakeven Strike level above which the	<u>Breakeven Strike of this Strategy from Expiry perspective:</u> Net Premium paid on the Strategy (<i>i.e. the difference between the premium paid on the primary leg and the premium credit received on the hedged leg</i>), must be crossed downwardly by the underlying below the Strike at which PE Long primary leg is initiated, by Expiry, in order that this Spread be profitable by Expiry. Thus, we need to determine the Breakeven Strike level below which the underlying must

underlying must close by Expiry, in order to bring the Strategy into profit.

Breakeven (BE) Strike for profit:

BE level is the level which the underlying must close above by Expiry, so as to yield profit on the Strategy. This BE level is determined by adding the Net Premium debit incurred on the Strategy, to the CE Long leg.

i.e., **BE Strike for this Strategy = CE Long Strike + Net Premium**

For example, if Nifty 17600 CE is bought at Rs. 200 premium per Lot and Nifty 17800 CE is sold at Rs. 150 premium per lot, then BE Strike will be $17600 + (200 - 150) = 17650$ CE Strike, to be profitable from Expiry perspective. That is by Expiry, Nifty must go up beyond 17650 Strike (in which case 17600 CE primary leg becomes an ITM).

Higher the underlying closes by Expiry, above the aforesaid BE level, higher will be the profit generated on this Spread (until the Max Profit level is reached).

Impact on BE level, due to Strike Difference:

Larger the difference between CE Long and CE Short Strike, larger will be the net premium debit, and accordingly larger will be the Breakeven required for profit on the Strategy, from Expiry perspective.

Also, the Breakeven Strike gets larger if a CE Spread is initiated on a farther Expiry series than closer Expiry series, on same Strikes of CEs (*eg: both primary & hedged leg CEs are initiated on Next Month Expiry series than Current Month Expiry series*). This is because the net premium

close by Expiry, in order to bring the Strategy into profit.

Breakeven (BE) Strike for profit:

BE level is the level which the underlying must close below by Expiry, so as to yield profit on the Strategy. This BE level is determined by deducting the Net Premium debit incurred on the Strategy, from the PE Long leg.

i.e., **BE Strike for this Strategy = PE Long Strike - Net Premium**

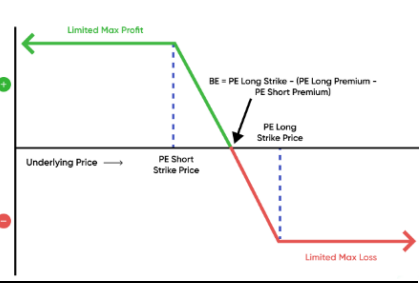
For example, if Nifty 17500 PE is bought at Rs. 250 premium per Lot and Nifty 17300 PE is sold at Rs. 180 premium per lot, then BE Strike will be $17500 - (250 - 180) = 17430$ PE Strike, to be profitable from Expiry perspective. That is by Expiry, Nifty must go down below 17430 (in which case 17500 PE primary leg becomes an ITM).

Lower the underlying closes by Expiry, below the aforesaid BE level, higher will be the profit generated on this Spread (until the Max Profit level is reached).

Impact on BE level, due to Strike Difference:

Larger the difference between PE Long and PE Short Strike, larger will be the net premium debit, and accordingly larger will be the Breakeven required for profit on the Strategy, from Expiry perspective.

Also, the Breakeven Strike gets larger if a PE Spread is initiated on a farther Expiry series than closer Expiry series, on same Strikes of PEs (*eg: both primary & hedged leg PEs are initiated on Next Week Expiry series than Current Week Expiry series*). This is because the net premium debit paid on the Spread increases as we go on

debit paid on the Spread increases as we go on farther Expiry series, even though the primary & hedged leg CE Strikes are kept same.	farther Expiry series, even though the primary & hedged leg PE Strikes are kept same.
<u>Payoff Chart for Bull CE Spread</u> Bull Call Debit Spread 	<u>Payoff Chart for Bear PE Spread</u> Bear Put Debit Spread 
<u>Maximum Loss in this Strategy from Expiry perspective:</u> Net Premium debit incurred on the overall Strategy (i.e. the difference between the premium paid on the primary leg and the premium credit collected on the hedged leg), is the maximum loss that may be incurred in this Strategy, i.e. Max Loss on CE Spread = Premium Paid on Long leg – Premium Credit Received on Short Leg <i>For example, if Nifty 17600 CE is bought at Rs. 200 premium per Lot and Nifty 17800 CE is sold at Rs. 150 premium per Lot, then Max Loss will be Rs 200 – Rs. 150 per lot = Rs. 50 per Lot from Expiry perspective.</i> <u>Impact on Max Loss amount, due to Strike Difference:</u> Larger the difference between CE Long and CE Short Strike, larger will be the net premium debit, and accordingly larger will be the Breakeven required for profit from Expiry perspective; which	<u>Maximum Loss in this Strategy from Expiry perspective:</u> Net Premium debit incurred on the overall Strategy (i.e. the difference between the premium paid on the primary leg and the premium credit collected on the hedged leg), is the maximum loss that may be incurred in this Strategy, i.e. Max Loss on PE Spread = Premium Paid – Premium Credit Received on Short Leg <i>For example, if Nifty 17500 PE is bought at Rs. 250 premium per Lot and Nifty 17300 PE is sold at Rs. 180 premium per Lot, then Max Loss will be Rs 250 – Rs. 180 per lot = Rs. 70 per Lot from Expiry perspective.</i> <u>Impact on Max Loss amount, due to Strike Difference:</u> Larger the difference between PE Long and PE Short Strike, larger will be the net premium debit, and accordingly larger will be the Breakeven required for profit from Expiry perspective; which will

will eventually lead to higher Max Loss on the Strategy. Thus, pre-calculated loss on the Strategy will help decide, the Strike at which Long & Short leg must be initiated.

Loss Level:

The CE Spread will yield profit only if the underlying closes above the BE Strike by Expiry, as discussed above, else the Strategy would yield loss. Therefore, if the underlying fails to cross the BE Strike upwardly and closes below the BE level by Expiry, then this Strategy would yield loss on the Spread.

Max Loss Level:

If the underlying fails to cross the BE Strike upwardly and closes below the CE Long Strike by Expiry, then this Strategy would yield Max Loss, to the extent of Net Premium debit paid on this Spread.

Loss Zone on the CE Debit Spread:

The profitability from Expiry perspective would arise in the Strategy, if the underlying crosses and closes above the Breakeven Strike level. Lower the underlying would close below the BE strike level, more loss would be generated on this Spread. However, once the underlying crosses the CE Long Strike downwardly by Expiry, then the Max Loss Level is achieved on the Strategy. Thereafter, any further fall in the underlying below the CE Long Strike, would not yield any further loss than the Max Loss determined on this Spread (*as per aforesaid calculations*).

Thus, the BE Strike level and the CE Long Strike is the loss zone from Expiry perspective of this Spread. If the

eventually lead to higher Max Loss on the Strategy. Thus, pre-calculated loss on the Strategy will help decide, the Strike at which Long & Short leg must be initiated.

Loss Level:

The PE Spread will yield profit only if the underlying closes below the BE Strike by Expiry, as discussed above, else the Strategy would yield loss. Therefore, if the underlying fails to cross the BE Strike downwardly and closes above the BE level by Expiry, then this Strategy would yield loss on the Spread.

Max Loss Level:

If the underlying fails to cross the BE Strike downwardly and closes above the PE Long Strike by Expiry, then this Strategy would yield Max Loss, to the extent of Net Premium debit paid on this Spread.

Loss Zone on the PE Debit Spread:

The profitability from Expiry perspective would arise in the Strategy, if the underlying crosses and closes below the Breakeven Strike level. Higher the underlying would close above the BE strike level, more loss would be generated on this Spread. However, once the underlying crosses the PE Long Strike upwardly by Expiry, then the Max Loss Level is achieved on the Strategy. Thereafter, any further rise in the underlying above the PE Long Strike, would not yield any further loss than the Max Loss determined on this Spread (*as per aforesaid calculations*).

Thus, the BE Strike level and the PE Long Strike is the loss zone from Expiry

underlying closes by Expiry, closer to the BE Strike, then less loss would be incurred on the Spread; but if the underlying closes by Expiry near the CE Long Strike then more loss would be generated on this Spread (<i>subject to Max Loss, when the underlying closes by Expiry, at or anywhere lower than the CE Long Strike</i>). Thus, if expected closing of the underlying by Expiry, seems to be below the BE level, then it is a Max Loss situation on the Strategy.	perspective of this Spread. If the underlying closes by Expiry, closer to the BE Strike, then less loss would be incurred on the Spread; but if the underlying closes by Expiry near the PE Long Strike then more loss would be generated on this Spread (<i>subject to Max Loss, when the underlying closes by Expiry, at or anywhere higher than the PE Long Strike</i>). Thus, if expected closing of the underlying by Expiry, seems to be above the BE level, then it is a Max Loss situation on the Strategy.
<u>Calculation of Maximum Reward in this Strategy:</u> Max reward is calculated as: • <i>[difference between the primary leg Strike and the hedged leg Strike]</i> minus • <i>[Net Premium paid on the Strategy i.e. difference between the Premium paid on the primary leg and the Premium credit received on the hedged leg]⁷</i> <i>For example, if Nifty 17600 CE is bought at Rs. 200 premium per Lot and Nifty 17800 CE is sold at Rs. 150 premium per Lot, then Max Reward will be:</i>	<u>Maximum Reward in this Strategy:</u> Max reward is calculated as: • <i>[difference between the primary leg Strike and the hedged leg Strike]</i> minus • <i>[Net Premium paid on the Strategy i.e. difference between the Premium paid on the primary leg and the Premium credit received on the hedged leg]⁸</i> <i>For example, if Nifty 17500 PE is bought at Rs. 250 premium per Lot and Nifty 17300 PE is sold at Rs. 180 premium per Lot, then Max Reward will be:</i>

⁷ Max Reward for CE Spread can also be calculated as the difference between the Breakeven Strike of primary leg and hedged leg, i.e. the difference between (i) Breakeven Strike of CE Buy (primary leg) = CE Strike + Premium paid; and (ii) Breakeven Strike of CE Sell (hedged leg) = CE Strike + Premium received.

⁸ Max Reward for PE Spread can also be calculated as the difference between the Breakeven Strike of primary leg and hedged leg, i.e. the difference between (i) Breakeven Strike of PE Buy (primary leg) = PE Strike - Premium paid; and (ii) Breakeven Strike of PE Sell (hedged leg) = PE Strike - Premium received.

$[17800 - 17600] - [200 - 150] = [200 - 50] = \text{Rs. } 150 \text{ per qty.}$

1 Lot Nifty has 50 qty, therefore in above example max reward would be Rs. 150 x 50 = 7500 per Lot.

Max Profit Level: The Max Profit (*as calculated above*) would be generated on this Spread, if the underlying moves up and crosses the Breakeven level and finally closes by Expiry, at the CE Short Strike or anywhere higher than the CE Short Strike.

Profit Zone on the CE Debit Spread:

The profitability from Expiry perspective would arise in the Strategy, if the underlying crosses and closes above the Breakeven Strike level. Higher the underlying would trend towards the CE Short Strike level, more and more profit would be generated on the Spread. However, once the underlying crosses the CE Short Strike upwardly, then the Max Profit Level is achieved on the Strategy. Thereafter, any further rise in the underlying, would not yield any further higher profit than the Max Profit determined on this Spread (*as per aforesaid calculations*).

Thus, the Profit Zone on this Spread, from Expiry perspective, can be said to be the starting upwardly from the BE Strike level of the Spread upto the CE Short Strike level. If the underlying closes by Expiry, closer towards the CE Short Strike in this profit zone, then higher profit would be generated, but if the underlying closes towards the BE Strike of this Strategy within the zone, then

$[17500 - 17300] - [250 - 180] = [200 - 70] = \text{Rs. } 130 \text{ per qty.}$

1 Lot Nifty has 50 qty, therefore in above example max reward would be Rs. 130 x 50 = 6500 per Lot.

Max Profit Level: The Max Profit (*as calculated above*) would be generated on this Spread, if the underlying falls and crosses below the Breakeven level and finally closes by Expiry, at PE Short Strike or anywhere lower than the PE Short Strike.

Profit Zone on the PE Debit Spread:

The profitability from Expiry perspective would arise in the Strategy, if the underlying crosses and closes below the Breakeven Strike level. Lower the underlying would trend towards the PE Short Strike level, more and more profit would be generated on the Spread. However, once the underlying crosses the PE Short Strike downwardly, then the Max Profit Level is achieved on the Strategy. Thereafter, any further fall in the underlying, would not yield any further higher profit than the Max Profit determined on this Spread (*as per aforesaid calculations*).

Thus, the Profit Zone on this Spread, from Expiry perspective, can be said to be the starting from below the BE Strike level of the Spread upto the PE Short Strike level. If the underlying closes by Expiry, closer towards the PE Short Strike in this profit zone, then higher profit would be generated, but if the underlying closes towards the BE Strike of this Strategy within the zone, then relatively

relatively less profit would be generated on the Spread.	less profit would be generated on the Spread.
<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level:</u> [CE Long Strike + Net Premium Debit paid on the Spread] <u>Min Profit Level:</u> If underlying closes by Expiry above the BE Level <u>Max Profit Level:</u> If underlying closes by Expiry at or anywhere higher than the CE Short Strike <u>Profit Zone:</u> If underlying closes by Expiry anywhere higher than the BE Level. If underlying closes at or higher than CE Short Strike, then Max Profit is generated; and if underlying closes towards the BE Level then less profit generated on the Spread. <u>Loss Starting Level:</u> If underlying closes by Expiry below the BE Level. <u>Max Loss Level:</u> If underlying closes by Expiry, at or below the CE Long Strike, then Max Loss (<i>i.e. to the extent of Net Premium debit paid on the Spread</i>) would be generated on the Spread. <u>Loss Zone:</u> If underlying closes by Expiry anywhere lower than the BE Level. If underlying closes at or lower than CE Long Strike, then Max Loss is generated; and if underlying closes towards the BE Level then less profit generated on the Spread.	<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level:</u> [PE Long Strike - Net Premium Debit paid on the Spread] <u>Min Profit Level:</u> If underlying closes by Expiry below the BE Level <u>Max Profit Level:</u> If underlying closes by Expiry at or anywhere lower than the PE Short Strike <u>Profit Zone:</u> If underlying closes by Expiry anywhere lower than the BE Level. If underlying closes at or lower than PE Short Strike, then Max Profit is generated; and if underlying closes towards the BE Level then less profit generated on the Spread. <u>Loss Starting Level:</u> If underlying closes by Expiry above the BE Level. <u>Max Loss Level:</u> If underlying closes by Expiry, at or higher than the PE Long Strike, then Max Loss (<i>i.e. to the extent of Net Premium debit paid on the Spread</i>) would be generated on the Spread. <u>Loss Zone:</u> If underlying closes by Expiry anywhere higher than the BE Level. If underlying closes at or higher than PE Long Strike, then Max Loss is generated; and if underlying closes towards the BE Level then less loss generated on the Spread.
<u>Risk & Reward in a CE Spread:</u> The ratio between the Max Loss and the Max Reward gives the Risk & Reward ratio for this Strategy.	<u>Risk & Reward in a PE Spread:</u> The ratio between the Max Loss and the Max Reward gives the Risk & Reward ratio for this Strategy.

A CE Spread initiated on ITM CEs (*for both primary & hedged leg*), has a large net premium debit in absolute terms, and therefore, the Max Loss is quite high in an ITM Spread, as compared to an OTM CE Spread (*with both primary & hedged leg initiated on OTM CEs*).

Also, since, Max Reward in this Spread is calculated as the difference between the: [Strike Difference and the Net premium paid on the Strategy], therefore, an ITM CE Spread (*initiated on ITM CEs for both primary & hedged leg*), has lesser Max Reward than an OTM CE Spread (*with both primary & hedged leg initiated on OTM CEs*), with same Strike width between the CE Long & CE Short leg. This is because, a CE Spread initiated on ITM CEs (*for both primary & hedged leg*), has a large net premium debit in absolute terms than a CE Spread initiated on OTM CEs (*for both primary & hedged leg*).

Accordingly, the Risk-to-Reward Ratio in a CE Spread, is favourable in an OTM CE Spread than an ITM CE Spread. In case Volatility is too high (like India VIX is above 25 or 30 level), then an ITM-ATM CE Spread may be considered; else during other times OTM-OTM CE Spread must be considered.

Further, wider the Strike difference between the Long CE leg and CE Short leg, more favourable the Risk-to-Reward gets (*due to net premium debit getting lower*), however, it must be borne in mind that from Expiry perspective, the underlying must close above the Breakeven Strike of the Strategy and to be able to reap Max Reward on the Strategy the underlying must go much

A PE Spread initiated on ITM PEs (*for both primary & hedged leg*), has a large net premium debit in absolute terms, and therefore, the Max Loss is quite high in an ITM Spread, as compared to an OTM PE Spread (*with both primary & hedged leg initiated on OTM PEs*).

Also, since, Max Reward in this Spread is calculated as the difference between the: [Strike Difference and the Net premium paid on the Strategy], therefore, an ITM PE Spread (*initiated on ITM PEs for both primary & hedged leg*), has lesser Max Reward than an OTM PE Spread (*with both primary & hedged leg initiated on OTM PEs*), with same Strike width between the PE Long & PE Short leg. This is because, a PE Spread initiated on ITM PEs (*for both primary & hedged leg*), has a large net premium debit in absolute terms than a PE Spread initiated on OTM PEs (*for both primary & hedged leg*).

Accordingly, the Risk-to-Reward Ratio in a PE Spread, is favourable in an OTM PE Spread than an ITM PE Spread. In case Volatility is too high (like India VIX is above 25 or 30 level), then an ITM-ATM PE Spread may be considered; else during other times OTM-OTM PE Spread must be considered.

Further, wider the Strike difference between the Long PE leg and PE Short leg, more favourable the Risk-to-Reward gets (*due to net premium debit getting lower*), however, it must be borne in mind that from Expiry perspective, the underlying must close below the Breakeven Strike of the Strategy and to be able to reap Max Reward on the Strategy the underlying must go much lower below the Breakeven Strike of the

higher above the Breakeven Strike of the Strategy i.e. upto the Max Reward level of the Strategy, calculated as the difference between the: [Strike Difference and the Net premium paid on the Strategy]. Therefore, ideally, if there is a clear view of more than 1% to 1.5% quick move in the underlying, then a CE Spread with little wider Strike Difference, in Near OTM CEs, on a closer Expiry series may be considered. However, if the upmove in the underlying is expected after sometime (or over longer time), then such position on CE Spread may be created on a farther Expiry series (<i>like Next Month Expiry series etc.</i>).	Strategy i.e. upto the Max Reward level of the Strategy, calculated as the difference between the: [Strike Difference and the Net premium paid on the Strategy]. Therefore, ideally, if there is a clear view of more than 1% to 1.5% quick fall in the underlying, then a PE Spread with little wider Strike Difference, in Near OTM PEs, on a closer Expiry series may be considered. However, if the fall in the underlying is expected after sometime (or over longer time), then such position on PE Spread may be created on a farther Expiry series (<i>like Next Month Expiry series etc.</i>).
<u>Options behaviour:</u> • It is pertinent to note that by Expiry, if the primary leg becomes an ITM (then its final LTP if higher than at which it was bought, will yield profit), and the hedged leg if expires as an OTM then the entire Premium at which CE was Shorted for the hedged leg will also be a profit in this Strategy. However, if closer to Expiry both primary and hedged leg are OTMs and the Strategy is in profit, then the profit must be booked before Expiry because otherwise the profit in the primary leg would become zero (due to Theta impact on primary leg and hedged leg, both being OTMs). • Therefore, it is very important to keep track of the Breakeven Strike and to examine if the underlying would sustain above the BE Strike of the Strategy or not by Expiry. If	<u>Options behaviour:</u> • It is pertinent to note that by Expiry, if the primary leg becomes an ITM (then its final LTP if higher than at which it was bought, will yield profit), and the hedged leg if expires as an OTM then the entire Premium at which PE was Shorted for the hedged leg will also be a profit in this Strategy. However, if closer to Expiry both primary and hedged leg are OTMs and the Strategy is in profit, then the profit must be booked before Expiry because otherwise the profit in the primary leg would become zero (due to Theta impact on primary leg and hedged leg, both being OTMs). • Therefore, it is very important to keep track of the Breakeven Strike and to examine if the underlying would sustain below the BE Strike of the Strategy or not by Expiry. If not,

not, then the profits if generated on the Spread must be booked before Expiry.

- Rise in Volatility may not adversely impact this Strategy, as rise in Volatility would be favourable to the CE Long primary leg; and if the CE Short hedged leg continues to be an OTM until Expiry then even if rising Volatility increases the Premium value of the hedged leg, then also it would eventually become zero and yield profit if the hedged leg CE Short position happens to be an OTM on Expiry. Therefore, at any time before Expiry, if rising state of Volatility adds impetus to profitability in this Strategy, then the profit must be booked before the favourable impact of Volatility is lost.
- Falling state of Volatility may not be favourable to this Strategy, as the drop in Volatility will erode the Premium value of both the primary leg and the hedged leg and the Net Premium paid may get difficult to be realised in order to get profitable in this Strategy. Moreover, if the impact of falling Volatility lasts longer then the erosion of Premium due to Volatility crash would get coupled with the Theta impact, making all the more difficult to realise and cross-over the Net Premium paid in order to get profitable in this Strategy. Only strong favourable bullish momentum can help overcome the adverse impact of Volatility crash and Theta decay. A sideways

then the profits if generated on the Spread must be booked before Expiry.

- Rise in Volatility may not adversely impact this Strategy, as rise in Volatility would be favourable to the PE Long primary leg; and if the PE Short hedged leg continues to be an OTM until Expiry then even if rising Volatility increases the Premium value of the hedged leg, then also it would eventually become zero and yield profit if the hedged leg PE Short position happens to be an OTM on Expiry. Therefore, at any time before Expiry, if rising state of Volatility adds impetus to profitability in this Strategy, then the profit must be booked before the favourable impact of Volatility is lost.
- Falling state of Volatility may not be favourable to this Strategy, as the drop in Volatility will erode the Premium value of both the primary leg and the hedged leg and the Net Premium paid may get difficult to be realised in order to get profitable in this Strategy. Moreover, if the impact of falling Volatility lasts longer then the erosion of Premium due to Volatility crash would get coupled with the Theta impact, making all the more difficult to realise and cross-over the Net Premium paid in order to get profitable in this Strategy. Only strong favourable bearish momentum can help overcome the adverse impact of Volatility crash and Theta decay. A sideways

movement in the underlying will further aggravate the chances of profitability in this Strategy. • Delta play between the primary leg and the hedged leg is separately discussed hereinbelow.	movement in the underlying will further aggravate the chances of profitability in this Strategy. • Delta play between the primary leg and the hedged leg is separately discussed hereinbelow.
<u>Strike / Delta value:</u> The Delta difference between the primary leg and the hedged leg will help maintain a reasonable control on profit & loss scenario in this Strategy. Delta difference can be ensured by selecting appropriate distance CE Strikes for this Strategy. It must be borne in mind that larger the Strike difference between CE Long & CE Short, the max profit on the Strategy increases and the risk & reward is more favourable; but the Breakeven Strike gets even larger in order to reap profit on the Strategy (<i>thus, more bullish move is required in the underlying</i>). Therefore, for a strong conviction bullish view, an OTM CE of lower Strike having higher Delta value can be bought as the primary leg; but a Far OTM CE of higher Strike having lower Delta value can be sold as the hedged leg. When bullish view has conviction, then a suitable larger Delta difference can be maintained between the primary leg and the hedged leg, i.e. higher Delta value on primary leg would yield more profit on bullish uptrend and a lower Delta on hedged leg would yield less loss. This larger Delta difference can be maintained by maintaining suitable larger gap between the Strikes at which primary leg and the hedged leg are initiated of the	<u>Strike / Delta value:</u> The Delta difference between the primary leg and the hedged leg will help maintain a reasonable control on profit & loss scenario in this Strategy. Delta difference can be ensured by selecting appropriate distance PE Strikes for this Strategy. It must be borne in mind that larger the Strike difference between PE Long & PE Short, the max profit on the Strategy increases and the risk & reward is more favourable; but the Breakeven Strike gets even larger in order to reap profit on the Strategy (<i>thus, more bearish move is required in the underlying</i>). Therefore, for a strong conviction bearish view, an OTM PE of higher Strike having higher Delta value can be bought as the primary leg; but a Far OTM PE of lower Strike having lower Delta value can be sold as the hedged leg. When bearish view has conviction, then a suitable larger Delta difference can be maintained between the primary leg and the hedged leg, i.e. higher Delta value on primary leg would yield more profit on bearish downtrend and a lower Delta on hedged leg would yield less loss. This larger Delta difference can be maintained by maintaining suitable larger gap between the Strikes at which primary leg and the hedged leg are initiated of the same Expiry. Because there is conviction on the

same Expiry. Because there is conviction on the bullish view, the wider Breakeven (due to larger Strike difference) should not be an hinderance to reap profit on the Strategy, and a much favourable Risk-to-Reward can be targeted. However, when bullish view does not have conviction and there seems uncertainty about continuation of bullish trend, then a suitable smaller Delta difference can be maintained between the primary leg and the hedged leg, i.e. the primary leg would yield more loss (due to its higher Delta value) on reversal of uptrend and the hedged leg because of having not too low Delta value than that of the primary leg would yield decent profit on reversal of uptrend. This smaller Delta difference can be ensured by maintaining suitable smaller gap between the Strikes at which primary leg and the hedged leg are initiated of the same Expiry. Due to smaller Strike difference, the Breakeven for generating profit would also be smaller thus if the uptrend remains intact, then a slight uptrend move in the underlying crossing above the smaller BE Level, would make the Strategy profitable.	bearish view, the wider Breakeven (due to larger Strike difference) should not be an hinderance to reap profit on the Strategy, and a much favourable Risk-to-Reward can be targeted. However, when bearish view does not have conviction and there seems uncertainty about continuation of bearish trend, then a suitable smaller Delta difference can be maintained between the primary leg and the hedged leg, i.e. the primary leg would yield more loss (due to its higher Delta value) on reversal of bearish trend and the hedged leg because of having not too low Delta value than that of the primary leg would yield decent profit on reversal of downtrend. This smaller Delta difference can be ensured by maintaining suitable smaller gap between the Strikes at which primary leg and the hedged leg are initiated of the same Expiry. Due to smaller Strike difference, the Breakeven for generating profit would also be smaller thus if the downtrend remains intact, then a slight downtrend move in the underlying crossing the smaller BE Level, would make the Strategy profitable.
<u>Selection of Option Strikes:</u> Basis aforesaid factors, depending on the intended holding time of the trade, a suitable CE Option Strike levels of a particular Expiry series and Delta value may be selected. For higher Risk and Reward and less margin for this Strategy: OTM CE Long and Far OTM CE Short in Current Expiry series can be considered. Further,	<u>Selection of Option Strikes:</u> Basis aforesaid factors, depending on the intended holding time of the trade, a suitable PE Option Strike levels of a particular Expiry series and Delta value may be selected. For higher Risk and Reward and less margin for this Strategy: OTM PE Long and Far OTM PE Short in Current Expiry series can be considered. Further,

it may be considered in OTM-OTM CE Spread, that the CE Long primary leg is such Far OTM Strike, which is slightly below some major Resistance level (*as per Technical Analysis / Chart reading*) and the CE Short hedged leg is higher than the said major Resistance level on the upside. This way it can be attempted to ensure that if the bullish trend sustains as expected then the primary leg would generate profit due to the upmove in the underlying; but also if the underlying by Expiry closes near the said major Resistance level, then even the CE Short leg would generate profit to the extent of the premium credit collected on the hedged leg (as it would expire worthless as OTM). Thus, the Strategy in such situation would generate the max profit (*as per calculations discussed above*). In such situation, it must be ensured that the CE Long primary leg does not expire as ATM / OTM; and therefore, profit generated on the primary leg must be booked, if the underlying appears to reverse from near the Resistance level.

It must be borne in mind that larger the Strike difference between CE Long & CE Short, the max profit on the Strategy increases and the risk & reward is more favourable; but the Breakeven Strike gets even larger in order to reap profit on the Strategy (*thus, more bullish move is required in the underlying*).

Also, the Max Loss and Max Reward in the Strategy must be calculated, as per the calculations explained above, before initiating this CE Spread Strategy, so as to determine a balanced Strike selection for playing this Spread.

it may be considered in OTM-OTM PE Spread, that the PE Long primary leg is such Far OTM Strike, which is slightly above some major Support level (*as per Technical Analysis / Chart reading*) and the PE Short hedged leg is lower than the said major Support level on the downside. This way it can be attempted to ensure that if the bearish trend sustains as expected then the primary leg would generate profit due to the downmove in the underlying; but also if the underlying by Expiry closes near the said major Support level, then even the PE Short leg would generate profit to the extent of the premium credit collected on the hedged leg (as it would expire worthless as OTM). Thus, the Strategy in such situation would generate the max profit (*as per calculations discussed above*). In such situation, it must be ensured that the PE Long primary leg does not expire as ATM / OTM; and therefore, profit generated on the primary leg must be booked, if the underlying appears to reverse from near the Support level.

It must be borne in mind that larger the Strike difference between PE Long & PE Short, the max profit on the Strategy increases and the risk & reward is more favourable; but the Breakeven Strike gets even larger in order to reap profit on the Strategy (*thus, more bearish move is required in the underlying*).

Further, the Max Loss and Max Reward in the Strategy must be calculated, as per the calculations explained above, before initiating this PE Spread Strategy, so as to determine a balanced Strike selection for playing this Spread.

If trade goes as per plan:

The underlying remains bullish, and the CE Long primary leg will generate profit. But as the underlying moves higher, the hedged CE Short leg will generate loss (*because the LTP of CE Short leg will rise due to underlying going upward*). However, the Delta difference between the primary leg and hedged leg will bring the net position in profit.

But as the underlying keeps going higher quickly with strong momentum, there may come a time when the Strategy will cross the Max Reward level. Then beyond such level, if the underlying keeps trending further upwardly, then once Max Reward level is achieved by the Strategy then no further profit can be expected on the Strategy. Hence, in such situation, the Max profit on the Strategy must be immediately booked.

If underlying movement is slow / sideways:

If the movement of the underlying becomes slow / sluggish in its upward movement or if the underlying keeps fluctuating in a range, then the Theta impact would cause erosion in the Premium value of both CE Long and CE Short leg. Thus, time decay may result in some loss situation in this Strategy with long holding period. Therefore, if it appears that by Expiry, the BE Strike level would not be crossed upwardly by the underlying on sustained basis, then Max Loss would occur on the Strategy. In such situation, suitable adjustments (*as discussed below*) may be considered to mitigate the Max Loss situation on the Strategy by Expiry.

If trade goes as per plan:

The underlying remains bearish, and the PE Long primary leg will generate profit. But as the underlying moves lower, the hedged PE Short leg will generate loss (*because the LTP of PE Short leg will rise due to underlying going downward*). However, the Delta difference between the primary leg and hedged leg will bring the net position in profit.

But as the underlying keeps going lower quickly with strong momentum, there may come a time when the Strategy will cross the Max Reward level. Then beyond such level, if the underlying keeps trending further downwardly, then once Max Reward level is achieved by the Strategy then no further profit can be expected on the Strategy. Hence, in such situation, the Max profit on the Strategy must be immediately booked.

If underlying movement is slow / sideways:

If the movement of the underlying becomes slow / sluggish in its downward movement or if the underlying keeps fluctuating in a range, then the Theta impact would cause erosion in the Premium value of both PE Long and PE Short leg. Thus, time decay may result in some loss situation in this Strategy with long holding period. Therefore, if it appears that by Expiry, the BE Strike level would not be crossed downwardly by the underlying on sustained basis, then Max Loss would occur on the Strategy. In such situation, suitable adjustments (*as discussed below*) may be considered to mitigate the Max Loss situation on the Strategy by Expiry.

<u>If trend reverses on the bearish side, and trade does not go as per plan:</u> If the underlying gets in a downtrend, then the primary leg of CE Long will generate limited loss to the extent of Premium paid. But with the underlying falling down, the hedged CE Short leg will generate limited profit to the extent of Premium received on the Short position. Thus, the CE Short hedged leg will protect the loss in CE Long primary leg to the extent of Premium collected on the CE Short hedged leg. If the underlying keeps falling even further then the Net Premium (<i>i.e. the Premium paid on the primary leg and the Premium collected on CE Short leg</i>) will be the total Max Loss till Expiry. This final loss to the extent of Net Premium debit on the Strategy, in the event of reversal of uptrend in downward direction, can be contained by making certain adjustments (<i>as discussed below here</i>).	<u>If trend reverses on the bullish side, and trade does not go as per plan:</u> If the underlying gets in an uptrend, then the primary leg of PE Long will generate limited loss to the extent of Premium paid. But with the underlying rising up, the hedged PE Short leg will generate limited profit to the extent of Premium received on the Short position. Thus, the PE Short hedged leg will protect the loss in PE Long primary leg to the extent of Premium collected on the PE Short hedged leg. If the underlying keeps rising even further then the Net Premium (<i>i.e. the Premium paid on the primary leg and the Premium collected on PE Short leg</i>) will be the total Max Loss till Expiry. This final loss to the extent of Net Premium debit on the Strategy, in the event of reversal of downtrend in upward direction, can be contained by making certain adjustments (<i>as discussed below here</i>).
<u>Adjustments (if bullish view and this Strategy does not go as per plan):</u> Since, this strategy is a Debit spread, therefore, the Net Premium (<i>i.e. the difference between the Premium paid on primary leg and the Premium credit collected in the hedged leg</i>) need to be first recovered for this Spread to generate profit from Expiry perspective; and accordingly the underlying must cross-over the BE Strike level upwardly on sustained basis. However, if the bullish trend reverses towards downward direction, then the Net Premium paid on the overall Spread, will be the final amount of Max Loss that	<u>Adjustments (if bearish view and this Strategy does not go as per plan):</u> Since, this strategy is a Debit spread, therefore, the Net Premium (<i>i.e. the difference between the Premium paid on primary leg and the Premium credit collected in the hedged leg</i>) need to be first recovered for this Spread to generate profit from Expiry perspective; and accordingly the underlying must cross-over the BE Strike level downwardly on sustained basis. However, if the bearish trend reverses in the upward direction, then the Net Premium paid on the overall Spread, will be the final amount of Max Loss that may

may be incurred on this Strategy by Expiry. Thus, upon reversal, this Net Premium amount need to be covered up by making suitable adjustments.

The following adjustments can be considered to cover up for the potential Max Loss that may occur in this Strategy to the tune of Net Premium: (i) Conversion of Bull CE Spread into Call Ratio Spread (through Short CE); or (ii) Long PE; or (iii) Short PE. These adjustments are discussed below:

- (i) Counter Adjustment through Short Option (Conversion to Call Ratio Spread): In case of a downtrend, **farther OTM CEs can be sold** (additional Short CEs). Idea in this adjustment is to pick up a suitable Far OTM CE for Shorting, such that this Far OTM CE expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This additional CE Short can be initiated on such Premium so as to cover for the Net Premium amount on the original Strategy. Selection of a Far OTM CE for this adjustment is important because even if the downtrend again reverses on the bullish side, this additional CE must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the Net Premium Debit in the original Strategy and the likely downtrend and the Premium available on Far OTM CEs (*of same Strike as that of*

be incurred on this Strategy by Expiry. Thus, upon reversal, this Net Premium amount need to be covered up by making suitable adjustments.

The following adjustments can be considered to cover up for the potential Max Loss that may occur in this Strategy to the tune of Net Premium: (i) Conversion of Bear PE Spread into Put Ratio Spread (through Short PE); or (ii) Long CE; or (iii) Short CE. These adjustments are discussed below:

- (i) Counter Adjustment through Short Option (Conversion to Put Ratio Spread): In case of an uptrend, **farther OTM PEs can be sold** (additional Short PEs). Idea in this adjustment is to pick up a suitable Far OTM PE for Shorting, such that this Far OTM PE expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This additional PE Short can be initiated on such Premium so as to cover for the Net Premium amount on the original Strategy. Selection of a Far OTM PE for this adjustment is important because even if the uptrend again reverses on the bearish side, this additional PE must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the Net Premium Debit in the original Strategy and the likely uptrend and the Premium available on Far OTM PEs (*of same Strike as that of hedged leg or even lower Far OTM Strike*),

hedged leg or even higher Far OTM Strike), suitable number of Short CEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short CE in comparison to the original number of Lots initiated on the Strategy, so as to bring the original Bull CE Strategy on to an overall negative Delta position to play the bearish reversal. In this situation there will be more CE Short than CE Long and therefore the original Bull CE Spread gets converted into Call Ratio Spread (*this Ratio Spread is separately discussed in this Chapter*). These additional CE Short should be initiated at such Far OTM CE, which may be the same Strike at which hedged leg was originally initiated or at even higher Far OTM Strike, depending on the Premium available. However, selling additional CEs will require higher margin / capital to Short CEs and MTM requirements will also have to be met.

- (ii) Counter Adjustment through Long Option: If there seems to be a trending downtrend with momentum, then a **PE can be bought** (Long PE). Buying a PE to protect the downside risk in this Strategy will add up another debit position, therefore this PE Long should only be prudent to initiate only if there is strong momentum for the downward direction. This

suitable number of Short PEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short PE in comparison to the original number of Lots initiated on the Strategy, so as to bring the original Bear PE Strategy on to an overall positive Delta position to play the bullish reversal. In this situation there will be more PE Short than PE Long and therefore the original Bear PE Spread gets converted into Put Ratio Spread (*this Ratio Spread is separately discussed in this Chapter*). These additional PE Short should be initiated at such Far OTM PE, which may be the same Strike at which hedged leg was originally initiated or at even lower Far OTM Strike, depending on the Premium available. However, selling additional PEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.

- (ii) Counter Adjustment through Long Option: If there seems to be a trending uptrend with momentum, then a **CE can be bought** (Long CE). Buying a CE to protect the upside risk in this Strategy will add up another debit position, therefore this CE Long should only be prudent to initiate only if there is strong momentum for the upward direction. This Long CE will help overcome the loss of Net Premium

Long PE will help overcome the loss of Net Premium amount in this Strategy upon reversal. If this PE generates profit to the tune of Net Premium then it would be advisable to book the profit on this Long PE position. The reversal on downside can be played by a naked PE or a Bear PE Spread Strategy. Further, Long PE should be initiated at a Strike having Delta value higher than the current Delta value of the Long CE primary leg (*i.e. at a higher Strike than the CE buy Strike*), so that in case of reversal on downtrend, Long PE should generate more profit than the loss generated by the Long CE. Also, depending upon the Net Premium Debit in the original Strategy and the likely downtrend momentum, suitable number of Long PEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to Long PE in comparison to the original number of Lots initiated on the Strategy, so as to bring the original Bull CE Strategy on to an overall negative Delta position to play the bearish reversal.

- (iii) Adjustment through Pyramiding: If the downtrend is expected to be trending but limited, then **even Farther OTM PEs can be sold** (PE Short) below the major support area of the underlying, which is expected not to be breached by the

amount in this Strategy upon reversal. If this CE generates profit to the tune of Net Premium then it would be advisable to book the profit on this Long CE position. The reversal on upside can be played by a naked CE or a Bull CE Spread Strategy. Further, Long CE should be initiated at a Strike having Delta value higher than the current Delta value of the Long PE primary leg, so that in case of reversal towards uptrend, Long CE should generate more profit than the loss generated by the Long PE. Also, depending upon the Net Premium Debit in the original Strategy and the likely uptrend momentum, suitable number of Long CEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to Long CE in comparison to the original number of Lots initiated on the Strategy, so as to bring the original Bear PE Strategy on to an overall positive Delta position to play the bullish reversal.

- (iii) Adjustment through Pyramiding: If the uptrend is expected to be trending but limited, then **even Farther OTM CEs can be sold** (CE Short) above the major resistance area of the underlying, which is expected not to be breached by the underlying by Expiry. Idea in this adjustment is to pick up suitable Far OTM CEs for Shorting, such that this Far OTM CEs expires worthless

underlying by Expiry. Idea in this adjustment is to pick up suitable Far OTM PEs for Shorting, such that this Far OTM PEs expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This PE Short will help cover the Net Premium paid on this Strategy. Selection of a Far OTM PE for this adjustment is important because even if the downtrend continues, this additional PE must be such which can be expected to be not breached by the underlying by Expiry and to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the Net Premium Debit in the original Strategy and the likely downtrend and the Premium available on Far OTM PEs (of even lower Far OTM Strike below Support area), suitable number of Short PEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy, by the profit yielded by these Short PEs due to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short PE in comparison to the original number of Lots initiated on the Strategy. PE Short positions (of same Expiry series as that of the hedged leg) can also be added in a pyramidal structure. As the downtrend continues Far OTM PEs' Premium would rise, therefore, Short PEs positions can be added at

as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This CE Short will help cover the Net Premium paid on this Strategy. Selection of a Far OTM CE for this adjustment is important because even if the uptrend continues, this additional CE must be such which can be expected to be not breached by the underlying by Expiry and to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the Net Premium Debit in the original Strategy and the likely uptrend and the Premium available on Far OTM CEs (*of even higher Far OTM Strike above Resistance area*), suitable number of Short CEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy, by the profit yielded by these Short CEs due to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short CE in comparison to the original number of Lots initiated on the Strategy. CE Short positions (*of same Expiry series as that of the hedged leg*) can also be added in a pyramidal structure. As the uptrend continues Far OTM CEs' Premium would rise, therefore, Short CEs positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining decent Premium values. *For example, when the uptrend continues in Nifty, a Far OTM CE at 18000 having Premium*

subsequent lower Strike levels as the downtrend continues with lower PEs gaining decent Premium values. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16500 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 16400 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.* This **Shorting of PEs in a pyramiding manner** may ensure a lower Breakeven strike and thus greater probability of profiting due to Theta decay on these bunch of Short PEs on Expiry. However, selling additional PEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.

of Rs. 50 can be sold, thereafter when the Nifty rises further, subsequent higher CE at 18500 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on. This **Shorting of CEs in a pyramiding manner** may ensure a higher Breakeven strike and thus greater probability of profiting due to Theta decay on these bunch of Short CEs on Expiry. However, selling additional CEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.

BULL PUT CREDIT SPREAD & BEAR CALL CREDIT SPREAD

Bullish and Bearish view can be played through Short Options with hedged positions.

When the view on the underlying is bullish to sideways, we can play such view by being Short on Put Options (i.e. sell PE Options) as our main position (the **primary leg**). This primary leg can be hedged by introducing a hedged leg with a bearish view by buying Put Options (i.e. buy PE Options), of the same number of Lots as in the primary leg (i.e. in the ratio of 1:1 in terms of Lots/ quantity), on the same underlying with same Expiry series (the **hedged leg**). This hedged position/ strategy where a bullish primary leg initiated with Short PE positions with higher Premium, is hedged with a PE Long position with lesser Premium than the primary leg, on the same underlying and of same Expiry series – it is called a **Bull Put Spread Strategy or Put Credit Strategy**. It is a Vertical Spread (i.e. involving two same side Options of same Expiry series on different Strikes).

Likewise, when the view on the underlying is bearish to sideways, we can play such view by being Short on Call Options (i.e. sell CE Options) as our main position (the **primary leg**). This primary leg can be hedged by introducing a hedged leg with a bullish view by buying Call Options (i.e. buy CE Options), of the same number of Lots as in the primary leg (i.e. in the ratio of 1:1 in terms of Lots/ quantity), on the same underlying with same Expiry series (the **hedged leg**). This hedged position/ strategy where a bearish primary leg initiated with Short CE positions having higher Premium, is hedged with a Call Long position having lesser Premium, on the same underlying and of same Expiry series – it is called a **Bear Call Spread Strategy or Call Credit Strategy**. It is a Vertical Spread (i.e. involving two same side Options of same Expiry series on different Strikes).

These Strategies have limited profit potential and pre-defined max loss.

With this background, now let us delve into discussing the Bull Put Spread Strategy and Bear Call Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Bull Put Spread Strategy	Bear Call Spread Strategy
Trade Legs: • Short PE of higher Strike with higher Premium (<i>primary leg</i>) • Long PE of lower Strike with lower Premium (<i>hedged leg</i>) Equal number of Lots in primary and hedged leg; and both legs must be of same Expiry series.	Trade Legs: • Short CE of lower Strike with higher Premium (<i>primary leg</i>) • Long CE of higher Strike with lower Premium (<i>hedged leg</i>) Equal number of Lots in primary and hedged leg; and both legs must be of same Expiry series.
Example: • Sell 5 Lots Nifty 17400 PE of Current Month Expiry (at Rs. 50 per Lot) • Buy 5 Lots Nifty 17100 PE of Current Month Expiry (at Rs. 25 per Lot)	Example: • Sell 2 Lots Nifty 17200 CE of Current Week Expiry (at Rs. 75 per Lot) • Buy 2 Lots Nifty 17500 CE of Current Week Expiry (at Rs. 50 per Lot)
Objective: Objective is to play bullish-to-sideways view through selling PEs (as the primary leg). Further, in order to mitigate the risk / loss that may arise if the primary leg with bullish-to-sideways view gets reversed for downtrend, a hedged leg by buying PE (<i>at a lower Strike than PE Short</i>) with bearish view is also initiated simultaneously with the primary leg. Thus, in this Strategy, bullish view generates a limited profit on the primary leg to the maximum extent of the Net Premium credit collected on the Strategy (<i>i.e. premium credit collected on primary leg – premium debit incurred on the hedged leg</i>). However, in case of a downward reversal, the unlimited loss that may occur in the primary leg (<i>PE sell will start giving</i>	Objective: Objective is to play bearish-to-sideways view through selling CEs (as the primary leg). Further, in order to mitigate the risk / loss that may arise if the primary leg with bearish-to-sideways view gets reversed for an uptrend, a hedged leg by buying CE (<i>at a higher Strike than CE Short</i>) with bullish view is also initiated simultaneously with the primary leg. Thus, in this Strategy, bearish view generates a limited profit on the primary leg to the maximum extent of the Net Premium credit collected on the Strategy (<i>i.e. premium credit collected on primary leg – premium debit incurred on the hedged leg</i>). However, in case of an upward reversal, the unlimited loss that may occur in the primary leg (<i>CE sell will start giving</i>

<i>unlimited loss if underlying reverses for a downtrend</i>) would be covered by the hedged leg (i.e. PE Long) initiated with a bearish view. Thus, the risk upon reversal is also limited in this Strategy. Therefore, this Strategy is suitable for a rangebound-to-bullish view in the underlying, and generates a limited profit if the trend goes right; and a limited max loss if the trend reverses on the downward.	<i>unlimited loss if underlying reverses for an uptrend</i>) would be covered by the hedged leg (i.e. CE Long) initiated with a bullish view. Thus, the risk upon reversal is also limited in this Strategy. Therefore, this Strategy is suitable for a rangebound-to-bearish view in the underlying, and generates a limited profit if the trend goes right; and a limited max loss if the trend reverses on the upward.
<u>Demerits:</u> • Since this Strategy is implemented using Far OTM PE (in order to gain Theta benefit on the primary leg), sometime during low Volatility period, sufficient Premium may not be available in Far OTM PEs. • This Strategy can yield profit on the upside to the extent of Net Premium credit collected on the Strategy (<i>premium credit on primary leg – premium debit on hedged leg</i>). Therefore, after max profit level is achieved in this Strategy, then in order to play further bullish move in the underlying, fresh bullish positions will have to be initiated. Thus, the profit in this Strategy is limited, i.e. the Max Reward is limited.	<u>Demerits:</u> • Since this Strategy is implemented using Far OTM CE (in order to gain Theta benefit on the primary leg), sometime during low period, sufficient Premium may not be available in Far OTM CEs. • This Strategy can yield profit on the downside to the extent of Net Premium credit collected on the Strategy (<i>premium credit on primary leg – premium debit on hedged leg</i>). Therefore, after max profit level is achieved in this Strategy, then in order to play further bearish move in the underlying, fresh bearish positions will have to be initiated. Thus, the profit in this Strategy is limited, i.e. the Max Reward is limited.
<u>Benefits of Bull Put Spread:</u> • This Strategy requires low margin / capital.	<u>Benefits of Bear Call Spread:</u> • This Strategy requires low margin / capital.

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| <ul style="list-style-type: none"> • This Spread strategy will be suitable for a bullish to sideways view. A rangebound or slow uptrend generates profit in the primary leg due to erosion of time value owing to such movement in the underlying coupled with Theta impact. • In this Strategy, two factors help in generating profit: (i) bullish to sideways move in the underlying; and (ii) Theta impact on the primary leg. Therefore, this Strategy is mainly created in Far OTM PE Options. • It is a Net Premium Credit Strategy. Since primary leg comprises of selling higher Strike PE, the Premium on PE Short is the amount of Premium collected. The hedged leg comprises of buying lower Strike PE, therefore the Premium at which PE is bought is the amount of Premium paid. Since, primary leg comprises of higher Strike PE and hedged leg of lower Strike PE, the primary leg will have more Premium than the hedged leg. Thus, in this Strategy, Short is initiated at higher Premium and Long at lower Premium, thus making it a Credit Strategy. Accordingly, in this Strategy, the Net Credit of Premium need to be protected for profit in this Strategy. • The Net Credit Premium, increases the loss area in this Strategy by defining the Breakeven Strike. Thus, from Expiry perspective, if | <ul style="list-style-type: none"> • This Spread strategy will be suitable for a bearish to sideways view. A rangebound or slow downtrend generates profit in the primary leg due to erosion of time value owing to such movement in the underlying coupled with Theta impact. • In this Strategy, two factors help in generating profit: (i) bearish to sideways move in the underlying; and (ii) Theta impact on the primary leg. Therefore, this Strategy is mainly created in Far OTM CE Options. • It is a Net Premium Credit Strategy. Since primary leg comprises of selling lower Strike CE, the Premium on CE Short is the amount of Premium collected. The hedged leg comprises of buying higher Strike CE, therefore the Premium at which CE is bought is the amount of Premium paid. Since, primary leg comprises of lower Strike CE and hedged leg of higher Strike CE, the primary leg will have more Premium than the hedged leg. Thus, in this Strategy, Short is initiated at higher Premium and Long at lower Premium, thus making it a Credit Strategy. Accordingly, in this Strategy, the Net Credit of Premium need to be protected for profit in this Strategy. • The Net Credit Premium, increases the loss area in this Strategy by defining the Breakeven Strike. Thus, from Expiry perspective, if the bearish to sideways move in the underlying reverses, then the loss |
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the bullish to sideways move in the underlying reverses, then the loss would occur on this Strategy when the underlying closes below the Breakeven Strike of this Strategy by Expiry (<i>discussed below here</i>). • The risk upon reversal towards a downtrend, is limited in this Strategy, i.e. the Max Loss is limited.	would occur on this Strategy when the underlying closes above the Breakeven Strike of this Strategy by Expiry (<i>discussed below here</i>). • The risk upon reversal towards an uptrend, is limited in this Strategy, i.e. the Max Loss is limited.
<u>Breakeven Strike of this Strategy from Expiry perspective:</u> Net Premium Credit received on the overall Strategy (<i>i.e. the difference between the premium credit collected on the primary leg and the premium debit paid on the hedged leg</i>) subtracted from the primary leg PE Short Strike, defines the Breakeven Strike in this Strategy. The underlying must not downwardly cross the Breakeven Strike, from Expiry perspective in order that this Spread be profitable by Expiry. Thus, we need to determine the Breakeven Strike level below which the underlying must not close by Expiry, in order to bring the Strategy into profit. <u>Breakeven (BE) Strike for determining Loss level:</u> BE level in this Spread is the level which the underlying must not close below by Expiry, so as to yield profit on the Strategy. This BE level is determined by subtracting the Net Premium credit collected on the overall Strategy, from the PE Short primary leg. i.e., BE Strike for this Strategy =	<u>Breakeven Strike of this Strategy from Expiry perspective:</u> Net Premium Credit received on the overall Strategy (<i>i.e. the difference between the premium credit collected on the primary leg and the premium debit paid on the hedged leg</i>) added to the primary leg CE Short Strike, defines the Breakeven Strike in this Strategy The underlying must not upwardly cross the Breakeven Strike, from Expiry perspective in order that this Spread be profitable by Expiry. Thus, we need to determine the Breakeven Strike level above which the underlying must not close by Expiry, in order to bring the Strategy into profit. <u>Breakeven (BE) Strike for determining Loss level:</u> BE level in this Spread is the level which the underlying must not close above by Expiry, so as to yield profit on the Strategy. This BE level is determined by adding the Net Premium credit collected on the overall Strategy, to the CE Short primary leg.

PE Short Strike - Net Premium Credit collected on the Spread

For example: If

- Nifty 17400 PE is Shorted at premium of Rs. 300 per Lot; and
- Nifty 17100 PE is Long at premium of Rs. 100 per Lot

then the BE Strike of this Strategy will be:
 $17400 - (300 - 100) = 17200$ PE Strike.

This Breakeven Strike of 17200 PE must not be breached downwardly by the underlying, in order that this Strategy be profitable from Expiry perspective. Thus, by Expiry, Nifty must not go down below 17200 Strike; and if Nifty expires above the PE Short Strike of 17400, then the entire Net Premium of Rs. 200 per Lot will be the profit in this Strategy.

Impact on BE level, due to Strike Difference:

Larger the difference between PE Short and PE Long Strike, larger will be the net premium credit collected on the Spread, and accordingly larger will be the Breakeven level for the loss to occur on the Strategy on the downside, from Expiry perspective.

Also, the Breakeven Strike gets larger if a PE Credit Spread is initiated on a farther Expiry series than closer Expiry series, on same Strikes of PEs (eg: both primary & hedged leg PEs are initiated on Next Month Expiry series than Current Month Expiry series). This is because the net premium credit collected on the Spread increases as we go on farther Expiry series, even though the primary & hedged leg PE Strikes are kept same.

i.e., BE Strike for this Strategy = CE Short Strike + Net Premium Credit collected on the Spread

For example: If

- Nifty 17200 CE is Shorted at premium of Rs. 250 per Lot; and
- Nifty 17500 CE is Long at premium of Rs. 150

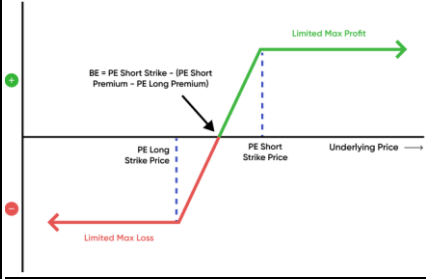
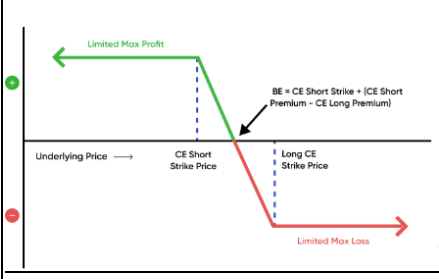
then the BE Strike of this Strategy will be:
 $17200 + (250 - 150) = 17300$ CE Strike.

This Breakeven Strike of 17300 CE must not be breached upwardly by the underlying, in order that this Strategy be profitable from Expiry perspective. Thus, by Expiry, Nifty must not go up above 17300 Strike; and if Nifty expires below the CE Short Strike of 17200, then the entire Net Premium of Rs. 100 per Lot will be the profit in this Strategy.

Impact on BE level, due to Strike Difference:

Larger the difference between CE Short and CE Long Strike, larger will be the net premium credit collected on the Spread, and accordingly larger will be the Breakeven level for the loss to occur on the Strategy on the upside, from Expiry perspective.

Also, the Breakeven Strike gets larger if a CE Credit Spread is initiated on a farther Expiry series than closer Expiry series, on same Strikes of CEs (eg: both primary & hedged leg CEs are initiated on Next Month Expiry series than Current Month Expiry series). This is because the net premium credit collected on the Spread increases as we go on farther Expiry series, even

	though the primary & hedged leg CE Strikes are kept same.
Payoff Chart for Bull PE Credit Spread Bull Put Credit Spread 	Payoff Chart for Bear CE Credit Spread Bear Call Credit Spread 
Maximum Loss in this Strategy from Expiry perspective: Max Loss can also be calculated as the⁹: • [difference between the primary leg Strike and the hedged leg Strike] minus • [Net Credit of the Premium received on the Spread i.e. difference between the Premium collected on the primary leg and the Premium paid on the hedged leg]. <i>For example, if:</i>	Maximum Loss in this Strategy from Expiry perspective: Max Loss can also be calculated as the¹⁰: • [difference between the primary leg Strike and the hedged leg Strike] minus • [Net Credit of the Premium received on the Spread i.e. difference between the Premium collected on the primary leg and the Premium paid on the hedged leg]. <i>For example, if:</i>

⁹ Max Loss can also be calculated as the difference between the Breakeven Strike of primary leg and hedged leg, i.e. the difference between: (i) Breakeven Strike of PE Short (primary leg) = PE Strike - Premium collected; and (ii) Breakeven Strike of PE buy (hedged leg) = PE Strike - Premium paid.

¹⁰ Max Loss can also be calculated as the difference between the Breakeven Strike of primary leg and hedged leg, i.e. the difference between (i) Breakeven Strike of CE Short (primary leg) = CE Strike + Premium collected; and (ii) Breakeven Strike of CE buy (hedged leg) = CE Strike + Premium paid.

- Nifty 17400 PE is Shorted at premium of Rs. 300 per Lot; and
- Nifty 17100 PE is Long at premium of Rs. 100 per Lot

then Max Loss will be: $[17400-17100] - [300-100] = [300 - 200] = \text{Rs. } 100 \text{ per qty,}$

i.e. $\text{Rs. } 100 \times 50 = \text{Rs. } 5000 \text{ per Lot of Nifty is the Max Loss on the aforesaid Credit Spread.}$

Impact on Max Loss amount, due to Strike Difference:

Larger the difference between PE Short and PE Long Strike, larger will be the net premium credit collected on the Spread, and accordingly larger will be the Breakeven below which the loss would occur from Expiry perspective. However, **larger difference between the primary leg and hedged leg increases the Max Loss on the Strategy.** Thus, pre-calculated Max Loss on the Strategy will help decide, the Strike at which PE Short & PE Long leg must be initiated.

Loss Zone:

This PE Spread will yield profit only if the underlying closes above the BE Strike by Expiry, as discussed above, else the Strategy would yield loss.

Therefore, **if the underlying falls down and crosses the BE Strike downwardly and closes below the BE level of this Spread by Expiry, then this Strategy would yield loss.** Lower the underlying closes by Expiry below the BE level of this Spread, higher the loss this Spread would generate. But the Max Loss on this Spread is limited (*which can be determined as per the calculations*

- Nifty 17200 CE is Shorted at premium of Rs. 250 per Lot; and
- Nifty 17500 CE is Long at premium of Rs. 150,

then Max Loss will be: $[17500-17200] - [250-150] = [300 - 100] =$

$\text{Rs. } 200 \text{ per qty,}$

i.e. $\text{Rs. } 200 \times 50 = \text{Rs. } 10,000 \text{ per Lot of Nifty is the Max Loss on the aforesaid Credit Spread.}$

Impact on Max Loss amount, due to Strike Difference:

Larger the difference between CE Short and CE Long Strike, larger will be the net premium credit collected on the Spread, and accordingly larger will be the Breakeven above which the loss would occur from Expiry perspective. However, **larger difference between the primary leg and hedged leg increases the Max Loss on the Strategy.** Thus, pre-calculated Max Loss on the Strategy will help decide, the Strike at which CE Short & CE Long leg must be initiated.

Loss Zone:

This CE Spread will yield profit only if the underlying closes below the BE Strike by Expiry, as discussed above, else the Strategy would yield loss.

Therefore, **if the underlying rises higher and crosses the BE Strike upwardly and closes above the BE level of this Spread by Expiry, then this Strategy would yield loss.** Higher the underlying closes by Expiry above the BE level of this Spread, higher the loss this Spread would generate. But the Max Loss on this Spread is limited (*which can be determined as per*

mentioned above) which is generated when the underlying closes below the PE Long Strike, by Expiry.

Thus, if the underlying crosses below the BE Strike of this Spread on closing basis by Expiry, then the Spread would generate loss. This loss would be less, if the underlying closes just below the BE Strike level of the Spread; but if the underlying closes near the PE Long Strike level, then the Spread would generate higher loss (*which may extend upto Max Loss, if the underlying closes below the PE Long Strike*).

Max Loss Level:

The Max Loss is generated by this Spread if the underlying falls down crossing below the BE level of this Spread and further crosses and closes below the PE Long Strike by Expiry. Thus, the **Max Loss level is achieved on this Spread when the underlying crosses and closes anywhere below the PE Long Strike by Expiry**. It does not matter how much more the underlying falls below the PE Long Strike by Expiry, because the Max Loss would be fixed and limited, if by Expiry the underlying closes anywhere below the PE Long Strike.

Loss Zone:

If the underlying by Expiry closes below the Breakeven Strike, then this Spread would suffer loss. Max Loss level is when the underlying closes at or below the PE Long Strike. Therefore, loss zone of this Spread would be between the BE Strike and PE Long Strike. If underlying closes by Expiry within this zone towards the PE Long Strike then more loss would be generated on this Spread; but if the

the calculations mentioned above) which is generated when the underlying closes above the CE Long Strike, by Expiry.

Thus, if the underlying crosses above the BE Strike of this Spread on closing basis by Expiry, then the Spread would generate loss. This loss would be less, if the underlying closes by Expiry just above the BE Strike level of the Spread; but if the underlying closes by Expiry near the CE Long Strike level, then the Spread would generate higher loss (*which may extend upto Max Loss, if the underlying closes above the CE Long Strike*).

Max Loss Level:

The Max Loss is generated by this Spread if the underlying rises higher crossing above the BE level of this Spread and further crosses and closes above the CE Long Strike by Expiry. Thus, the **Max Loss level is achieved on this Spread when the underlying crosses and closes anywhere above the CE Long Strike by Expiry**. It does not matter how much more the underlying trends higher than the CE Long Strike by Expiry, because the Max Loss would be fixed and limited, if by Expiry the underlying closes anywhere above the CE Long Strike.

Loss Zone:

If the underlying by Expiry closes above the Breakeven Strike, then this Spread would suffer loss. Max Loss level is when the underlying closes at or above the CE Long Strike. Therefore, loss zone of this Spread would be between the BE Strike and CE Long Strike. If underlying closes by Expiry within this zone towards the CE Long Strike then more loss would be generated on this Spread; but if the

underlying closes towards the BE Strike then less loss would be incurred on this Spread.

Thus, if expected closing of the underlying by Expiry, seems to be below the BE level of this Spread, then it indicates that the Strategy would yield loss (*which may get extended to the Max Loss situation on the Strategy if the underlying further falls down and closes below the PE Long Strike by Expiry*).

Calculation of Maximum Reward in this Strategy:

Net Premium Credit received on the overall Strategy (*i.e. the difference between the premium credit collected on the primary leg and the premium debit paid on the hedged leg*), is the Maximum Profit / Reward in this Strategy.

For example, if:

- Nifty 17400 PE is Shorted at premium of Rs. 300 per Lot; and
- Nifty 17100 PE is Long at premium of Rs. 100 per Lot

then Max Profit will be: Rs. 300 – Rs. 100 = Rs. 200 per qty

i.e. Rs 200 x 50 = Rs. 10,000 per Lot of Nifty

The ratio between the Max Loss and the Max Reward gives the Risk & Reward ratio for this Strategy.

Max Profit Level:

The Max Profit (*as calculated above*) would be generated on this Spread, if the underlying closes at or anywhere higher than the PE Short Strike. Consequently,

underlying closes towards the BE Strike then less loss would be incurred on this Spread.

Thus, if expected closing of the underlying by Expiry, seems to be above the BE level of this Spread, then it indicates that the Strategy would yield loss (*which may get extended to the Max Loss situation on the Strategy if the underlying keep rising higher and closes above the CE Long Strike by Expiry*).

Calculation of Maximum Reward in this Strategy:

Net Premium Credit received on the overall Strategy (*i.e. the difference between the premium credit collected on the primary leg and the premium debit paid on the hedged leg*), is the Maximum Profit / Reward in this Strategy.

For example, if:

- Nifty 17200 CE is Shorted at premium of Rs. 250 per Lot; and
- Nifty 17500 CE is Long at premium of Rs. 150

then Max Profit will be: Rs. 250 – Rs. 150 = Rs. 100 per qty

i.e. Rs 100 x 50 = Rs. 5,000 per Lot of Nifty

The ratio between the Max Loss and the Max Reward gives the Risk & Reward ratio for this Strategy.

Max Profit Level:

The Max Profit (*as calculated above*) would be generated on this Spread, if the underlying closes at or anywhere lower than the CE Short Strike. Consequently, in aforesaid situation, CE Short expires as

in aforesaid situation, PE Short expires as an ATM/OTM and the PE Long leg expires as an OTM. Thus, the Net Premium Credit collected on this Spread will be realized on Expiry as the Max Profit.

Thus, **in order to realize the Max Profit potential on this Spread, the underlying must close by Expiry at or anywhere above the PE Short Strike** of this Spread. Any further rise in the underlying, after crossing the PE Short Strike upwardly, would not yield any further higher profit than the Max Profit determined on this Spread *(as per aforesaid calculations)*

Profit Zone on this PE Spread:

The profitability from Expiry perspective would arise in the Strategy, if the underlying closes above the Breakeven Strike level of this Spread *(because below this BE level, the loss situation will arise on this Spread)*. Therefore, profit would be realised on this Spread if the underlying closes by Expiry anywhere between the BE Strike level of this Spread and the PE Short Strike. This is the profit zone for this Spread.

Thus, if the underlying closes by Expiry above the BE Strike of this Spread, then the Spread would generate profit. This profit would be less, if the underlying closes just above the BE Strike level of the Spread; but if the underlying closes near the PE Short Strike level, then the Spread would generate higher profit *(which may extend upto Max Profit, if the underlying closes at or above the PE Short Strike by Expiry)*.

an ATM/OTM and the CE Long leg expires as an OTM. Thus, the Net Premium Credit collected on this Spread will be realized on Expiry as the Max Profit.

Thus, **in order to realize the Max Profit potential on this Spread, the underlying must close by Expiry at or anywhere below the CE Short Strike** of this Spread. Any fall in the underlying, after crossing the CE Short Strike downwardly, would not yield any further higher profit than the Max Profit determined on this Spread *(as per aforesaid calculations)*

Profit Zone on this CE Spread:

The profitability from Expiry perspective would arise in the Strategy, if the underlying closes below the Breakeven Strike level of this Spread *(because above this BE level, the loss situation will arise on this Spread)*. Therefore, profit would be realised on this Spread if the underlying closes by Expiry anywhere between the BE Strike level of this Spread and the CE Short Strike. This is the profit zone for this Spread.

Thus, if the underlying closes by Expiry below the BE Strike of this Spread, then the Spread would generate profit. This profit would be less, if the underlying closes just below the BE Strike level of the Spread; but if the underlying closes near the CE Short Strike level, then the Spread would generate higher profit *(which may extend upto Max Profit, if the underlying closes at or below the CE Short Strike by Expiry)*.

<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level:</u> [PE Short Strike – Net Premium Credit collected on the Spread] <u>Min Profit Level:</u> If underlying closes by Expiry just above the BE Level <u>Max Profit Level:</u> If underlying closes by Expiry at or anywhere higher than the PE Short Strike <u>Profit Zone:</u> If underlying closes by Expiry between the BE Level and the PE Short Strike. Closer to PE Short Strike, higher profit is generated; and if underlying closes towards the BE Level then less profit generated on the Spread. <u>Loss Starting Level:</u> If underlying closes by Expiry below the BE Level <u>Max Loss Level:</u> If underlying closes by Expiry at or anywhere lower than the PE Long Strike. <u>Loss Zone:</u> If underlying closes by Expiry between the BE Level and the PE Long Strike. Closer to PE Long Strike, higher loss is generated; and if underlying closes towards the BE Level then less loss generated on the Spread.	<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level:</u> [CE Short Strike + Net Premium Credit collected on the Spread] <u>Min Profit Level:</u> If underlying closes by Expiry just below the BE Level <u>Max Profit Level:</u> If underlying closes by Expiry at or anywhere lower than the CE Short Strike <u>Profit Zone:</u> If underlying closes by Expiry between the BE Level and the CE Short Strike. Closer to CE Short Strike, higher profit is generated; and if underlying closes towards the BE Level then less profit generated on the Spread. <u>Loss Starting Level:</u> If underlying closes by Expiry above the BE Level <u>Max Loss Level:</u> If underlying closes by Expiry at or anywhere higher than the CE Long Strike. <u>Loss Zone:</u> If underlying closes by Expiry between the BE Level and the CE Long Strike. Closer to CE Long Strike, higher loss is generated; and if underlying closes towards the BE Level then less loss generated on the Spread.
<u>Options behaviour:</u> It is pertinent to note that this Strategy is a Net Premium Credit strategy. Thus, by Expiry, if both the primary leg and hedged leg are OTMs then the Net Credit will be the Max Profit in this Strategy (due	<u>Options behaviour:</u> It is pertinent to note that this Strategy is a Net Premium Credit strategy. Thus, by Expiry, if both the primary leg and hedged leg are OTMs then the Net Credit will be the Max Profit in this Strategy (due

to Theta impact on primary leg and hedged leg, both being OTMs). • Rise in Volatility may not adversely impact this Strategy, even if rise in Volatility would be favourable to the PE Long hedged leg and not on the PE Short primary leg. This is owing to the fact that if the both the legs continue to be an OTM until Expiry then even if rising Volatility increases their Premium value, then also it would eventually become zero and yield profit to the extent of Net Premium credit on Expiry. • Falling state of Volatility will also help this Strategy to realise the profit quickly, as the drop in Volatility will erode the Premium value of both the primary leg and the hedged leg and the Net Premium credit would be realised as profit sooner as Theta impact too would fasten the erosion of the Premium. • Delta play between the primary leg and the hedged leg is separately discussed hereinbelow.	to Theta impact on primary leg and hedged leg, both being OTMs). • Rise in Volatility may not adversely impact this Strategy, even if rise in Volatility would be favourable to the CE Long hedged leg and not on the CE Short primary leg. This is owing to the fact that if the both the legs continue to be an OTM until Expiry then even if rising Volatility increases their Premium value, then also it would eventually become zero and yield profit to the extent of Net Premium credit on Expiry. • Falling state of Volatility will also help this Strategy to realise the profit quickly, as the drop in Volatility will erode the Premium value of both the primary leg and the hedged leg and the Net Premium credit would be realised as profit sooner as Theta impact too would fasten the erosion of the Premium. • Delta play between the primary leg and the hedged leg is separately discussed hereinbelow.
<u>Strike / Delta value:</u> The Delta difference between the primary leg and the hedged leg will help maintain a reasonable control on profit & loss scenario in this Strategy. Delta difference can be ensured by selecting appropriate distance PE Strikes for this Strategy. Since, in this Strategy (which is a Net Credit Strategy), besides the direction of	<u>Strike / Delta value:</u> The Delta difference between the primary leg and the hedged leg will help maintain a reasonable control on profit & loss scenario in this Strategy. Delta difference can be ensured by selecting appropriate distance CE Strikes for this Strategy. Since, in this Strategy (which is a Net Credit Strategy), besides the direction of the underlying, Theta decay also plays an

the underlying, Theta decay also plays an important role to ensure profit. Therefore, Far OTM PEs are selected for this Strategy. In order to benefit from Theta decay, the PE Short for the primary leg should be initiated at such a Strike which the underlying is expected to not breach by Expiry. Also, the primary leg should have sufficient Premium to be credited. Once, primary hedge is selected then the hedged leg must be simultaneously initiated at a suitable Strike distance.

When bullish to sideways view has conviction, then a suitable **smaller Delta difference can be maintained** between the primary leg and the hedged leg, as the Risk-to-Reward Ratio is more favourable. This smaller Delta difference can be ensured by maintaining suitable smaller gap between the Strikes at which primary leg and the hedged leg. Also, in case of a strong conviction based view, a near OTM can also be selected for initiating the PE Short primary leg (*instead of a much farther OTM Strike for the primary leg*).

However, when bullish to sideways view does not have conviction and there seems uncertainty about continuation of bullish trend to sideways move of the underlying, then a suitable **larger Delta difference can be maintained** between the primary leg and the hedged leg, as such Strike difference helps to expand the Breakeven Strike of the Strategy. This widening of the Breakeven area due to larger Strike difference between the primary leg and hedged leg helps to enhance the profit probability and also enhances the max profit potential on the

important role to ensure profit. Therefore, Far OTM CEs are selected for this Strategy. In order to benefit from Theta decay, the CE Short for the primary leg should be initiated at such a Strike which the underlying is expected to not breach by Expiry. Also, the primary leg should have sufficient Premium to be credited. Once, primary hedge is selected then the hedged leg must be simultaneously initiated at a suitable Strike distance.

When bearish to sideways view has conviction, then a suitable **smaller Delta difference can be maintained** between the primary leg and the hedged leg, as the Risk-to-Reward Ratio is more favourable. This smaller Delta difference can be ensured by maintaining suitable smaller gap between the Strikes at which primary leg and the hedged leg. Also, in case of a strong conviction based view, a near OTM can also be selected for initiating the CE Short primary leg (*instead of a much farther OTM Strike for the primary leg*).

However, when bearish to sideways view does not have conviction and there seems uncertainty about continuation of bearish trend to sideways move of the underlying, then a suitable **larger Delta difference can be maintained** between the primary leg and the hedged leg, as such Strike difference helps to expand the Breakeven Strike of the Strategy. This widening of the Breakeven area due to larger Strike difference between the primary leg and hedged leg helps to enhance the profit probability and also enhances the max profit potential on the Strategy (*due to increase in Net Premium Credit received on*

Strategy (due to increase in Net Premium Credit received on the Strategy due to larger Strike difference). However, while larger Breakeven is gained and overall profit potential enhanced due to larger Strike difference, such Strike selection also enhances the Max Loss situation. Thus, larger Strike difference results in overall Risk-to-Reward Ratio on the Strategy, not so favourable. Also, in case of a not very strong conviction based view, Far OTMs must be selected for initiating the PE Short primary leg (instead of a Near OTM Strike for the primary leg).	the Strategy due to larger Strike difference). However, while larger Breakeven is gained and overall profit potential enhanced due to larger Strike difference, such Strike selection also enhances the Max Loss situation. Thus, larger Strike difference results in overall Risk-to-Reward Ratio on the Strategy, not so favourable. Also, in case of a not very strong conviction based view, Far OTMs must be selected for initiating the CE Short primary leg (instead of a Near OTM Strike for the primary leg).
<u>Selection of Option Strikes:</u> Basis aforesaid factors, depending on the intended holding time of the trade, a suitable Far OTM PE Option Strike levels of a particular Expiry series and Delta value may be selected. If Far OTM PE for Shorting as the primary leg has sufficient Premium in the current Expiry series, then it is always advisable to go for closer Expiry series, as it will have higher Theta value to benefit from quick time decay. However, if the sufficient Premium is not available in current Expiry series then subsequent Expiry series may be considered, but the holding time will be higher to benefit from Theta (in which case it is important to assess that by increasing the holding time, the underlying should not appear to be bearish enough to breach the Far OTM PE Strike level at which Short is intended). Further, it must be ensured here that the PE Short primary leg is such Far OTM	<u>Selection of Option Strikes:</u> Basis aforesaid factors, depending on the intended holding time of the trade, a suitable Far OTM CE Option Strike levels of a particular Expiry series and Delta value may be selected. If Far OTM CE for Shorting as the primary leg has sufficient Premium in the current Expiry series, then it is always advisable to go for closer Expiry series, as it will have higher Theta value to benefit from quick time decay. However, if the sufficient Premium is not available in current Expiry series then subsequent Expiry series may be considered, but the holding time will be higher to benefit from Theta (in which case it is important to assess that by increasing the holding time, the underlying should not appear to be bullish enough to breach the Far OTM CE Strike level at which Short is intended). Further, it must be ensured here that the CE Short primary leg is such Far OTM

Strike, which is below some major Support level (<i>as per Technical Analysis / Chart reading</i>), such that by Expiry the underlying does not breach the said major Support level on the downside, thereby causing the PE Short Strike expire worthless as OTM and thus realising the max profit equivalent to the Net Premium Credit collected on this Strategy. Further, if the view is backed by strong conviction, then relatively Near OTMs can be opted for the primary Short leg (<i>instead of a Far OTM</i>). Further, in such case, smaller Strike difference can be maintained between the primary leg and Short leg. However, when bullish to sideways view does not have conviction and there seems uncertainty about continuation of bullish trend to sideways move of the underlying, then Far OTM must be selected for the primary Short leg; and further larger Strike difference may be maintained between the primary leg and the Short leg in order to have a wider Breakeven area.	Strike, which is above some major Resistance level (<i>as per Technical Analysis / Chart reading</i>), such that by Expiry the underlying does not breach the said major Resistance level on the upside, thereby causing the CE Short Strike expire worthless as OTM and thus realising the max profit equivalent to the Net Premium Credit collected on this Strategy. Further, if the view is backed by strong conviction, then relatively Near OTMs can be opted for the primary Short leg (<i>instead of a Far OTM</i>). Further, in such case, smaller Strike difference can be maintained between the primary leg and Short leg. However, when bearish to sideways view does not have conviction and there seems uncertainty about continuation of bearish trend to sideways move of the underlying, then Far OTM must be selected for the primary Short leg; and further larger Strike difference may be maintained between the primary leg and the Short leg in order to have a wider Breakeven area.
<u>If trade goes as per plan:</u> The underlying remains limited bullish to sideways, then the PE Short primary leg will generate profit. But as the underlying moves higher, the hedged PE Long leg will generate loss (<i>because the LTP of PE will fall due to underlying going upward</i>). However, the Delta difference between the primary leg and hedged leg will bring the net position in profit, to	<u>If trade goes as per plan:</u> The underlying remains limited bearish to sideways, then the CE Short primary leg will generate profit. But as the underlying moves lower, the hedged CE Long leg will generate loss (<i>because the LTP of CE will fall due to underlying going downward</i>). However, the Delta difference between the primary leg and hedged leg will bring the net position in profit, to the

the maximum extent of Net Premium Credit on the Strategy. But as the underlying keeps going higher quickly with strong momentum, there may come a time when the Premium on the PE short leg would exhaust completely (and so much so the Net Premium credit). Then at such time the maximum reward has been achieved and therefore both the legs of this Strategy must be square-off and profit must be booked, because the limited profit potential on the Strategy has been reaped. <u>If underlying movement is slow / sideways:</u> However, if the movement of the underlying becomes slow / sluggish in its upward movement or if the underlying keeps fluctuating in a range, then the Theta impact would cause erosion in the Premium value of both PE Short (primary leg) and PE Long (hedged leg). However, since the primary leg has more Premium than the hedged leg, hence the decay of the Net Premium Credit due to rangebound movement / Theta impact will result in profit in this Strategy. <u>If trade does not go as per plan:</u> Upon reversal of the trend towards a downtrend, PE Sell primary leg would start generating losses, which gets covered up by the hedged leg. Thus, in case of a fall in the underlying, breaching the Breakeven Strike of the Strategy on the downside, Max Loss situation may arise in the Strategy (<i>which is calculated as the difference between the Breakeven</i>	maximum extent of Net Premium Credit on the Strategy. But as the underlying keeps going lower quickly with strong momentum, there may come a time when the Premium on the CE short leg would exhaust completely (and so much so the Net Premium credit). Then at such time the maximum reward has been achieved and therefore both the legs of this Strategy must be square-off and profit must be booked, because the limited profit potential on the Strategy has been reaped. <u>If underlying movement is slow / sideways:</u> However, if the movement of the underlying becomes slow / sluggish in its downward movement or if the underlying keeps fluctuating in a range, then the Theta impact would cause erosion in the Premium value of both CE Short (primary leg) and CE Long (hedged leg). However, since the primary leg has more Premium than the hedged leg, hence the decay of the Net Premium Credit due to rangebound movement / Theta impact will result in profit in this Strategy. <u>If trade does not go as per plan:</u> Upon reversal of the trend towards uptrend, CE Sell primary leg would start generating losses, which gets covered up by the hedged leg. Thus, in case of an upward move in the underlying, breaching the Breakeven Strike of the Strategy on the upside, Max Loss situation may arise in the Strategy (<i>which is calculated as the difference between the Breakeven Strikes of the primary leg and the hedged leg</i>).
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<i>Strikes of the primary leg and the hedged leg).</i> However, some adjustments can be considered in order to contain / mitigate the Max Loss situation in this Strategy <i>(as discussed below here)</i>.	However, some adjustments can be considered in order to contain / mitigate the Max Loss situation in this Strategy <i>(as discussed below here)</i>.
<u>Adjustments (if bullish to sideways view and this Strategy does not go as per plan):</u> Since, this Strategy is a Credit Spread, therefore, the Net Premium received (<i>i.e. the difference between the Premium received on the primary leg and the Premium paid in the hedged leg</i>) need to be protected for profit from Expiry perspective. Further, if the bullish to sideways trend reverses in the downward direction, then the Strategy may potentially yield the Max Loss (<i>calculated as already explained above</i>) by Expiry, if the Breakeven Strike of the Strategy is breached on the downside. Thus, upon reversal, this potential Max Loss amount need to be covered up by making suitable adjustments. The following adjustments can be considered to cover up for the potential loss that may occur in this Strategy (<i>which may extend to the maximum extent of Max Loss</i>): (i) Long PEs; or (ii) Short CEs; or (iii) Short PEs. These adjustments are discussed below. (i) <u>Counter Adjustment through Long Option:</u> If there seems to be a trending downtrend with momentum, then a PE can be bought (Long PE). Buying an	<u>Adjustments (if bearish view and this Strategy does not go as per plan):</u> Since, this Strategy is a Credit Spread, therefore, the Net Premium received (<i>i.e. the difference between the Premium received on the primary leg and the Premium paid in the hedged leg</i>) need to be protected for profit from Expiry perspective. Further, if the bearish to sideways trend reverses in the upward direction, then the Strategy may potentially yield the Max Loss (<i>calculated as already explained above</i>) by Expiry, if the Breakeven Strike of the Strategy is breached on the upside. Thus, upon reversal, this potential Max Loss amount need to be covered up by making suitable adjustments. The following adjustments can be considered to cover up for the potential loss that may occur in this Strategy (<i>which may extend to the maximum extent of Max Loss</i>): (i) Long CEs; or (ii) Short PEs; or (iii) Short CEs. These adjustments are discussed below. (i) <u>Counter Adjustment through Long Option:</u> If there seems to be a trending uptrend with momentum, then a CE can be bought (Long CE). Buying an additional CE to protect the upside risk in this Strategy will add up another debit position (in addition to the debit

additional PE to protect the downside risk in this Strategy will add up another debit position (in addition to the debit position in the hedged leg), therefore this PE Long should only be prudent to initiate only if there is strong momentum for the downward direction. This Long PE will help overcome the Max Loss amount that may incur in this Strategy upon reversal. The reversal on downside can be played by a naked PE or a Bear PE Spread Strategy. Further, Long PE should be initiated at a Strike having Delta value higher than the current Delta value of the Short PE primary leg (i.e. at a higher Strike than the PE sell Strike), so that in case of reversal on downtrend, Long PE should generate more profit than the loss generated by the Short PE primary leg. Also, depending upon the Max Loss in the original Strategy and the likely downtrend momentum, suitable number of Long PEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to Long PE in comparison to the original number of Lots initiated on the Strategy. It must be ensured that addition of these Long PEs, turn the net Delta position on this Strategy to negative Delta, in order to reap advantage of the bearish move in the underlying on the overall Strategy. If the Long PEs generates

position in the hedged leg), therefore this CE Long should only be prudent to initiate only if there is strong momentum for the upward direction. This Long CE will help overcome the Max Loss amount that may incur in this Strategy upon reversal. The reversal on upside can be played by a naked CE or a Bull CE Spread Strategy. Further, Long CE should be initiated at a Strike having Delta value higher than the current Delta value of the Short CE primary leg (i.e. at a lower Strike than the CE sell Strike), so that in case of reversal on uptrend, Long CE should generate more profit than the loss generated by the Short CE primary leg. Also, depending upon the Max Loss in the original Strategy and the likely uptrend momentum, suitable number of Long CEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to Long CE in comparison to the original number of Lots initiated on the Strategy. It must be ensured that addition of these Long CEs, turn the net Delta position on this Strategy to positive Delta, in order to reap advantage of the bullish move in the underlying on the overall Strategy. If the Long CEs generates profit to the tune of pre-calculated Max Loss amount in this Strategy, then it would be advisable to book the profit on this Long CE position.

profit to the tune of pre-calculated Max Loss amount in this Strategy, then it would be advisable to book the profit on this Long PE position.

- (ii) Counter Adjustment through Short Option: If there seems to be a slow downtrend, then **Far OTM CEs can be sold** (Short CE) to play the downtrend. Idea in this adjustment is to pick up a suitable Far OTM CE for Shorting, such that this Far OTM CE expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This CE Short will help cover the pre-calculated Max Loss that may be generated on this Strategy. Selection of a Far OTM CE for this adjustment is important because even if the downtrend again reverses on the bullish side, this additional CE must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential Max Loss in the original Strategy and the likely downtrend and the Premium available on Far OTM CEs, suitable number of Short CEs can be considered to be added as an adjustment to absorb or outweigh the Max Loss in the Strategy (*i.e. total premium credit collected on these CE Shorts must be equivalent to the Max Loss, in Rupees term*). Generally, at least 2 to 4 times more Lot quantity may be required

- (ii) Counter Adjustment through Short Option: If there seems to be a slow uptrend, then **Far OTM PEs can be sold** (Short PE) to play the uptrend. Idea in this adjustment is to pick up a suitable Far OTM PE for Shorting, such that this far OTM PE expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This PE Short will help cover the pre-calculated Max Loss that may be generated on this Strategy. Selection of a far OTM PE for this adjustment is important because even if the uptrend again reverses on the bearish side, this additional PE must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential Max Loss in the original Strategy and the likely uptrend and the Premium available on Far OTM PEs, suitable number of Short PEs can be considered to be added as an adjustment to absorb or outweigh the Max Loss in the Strategy (*i.e. total premium credit collected on these PE Shorts must be equivalent to the Max Loss, in Rupees term*). Generally, at least 2 to 4 times more Lot quantity may be required to be added to Short PE in comparison to the original number of Lots initiated on the Strategy. These additional PE Short should be initiated at such Far OTM PEs, which may have reasonable Premium and is expected to expire worthless as OTM on Expiry.

to be added to Short CE in comparison to the original number of Lots initiated on the Strategy. These additional CE Short should be initiated at such Far OTM CEs, which may have reasonable Premium and is expected to expire worthless as OTM on Expiry. However, selling additional CEs will require higher margin / capital to Short CEs and MTM requirements will also have to be met.

(iii) Adjustment through Pyramiding:

If the downtrend is expected to be trending but limited, then **even Farther OTM PEs can be sold** (PE Short) below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry. Idea in this adjustment is to pick up a suitable Far OTM PEs for Shorting, such that this Far OTM PE expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This PE Short will help cover the pre-calculated Max Loss that may be generated on this Strategy. Selection of a Far OTM PE for this adjustment is important because even if the downtrend continues, this additional PE must be such which can be expected to be not breached by the underlying by Expiry and to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential pre-calculated Max

However, selling additional PEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.

(iii) Adjustment through Pyramiding: If the uptrend is expected to be trending but limited, then **even Farther OTM CEs can be sold** (CE Short) above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry. Idea in this adjustment is to pick up a suitable Far OTM CEs for Shorting, such that this Far OTM CE expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This CE Short will help cover the pre-calculated Max Loss that may be generated on this Strategy. Selection of a Far OTM CE for this adjustment is important because even if the uptrend continues, this additional CE must be such which can be expected to be not breached by the underlying by Expiry and to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential pre-calculated Max Loss in the original Strategy and the likely uptrend and the Premium available on Far OTM CEs (of even higher Far OTM Strike above Resistance area), suitable number of Short CEs can be considered to be added as an adjustment to absorb or outweigh the potential Max Loss in the Strategy, by the profit yielded by

Loss in the original Strategy and the likely downtrend and the Premium available on Far OTM PEs (of even lower Far OTM Strike below Support area), suitable number of Short PEs can be considered to be added as an adjustment to absorb or outweigh the potential Max Loss in the Strategy, by the profit yielded by these Short PEs due to time decay on Expiry (*i.e. total premium credit collected on these PE Shorts must be equivalent to the Max Loss on the original Strategy, in Rupees term*). Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short PE in comparison to the original number of Lots initiated on the Strategy. PE Short positions (of same Expiry series as that of the primary leg) can also be added in a pyramidal structure. As the downtrend continues Far OTM PEs' Premium would rise, therefore, Short PEs positions can be added at subsequent lower Strike levels as the downtrend continues with lower PEs gaining decent Premium values. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16500 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 16400 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.* This **Shorting of PEs in a pyramiding manner** may ensure a lower

these Short CEs due to time decay on Expiry (*i.e. total premium credit collected on these CE Shorts must be equivalent to the Max Loss on the original Strategy, in Rupees term*). Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short CE in comparison to the original number of Lots initiated on the Strategy. CE Short positions (of same Expiry series as that of the primary leg) can also be added in a pyramidal structure. As the uptrend continues Far OTM CEs' Premium would rise, therefore, Short CEs positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining decent Premium values. *For example, when the uptrend continues in Nifty, a Far OTM CE at 18000 having Premium of Rs. 50 can be sold, thereafter when the Nifty rises further, subsequent higher CE at 18500 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.* This **Shorting of CEs in a pyramiding manner** may ensure a higher Breakeven strike and thus greater probability of profiting due to Theta decay on these bunch of Short CEs on Expiry. However, selling additional CEs will require higher margin / capital to Short CEs and MTM requirements will also have to be met.

Breakeven strike and thus greater probability of profiting due to Theta decay on these bunch of Short PEs on Expiry. However, selling additional PEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.	
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CALL RATIO SPREAD & PUT RATIO SPREAD

Mildly Bullish and Mildly Bearish view can be played through Ratio Spreads i.e. by employing Options in different proportion/ ratio in the primary leg and hedged leg. In this Strategy, there are less Longs on the primary leg and more Shorts on the hedged leg, usually in ratio of 1:2, 2:3 or 1:3 etc., on the same underlying with same Expiry series at different Strike levels.

Call Ratio Spread:

When the view on the underlying is mildly bullish, we can play the upmove by being Long on CE Options (i.e. buy CE Options) as our main position (the **primary leg**). This primary leg can be hedged by introducing a hedged leg with a bearish view by Shorting Far OTM Call Options (i.e. sell CE Options) on the same underlying with same Expiry series (the **hedged leg**), like it is done in a Bull Call Spread Strategy. However, the hedged leg in this Strategy, will have more quantity / Lots than the primary leg. For example, the primary leg may have 1 Long CE and the hedged leg may have 2 or 3 Short CEs. Thus, the ratio of Lots between the primary leg and the hedged leg may be 1: 2 or 1:3 or 2:3 and so on.

In this Strategy:

- the mild bullish move is played using the Long CE in the primary leg, which will yield profit due to the upmove in the underlying;
- the hedged leg has more quantity of CE Shorts initiated at such higher Far OTM Strike, which is expected to be not breached by the underlying by Expiry (i.e. above the Resistance area), so that on Expiry these CE Short positions on the hedged leg will expire worthless as an OTM thereby yielding profit due to Theta play; and
- usually it is ensured that the Premium credit received on aggregate basis on the CE Short leg is higher than the Premium paid on the CE Long primary leg. Thus, essentially this Strategy is a Credit Spread from net Premium perspective.

This Strategy where a bullish primary leg initiated with Long CE positions at lower Strike with higher Premium; and this primary leg is hedged with Far

OTM Call Short positions at higher Strike with lower Premium with more quantity (*all Shorts on the same Strike*) than the CEs in the primary leg, on the same underlying and of same Expiry series – it is called a **Call Ratio Spread Strategy**. It is a vertical Credit Spread¹¹.

Put Ratio Spread:

When the view on the underlying is mildly bearish, we can play the down move in the underlying, by being Long on PE Options (i.e. buy PE Options) as our main position (the **primary leg**). This primary leg can be hedged by introducing a hedged leg with a bullish view by Shorting Far OTM Put Options (i.e. sell PE Options) on the same underlying with same Expiry series (the **hedged leg**), like it is done in a Bear Put Spread Strategy. However, the hedged leg in this Strategy, will have more quantity / Lots than the primary leg. For example, the primary leg may have 1 Long PE and the hedged leg may have 2 or 3 Short PEs. Thus, the ratio of Lots between the primary leg and the hedged leg may be 1: 2 or 1:3 or 2:3 and so on.

In this Strategy:

- the mild bearish move is played using the Long PE in the primary leg, which will yield profit due to the downward move in the underlying; and
- the hedged leg has more quantity of PE Shorts initiated at such lower Far OTM Strike, which is expected to be not breached by the underlying by Expiry (i.e. below the Support area), so that on Expiry these PE Short positions on the hedged leg will expire worthless as an OTM thereby yielding profit due to Theta play; and

¹¹ However, if the view is bullish, then instead of Call Ratio Credit Spread, a trader must consider **Call Ratio Backspread Strategy**. In Call Ratio Backspread, bullish expectation on the underlying is played by having more Long CEs than CE Short, typically in the ratio of 2:1, 3:2, or 3:1 etc. This may comprise of 2 OTM CE Long primary leg and 1 ITM CE Short as hedged leg on same Expiry series; or 2 ITM CE Long and 1 OTM CE Short. Thus, Call Ratio Backspread is a Net Premium Debit Strategy (*i.e. with more Premium paid for the CE Long than Premium Credit collected on the Short leg, due to different quantity initiated on Long leg and Short leg*). In this Strategy, the upside profit potential is unlimited and the downside risk is limited to the maximum extent of the Net Premium Debit incurred on the Strategy. It is a Vega positive Strategy.

- usually it is ensured that the Premium credit received on aggregate basis on the PE Short leg is higher than the Premium paid on the PE Long primary leg. Thus, essentially this Strategy is a Credit Spread from net Premium perspective.

This Strategy where a bearish primary leg initiated with Long PE positions at higher Strike with higher Premium; and this primary leg is hedged with Far OTM Put Short positions at lower Strike with lower Premium with more quantity (*all Shorts on the same Strike*) than the PEs in the primary leg, on the same underlying and of same Expiry series – it is called a **Put Ratio Spread Strategy**. It is a vertical Credit Spread¹².

With this background, now let us delve into discussing the Call Ratio Spread Strategy and Put Ratio Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Call Ratio Spread Strategy	Put Ratio Spread Strategy
Trade Legs: • Long CE of lower Strike with higher Premium (<i>primary leg</i>) • Short CE of higher Strike with lower Premium (<i>hedged leg</i>) Hedged leg initiated at Far OTM CE Strike (above Resistance area) with more Lots than in the primary leg. All CE Shorts may or may not be on the same	Trade Legs: • Long PE of higher Strike with higher Premium (<i>primary leg</i>) • Short PE of lower Strike with lower Premium (<i>hedged leg</i>) Hedged leg initiated at Far OTM PE Strike (below Support area) with more Lots than in the primary leg. All PE Shorts may or may not be on the same

¹² However, if the view is bearish, then instead of Put Ratio Credit Spread, a trader must consider **Put Ratio Backspread Strategy**. In Put Ratio Backspread, bearish expectation on the underlying is played by having more Long PEs than PE Short, typically in the ratio of 2:1, 3:2, or 3:1 etc. This may comprise of 2 OTM PE Long primary leg and 1 ITM PE Short as hedged leg on same Expiry series; or 2 ITM PE Long and 1 OTM PE Short, etc. Thus, Put Ratio Backspread is a Net Premium Debit Strategy (*i.e. with more Premium paid for the PE Long than Premium Credit collected on the PE Short leg, due to different quantity initiated on Long leg and Short leg*). In this Strategy, the downside profit potential is unlimited and the upside risk is limited to the maximum extent of the Net Premium Debit incurred on the Strategy. It is a Vega positive Strategy.

Strike. Also, both primary and hedged legs pertain to same Expiry series. Further, aggregate Premium Credit collected on CE Short leg is ensured to be higher than the Premium paid for the CE Long leg. This will make the Strategy as a Credit Spread from net Premium perspective, on the Strategy.	Strike. Also, both primary and hedged legs pertain to same Expiry series. Further, aggregate Premium Credit collected on PE Short leg is ensured to be higher than the Premium paid for the PE Long leg. This will make the Strategy as a Credit Spread from net Premium perspective, on the Strategy.
Example: • Buy 1 Lot Nifty 17000 CE of Current Month Expiry (at Rs. 200 per Lot); and • Sell 2 Lot Nifty 17600 CE of Current Month Expiry (at Rs. 120 per Lot) <i>Both legs of Current Month Expiry series (expecting Resistance as per technical analysis to be at 17500).</i> <i>Further, aggregate Premium Credit of CE Short leg is Rs. 240, whereas total Premium Paid for CE Long leg is only Rs. 200. Thus, net Premium Credit of Rs. 40 on the Strategy (i.e. $240-200=40$).</i>	Example: • Buy 1 Lot Nifty 17800 PE of Current Week Expiry (at Rs. 180 per Lot); and • Sell 2 Lot Nifty 17300 PE of Current Week Expiry (at Rs. 100 per Lot) <i>Both legs of Current Week Expiry series (expecting Support as per technical analysis to be at 17200)</i> <i>Further, aggregate Premium Credit of PE Short leg is Rs. 200, whereas total Premium Paid for PE Long leg is only Rs. 180. Thus, net Premium Credit of Rs. 20 on the Strategy (i.e. $200-180=20$).</i>
Objective: Objective is to play mild bullish view through buying CEs (as the primary leg). Further, relatively more quantities are initiated as Short at Far OTM CE Strike above Resistance level, in order to gain from time decay on Expiry (as these OTM CE Short positions will become zero if expire as OTM).	Objective: Objective is to play mild bearish view through buying PEs (as the primary leg). Further, relatively more quantities are initiated as Short at Far OTM PE Strike below Support level, in order to gain from time decay on Expiry (as these OTM PE Short positions will become zero if expire as OTM).

Further, same number of CEs in the primary and hedged leg will act as Bull Call Spread. However, extra CE Short as part of the hedged leg will suitably cover the downside risk of reversal in the downward direction. The extra CE Short position makes this Strategy a Net Premium Credit strategy, hence upon reversal in the downward direction this Strategy would yield profit to the maximum extent of Net Premium Credit on the Strategy. This Strategy would generate limited profit on the downside or if the Breakeven Strike of this Strategy is not breached by the underlying on the upside by Expiry. However, if the BE strike of this Strategy is breached by the underlying on the upside by Expiry, then this Strategy would generate unlimited loss (<i>i.e. higher the underlying closes by Expiry, after breaching the BE Strike of the Strategy on the upside, higher would be the loss generated</i>). Thus, this Strategy bears limited profit and unlimited loss potential.	Further, same number of PEs in the primary and hedged leg will act as Bear Put Spread. However, extra PE Short as part of the hedged leg will suitably cover the risk of reversal in the upward direction. The extra PE Short position makes this Strategy a Net Premium Credit strategy, hence upon reversal in the upward direction this Strategy would yield profit to the maximum extent of Net Premium Credit on the Strategy. This Strategy would generate limited profit on the upside or if the Breakeven Strike of this Strategy is not breached by the underlying on the downside by Expiry. However, if the BE strike of this Strategy is breached by the underlying on the downside by Expiry, then this Strategy would generate unlimited loss (<i>i.e. lower the underlying closes by Expiry, after breaching the BE Strike of the Strategy on the downside, higher would be the loss generated</i>). Thus, this Strategy bears limited profit and unlimited loss potential.
<u>Demerits:</u> • If VIX is low, there may not be reasonable Premium to create Shorts thereon for the hedged leg. Such situations will require more Shorts to be initiated in order to have a reasonable aggregate Premium value to target from Theta decay perspective. • Since, there are more Shorts than Long, therefore there will be a higher margin /capital requirement	<u>Demerits:</u> • If VIX is low, there may not be reasonable Premium to create Shorts thereon for the hedged leg. Such situations will require more Shorts to be initiated in order to have a reasonable aggregate Premium value to target from Theta decay perspective. • Since, there are more Shorts than Long, therefore there will be a higher margin /capital requirement and

and also MTM requirements will also have to be adhered. • This Spread strategy will be suitable for a mild bullish view which must not breach the identified Resistance level by Expiry. Strong momentum bullish uptrend may cause this Strategy to suffer unlimited loss (because CE Shorts are more than the Long CEs). Thus, this Strategy has an upside risk of unlimited loss. • It is a Strategy with limited profit potential and unlimited loss potential. • Thus, from Expiry perspective, the bullish move in the underlying must not cross above the Breakeven Strike of this Strategy (<i>discussed below here</i>).	also MTM requirements will also have to be adhered. • This Spread strategy will be suitable for a mild bearish view which must not breach the identified Support level by Expiry. Strong momentum bearish trend may cause this Strategy to suffer unlimited loss (because PE Shorts are more than the Long PEs). Thus, this Strategy has a downside risk of unlimited loss. • It is a Strategy with limited profit potential and unlimited loss potential. • Thus, from Expiry perspective, the bearish move in the underlying must not cross below the Breakeven Strike of this Strategy (<i>discussed below here</i>).
<u>Benefits of Call Ratio Spread:</u> • This is a very suitable Strategy for a mild bullish to sideways trend of the underlying, as the primary leg will yield profit on upmove and the hedged leg too will yield profit due to Theta decay on Expiry in case of both mild bullish to sideways movement of the underlying. • Moreover, usually this Strategy is a Net Credit Strategy i.e. while Short per Lot is initiated at a lower Premium bearing Far OTM CE Strike but the collective Premium received in the hedged leg by Shorting CEs is higher than the Premium paid on the Long CE initiated as the primary leg.	<u>Benefits of Put Ratio Spread:</u> • This is a very suitable Strategy for a mild bearish to sideways trend of the underlying, as the primary leg will yield profit on down move of the underlying and the hedged leg too will yield profit due to Theta decay on Expiry in case of both mild bearish to sideways movement of the underlying. • Moreover, usually this Strategy is a Net Credit Strategy i.e. while Short per Lot is initiated at a lower Premium bearing Far OTM PE Strike but the collective Premium received in the hedged leg by Shorting PEs is higher than the Premium paid on the Long PE

Therefore, from Expiry perspective, this Net Credit Premium need to be protected to become profitable (by selection of Far OTM CE Strike for the hedged leg above Resistance level). • Thus, if the underlying by Expiry closes anywhere below the Breakeven Strike, this Strategy will yield some limited Profit. • This Strategy being a Net premium Credit Strategy owing to more number of CE Shorts, therefore this situation fully takes care of the reversal of trend in the opposite direction i.e reversal on downward direction, without the need of any adjustments. From Expiry perspective, reversal in downward direction would yield profit, without making any adjustments, to the extent of Net Premium received on the Strategy.	initiated as the primary leg. Therefore, from Expiry perspective, this Net Credit Premium need to be protected to become profitable (by selection of Far OTM PE Strike for the hedged leg below Support level). • Thus, if the underlying by Expiry closes anywhere above the Breakeven Strike, this Strategy will yield some limited Profit. • This Strategy being a Net premium Credit Strategy owing to more number of PE Shorts, therefore this situation fully takes care of the reversal of trend in the opposite direction i.e reversal on upward direction, without the need of any adjustments. From Expiry perspective, reversal in upward direction would yield profit, without making any adjustments, to the extent of Net Premium received on the Strategy.
<u>Breakeven Strike of this Strategy from Expiry perspective:</u> The Breakeven Strike (BE) in case of a CE Ratio Spread, need to be understood as explained below: (i) The CE Short leg's BE Strike is CE Short Strike + premium credit received on CE Short leg. This means that when the underlying crosses upwardly beyond this BE Strike level and closes by Expiry higher than the said BE level, then the CE Short leg from Expiry perspective would yield loss on the CE Short leg.	<u>Breakeven Strike of this Strategy from Expiry perspective:</u> The Breakeven Strike (BE) in case of a PE Ratio Spread, need to be understood as explained below: (i) The PE Short leg's BE Strike is PE Short Strike - premium credit received on PE Short leg. This means that when the underlying crosses downwardly below this BE Strike level and closes by Expiry lower than the said BE level, then the PE Short leg from Expiry perspective would yield loss on the PE Short leg. (ii) But from a PE Ratio perspective, since we also have a PE Long position

(ii) But from a CE Ratio perspective, since we also have a CE Long position on the primary leg, therefore, if CE Short leg reaches its BE strike level on the upside, then the CE Long leg would be generating profit (*because it is on higher Delta than the Short leg*). This profit generated on the CE Long leg due to upside move in the underlying, would further add up to the BE level on the CE Short leg. Thus, in order to define the BE level on overall basis on the CE Ratio Spread Strategy, we need to calculate the tentative net profit that would be generated on the CE Long leg if the underlying reaches upwardly upto the BE level of the CE Short leg.

This net profit on the CE Long is determined as per calculation given below:

[Strike difference between CE Long & Short leg] *minus* [Net premium debit, per single Lot basis between CE Long & Short leg]

Accordingly, the **BE Strike on the CE Ratio Spread**, would be the sum of (i) & (ii) above, i.e:

[BE of CE Short leg] + [(Strike difference-Net Premium Debit per Lot basis)].

This implies that if the underlying by Expiry closes above this BE Strike level on the upside, then the CE Ratio Spread would generate loss. Higher the underlying would move above this BE

on the primary leg, therefore, if PE Short leg reaches its BE strike level on the downside, then the PE Long leg would be generating profit (*because it is on higher Delta than the Short leg*). This profit generated on the PE Long leg due to downside move in the underlying, would further add up to the BE level on the PE Short leg. Thus, in order to define the BE level on overall basis on the PE Ratio Spread Strategy, we need to calculate the tentative net profit that would be generated on the PE Long leg if the underlying reaches downwardly upto the BE level of the PE Short leg.

This net profit on the PE Long is determined as per calculation given below:

[Strike difference between PE Long & Short leg] *minus* [Net premium debit, per single Lot basis between PE Long & Short leg]

Accordingly, the **BE Strike on the PE Ratio Spread**, would be (i) *minus* (ii) above, i.e:

[BE of PE Short leg] - [(Strike difference-Net Premium Debit per Lot basis)].

This implies that if the underlying by Expiry closes below this BE Strike level on the downside, then the PE Ratio Spread would generate loss. Lower the underlying would move below this BE level, the PE Ratio Spread would enter unlimited loss area.

For example, if:

- 1 Lot Nifty 17500 PE is bought at Rs. 250 premium (primary leg); and

level, the CE Ratio Spread would enter unlimited loss area.

For example, if:

- 1 Lot Nifty 17600 CE is bought at premium of Rs. 200 per Lot (primary leg); and
- 2 Lot Nifty 17800 CE is sold at premium of Rs. 150 per Lot (hedged leg)

then, the BE Strike of this CE Ratio Spread Strategy will be: $[17800 + 150] + [200 - 50] = 17950 + 150 = 18,100$ CE Strike

Thus, by Expiry, Nifty must not close above the BE Strike of the overall CE Ratio Spread, which is 18100 CE Strike. And if Nifty expires below the CE Short Strike of 17800, then the primary leg may be in profit and the entire aggregate Premium of Rs. 300 received on the hedged leg will be the profit in this Strategy.

However, it must be borne in mind that if the CE buy primary leg is not an ITM on or near Expiry, then it is better to book profit on the CE buy leg before its Premium becomes zero due to Theta effect on Expiry.

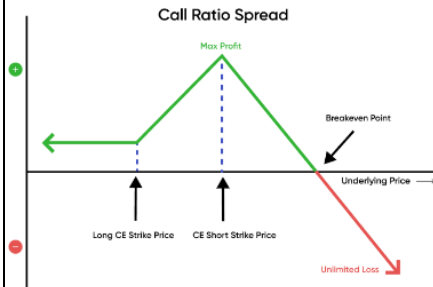
- 2 Lots Nifty 17300 PE is sold at Rs. 150 premium per Lot (hedged leg)

then, the BE Strike of this PE Ratio Spread Strategy will be: $[17300 - 150] - [200 - 100] = 17150 - 100 = 17,050$ PE Strike

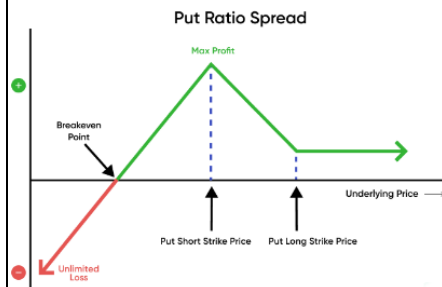
Thus, by Expiry, Nifty must not go down below the BE Strike of the overall PE Ratio Spread, which is 17050 PE Strike. And if Nifty expires above the PE Short Strike of 17300, then the primary leg may be in profit and the entire aggregate Premium of Rs. 300 received on the PE Short hedged leg will be the profit in this Strategy.

However, it must be borne in mind that if the PE buy primary leg is not an ITM on or near Expiry, then it is better to book profit on the PE buy leg before its Premium becomes zero due to Theta effect on Expiry.

Payoff for Call Ratio Spread



Payoff for Put Ratio Spread



Loss in this Strategy from Expiry perspective:

Since, there are more Shorts than Long, therefore, this CE Ratio Spread will have more premium credits than premium debit. This implies that the overall Delta position on the overall CE Ratio Spread would be negative. Therefore, if the trend becomes extreme bullish such that the underlying keeps trending higher crossing above the BE Strike of the overall CE Ratio Spread (*thereby implying that both CE buy and CE sell Strikes have become ITM*), then the CE Long will generate profit but this profit will be much less than the loss generated on CE Short leg (which will generate unlimited loss scenario) if the trend remains bullish making higher moves. Higher the underlying moves and closes above the Breakeven Strike, higher will be the loss generated on this Strategy. Thus, this Strategy has potential of generating unlimited loss situation.

Loss Level:

If the underlying by Expiry closes anywhere above the Breakeven Strike of this Strategy, then this Strategy would generate loss.

Calculation of Final Loss on Expiry:

Therefore, from Expiry perspective, the difference between final Premium of CE Short leg and the final Premium of CE buy leg on Expiry will determine the actual quantum of loss in this Strategy. The max loss would enter unlimited territory if the underlying keeps trending higher breaching the Breakeven Strike of this CE Ratio Spread.

Loss in this Strategy from Expiry perspective:

Since, there are more Shorts than Long, therefore, this PE Ratio Spread will have more premium credits than premium debit. This implies that the overall Delta position on the overall PE Ratio Spread would be positive. Therefore, if the trend becomes extreme bearish such that the underlying keeps trending lower crossing below the BE Strike of the overall PE Ratio Spread (*thereby implying that both PE buy and PE sell Strikes have become ITM*), then the PE Long will generate profit but this profit will be much less than the loss generated on PE Short leg (which will generate unlimited loss scenario) if the trend remains bearish making lower lows. Lower the underlying moves and closes below the Breakeven Strike, higher will be the loss generated on this Strategy. Thus, this Strategy has potential of generating unlimited loss situation

Loss Level:

If the underlying by Expiry closes anywhere below the Breakeven Strike of this Strategy, then this Strategy would generate loss.

Calculation of Final Loss on Expiry:

Therefore, from Expiry perspective, the difference between final Premium of PE Short leg and the final Premium of PE buy leg on Expiry will determine the actual quantum of loss in this Strategy. The max loss would enter unlimited territory if the underlying keeps trending lower breaching the Breakeven Strike of this PE Ratio Spread.

<u>Profit in this Strategy:</u> <u>Minimum Profit:</u> Since, there are more Shorts than Long, therefore, this CE Ratio Spread will have more premium credits than premium debit, hence, this Strategy is a Net Premium Credit Strategy. Therefore, if the underlying by Expiry closes anywhere below the CE Long Strike, then the Net Premium Credit (<i>i.e. total premium credit collected on Short leg – premium debit paid on the Long leg</i>) collected on the Strategy will be the limited profit yield on the Strategy. Thus, the minimum profit yield in a Call Ratio Credit Spread, can be pre-determined by calculating the Net Premium Credit on the Strategy. <u>Maximum Profit Level:</u> If the underlying by Expiry closes at the CE Short Strike, then Maximum profit yield would be realised on this Strategy, which can be pre-determined at calculated as explained below. <u>Calculation of Maximum Profit:</u> Max profit on this Strategy can be calculated as: • <i>[max profit on the equal qty of Bull CE Spread¹³]</i> plus	<u>Profit in this Strategy:</u> <u>Minimum Profit:</u> Since, there are more Shorts than Long, therefore, this PE Ratio Spread will have more premium credits than premium debit, hence, this Strategy is a Net Premium Credit Strategy. Therefore, if the underlying by Expiry closes anywhere above the PE Long Strike, then the Net Premium Credit (<i>i.e. total premium credit collected on Short leg – premium debit paid on the Long leg</i>) collected on the Strategy will be the limited profit yield on the Strategy. Thus, the minimum profit yield in a Put Ratio Credit Spread, can be pre-determined by calculating the Net Premium Credit on the Strategy. <u>Maximum Profit Level:</u> If the underlying by Expiry closes at the PE Short Strike, then Maximum profit yield would be realised on this Strategy, which can be pre-determined at calculated as explained below. <u>Calculation of Maximum Profit:</u> Max profit on this Strategy can be calculated as: • <i>[max profit on the equal qty of Bear PE Spread¹⁴]</i> plus
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¹³ Max Profit in Bull CE Spread is calculated for each quantity as: *[difference between Long & Short Strike]* - Net Premium debit paid on the Spread

¹⁴ Max Profit in Bear PE Spread is calculated for each quantity as: *[difference between Long & Short Strike]* - Net Premium debit paid on the Spread

• [aggregate Premium Credit Received on extra CE Short] <u>For example, if:</u> • 1 Lot Nifty 17600 CE is bought at premium of Rs. 200 per Lot (primary leg); and • 2 Lot Nifty 17800 CE is sold at premium of Rs. 150 per Lot (hedged leg) then, the Max Reward will be: (a) Max reward on 1 Lot Bull CE Spread = $[(17800-17600) - (200-150)] \times 50 = \text{Rs. } 7500$; and (b) Max reward on extra 1 Lot CE Short = $[150] \times 50 = \text{Rs. } 7500$. Thus, total max reward on above CE Ratio Spread is (a) + (b) = Rs. 15000. However, if the same Call Ratio Spread would be initiated with higher quantity, then the Max Profit as per aforesaid formula would be as calculated below. <u>Suppose:</u> • 5 Lot Nifty 17600 CE is bought at premium of Rs. 200 per Lot (primary leg); and • 10 Lot Nifty 17800 CE is sold at premium of Rs. 150 per Lot (hedged leg) then, the Max Reward will be: (a) Max reward on 1 Lot Bull CE Spread = $[(17800-17600) - (200-150)] \times 50 = \text{Rs. } 7500$. Therefore, for 5 Lots on Long leg, max profit would be = Rs. 37,500; and	• [aggregate Premium Credit Received on extra PE Short] <u>For example, if:</u> • 1 Lot Nifty 17500 PE is bought at Rs. 250 premium (primary leg); and • 2 NiftyNifty 17300 PE is sold at Rs. 150 premium per Lot (hedged leg) then, the Max Reward will be: (a) Max reward on 1 Lot Bear PE Spread = $[(17500-17300) - (250-150)] \times 50 = \text{Rs. } 5000$; and (b) Max reward on extra 1 Lot PE Short = $[150] \times 50 = \text{Rs. } 7500$. Thus, total max reward on above PE Ratio Spread is (a) + (b) = Rs. 12500 However, if the same Put Ratio Spread would be initiated with higher quantity, then the Max Profit as per aforesaid formula would be as calculated below. <u>Suppose:</u> • 5 Lot Nifty 17500 PE is bought at Rs. 250 premium (primary leg); and • 10 Lot Nifty 17300 PE is sold at Rs. 150 premium per Lot (hedged leg) then, the Max Reward will be: (a) Max reward on 1 Lot Bear PE Spread = $[(17500-17300) - (250-150)] \times 50 = \text{Rs. } 5000$. Therefore, for 5 Lots on Long leg, max profit would be = Rs. 25,000; and (b) Max reward on extra 1 Lot PE Short = $[150] \times 50 = \text{Rs. } 7500$. Therefore, for
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(b) *Max reward on extra 1 Lot CE Short = $[150] \times 50 = \text{Rs. } 7500$. Therefore, for extra 5 Lots on Short leg, max profit would be = Rs. 37,500*

Thus, total max reward on above CE Ratio Spread is (a) + (b) = Rs. 75,000.

This max profit on CE Ratio Spread would be generated if the underlying moves higher and closes right at the CE Short Strike. In such situation, the CE Long leg would get benefitted from the upmove in the underlying and due to Expiry happening at the CE Short leg, the CE Long would be an ITM (*thus its profit would be protected*) and CE Short would expire worthless as an ATM / near OTM (*thus generating full premium credit on CE Short leg as profit*). Thus, max profit on this Strategy is limited.

Profit Level on overall Strategy:

If the underlying by Expiry closes anywhere below the Breakeven Strike of the Strategy, then this Strategy would yield some profit.

Profit Zone(s) in this Strategy:

There are following three profit zones in this Strategy from Expiry perspective:

- (i) If the underlying by Expiry closes below the CE Long leg, then Min profit to the extent of Net Premium Credit would be generated on this Strategy. Thus, in this profit zone, only Min profit amount would be generated on this Strategy.
- (ii) If the underlying by Expiry closes between the CE Long Strike and CE Short Strike. Higher the

extra 5 Lots on Short leg, max profit would be = Rs. 37,500.

Thus, total max reward on above PE Ratio Spread is (a) + (b) = Rs. 62,500

This max profit on PE Ratio Spread would be generated if the underlying moves lower and closes right at the PE Short Strike. In such situation, the PE Long leg would get benefitted from the downmove in the underlying and due to Expiry happening at the PE Short leg, the PE Long would be an ITM (*thus its profit would be protected*) and PE Short would expire worthless as an ATM / near OTM (*thus generating full premium credit on PE Short leg as profit*). Thus, max profit on this Strategy is limited.

Profit Level on overall Strategy:

If the underlying by Expiry closes anywhere above the Breakeven Strike of the Strategy, then this Strategy would yield some profit.

Profit Zone(s) in this Strategy:

There are following three profit zones in this Strategy from Expiry perspective:

- (i) If the underlying by Expiry closes above the PE Long leg, then Min profit to the extent of Net Premium Credit would be generated on this Strategy. Thus, in this profit zone, only Min profit amount would be generated on this Strategy.
- (ii) If the underlying by Expiry closes between the PE Long Strike and PE Short Strike. Lower the underlying closes towards PE Short Strike, higher will be the profit generated on this Strategy. If the underlying

underlying closes towards CE Short Strike, higher will be the profit generated on this Strategy. If the underlying closes at the CE Short Strike on Expiry, then max profit will be realised on this Strategy (<i>as per calculations explained above</i>). Thus, in this profit zone, profit on this Strategy would be between Min profit to Max profit amount. (iii) If the underlying by Expiry closes between the CE Short Strike and Breakeven Strike of the Strategy. Higher the underlying closes towards Breakeven Strike, lower will be the profit generated within this zone. Thus, in this profit zone, profit on this Strategy would be between Max profit amount to zero profit. However, if the underlying closes above the Breakeven Strike on Expiry, then max loss situation arise on this Strategy (<i>as already explained above</i>).	closes at the PE Short Strike on Expiry, then max profit will be realised on this Strategy (<i>as per calculations explained above</i>). Thus, in this profit zone, profit on this Strategy would be between Min profit to Max profit amount. (iii) If the underlying by Expiry closes between the PE Short Strike and Breakeven Strike of the Strategy. Lower the underlying closes towards Breakeven Strike, lower will be the profit generated within this zone. Thus, in this profit zone, profit on this Strategy would be between Max profit amount to zero profit. However, if the underlying closes below the Breakeven Strike on Expiry, then max loss situation arise on this Strategy (<i>as already explained above</i>).
<u>Profit & Loss Levels in this Strategy from Expiry perspective:</u> <u>BE Level:</u> $[BE \text{ of CE Short leg}] + [(Strike \text{ difference} - Net \text{ Premium Debit})]$ <u>Min Profit Level:</u> If the underlying closes anywhere below CE Long Strike. <u>Min Profit Amount:</u> Is equal to Net Premium Credit collected on the Strategy. <u>Max Profit Level:</u> If the underlying closes at CE Short Strike.	<u>Profit & Loss Levels in this Strategy from Expiry perspective:</u> <u>BE Level:</u> $[BE \text{ of PE Short leg}] - [(Strike \text{ difference} - Net \text{ Premium Debit})]$ <u>Min Profit Level:</u> If the underlying closes anywhere above PE Long Strike. <u>Min Profit Amount:</u> Is equal to Net Premium Credit collected on the Strategy. <u>Max Profit Level:</u> If the underlying closes at PE Short Strike.

<u>Max Profit Amount:</u> Limited amount of Max profit can be generated on the Strategy (<i>as per calculations given above</i>). <u>Profit Zone:</u> If the underlying closes anywhere below the Breakeven Strike of the Strategy. <u>Loss Level:</u> If the underlying closes anywhere above the Breakeven Strike of the Strategy. <u>Max Loss Amount:</u> Max loss can be unlimited on this Strategy as the underlying keeps trending higher than the Breakeven Strike of this Strategy.	<u>Max Profit Amount:</u> Limited amount of Max profit can be generated on the Strategy (<i>as per calculations given above</i>). <u>Profit Zone:</u> If the underlying closes anywhere above the Breakeven Strike of the Strategy. <u>Loss Level:</u> If the underlying closes anywhere below the Breakeven Strike of the Strategy. <u>Max Loss Amount:</u> Max loss can be unlimited on this Strategy as the underlying keeps trending lower than the Breakeven Strike of this Strategy.
<u>Options Behaviour:</u> Idea is to play limited bullish move through initiating CE buy as the primary leg; and to hedge this primary leg with same quantity Far OTM CE Short (as typically done in Bull CE Debit spread Strategy), thus yielding profit on the CE buy leg if it expires as an ITM on Expiry. However, if near to Expiry, the CE buy is in profit due to the bullish move of the underlying but does not seem to expire as an ITM on Expiry then it is better to book profit on the CE buy leg and to hold the CE Short positions until Expiry to let them expire as OTM on Expiry (<i>provided the trading account has enough margin to support the naked CE Short positions, after CE Long is squared-off for booking profit</i>). Further , in this Strategy, since Short leg has more Premium Credit than the Premium paid on CE Long leg therefore, the Strategy is basically a Net Credit Strategy from Premium perspective. Thus, if the underlying closes by Expiry	<u>Options Behaviour:</u> Idea is to play limited bearish move through initiating PE buy as the primary leg; and to hedge this primary leg with same quantity Far OTM PE Short (as typically done in Bear PE Debit spread Strategy), thus yielding profit on the PE buy leg if it expires as an ITM on Expiry. However, if near to Expiry, the PE buy is in profit due to the bearish move of the underlying but does not seem to expire as an ITM on Expiry then it is better to book profit on the PE buy leg and to hold the PE Short positions until Expiry to let them expire as OTM on Expiry (<i>provided the trading account has enough margin to support the naked PE Short positions, after PE Long is squared-off for booking profit</i>). Further , in this Strategy, since Short leg has more Premium Credit than the Premium paid on PE Long leg therefore, the Strategy is basically a Net Credit Strategy from Premium perspective. Thus, if the underlying closes by Expiry above the PE Long leg then both PE Long

below the CE Long leg then both CE Long leg and CE Short leg expires as an OTM, thereby generating Min Profit equivalent to the Net Premium Credit collected on the Strategy. Thus, there is no downside risk in this Net Credit Ratio Spread. In this Strategy, selection of CE Short Strike for the hedged leg is very important, as it must be such where the underlying is not expected to reach on the upside by Expiry (thus, the CE Short must be above the Resistance level). Additionally, in this Strategy, more quantity of CE Shorts (which are higher than the Resistance level) are added which are much farther OTM CEs as compared to CEs on the Long leg (<i>which are usually selected as ITMs or Near OTMs</i>). Thus, the impact of Theta is more on the Short legs than the Long leg, which helps generate net profit on the Strategy even if the underlying keeps hovering within a range. However, if the underlying gets super bullish, so as to breach the Breakeven Strike and trend higher, then since there are more CE Short positions than CE Long positions, therefore, the Strategy may start exhibiting virtual loss, which may convert to actual loss situation if the underlying closes by Expiry higher than the BE Strike of the Strategy. Thus, there is an unlimited upside risk in this Strategy, beyond the BE Strike.	leg and PE Short leg expires as an OTM, thereby generating Min Profit equivalent to the Net Premium Credit collected on the Strategy. Thus, there is no upside risk in this Net Credit Ratio Spread. In this Strategy, selection of PE Short Strike for the hedged leg is very important, as it must be such where the underlying is not expected to reach on the downside by Expiry (thus, the PE Short must be above below the Support level). Additionally, in this Strategy, more quantity of PE Shorts (which are below the Support level) are added which are much farther OTM PEs as compared to PEs on the Long leg (<i>which are usually selected as ITMs or Near OTMs</i>). Thus, the impact of Theta is more on the Short legs than the Long leg, which helps generate net profit on the Strategy even if the underlying keeps hovering within a range. However, if the underlying gets super bearish, so as to breach the Breakeven Strike and trend lower, then since there are more PE Short positions than PE Long positions, therefore, the Strategy may start exhibiting virtual loss, which may convert to actual loss situation if the underlying closes by Expiry lower than the BE Strike of the Strategy. Thus, there is an unlimited downside risk in this Strategy, beyond the BE Strike.
<u>Selection of Option Strikes:</u> Depending upon the limited bullish move, suitable Delta value lower Strike	<u>Selection of Option Strikes:</u> Depending upon the limited bearish move, suitable Delta value higher PE

CE (ITM or near OTM) can be bought for the primary leg, which is slightly below the major Resistance level. For the hedged leg, higher Strike Far OTM CEs with suitable Premium amount can be Shorted, such that a Net Premium Credit can be ensured on the Strategy. Further, such Far OTM CEs must be above such Resistance level, which the underlying should not breach on Expiry and consequently entire credit of Premium on the hedged leg is earned on Expiry due to Theta impact. Basis aforesaid factors, suitable CE Option Strike levels of a particular Expiry series may be selected.	(ITM or near OTM) can be bought for the primary leg which is slightly above than the major Support level. For the hedged leg, lower Far OTM PEs with suitable Premium amount can be Shorted, such that a Net Premium Credit can be ensured on the Strategy. Further, such Far OTM PEs must be below such Support level, which the underlying should not breach on Expiry and consequently entire credit of Premium on the hedged leg is earned on Expiry due to Theta impact. Basis aforesaid factors, suitable PE Option Strike levels of a particular Expiry series may be selected.
<u>If trade goes as per plan:</u> If the underlying remains bullish, then the CE Long primary leg will generate profit. But as the underlying moves higher, the hedged CE Short leg will generate loss (<i>because the LTP of CE Short leg will rise due to underlying going upward</i>). However, the selection of this CE Short Strike must be such that the underlying will not breach this Strike upwardly by Expiry and will therefore expire worthless as an OTM on Expiry (even though it was exhibiting loss due to bullish move of the underlying, prior to Expiry). Thus, if the limited bullish move goes as per plan then the CE buy primary leg would generate profit due to bullish move. Further, if the CE buy does not become an ITM on Expiry then the profit on this CE buy leg must be booked	<u>If trade goes as per plan:</u> If the underlying remains bearish, then the PE Long primary leg will generate profit. But as the underlying moves lower, the hedged PE Short leg will generate loss (<i>because the LTP of PE Short leg will rise due to underlying going downward</i>). However, the selection of this PE Short Strike must be such that the underlying will not breach this Strike downwardly by Expiry and will therefore expire worthless as an OTM on Expiry (even though it was exhibiting loss due to bearish move of the underlying, prior to Expiry). Thus, if the limited bearish move goes as per plan then the PE buy primary leg would generate profit due to bearish move. Further, if the PE buy does not become an ITM on Expiry then the profit on this PE buy leg must be booked before Expiry (because if the PE buy leg is an

before Expiry (because if the CE buy leg is an OTM then its Premium will become zero on Expiry). However, if the CE buy leg becomes an ITM on Expiry, then its final LTP will determine the profit on the CE buy primary leg (*i.e. if the final LTP is higher than its buying price*).

So far as the CE Short hedged leg is concerned, if the underlying does not breach the Breakeven Strike then profit is generated on the hedged leg.

Thus, on such limited bullish move, both the primary leg and the hedged leg generates profit, and the max profit (*which can be pre-calculated, as explained above*) would be generated on this Strategy if the underlying closes by Expiry just near the CE Short leg on the upside.

If movement of the underlying is slow / sideways:

However, if the movement of the underlying becomes slow / sluggish in its upward movement or if the underlying keeps fluctuating in a range, then the Theta impact may cause erosion in the Premium value of both CE Long and CE Short leg. However, since this Strategy is a Net Premium Credit strategy (*owing to the fact that there are more CE Shorts than CE Long and Short Strike is farther OTM than the Long Strike*), the Net Premium Credited would be the maximum profit in such situation by Expiry if the underlying closes by Expiry below the CE Long leg (*in which situation both Long & Short Strike CEs would expire as OTM*). However, if the underlying closes by Expiry above the CE Long leg but

OTM then its Premium will become zero on Expiry). However, if the PE buy leg becomes an ITM on Expiry, then its final LTP will determine the profit on the PE buy primary leg (*i.e. if the final LTP is higher than its buying price*).

So far as the PE Short hedged leg is concerned, if the underlying does not breach the Breakeven Strike profit is generated on the hedged leg.

Thus, on such limited bearish move, both the primary leg and the hedged leg generates profit, and the max profit (*which can be pre-calculated, as explained above*) would be generated on this Strategy if the underlying closes by Expiry just near the PE Short leg on the downside.

If movement of the underlying is slow / sideways:

However, if the movement of the underlying becomes slow / sluggish in its downward movement or if the underlying keeps fluctuating in a range, then the Theta impact may cause erosion in the Premium value of both PE Long and PE Short leg. However, since this Strategy is a Net Premium Credit strategy (*owing to the fact that there are more PE Shorts than PE Long and Short Strike is farther OTM than the Long Strike*), the Net Premium Credited would be the maximum profit in such situation by Expiry if the underlying closes by Expiry above the PE Long leg (*in which situation both Long & Short Strike PEs would expire as OTM*). However, if the underlying closes by Expiry below the PE Long leg but higher than the PE Short leg, then some higher

lower than the CE Short leg, then some higher profit would be generated on this Strategy (*as CE Long Strike in such situation would expire as an ITM*).

If trade reverses for a downtrend:

If the underlying reverses in a downtrend instead of a limited bullish upmove as anticipated, then this Strategy will automatically cover the bearish move from any loss, because there are already more CE Shorts than CE Long and the Strategy is a Net Credit Strategy. Therefore, upon reversal on the downtrend, the Net Premium Credit in this Strategy will be the maximum profit from Expiry perspective and will not require any adjustments to be made to the existing Strategy.

If trade does not go as per plan:

However, if the underlying moves higher than the Breakeven Strike of the CE Short leg then the Strategy may generate loss (*after setting-off the profit generated on the CE buy primary leg*). In such scenario, certain adjustments may be required to be made (*as discussed below here*).

Adjustments (if limited bullish view and this Strategy does not go as per plan):

If the underlying moves higher than the Breakeven Strike on the CE side, then this Strategy enters towards an unlimited loss scenario, because, then it implies that both CE buy and CE Short leg have become an ITM. In such a scenario, the Long CE will cover the losses arising on the CE Short leg to some extent as the underlying moves higher, but that will

profit would be generated on this Strategy (*as PE Long Strike in such situation would expire as an ITM*).

If trade reverses for an uptrend:

If the underlying reverses in an uptrend instead of a limited bearish downward move as anticipated, then this Strategy will automatically cover the bullish move from any loss, because there are already more PE Shorts than PE Long and the Strategy is a Net Credit Strategy. Therefore, upon reversal on the upside, the Net Premium Credit in this Strategy will be the maximum profit from Expiry perspective and will not require any adjustments to be made to the existing Strategy.

If trade does not go as per plan:

However, if the underlying moves lower than the Breakeven Strike of the PE Short leg then the Strategy may generate loss (*after setting-off the profit generated on the PE buy primary leg*). In such scenario, certain adjustments may be required to be made (*as discussed below here*).

Adjustments (if limited bearish view and this Strategy does not go as per plan):

If the underlying moves lower than the Breakeven Strike on the PE side, then this Strategy enters towards an unlimited loss scenario, because, then it implies that both PE buy and PE Short leg have become an ITM. In such a scenario, the Long PE will cover the losses arising on the PE Short leg to some extent as the underlying moves lower, but that will not

not be sufficient to cover the losses that will be incurred on the CE Short leg as there are more CE Shorts than CE buy in this Strategy. Thus, from Expiry perspective the loss incurred on the CE Short leg on Expiry minus the profit on the CE buy leg, would be the actual loss on Expiry (*calculated basis their final LTP on Expiry*). In this situation, certain adjustments can be made in order to curtail the potential loss scenario in this Strategy.

The following adjustments can be considered to cover up for the potential loss that may occur in this Strategy: (i) Long CEs; or (ii) Short PEs. These adjustments are discussed below.

- (i) Counter Adjustment through Long Option: If there seems to be a trending uptrend with momentum, then **CEs can be bought** (Long CE). Buying CEs to protect the upside risk in this Strategy will add up another debit position, therefore this CE Long should only be prudent to initiate only if there is strong momentum for the upward direction. This Long CE will help overcome the loss accruing on this Strategy arising due to more CE Shorts. However, Long CEs should be initiated at Strike having Delta value higher than the current Delta value of the Short CE hedged leg (*i.e. at a lower Strike than the CE sell Strike*), so that in case of continuation of strong uptrend, these fresh Long CEs should generate more profit than the loss generated by the Short CEs hedged

be sufficient to cover the losses that will be incurred on the PE Short leg as there are more PE Shorts than PE buy in this Strategy. Thus, from Expiry perspective the loss incurred on the PE Short leg on Expiry minus the profit on the PE buy leg, would be the actual loss on Expiry (*calculated basis their final LTP on Expiry*). In this situation, certain adjustments can be made in order to curtail the potential loss scenario in this Strategy.

The following adjustments can be considered to cover up for the potential loss that may occur in this Strategy: (i) Long PEs; or (ii) Short CEs. These adjustments are discussed below.

- (i) Counter Adjustment through Long Option: If there seems to be a trending downtrend with momentum, then **PEs can be bought** (Long PE). Buying PEs to protect the downside risk in this Strategy will add up another debit position, therefore this PE Long should only be prudent to initiate only if there is strong momentum for the downward direction. This Long PE will help overcome the loss accruing on this Strategy arising due to more PE Shorts. However, Long PEs should be initiated at Strike having Delta value higher than the current Delta value of the Short PE hedged leg (*i.e. at a higher Strike than the PE sell Strike*), so that in case of continuation of strong downtrend, these fresh Long PEs should generate more profit than the loss generated by the Short PEs hedged leg. Also, depending upon the likely

leg. Also, depending upon the likely uptrend momentum, suitable number of Long CEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy i.e. by ensuring that the net Delta position gets sufficiently net positive on the overall Strategy to benefit from the bullish move in the underlying. Atleast fresh Long CEs equal to extra Lot on CE Short leg must be added. These fresh Long CEs at higher Delta would turn the CE Ratio into a Bull CE Spread. If the Long CEs generates profit covering up the loss generated by the CE Short leg, then it would be advisable to immediately book the profit on the Strategy.

- (ii) Counter Adjustment through Short Option: If the uptrend is expected to be continue but not with very strong momentum (and may be expected to even reverse downwardly), then **Far OTM PEs can be sold** (PE Short) below the major Support area of the underlying, which is expected not to be breached by the underlying by Expiry in case of a downtrend move. Idea in this adjustment is to pick up suitable Far OTM PEs for Shorting, such that this far OTM PEs expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This PE Short will help cover the loss generated on the original Strategy, if the

downtrend momentum, suitable number of Long PEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy i.e. by ensuring that the net Delta position gets sufficiently net negative on the overall Strategy to benefit from the bearish move in the underlying. Atleast fresh Long PEs equal to extra Lot on PE Short leg must be added. These fresh Long PEs at higher Delta would turn the PE Ratio into a Bear PE Spread. If the Long PEs generates profit covering up the loss generated by the PE Short leg, then it would be advisable to immediately book the profit on the Strategy.

- (ii) Counter Adjustment through Short Option: If the downtrend is expected to be continued but not with very strong momentum (and may be expected to even reverse upwardly), then **Far OTM CEs can be sold** (CE Short) above the major Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry in case of an uptrend move. Idea in this adjustment is to pick up suitable Far OTM CEs for Shorting, such that this Far OTM CEs expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This CE Short will help cover the loss generated on the original Strategy, if the underlying expires below the Strike at which PE Short is initiated in the hedged

underlying expires above the Strike at which CE Short is initiated in the hedged leg. Further, depending upon the potential loss that may be incurred in the original Strategy if the underlying expires above the Breakeven Strike of the Strategy, suitable number of Far OTM PEs (of lower Far OTM Strike below Support area) can be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these Short PEs due to time decay on Expiry. Generally, atleast 4 to 8 times more Lot quantity may be required to be added to Short PE in comparison to the original number of extra Lots in the CE Short hedged leg initiated on the original Strategy i.e. by ensuring that the net Delta position gets sufficiently net positive on the overall Strategy to benefit from the bullish move in the underlying. However, selling additional PEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.	leg. Further, depending upon the potential loss that may be incurred in the original Strategy if the underlying expires below the Breakeven Strike of the Strategy, suitable number of Far OTM CEs (of higher Far OTM Strike above Resistance area) can be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these Short CEs due to time decay on Expiry. Generally, atleast 4 to 8 times more Lot quantity may be required to be added to Short CE in comparison to the original number of extra Lots in the PE Short hedged leg initiated on the original Strategy i.e. by ensuring that the net Delta position gets sufficiently net negative on the overall Strategy to benefit from the bearish move in the underlying. However, selling additional CEs will require higher margin / capital to Short CEs and MTM requirements will also have to be met.
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CALL CALENDAR SPREAD & PUT CALENDAR SPREAD

Rangebound-to-Mild Bullish and **Rangebound-to-Mild Bearish** view can be played through Calendar Spreads. When the Long Option and the Short Option in a Spread Strategy, are initiated on different Expiry series, then such Spreads are called **Calendar Spreads** (also called as **Time Spreads** or **Horizontal Spreads**). Mostly, Calendar Spread Strategy consists of: Short leg on closer Expiry series and Long leg on farther Expiry series, thus are also referred to as **Long Calendar Spread**. However, a Calendar Spread can also be initiated with Short leg on farther Expiry series and the Long leg on closer Expiry series. Such a Calendar Spread is called as **Reverse Calendar Spread** (also called as **Reverse Time Spreads** or **Reverse Horizontal Spreads**). Such Reverse Calendar Spread is a net Premium credit Strategy, and is therefore a **Short Calendar Spread**.

Further, when the primary leg (Short Option) and the hedged leg (Long Option) in a Call Spread Strategy or Put Spread Strategy, are initiated not only on different Expiry series but also on different Strikes, then such Calendar Spreads are called **Diagonal Spreads**. It is called a Diagonal Spread because it combines features of a Horizontal (Calendar) Spread and a Vertical Spread¹⁵.

Here, we are going to discuss about the Calendar Spread. The Calendar Spread can be made on Call side as well as on Put side, depending upon the view on the movement in the underlying. Let us get an overview on the Call side and Put side of this Calendar Spread.

Call side Calendar Spread:

When the view on the underlying is sideways-to-mild bullish, we can play the limited uptrend / rangebound movement in the underlying through Long Calendar Spread Strategy on the CE side:

- Shorting ATM / OTM Call Options of a closer Expiry Series (the **primary leg**); and

¹⁵ Vertical Spread involves two same side Options of same Expiry series on different Strikes.

- initiating a Long CE on same Strike ATM /OTM position of a farther Expiry Series (the **hedged leg**).

In this Spread, we are calling the CE Short leg as the primary leg, as we expect the CE Short leg of the Strategy to primarily generate profit due to erosion in its Premium value; and the expectation from the CE Long leg is to yield profit from a straight mild-bullish move in the underlying (besides covering for any losses that may occur on the CE Short leg, if the underlying gets super-bullish).

Further, in this Call side Calendar Spread, the CE Short leg is on closer Expiry series and the CE Long leg is on farther Expiry series, therefore, this Long Calendar Spread is a net Premium debit Strategy. Also, the primary leg and the hedged leg have the same number of Lots (*i.e. the quantity is in the ratio of 1:1 in terms of Lots/ quantity*), on the same underlying but on different Expiry series and at same ATM / OTM Strike. Thus, overall this Strategy is a **Call Calendar Spread (Long) Strategy**.¹⁶

Put side Calendar Spread:

Likewise, when the view on the underlying is sideways-to-mild bearish, we can play the limited downtrend / rangebound movement in the underlying through Long Calendar Spread Strategy on the PE side:

- Shorting ATM / OTM Put Options of a closer Expiry Series (the **primary leg**); and
- initiating a Long PE on same Strike ATM /OTM position of a farther Expiry Series (the **hedged leg**).

In this Spread, we are calling the PE Short leg as the primary leg, as we expect the PE Short leg of the Strategy to primarily generate profit due to erosion in its Premium value; and the expectation from the PE Long leg is to yield profit

¹⁶ A Reverse Calendar Spread Strategy (as a Short Spread) on the CE side can be initiated for a rangebound-to-mild bearish view on the underlying, in which CE Short leg is initiated on ATM Strike of farther Expiry series and CE Long is initiated on ATM Strike of closer Expiry series. This Strategy is called as **Reverse Call Calendar Spread** or **Call Calendar Spread (Short) Strategy**.

from a straight mild-bearish move in the underlying (besides covering for any losses that may occur on the PE Short leg, if the underlying gets super-bearish).

Further in this Put Calendar Spread, PE Short leg is on closer Expiry series and the PE Long leg is on farther Expiry series, therefore, this Long Calendar Spread is a net Premium debit Strategy. Further, the primary leg and the hedged leg have the same number of Lots (*i.e. the quantity is in the ratio of 1:1 in terms of Lots/ quantity*), on the same underlying but on different Expiry series and at ATM Strike. Thus, overall this Strategy is a **Put Calendar Spread (Long) Strategy**.¹⁷

With this background, now let us delve into discussing the Call Calendar (Long) Spread Strategy and Put Calendar (Long) Spread Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Call Calendar (Long) Spread Strategy	Put Calendar (Long) Spread Strategy
Trade legs: • Short CE ATM of closer Expiry series (<i>primary leg</i>); and • Long CE ATM of farther Expiry series (<i>hedged leg</i>) Equal number of Lots in primary and hedged leg. CE Long leg being on farther Expiry series will have more Premium than the closer Expiry series CE Short, thus making it a Net Debit Strategy.	Trade legs: • Short PE ATM of closer Expiry series (<i>primary leg</i>); and • Long PE ATM of farther Expiry series (<i>hedged leg</i>) Equal number of Lots in primary and hedged leg. PE Long leg being on farther Expiry series will have more Premium than the closer Expiry series PE Short, thus making it a Net Debit Strategy.

¹⁷ A Reverse Calendar Spread Strategy (as a Short Spread) on the PE side can be initiated for a rangebound-to-mild bullish view on the underlying, in which PE Short leg is initiated on ATM Strike of farther Expiry series and PE Long is initiated on ATM Strike of closer Expiry series. This Strategy is called as **Reverse Put Calendar Spread** or **Put Calendar Spread (Short) Strategy**.

Example: • Nifty 1 Lot Short CE ATM 17000 (<i>at a premium of Rs. 200 per Lot</i>) Current Month Expiry • Nifty 1 Lot Long CE ATM 17000 (<i>at a premium of Rs. 300 per Lot</i>) of Next Month Expiry <i>Net premium debit incurred = premium paid – premium credit received = 300–200 = 100 per Lot.</i>	Example: • Nifty 1 Lot Short PE ATM 17000 (<i>at a premium of Rs. 200 per Lot</i>) Current Month Expiry • Nifty 1 Lot Long PE ATM 17000 (<i>at a premium of Rs. 300 per Lot</i>) of Next Month Expiry <i>Net premium debit incurred = premium paid – premium credit received = 300–200 = 100 per Lot.</i>
Objective: Objective is to play rangebound to mild bullish view through Shorting ATM CEs of near Expiry as the primary leg; and buying ATM CEs of farther Expiry series as the hedged leg. Same Strike CE of farther Expiry series will have more Premium than the closer Expiry series, but a farther Expiry series will have lower Theta than the same Strike on closer Expiry series. In this Strategy profit is targeted mainly on the CE Short primary leg (<i>which on higher Theta due to closer Expiry</i>), which will generate profit due to faster erosion in Time Value (than CE Long leg) due to mild bullish or rangebound movement in the underlying. This would be because CE Short leg has a closer Expiry than CE Long leg. This Strategy is played uptill the Expiry of the CE Short leg position (<i>which is on closer Expiry series than the CE Long</i>) in this Strategy. It is a limited reward and limited risk Strategy.	Objective: Objective is to play rangebound to mild bearish view through Shorting ATM PEs of near Expiry as the primary leg; and buying ATM PEs of farther Expiry series as the hedged leg. Same Strike PE of farther Expiry series will have more Premium than the closer Expiry series, but a farther Expiry series will have lower Theta than the same Strike on closer Expiry series. In this Strategy profit is targeted mainly on the PE Short primary leg (<i>which on higher Theta due to closer Expiry</i>), which will generate profit due to faster erosion in Time Value (than PE Long leg) due to mild bearish or rangebound movement in the underlying. This would be because PE Short leg has a closer Expiry than PE Long leg. This Strategy is played uptill the Expiry of the PE Short leg position (<i>which is on closer Expiry series than the PE Long</i>) in this Strategy. It is a limited reward and limited risk Strategy.

<u>Demerits:</u> • This Spread strategy will be suitable for a mild sideways-to-mild bullish move of the underlying. Extreme bullish or bearish move in the underlying may cause loss on the Strategy. • If the bullish move catches strong momentum, then the primary Short leg will start giving loss if the underlying crosses above the tentative Breakeven Strike of the CE Short hedged leg. In case of both strong bullish move in the underlying or extreme rise in Volatility, the CE Short will generate more loss than the profit generated on the CE Long leg. • In case the trend becomes strongly bullish, then the CE Short leg would start yielding MTM loss, thus requiring more capital to provide for MTM losses. • It is a Net Debit strategy i.e. Long CE leg has more premium debit incurred than the premium credit received on the CE Short leg (<i>because it is on the closer Expiry</i>). Thus, in case of extreme Volatility crash or strong bearish move in the underlying, the max loss to the extent of Net Premium debit paid on the Strategy, may be incurred. • It is a limited reward Strategy.	<u>Demerits:</u> • This Spread strategy will be suitable for a sideways-to-mild bearish move of the underlying. Extreme bearish or bullish move in the underlying may cause loss on the Strategy. • If the bearish move catches strong momentum, then the primary Short leg will start giving loss if the underlying crosses below the tentative Breakeven Strike of the PE Short hedged leg. In case of both strong bearish move in the underlying or extreme rise in Volatility, the PE Short will generate more loss than the profit generated on the PE Long leg. • In case the trend becomes strongly bearish, then the PE Short leg would start yielding MTM loss, thus requiring more capital to provide for MTM losses. • It is a Net Debit strategy i.e. Long PE leg has more premium debit incurred than the premium credit received on the PE Short leg (<i>because it is on the closer Expiry</i>). Thus, in case of extreme Volatility crash or strong bullish move in the underlying, the max loss to the extent of Net Premium debit paid on the Strategy, may be incurred. • It is a limited reward Strategy.
<u>Benefits CE Calendar Spread:</u> • This Strategy requires low margin / capital.	<u>Benefits of PE Calendar Spread:</u> • This Strategy requires low margin / capital.

• This is a very suitable Strategy for a sideways-to-mild bullish trend. This Strategy is played to benefit from faster Theta decay on CE Short leg than CE Long leg. • The risk is limited to the extent of Net Premium paid on the Strategy, i.e. Max Loss is limited on the downside risk. • If the underlying remains rangebound, then in this Strategy, the CE Short primary leg (<i>which on higher Theta due to closer Expiry</i>), will generate profit due to faster erosion in Time Value (than CE Long leg) due to rangebound movement in the underlying. • If there occurs any limited bullish move in the underlying, then also this Strategy generates profit, because CE Long leg would become an ITM generating profit with relatively less erosion in its Time Value; whereas, the CE Short primary leg, even if it becomes an ITM, would speedily loose substantial portion of its Time Value as its Expiry approach closer. Thus, the Strategy would be profitable in this scenario of mild bullish move in the underlying. • If there is a bearish move in the underlying, then too this Strategy would likely be profitable because CE Short leg would lose its premium by its Expiry, but the CE Long would have some premium left on the Expiry day of the CE Short leg.	• This is a very suitable Strategy for a sideways-to-mild bearish trend. This Strategy is played to benefit from faster Theta decay on PE Short leg than PE Long leg. • The risk is limited to the extent of Net Premium paid on the Strategy, i.e. Max Loss is limited on the upside risk. • If the underlying remains rangebound, then in this Strategy, the PE Short primary leg (<i>which on higher Theta due to closer Expiry</i>), will generate profit due to faster erosion in Time Value (than PE Long leg) due to rangebound movement in the underlying. • If there occurs any limited bearish move in the underlying, then also this Strategy generates profit, because PE Long leg would become an ITM generating profit with relatively less erosion in its Time Value; whereas, the PE Short primary leg, even if it becomes an ITM, would speedily loose substantial portion of its Time Value as its Expiry approach closer. Thus, the Strategy would be profitable in this scenario of mild bearish move in the underlying. • If there is a bullish move in the underlying, then too this Strategy would likely be profitable because PE Short leg would lose its premium by its Expiry, but the PE Long would have some premium left on the Expiry day of the PE Short leg.
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• Thus, we get a range in this Strategy, within which if the underlying closes on Expiry, then the Strategy yield profit. This makes it akin to Short Straddle (<i>except that Calendar Spread is a Net Premium Debit Strategy with limited loss on either side, whereas Short Straddle is a Net Premium Credit Strategy with unlimited risk on either side</i>).	• Thus, we get a range in this Strategy, within which if the underlying closes on Expiry, then the Strategy yield profit. This makes it akin to Short Straddle (<i>except that Calendar Spread is a Net Premium Debit Strategy with limited loss on either side, whereas Short Straddle is a Net Premium Credit Strategy with unlimited risk on either side</i>).
<u>Breakeven Strike of this Strategy from Expiry perspective:</u> The Breakeven of Calendar Spreads cannot be ascertained accurately (<i>as Long leg's premium value cannot be precisely ascertained on the Expiry of the Short leg, besides the impact of volatility situation prevailing at that time</i>). However, we can deploy with Strategy with a tentative idea about the Breakeven, as discussed below. This Strategy has an upside BE Strike and a downside BE Strike. These BE Strikes can be tentatively determined applying the following logic: • The BE Level for the CE Short leg, would be: CE Short Strike + Premium Credit of CE Short leg. Thus, if the underlying reaches upto this BE Strike level of CE Short leg, then CE Long leg (<i>being on the same Strike</i>) would also rise by about same points equivalent to the Premium Credit of the CE Short leg. Thus, effectively, on the upside the loss from Expiry perspective would not happen at the CE Short leg's BE Strike, but slightly more than twice the	<u>Breakeven Strike of this Strategy from Expiry perspective:</u> The Breakeven of Calendar Spreads cannot be ascertained accurately (<i>as Long leg's premium value cannot be precisely ascertained on the Expiry of the Short leg, besides the impact of volatility situation prevailing at that time</i>). However, we can deploy with Strategy with a tentative idea about the Breakeven, as discussed below. This Strategy has an upside BE Strike and a downside BE Strike. These BE Strikes can be tentatively determined applying the following logic: • The BE Level for the PE Short leg, would be: PE Short Strike – Premium Credit of PE Short leg. Thus, if the underlying reaches upto this BE Strike level of PE Short leg on the downside, then PE Long leg (<i>being on the same Strike</i>) would also rise by about same points equivalent to the Premium Credit of the PE Short leg. Thus, effectively, on the downside the loss from Expiry perspective would not happen at the PE Short leg's BE Strike, but slightly more than twice the Premium Credit

Premium Credit collected on the Short leg. Therefore, the BE Strike on the upper side of the Strategy can be tentatively calculated with the following formula:

BE Strike on the upside for this Strategy = CE Short Strike + (2 x Premium Credit of the CE Short)

Actual BE Strike on the upper side should be higher than that as determined from the above formula, because the CE Long leg would generate more profit (*i.e. greater than the Premium Credit collected on the CE Short if the underlying reaches upto the BE Strike of the CE Short leg, as CE Long leg is on higher Expiry and hence experiencing higher Delta advantage and lower Theta impact*). However, Volatility squeeze can cut down this extra cushion to the formation of BE Strike Level on the upper side for this Strategy.

- If the underlying takes a downward move, then the CE Short leg would cover the loss to the maximum extent of the Premium Credit collected on the CE Short leg, from Expiry perspective. So, we can say that the BE Strike of the Strategy on the downside can be atleast: CE Short Strike – Premium Credit of CE Short leg. Therefore, the BE Strike on the lower side of the Strategy can be tentatively calculated with the following formula:

collected on the Short leg. Therefore, the BE Strike on the lower side of the Strategy can be tentatively calculated with the following formula:

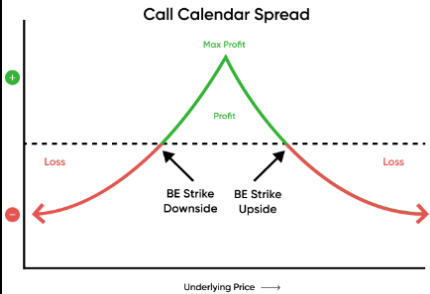
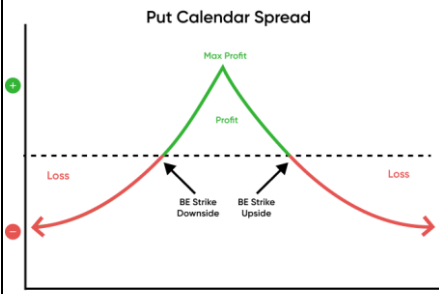
BE Strike on the downside for this Strategy = PE Short Strike – (2 x Premium Credit of the PE Short)

Actual BE Strike on the lower side should be higher than that as determined from the above formula, because the PE Long leg would generate more profit (*i.e. greater than the Premium Credit collected on the PE Short if the underlying reaches upto the BE Strike of the PE Short leg, as PE Long leg is on higher Expiry and hence experiencing higher Delta advantage and lower Theta impact*). However, Volatility squeeze can cut down this extra cushion to the formation of BE Strike Level on the lower side for this Strategy.

- If the underlying takes an upward move, then the PE Short leg would cover the loss to the maximum extent of the Premium Credit collected on the PE Short leg, from Expiry perspective. So, we can say that the BE Strike of the Strategy on the upside can be atleast: PE Short Strike + Premium Credit of PE Short leg. Therefore, the BE Strike on the upper side of the Strategy can be tentatively calculated with the following formula:

BE Strike on the upside for this Strategy = [PE Short Strike + Premium Credit of the PE Short]

BE Strike on the downside for this Strategy = [CE Short Strike – Premium Credit of the CE Short] Actual BE Strike on the lower side may get even smaller than that as determined from the above formula, because the CE Long leg may generate more loss (<i>as CE Long leg may be on a higher positive Delta by virtue of being on higher Expiry</i>). Further, Volatility squeeze may slightly reduce the BE Strike Level on the lower side for this Strategy. Thus, basis the aforesaid discussions and logic, we can conclude that we can tentatively determine the upper and lower BE Strike level for this Calendar Spread Strategy, applying the following formula: • BE Strike on the upside for this Strategy = CE Short Strike + (2 x Premium Credit of the CE Short) • BE Strike on the downside for this Strategy = CE Short Strike – Premium Credit of the CE Short. Therefore, from Expiry perspective (<i>i.e. Expiry of the CE Short leg, which is on closer Expiry than CE Long</i>), if the underlying closes between the upside BE Strike and the downside BE Strike, then this Strategy would yield profit. In the aforesaid example, where the trade legs of the Strategy are: • Nifty 1 Lot Short CE ATM 17000 (<i>at a premium of Rs. 200 per Lot</i>) Current Month Expiry	Actual BE Strike on the upper side may get even smaller than that as determined from the above formula, because the PE Long leg may generate more loss (<i>as PE Long leg may be on a higher negative Delta by virtue of being on higher Expiry</i>). Further, Volatility squeeze may slightly reduce the BE Strike Level on the upper side for this Strategy. Therefore, basis the aforesaid discussions and logic, we can conclude that we can tentatively determine the upper and lower BE Strike level for this Calendar Spread Strategy, applying the following formula: • BE Strike on the downside for this Strategy = PE Short Strike – (2 x Premium Credit of the PE Short) • BE Strike on the upside for this Strategy = PE Short Strike + Premium Credit of the PE Short. Thus, from Expiry perspective (<i>i.e. Expiry of the PE Short leg, which is on closer Expiry than PE Long</i>), if the underlying closes between the upside BE Strike and the downside BE Strike, then this Strategy would yield profit. In the aforesaid example, where the trade legs of the Strategy are: • Nifty 1 Lot Short PE ATM 17000 (<i>at a premium of Rs. 200 per Lot</i>) Current Month Expiry • Nifty 1 Lot long PE ATM 17000 (<i>at a premium of Rs. 300 per Lot</i>) of Next Month Expiry
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• Nifty 1 Lot long CE ATM 17000 (at a premium of Rs. 300 per Lot) of Next Month Expiry Then, BE Strike of the Strategy on the upside would be atleast: $17000 + (2 \times 200) = 17400$ CE; and BE Strike of the Strategy on the downside would be approx.: $17000 - 200 = 16800$ CE.	Then, BE Strike of the Strategy on the downside would be approx.: $17000 - 200 = 16700$ PE; and BE Strike of the Strategy on the upside would be: $17000 + 200 = 17200$ PE.
<u>Payoff for Call Calendar Spread:</u> 	<u>Payoff for Put Calendar Spread:</u> 
<u>Loss in this Strategy from Expiry perspective:</u> <u>Max Loss on the Strategy:</u> Net Premium incurred in the Strategy (<i>i.e. the difference between the: premium credit received on the primary leg and the premium paid on the hedged leg</i>), is the Maximum Loss that may be incurred in this Strategy when the underlying closes by Expiry beyond the Breakeven Strikes (<i>on either side</i>). In the aforesaid example, where the trade legs of the Strategy are: • Nifty 1 Lot Short CE ATM 17000 (at a premium of Rs. 200 per Lot) Current Month Expiry	<u>Loss in this Strategy from Expiry perspective:</u> <u>Max Loss on the Strategy:</u> Net Premium incurred in the Strategy (<i>i.e. the difference between the: premium credit received on the primary leg and the premium paid on the hedged leg</i>), is the Maximum Loss that may be incurred in this Strategy when the underlying closes by Expiry beyond the Breakeven Strikes (<i>on either side</i>). In the aforesaid example, where the trade legs of the Strategy are: • Nifty 1 Lot Short PE ATM 17000 (at a premium of Rs. 200 per Lot) Current Month Expiry

• Nifty 1 Lot long CE ATM 17000 (at a premium of Rs. 300 per Lot) of Next Month Expiry <i>Net premium debit incurred = premium paid – premium credit received = 300–200 = 100 per Lot.</i> Thus, Max Loss in this Strategy, on Expiry of the CE Short leg, would be Rs. 100 per quantity (<i>i.e. for Nifty Rs. 100 x 50 = Rs. 5000 per Lot</i>) when the underlying closes by Expiry beyond the Breakeven Strikes (<i>on either side</i>).	• Nifty 1 Lot long PE ATM 17000 (at a premium of Rs. 300 per Lot) of Next Month Expiry <i>Net premium debit incurred = premium paid – premium credit received = 300–200 = 100 per Lot.</i> Thus, Max Loss in this Strategy, on Expiry of the PE Short leg, would be Rs. 100 per quantity (<i>i.e. for Nifty Rs. 100 x 50 = Rs. 5000 per Lot</i>) when the underlying closes by Expiry beyond the Breakeven Strikes (<i>on either side</i>).
<u>Profit in this Strategy:</u> <u>Max Profit:</u> Maximum profit is generated in this Strategy when the underlying closes by Expiry at (or near) the CE Short Strike. Thus, if on Expiry, the underlying closes at (or near) the CE Short Strike, then the Short Strike position will expire as an ATM / OTM yielding complete Premium Credit of the CE Short leg as profit. At the same time, while even the CE Long would also be an ATM / OTM, it will still have sufficient premium value (<i>due to lower Theta decay, as it is of a farther Expiry series and there is ample time in its expiry</i>). Therefore, the profit generated on the Short leg <i>minus</i> the loss of premium on the CE Long leg, would still generate net profit on the Strategy. Thus, we can get a tentative idea about the Max profit. However, a precise Max profit will be difficult to ascertain (<i>because the final premium value of Long leg cannot be precisely ascertained at the expiry of the</i>	<u>Profit in this Strategy:</u> <u>Max Profit:</u> Maximum profit is generated in this Strategy when the underlying closes by Expiry at (or near) the PE Short Strike. Thus, if on Expiry, the underlying closes at (or near) the PE Short Strike, then the Short Strike position will expire as an ATM / OTM yielding complete Premium Credit of the PE Short leg as profit. At the same time, while even the PE Long would also be an ATM / OTM, it will still have sufficient premium value (<i>due to lower Theta decay, as it is of a farther Expiry series and there is ample time in its expiry</i>). Therefore, the profit generated on the Short leg <i>minus</i> the loss of premium on the PE Long leg, would still generate net profit on the Strategy. Thus, we can get a tentative idea about the Max profit. However, a precise Max profit will be difficult to ascertain (<i>because the final premium value of Long leg cannot be precisely ascertained at the expiry of the</i>

Short leg; besides the impact of prevailing volatility on the Long at that time).

Profit Level on overall Strategy:

If the underlying by Expiry closes anywhere between the upside and downside Breakeven Strikes of the Strategy, then this Strategy would yield some profit.

Profit Zone(s) in this Strategy:

There are following two profit zones in this Strategy from Expiry perspective:

- (i) If the underlying by Expiry closes between the downside Breakeven Strike and CE Short Strike, then some profit would be generated on this Strategy. Higher the underlying closes towards CE Short Strike, higher will be the profit generated on this Strategy. If the underlying closes at (or near) the CE Short Strike on Expiry, then limited max profit will be realised on this Strategy. However, if the underlying crosses beyond the BE Strike on the downside, then limited loss may be incurred.
- (ii) If the underlying by Expiry closes between the CE Short Strike and upside Breakeven Strike, then some profit would be generated on this Strategy. Higher the underlying closes towards BE Strike on the upside, lower will be the profit generated on this Strategy. If the underlying closes at (or near) the CE Short Strike on Expiry, then limited max profit will be realised on this Strategy. However, if the underlying crosses

Short leg; besides the impact of prevailing volatility on the Long leg at that time).

Profit Level on overall Strategy:

If the underlying by Expiry closes anywhere between the upside and downside Breakeven Strikes of the Strategy, then this Strategy would yield some profit.

Profit Zone(s) in this Strategy:

There are following two profit zones in this Strategy from Expiry perspective:

- (i) If the underlying by Expiry closes between the downside Breakeven Strike and PE Short Strike, then some profit would be generated on this Strategy. Higher the underlying closes towards PE Short Strike, higher will be the profit generated on this Strategy. If the underlying closes at (or near) the PE Short Strike on Expiry, then limited max profit will be realised on this Strategy. However, if the underlying crosses beyond the BE Strike on the downside, then limited loss may be incurred.
- (ii) If the underlying by Expiry closes between the PE Short Strike and upside Breakeven Strike, then some profit would be generated on this Strategy. Higher the underlying closes towards BE Strike on the upside, lower will be the profit generated on this Strategy. If the underlying closes at (or near) the PE Short Strike on Expiry, then limited max profit will be realised on this Strategy. However, if the underlying crosses beyond the BE

beyond the BE Strike on the upside, then limited loss may be incurred on Expiry of the Short leg in this Strategy.	Strike on the upside, then limited loss may be incurred on Expiry of the Short leg in this Strategy.
<u>Options behaviour:</u> • This Strategy is basically adopted to benefit from Theta decay on the CE Short primary leg initiated on closer Expiry series, which has higher Theta decay than the Theta decay on CE Long leg initiated on farther Expiry, even though both CE Short and CE Long are initiated on ATM strikes of respective Expiry series. • Since, intention on this Strategy is to generate profit out of faster Theta decay on CE Short leg, therefore it must be targeted that sufficient premium value credit is received on the CE Short leg. • Higher the Premium credit on Short leg, lower the risk / Max Loss on the Strategy, because the Max Loss would be the Net premium Debit incurred on the overall Strategy. • This Strategy is designed for a rangebound underlying to mild bullish move in the underlying, such that the underlying is not expected to breach the Breakeven Strike(s) of the Strategy, to reap Profit on the Strategy. • In case of mild bullish move of the underlying, the primary leg generates profit due to erosion in its Time Value with approaching	<u>Options behaviour:</u> • This Strategy is basically adopted to benefit from Theta decay on the PE Short primary leg initiated on closer Expiry series, which has higher Theta decay than the Theta decay on PE Long leg initiated on farther Expiry, even though both PE Short and PE Long are initiated on ATM strikes of respective Expiry series. • Since, intention on this Strategy is to generate profit out of faster Theta decay on PE Short leg, therefore it must be targeted that sufficient premium value credit is received on the PE Short leg. • Higher the Premium credit on Short leg, lower the risk / Max Loss on the Strategy, because the Max Loss would be the Net premium Debit incurred on the overall Strategy. • This Strategy is designed for a rangebound underlying to mild bearish move in the underlying, such that the underlying is not expected to breach the Breakeven Strike(s) of the Strategy, to reap Profit on the Strategy. • In case of mild bearish move of the underlying, the primary leg generates profit due to erosion in its Time Value with approaching Expiry; and the hedged leg generates

Expiry; and the hedged leg generates profits due to mild bullish move. However, in case of extreme gapup or bullish move beyond the upside Breakeven Strike of the Strategy, both CE short leg and CE Long leg may become an ITM and both would rise in their premium value and the Strategy may yield some loss and may require adjustments to be made. However, in this situation, the CE short leg even if it becomes an ITM, would have some Time Value left (*which may be lost on its Expiry, thus reducing the final premium value of the CE Short Strike*).

- However, if the underlying falls down heavily (*or makes a huge gapdown*), then in such extreme bearish situation, when the underlying would close by Expiry crossing below the downside BE Strike, this Strategy can yield a limited max loss upto a maximum extent of the Net Premium Debit incurred on the overall Strategy.
- Slight rise in Volatility may not adversely impact this Strategy, as slight rise in Volatility would be favourable to the CE Long leg. Further, slight rise in Volatility may adversely impact the CE Short leg, however, if the underlying by Expiry remains between the Breakeven Strike(s) of the Strategy then CE Short leg would also generate some profit due to erosion in its Time Value by its Expiry (*thereby nullifying the adverse impact of rise in its premium value due to*

profits due to mild bearish move. However, in case of extreme gapdown or bearish move below the downside Breakeven Strike of the Strategy, both PE short leg and PE Long leg may become an ITM and both would rise in their premium value and the Strategy may yield some loss and may require adjustments to be made. However, in this situation, the PE short leg even if it becomes an ITM, would have some Time Value left *which may be lost on its Expiry, thus reducing the final premium value of the PE Short Strike*).

- However, if the underlying rises up swiftly (*or makes a huge gapup*), then in such extreme bullish situation, when the underlying would close by Expiry crossing above the upside BE Strike, this Strategy can yield a limited max loss upto a maximum extent of the Net Premium Debit incurred on the overall Strategy.
- Slight rise in Volatility may not adversely impact this Strategy, as slight rise in Volatility would be favourable to the PE Long leg. Further, slight rise in Volatility may adversely impact the PE Short leg, however, if the underlying by Expiry remains between the Breakeven Strike(s) of the Strategy then PE Short leg would also generate some profit due to erosion in its Time Value by its Expiry (*thereby nullifying the adverse impact of rise in its premium value due to slight rise in*

<i>slight rise in Volatility</i>) as it becomes zero when it expires as an OTM). Falling state of Volatility may be favourable to this Strategy, as the drop in Volatility will erode the Premium value of both the primary leg and the hedged leg. However, the fall in Volatility is likely to eventually cause more drop in the Premium of the primary Short leg than the hedged Long leg, as the fall in Volatility will get a further impetus by the higher Theta impact on the primary Short leg.	<i>Volatility</i>) as it becomes zero when it expires as an OTM. Falling state of Volatility may be favourable to this Strategy, as the drop in Volatility will erode the Premium value of both the primary leg and the hedged leg. However, the fall in Volatility is likely to eventually cause more drop in the Premium of the primary Short leg than the hedged Long leg, as the fall in Volatility will get a further impetus by the higher Theta impact on the primary Short leg.
<u>If trade goes as per plan and underlying remains rangebound:</u> If the movement of the underlying remains sluggish and rangebound, then the Theta impact would cause erosion in the Premium value of both CE Long and CE Short leg. However, CE Short leg would suffer more from Theta decay/erosion in its Time Value than the CE long leg and thus the Strategy would generate profit on overall basis.	<u>If trade goes as per plan and underlying remains rangebound:</u> If the movement of the underlying remains sluggish and rangebound, then the Theta impact would cause erosion in the Premium value of both PE Long and PE Short leg. However, PE Short leg would suffer more from Theta decay/erosion in its Time Value than the PE long leg and thus the Strategy would generate profit on overall basis.
<u>If trade goes as per plan with limited bullish move:</u> If the underlying remains limited bullish, with underlying being slightly below the upside Breakeven Strike of the Strategy, then the CE Long leg will generate profit due to mild bullish move in the underlying and less erosion in its Time Value by virtue of being on a farther Expiry series. Further, the CE Short leg would also generate profit to the extent of erosion in its Time Value due to expiry Theta effect. Thus, the Strategy would generate profit on overall basis.	<u>If trade goes as per plan with limited bearish move:</u> If the underlying remains limited bearish, with underlying being slightly above the downside Breakeven Strike of the Strategy, then the PE Long leg will generate profit due to mild bearish move in the underlying and less erosion in its Time Value by virtue of being on a farther Expiry series. Further, the PE Short leg would also generate profit to the extent of erosion in its Time Value due to expiry Theta effect. Thus, the Strategy would generate profit on overall basis.

If trade goes as per plan with limited bearish move:

If the underlying remains limited bearish, with underlying closing above the downside Breakeven Strike of the Strategy, then the CE Short will expire as an OTM yielding its entire Premium Credit as profit; but the CE Long leg will generate less loss due to relatively less erosion in its Time Value by virtue of being on a farther Expiry series. Thus, the Strategy would generate profit on overall basis.

If trade does not go as per plan:

- If the underlying gets into extreme downtrend (or huge gapdown), then the CE Short leg will generate profit due to erosion in its premium value, may be to the maximum extent of premium credit received on the CE Short leg. However, the CE Long will generate limited loss to the extent of Premium paid. However, since, the overall Strategy is a Net Premium debit Strategy, therefore, in case of extreme bearish move in the underlying (*crossing below the downside Breakeven Strike of the Strategy*), the overall Strategy may yield Max Loss to the extent of the Net Premium debit incurred on the Strategy. This Max Loss situation may be mitigated by making certain adjustments (*as discussed below here*).
- If the underlying gets into a strong bullish momentum or huge gapup (*as against a limited bullish move as originally expected in the Strategy*), then the hedged leg of CE Long will

If trade goes as per plan with limited bullish move:

If the underlying remains limited bullish, with underlying closing below the upside Breakeven Strike of the Strategy, then the PE Short will expire as an OTM yielding its entire Premium Credit as profit; but the PE Long leg will generate less loss due to relatively less erosion in its Time Value by virtue of being on a farther Expiry series. Thus, the Strategy would generate profit on overall basis.

If trade does not go as per plan:

- If the underlying gets into extreme uptrend (or huge gapup), then the PE Short leg will generate profit due to erosion in its premium value, may be to the maximum extent of premium credit received on the PE Short leg. However, the PE Long will generate limited loss to the extent of Premium paid. However, since, the overall Strategy is a Net Premium debit Strategy, therefore, in case of extreme bullish move in the underlying (*crossing above the upside Breakeven Strike of the Strategy*), the overall Strategy may yield Max Loss to the extent of the Net Premium debit incurred on the Strategy. This Max Loss situation may be mitigated by making certain adjustments (*as discussed below here*).
- If the underlying gets into a strong bearish momentum or huge gapdown (*as against a limited bearish move as originally expected in the Strategy*), then the hedged leg of PE Long will generate profit. But with the underlying falling fast (*crossing*

generate profit. But with the underlying rising fast (<i>crossing above the upside Breakeven Strike of the Strategy</i>), the primary leg comprising of CE Short leg will generate loss and if the strong bullish momentum continues in the underlying, then potential loss that may arise on the Strategy may need to be contained by making certain adjustments (<i>as discussed below here</i>).	<i>below the downside Breakeven Strike of the Strategy</i>), the primary leg comprising of PE Short leg will generate loss and if the strong bearish momentum continues in the underlying, then potential loss that may arise on the Strategy may need to be contained by making certain adjustments (<i>as discussed below here</i>).
<u>Adjustments (if the underlying gets into a downward trend and this Strategy does not go as per plan):</u> This strategy is a Debit Calendar Spread, therefore, the Net Premium (<i>i.e. the difference between the Premium paid on hedged leg and the Premium collected in the primary leg</i>) could be the max loss on the Strategy from Expiry perspective (<i>i.e. expiry of the CE Short leg</i>), in case of a huge gapdown / bearish momentum trend in the underlying. The following adjustments can be considered to cover up for the potential loss that may occur in this Strategy to the max extent of Net Premium debit incurred on the overall Strategy: (i) Short CEs; or (ii) Long PEs. These adjustments are discussed below. (i) <u>Counter Adjustment through Short Option</u>: Far OTM CEs of same Expiry series as that of the hedged leg, above the Resistance level, having an aggregate Premium credit received on these fresh Short CEs equivalent (or more) to the Net Premium paid on the Strategy can be sold (<i>i.e.</i>	<u>Adjustments (if the underlying gets into an upward trend and this Strategy does not go as per plan):</u> This strategy is a Debit Calendar Spread, therefore, the Net Premium (<i>i.e. the difference between the Premium paid on hedged leg and the Premium collected in the primary leg</i>) could be the max loss on the Strategy from Expiry perspective (<i>i.e. expiry of the PE Short leg</i>), in case of a huge gapup / bullish momentum trend in the underlying. The following adjustments can be considered to cover up for the potential loss that may occur in this Strategy to the max extent of Net Premium debit incurred on the overall Strategy: (i) Short PEs; or (ii) Long CEs. These adjustments are discussed below. (i) <u>Counter Adjustment through Short Option</u>: Far OTM PEs of same Expiry series as that of the hedged leg, below the Support level, having an aggregate Premium credit received on these fresh Short PEs equivalent (or more) to the Net Premium paid on the Strategy can be sold (<i>i.e.</i> additional Short

additional Short CEs). Idea in this adjustment is to pick up suitable Far OTM CEs for Shorting, such that this Far OTM CEs expires worthless as an OTM on Expiry (*even if the downtrend again reverses on the bullish side*) thereby giving full Premium at which Short is initiated as profit. The additional CE Shorts can be initiated on such aggregate Premium so as to cover for the Net Premium debit amount on the original Strategy. As these additional CE Short would most likely be executed upon commencement of the downtrend, therefore, these additional CE Shorts would be on lower CE Strikes than original CE Short Strikes. However, if sufficient premium value is not available on the Far OTM CE Shorts of the Current Expiry series (*i.e. same Expiry series as that of the CE Short primary leg*), then these additional CE Shorts may be initiated on Far OTM CEs above a suitable Resistance level, of even Next Week (or even Next-to-Next Week) Expiry series. However, selling additional CEs will require higher margin / capital to Short CEs and MTM requirements will also have to be met.

- (ii) Counter Adjustments through Long PEs: If the downtrend is expected to be trending and continued bearish in the underlying with strong momentum, then it would be advisable to initiate Counter

PEs). Idea in this adjustment is to pick up suitable Far OTM PEs for Shorting, such that this Far OTM PEs expires worthless as an OTM on Expiry (*even if the uptrend again reverses on the bearish side*) thereby giving full Premium at which Short is initiated as profit. The additional PE Shorts can be initiated on such aggregate Premium so as to cover for the Net Premium debit amount on the original Strategy. As these additional PE Short would most likely be executed upon commencement of the uptrend, therefore, these additional PE Shorts would be on higher PE Strikes than original PE Short Strikes. However, if sufficient premium value is not available on the Far OTM PE Shorts of the Current Expiry series (*i.e. same Expiry series as that of the PE Short primary leg*), then these additional PE Shorts may be initiated on Far OTM PEs below a suitable Support level, of even Next Week (or even Next-to-Next Week) Expiry series. However, selling additional PEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.

- (ii) Counter Adjustments through Long CEs: If the uptrend is expected to be trending and continued bullish in the underlying with strong momentum, then it would be advisable to initiate Counter Adjustments through Long CE in Near OTMs (pertaining to Expiry series on

Adjustments through Long PE in Near OTMs (pertaining to Expiry series on which Long CEs are initiated). The number of Long PEs should be such that this PE Long leg must be on higher Delta on aggregate basis than the existing CE Long leg. Initiating such PE Long position will help cover the max loss that may be incurred on the Strategy to the extent of Net Premium debit on the Strategy. However, this PE Long positions must only be added when there is strong conviction of continuation of bearish momentum. Also, instead of naked Long PE positions as Counter Adjustment in this situation, Bear PE Debit Spread can also be initiated. However, even this PE Spread must be executed with such quantity, such that the Net Delta of the Spread must be higher than the Delta of the CE long leg on aggregate basis.

Adjustments (if the underlying gets into super bullish momentum and the limited bullish move in this Strategy does not go as per plan):

The original Call Calendar Spread Strategy is basically adopted to benefit from Theta decay on the Short leg initiated on closer Expiry series. However, if the underlying gets in a strong bullish momentum or makes a huge gapup, then the hedged leg of CE Long will generate profit. But with the underlying rising fast, the primary CE Short leg will generate loss, which if by its Expiry crosses above the Breakeven

which Long PEs are initiated). The number of Long CEs should be such that this CE Long leg must be on higher Delta on aggregate basis than the existing PE Long leg. Initiating such CE Long position will help cover the max loss that may be incurred on the Strategy to the extent of Net Premium debit on the Strategy. However, this CE Long positions must only be added when there is strong conviction of continuation of bullish momentum. Also, instead of naked Long CE positions as Counter Adjustment in this situation, Bull CE Debit Spread can also be initiated. However, even this CE Spread must be executed with such quantity, such that the Net Delta of the Spread must be higher than the Delta of the PE long leg on aggregate basis.

Adjustments (if the underlying gets into super bearish momentum and the limited bearish move in this Strategy does not go as per plan):

The original Put Calendar Spread Strategy is basically adopted to benefit from Theta decay on the Short leg initiated on closer Expiry series. However, if the underlying gets in a strong bearish momentum or makes a huge gapdown, then the hedged leg of PE Long will generate profit. But with the underlying falling fast, the primary PE Short leg will generate loss, which if by its Expiry crosses below the Breakeven Strike of the hedged leg, then the PE Short position will become an ITM. Even though the PE Long may also become an ITM in case of

Strike of the hedged leg, then the CE Short position will become an ITM. Even though the CE Long may also become an ITM in case of such huge bullish momentum in the underlying, but overall the Strategy may yield some loss.

Having said above, the loss situation on the Strategy, which may arise due to a strong momentum bullish move in the underlying can be mitigated by making following adjustments: (i) Long CE; or (ii) Short PE. These adjustments are explained below:

- (i) Counter Adjustment through Long Option: If there seems to be a trending uptrend with momentum, then additional CEs **can be bought** (Long CE) of the same Expiry series as that of the hedged leg (*so as to keep Theta impact relatively lower on these additional CEs than that of the primary CE Short leg*). Buying CEs to protect the upside risk in the hedged leg of this Strategy, will add up another debit position, therefore this CE Long should only be prudent to initiate only if there is strong momentum for the upward direction. This Long CE will help overcome the loss accruing on the Strategy due to super bullish move. However, Long CEs should be initiated at Strike having Delta value higher than the current Delta value of the Short CE leg (i.e. at a lower Strike than the CE sell Strike), so that in case of continuation of strong uptrend, Long CEs should

such huge bearish momentum in the underlying, but overall the Strategy may yield some loss.

Having said above, the loss situation on the Strategy, which may arise due to a strong momentum bearish move in the underlying can be mitigated by making following adjustments: (i) Long PE; or (ii) Short CE. These adjustments are explained below:

- (i) Counter Adjustment through Long Option: If there seems to be a trending downtrend with momentum, then additional PEs **can be bought** (Long PE) of the same Expiry series as that of the hedged leg (*so as to keep Theta impact relatively lower on these additional PEs, than that of the primary PE Short leg*). Buying PEs to protect the downside risk in the hedged leg of this Strategy, will add up another debit position, therefore this PE Long should only be prudent to initiate only if there is strong momentum for the downward direction. This Long PE will help overcome the loss accruing on the Strategy due to super bearish move. However, Long PEs should be initiated at Strike having Delta value higher than the current Delta value of the Short PE leg (i.e. at a higher Strike than the PE sell Strike), so that in case of continuation of strong downtrend, Long PEs should generate more profit than the loss generated by the Short PEs on the primary leg. Also, depending upon the likely downtrend momentum, suitable

generate more profit than the loss generated by the Short CEs on the primary leg. Also, depending upon the likely uptrend momentum, suitable number of Long CEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Suitable number of Long CEs can be added, so as to ensure that the overall Delta position on aggregate basis on the Strategy become positive. If the Long CEs generates profit covering up the loss generated by the CE Short leg, then it would be advisable to immediately book the profit on the Strategy and exit. This Counter Adjustment can also be done by initiating Bull CE Spread Strategy instead of initiating naked Long CEs. But in case of such Bull CE Spread too, it must be ensured that the Delta value of the overall Strategy remains positive so as to generate overall profit on the Strategy due to continued bullish momentum.

- (ii) Counter Adjustment through Short PEs: The loss accruing in the Short leg due to bullish momentum move in the underlying can also be adjusted by Shorting Far OTM PEs, which are below the Support level. Far OTM PEs of same Expiry series as that of the primary CE Short leg, below the Support level, having reasonable Premium credit (*so as to further enhance the Breakeven Strike by adding premium credits on the Strategy*) can be sold. Idea in this adjustment is to pick up a

number of Long PEs can be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Suitable number of Long PEs can be added, so as to ensure that the overall Delta position on aggregate basis on the Strategy become negative. If the Long PEs generates profit covering up the loss generated by the PE Short leg, then it would be advisable to immediately book the profit on the Strategy and exit. This Counter Adjustment can also be done by initiating Bear PE Spread Strategy instead of initiating naked Long PEs. But in case of such Bear PE Spread too, it must be ensured that the Delta value of the overall Strategy remains negative so as to generate overall profit on the Strategy due to continued bearish momentum.

- (ii) Counter Adjustment through Short CEs: The loss accruing in the short leg due to bearish momentum move in the underlying can also be adjusted by Shorting Far OTM CEs, which are above the Resistance level. Far OTM CEs of same Expiry series as that of the primary PE Short leg, above the Resistance level, having reasonable Premium credit (*so as to further enhance the Breakeven Strike by adding premium credits on the Strategy*) can be sold. Idea in this adjustment is to pick up a suitable Far OTM CEs for Shorting, such that this Far OTM CEs expires worthless as an OTM on Expiry (*even if the downtrend again reverses on the*

suitable Far OTM PEs for Shorting, such that this Far OTM PEs expires worthless as an OTM on Expiry (<i>even if the uptrend again reverses on the bearish side</i>) thereby giving full Premium at which PE Short is initiated as profit. If, however, sufficient premium value is not available on the Far OTM PE Shorts of the Current Expiry series (<i>i.e. same as that of the CE Short primary leg</i>), then these PE Shorts may be initiated on Far OTM PEs below the suitable Support level, of even Next Week (or even Next-to-Next Week) Expiry series in order to take the Delta benefit of bullish move. However, selling additional PEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.	<i>bullish side</i>) thereby giving full Premium at which CE Short is initiated as profit. If, however, sufficient premium value is not available on the Far OTM CE Shorts of the Current Expiry series (<i>i.e. same as that of the PE Short primary leg</i>), then these CE Shorts may be initiated on Far OTM CEs above the suitable Resistance level, of even Next Week (or even Next-to-Next Week) Expiry series in order to take the Delta benefit of bearish move. However, selling additional CEs will require higher margin / capital to Short PEs and MTM requirements will also have to be met.
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SHORT STRANGLE & IRON CONDOR

When a view is formed that irrespective of the intermittent directional movement of the underlying, eventually the underlying is expected to remain within a defined range; then such view can be played out by a neutral strategy employing Short Options positions which defines a range within which the underlying is expected to remain by Expiry of those Options.

Thus, when the view on the underlying is that it is expected to remain within a range upto the Expiry of relevant Options, and the same is played out by Shorting Naked Far OTM CE & PE Options pertaining to that Expiry series (*by which the underlying is expected to remain in a range or sideways movement*), then such a Strategy is called **Short Strangle**. In Short Strangle Strategy, Far OTM CE & Far OTM PE are sold in equal quantity, on the same underlying, pertaining to same Expiry series. In this Strategy, the expectation is that the underlying will remain, until the Expiry of the Options Shorted, between the Strike levels where the Shorts have been initiated. Short Strangle involves naked Short positions on CE & PE Options (involving two legs only). This Strategy generates Limited Profit, but may also generate Unlimited Loss if the range is breached by the underlying.

However, when the Short Strangle (naked Strategy) is hedged with Long Options on even Far OTM Strikes (*than the Strikes at which Short has been or intended to be initiated as part of Short Strangle Strategy*), then such Strategy is called **Iron Condor**. In Iron Condor Strategy, there is (i) Far OTM CE Short (**CE primary leg**) and even Far OTM CE Long (**CE hedged leg**), in equal quantity, on the same underlying pertaining to same Expiry series; and (ii) Far OTM PE Short (**PE primary leg**) and even Far OTM PE Long (**PE hedged leg**), in equal quantity, on the same underlying pertaining to same Expiry series. In essence, Iron Condor is pairing of Bear Call Credit Strategy and Bull Put Credit Strategy; and in aggregate involves 4 legs. Like in Short Strangle, in Iron Condor too, the expectation is that the underlying will remain, until the Expiry of the Options Shorted, between the Strike levels where the Shorts have been initiated; however hedged legs are added to the both the Short legs of Short Strangle in order to ensure that:

- (i) if the underlying happens to slip upwardly beyond the Strike at which CE Short is initiated, by Expiry of the CE Options Shorted, then the CE hedged leg will cover up for the losses (to some extent) that may be incurred on the CE primary leg, thereby converting the unlimited Max Loss situation of Short Strangle into Limited Max Loss in Iron Condor; and
- (ii) if the underlying happens to slip downwardly beyond the Strike at which PE Short is initiated, by Expiry of the PE Options Shorted, then the PE hedged leg will cover up for the losses (to some extent) that may be incurred on the PE primary leg, thereby converting the unlimited Max Loss situation of Short Strangle into Limited Max Loss in Iron Condor.

Thus, Iron Condor is a Strategy which generates Limited Profit, but also has limited risk (as it will generate Limited Max Loss, if the range is breached by the underlying).

With this background, now let us delve into discussing the Short Strangle Strategy and Iron Condor Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Short Strangle Strategy	Iron Condor Strategy
Trade Legs: • Short CE of Far OTM Strike (<i>primary CE leg</i>); and • Short PE of Far OTM Strike (<i>primary PE leg</i>) Equal number of Lots in both primary legs; and both Short legs must be of same Expiry series. Further, CE Short and PE Short must be of nearly same Premium value.	Trade Legs: • Short CE of lower Far OTM Strike with higher Premium (<i>CE primary leg</i>) • Long CE of higher Far OTM Strike with lower Premium (<i>CE hedged leg</i>); and • Short PE of higher Far OTM Strike with higher Premium (<i>PE primary leg</i>) • Long PE of lower Far OTM Strike with lower Premium (<i>PE hedged leg</i>)

	All the 4 legs (<i>i.e. two Short legs & two Long legs</i>) would be of same Expiry series, with equal quantity in each of the aforesaid four legs. The CE Short and PE Short must be of nearly same Premium value. The CE Long and PE Long must be of nearly same Premium value. It is a hedged Short Strangle, making a pair of Bear CE Credit Strategy and Bull PE Credit Strategy.
Example: <i>If ATM is at 17000, then for Short Strangle:</i> • <i>Sell 3 Lots Nifty 17500 CE of Current Week Expiry (at Rs. 155 per Lot); and</i> • <i>Sell 3 Lots Nifty 16500 PE of Current Week Expiry (at Rs. 135 per Lot)</i>	Example: <i>If ATM is at 17000, then for Iron Condor:</i> • <i>Sell 20 Lots Nifty 17500 CE of Current Month Expiry (at Rs. 150 per Lot)</i> • <i>Buy 20 Lots Nifty 17800 CE of Current Month Expiry (at Rs. 65 per Lot); and</i> • <i>Sell 20 Lots Nifty 16500 PE of Current Month Expiry (at Rs. 165 per Lot)</i> • <i>Buy 20 Lots Nifty 16200 PE of Current Month Expiry (at Rs. 75 per Lot)</i>
Objective: Objective is to play a Neutral / Non-directional or sideways / rangebound view, through selling Far OTM CEs and PEs (both as the primary leg), as the expectation is that the underlying will remain, until the Expiry of the Options Shorted, between the Strike levels where the Shorts have been initiated.	Objective: Objective is to play a Neutral / Non-directional or sideways / rangebound view, through selling Far OTM CEs and PEs (both as the primary legs), as the expectation is that the underlying will remain, until the Expiry of the Options Shorted, between the Strike levels where the Shorts have been

Far OTM CE Short leg defines the upper range; and Far OTM PE Short leg defines the lower range: within which the underlying is expected to remain in this Strategy. Farther the OTM strikes from the ATM, broader the range gets (but the Premium on OTM Strikes keeps getting lower). Thus, basis technical analysis and availability of decent Premium values on Far OTM Strikes, this Strategy may be implemented. It is a Net Credit Strategy, as both the Short legs get the credit of the Premium at which far OTM Strike Options are sold. Accordingly, this Strategy generates limited profit to the maximum extent of Premium collected on both the Short legs, if the underlying remains within the range defined by Shorting the two Options by Expiry of those Options.	initiated, just like in a naked Short Strangle Strategy. Also, in this Strategy: Far OTM CE Short leg defines the upper range; and Far OTM PE Short leg defines the lower range: within which the underlying is expected to remain in this Strategy. Farther the OTM Strikes from the ATM, broader the range gets (but the Premium on OTM Strikes keeps getting lower). Thus, basis technical analysis and availability of decent Premium values on Far OTM Strikes, this Strategy may be implemented. Further, in this Strategy: in order to mitigate the risk / loss that may arise if the primary Short legs are breached by the underlying, Long Options are also initiated simultaneously with the primary Short legs, such that this Strategy becomes hedged Short Strangle, comprising of a pair of Bear CE Credit Strategy and Bull PE Credit Strategy. Thus, in effect, Iron Condor comprising of Bull PE Credit Strategy and Bear CE Credit Strategy, converts the naked Short Strangle into a hedged Short Strangle so as to cover and limit the unlimited loss that may arise in a naked Short Strangle positions, to a limited Max Loss situation, if the underlying breaches the primary Short legs (on either side) and gets trending in that direction.
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Demerits:

- It comprises of naked Short positions.
- Since this Strategy is implemented by Shorting Far OTM CEs and PEs, it requires more capital/ margin and also sufficient capital for MTM adjustments also need to be ensured.
- This Strategy generates limited profit to the maximum extent of If there is a Volatility spike, then both the Short legs, will get adversely impacted but the Long leg would get favourably impacted, as there will addition of Time Value in the premium of both the Short & Long Options. This Volatility spike may exhibit virtual loss on the Strategy (*even if there is not much movement in the underlying in any particular direction*) Premium collected on both the Short legs, if the underlying remains within the range defined by Shorting the two Options by Expiry of those Options.
- The underlying as expected must remain within the range defined in this Strategy by Shorting Options at the relevant Strike, by Expiry of the Options Shorted. If the underlying breaks out and breaches the range beyond the Breakeven Strike of the Shorted Option, then this Strategy may yield unlimited loss. Thus, this Strategy is the kind with limited profit and unlimited loss.
- During low Volatility period, sufficient Premium may not be available in Far OTM CEs and PEs,

Demerits:

- Since, in this Strategy on each CE and PE sides, there is one Short position initiated at a higher Premium; and a Long position initiated at a lower Premium. Thus, each of the CE and PE legs have a Net Premium Credit (*i.e. Premium credit received on Short leg – Premium paid on Long leg*). This Net Credit Premium on Iron Condor Strategy is less than the aggregate Premium Credit on Short Strangle (*initiated on same Short Strikes, as that of in Iron Condor*). Therefore, the quantum of profit is less in Iron Condor than in Short Strangle if the underlying remains on Expiry within the range defined by the Short legs (initiated on the same Strikes in Iron Condor and Short Strangle).
- Since, in this Strategy, the Net Credit Premium is less than the aggregate Premium Credit collected in Short Strangle, therefore, the Breakeven Strike (upto which profitability is likely) in this Strategy gets reduced as compared to that in Short Strangle (*even when Shorts are initiated at the same Strikes in Iron Condor and Short Strangle*).
- This Strategy has limited profit potential.
- If there is a Volatility spike, then both the Short legs, will get adversely impacted but the

making this Strategy not viable from quantum of profit perspective. • If there is a Volatility spike, then both the Short legs, will get adversely impacted as there will be addition of Time Value in the premium of both the Options (even if there is not much movement in the underlying in any particular direction). This volatility spike may exhibit virtual loss on the Strategy.	Long leg would get favourably impacted, as there will addition of Time Value in the premium of both the Short & Long Options. This Volatility spike may exhibit virtual loss on the Strategy (<i>even if there is not much movement in the underlying in any particular direction</i>).
<u>Benefits of Short Strangle:</u> • This Strategy is suitable for a rangebound / sideways view. A rangebound movement of the underlying within the range defined by Shorting Far OTM Strike CEs and PEs, generates profit in both the Far OTM Short legs due to erosion of time value owing to such movement in the underlying. This Strategy is suitable when the range of the expected movement in the underlying is wider; and for narrow range Short Straddle Strategy may be considered. • With the passage of time, if the underlying remains within the range as expected, then both the Short legs continues to be OTM Strikes and starts getting profitable due to the rising Theta impact. If by Expiry of the Options Shorted, if the underlying remains within the defined range in this Strategy then both the Shorted legs would expire worthless as OTM, generating entire	<u>Benefits of Iron Condor:</u> • It is a hedged Strategy (<i>i.e. Iron Condor is hedged Short Strangle</i>). The unlimited Max Loss in naked Short Strangle gets capped to a pre-defined limited Max Loss in Iron Condor. • This Strategy is suitable for a rangebound / sideways view. A rangebound movement of the underlying within the range defined by Shorting Far OTM Strike CEs and PEs, generates profit in both the Far OTM Short legs due to erosion of Time Value owing to such movement in the underlying. This Strategy is suitable when the range of the expected movement in the underlying is wider; and for narrow range Short Straddle / Iron Fly Strategy may be considered. • Since, it is a hedged Strategy, the capital / margin required is less as compared to Short Strangle and the need for any

aggregate Premium collected on this Strategy as profit. • In this Strategy, two factors help in generating profit: (i) rangebound move in the underlying; and (ii) Theta impact on the primary leg. Therefore, this Strategy is a high winning probability Strategy if the defined range is maintained by the underlying. • Due to the increasing Theta impact with the approach of Options Expiry, this Strategy becomes suitable for deployment near Expiry if the view is aligned and favourable. • It is a Credit Strategy. Since both Short legs comprises of selling Far OTM Strikes, the Premium on both Short legs is the amount of aggregate Premium collected. Accordingly, in this Strategy, the aggregate Credit of Premium need to be protected for profit in this Strategy. • The aggregate Credit Premium collected on both Short legs, increases the loss area in this Strategy by defining the Breakeven Strike. Thus, from Expiry perspective, the underlying must not go down and cross below the Breakeven Strike of PE Short Strike and on the upper side the underlying must not go up and cross above the Breakeven Strike of CE Short Strike (<i>the Breakeven Strikes in this Strategy are discussed below here</i>). • Volatility crash is favourable on the Strategy, as the reduction in volatility causes erosion in the Time	MTM requirements would also be relatively less. • Since, less capital is required to implement this Strategy as compared to Short Strangle, more quantity/ Lots can be initiated in this Strategy for same amount of capital as compared to the Short Strangle. • While this Strategy has 2 Short Options (as primary legs) and 2 Long Options (as hedged legs), this Strategy is a Net Premium Credit Strategy as the Shorts are initiated at higher Premium than the Longs on the respective CE / PE sides between their primary and hedged legs. • Since this a hedged Strategy, therefore, any breakout by the underlying before Expiry on either side of the defined range is covered by the Long Options hedged leg on that side. Thus, this Strategy helps curtail the unlimited loss situation that may arise in Short Strangle, owing to the Long Options positions added in this Strategy (<i>provided such Long Options do not loose their Premium significantly due to Volatility crash or Theta decay</i>). • This Strategy is suitable for a rangebound / sideways view. A rangebound movement of the underlying within the range defined by Shorting Far OTM Strike CEs and PEs, generates limited profit in both the Far
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Value of both the primary Short legs, which yield profit on the Strategy. • However, Volatility spike will cause addition of Time Value in the premium of both the Options (even if there is not much movement in the underlying in any particular direction), thus exhibiting virtual loss on the Strategy. But so long the Breakeven Strike is not breached on either side, then inspite of increase in premium value and virtual loss on the Strategy due to volatility spike, there will not be an actual loss scenario on the Strategy.	OTM Short legs due to erosion of Time Value owing to such movement in the underlying. • Further, with the passage of time, if the underlying remains within the range as expected, then both the Short legs continues to be OTM Strikes and starts getting profitable due to the rising Theta impact. If by Expiry of the Options Shorted, if the underlying remains within the defined range in this Strategy then both the Short & Long legs on either sides would expire worthless as OTM, generating entire Net Premium Credit collected on this Strategy as profit. • Thus, like in Short Strangle, in this Strategy too, two factors help in generating profit: (i) rangebound move in the underlying; and (ii) Theta impact on the primary leg. Therefore, this Strategy is a high winning probability Strategy if the defined range is maintained by the underlying. • Volatility crash is favourable on the Strategy, as the reduction in volatility causes erosion in the Time Value of both the primary leg (inspite of erosion even on the hedged leg), which ultimately yield profit on the Strategy. • However, Volatility spike will cause addition of Time Value in the premium of both the Long
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& Short legs (*even if there is not much movement in the underlying in any particular direction*), thus exhibiting some virtual loss on the Strategy. But so long the Breakeven Strike is not breached on either side, then inspite of increase in premium value and virtual loss on the Strategy due to volatility spike, there will not be an actual loss scenario on the Strategy.

- The Net Credit Premium (received on both CE & PE side), increases the loss area in this Strategy by defining the Breakeven Strike. However, as compared to Short Strangle, the loss area or the Breakeven Strike on either side (*upto which profitability in the Strategy is ensured*) in this Strategy is lesser than in Short Strangle due to lesser Net Premium Credit collected in this Strategy (*as against aggregate Premium credit collected in Short Strangle*). Thus, from Expiry perspective, the underlying must not go down and close below the Breakeven Strike on the PE side; and on the upper side the underlying must not go up and close above the Breakeven Strike on the CE side Strike (*the Breakeven Strikes in this Strategy are discussed below here*).
- This is a limited loss Strategy.

<u>Breakeven Strike of this Strategy from Expiry perspective:</u> This Strategy comprises of naked CE Short at Far OTM Strike; and a naked PE Short at Far OTM Strike. This is a Credit Strategy as the Premium at which both Shorts are initiated, on aggregate basis is the Total Premium Credit received. The CE Short leg determines the upper range; and the PE Short leg determines the lower range in this Strategy. The Breakeven on the upper side (i.e. CE side) and lower side (i.e. PE side), is determined as follows: • <u>The Breakeven Strike on the CE side (upper side) is:</u> The CE Strike (at which Short is initiated) + aggregate Premium credit received on both CE & PE Shorts; and • <u>The Breakeven Strike on the PE side (lower side) is:</u> The PE Strike (at which Short is initiated) - aggregate Premium credit received on both CE & PE Shorts. Thus, if by Expiry of the relevant Options which have been Shorted, if the underlying does not breach the aforesaid Breakeven Strikes (either on the upper side or the lower side), then this Strategy would yield profit; but if by Expiry of the relevant Options, the underlying breaches either upper or lower side and goes beyond the relevant Breakeven Strike, then the Strategy would yield loss. In case of continuous movement of the underlying after breaching of the Breakeven Strike on either side by the underlying, an unlimited loss	<u>Breakeven Strike of this Strategy from Expiry perspective:</u> The upper range comprises of CE Short primary leg at higher Premium and CE Long hedged leg at lower Premium. Thus, there is a Net Premium Credit on the CE side of Iron Condor. Likewise, the lower range comprises of PE Short primary leg at higher Premium and PE Long hedged leg at lower Premium. Thus, there is a Net Premium Credit on the PE side of Iron Condor. The sum of the Net Premium Credit on the CE and PE Side is the aggregate Net Premium Credit received in this Strategy. Accordingly: • <u>the Breakeven Strike of the CE side in this Strategy (upper range) is:</u> CE Short primary leg + the aggregate Net Premium Credit in the Strategy; and • <u>the Breakeven Strike of the PE side in this Strategy (lower range) is:</u> PE Short primary leg - the aggregate Net Premium Credit in the Strategy. Thus, if by Expiry of the relevant Options, if the underlying does not breach the aforesaid Breakeven Strikes (either on the upper side or the lower side), then this Strategy would yield profit; but if by Expiry of the relevant Options, the underlying gets trending either on the upper side or lower side and goes beyond the relevant
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situation would arise (**Unlimited Loss situation**).

For example: If ATM is at 17000, then for Short Strangle: If Nifty 16500 PE is sold at Rs. 100 per Lot & Nifty 17500 CE is sold at Rs. 50 per Lot, then the BE Strike of this Strategy will be:

On CE side: $17500 + (100+50) = 17650$ CE Strike; and

On PE side: $16500 - (100+50) = 16350$ PE Strike

Thus, while this Strategy would yield total aggregate Premium of Rs. 150 per Lot as full profit if the underlying remains within the 16500 to 17500 range (i.e. the Strikes at which Shorts have been initiated). However, if Nifty crosses 17500 Strike upwardly then this Strategy would not yield loss so long the Breakeven Strike of 17650 is not breached upwardly by Nifty till Expiry.

Likewise, if Nifty crosses 16500 Strike downwardly then this Strategy would not yield loss so long the Breakeven Strike of 16350 is not breached downwardly by Nifty till Expiry.

However, in this Strategy, unlimited loss situation would arise, if either on the upside (i.e. CE side) or downside (i.e. PE side), the underlying breaks-out beyond the Breakeven Strike level of that particular side and closes by Expiry beyond the BE Level. Deeper the underlying keeps trending beyond the BE Level (either on CE side or PE side), higher would the Loss that would be generated on this Strategy.

Breakeven Strike on that side, then the Strategy would yield loss.

In case of continuous movement of the underlying after breaching of the Breakeven Strike on either side by the underlying, and closing downwardly below the PE Long Strike or closing above the CE Long Strike, would yield quantified Max Loss on this Strategy (**Limited Loss situation**).

For example: If Nifty 17500 CE is sold at Rs. 250 per Lot & Nifty 17800 CE is bought at Rs. 150, for the CE side of this Strategy; and Nifty 16500 PE is sold at Rs. 200 per Lot & Nifty 16200 PE is bought at Rs. 100 per Lot, for the PE side of this Strategy, then:

the Net Premium Credit received on this Strategy will be: $[(250+200) - (150+100)] = 450 - 250 = 200$

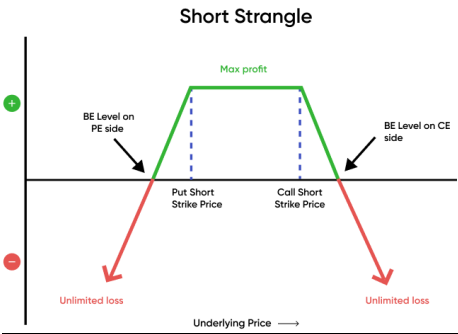
- *Breakeven Strike of this Strategy on upper range (CE side) will be: $17500 + 200 = 17700$ CE*
- *Breakeven Strike of this Strategy on lower range (PE side) will be: $16500 - 200 = 16300$ PE*

If the underlying breaches the upper Breakeven Strike i.e. 17700 CE and keeps trending higher, then limited loss would accrue on this Strategy on the upper side.

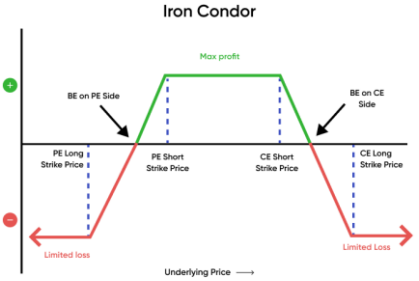
Likewise, if the underlying breaches the lower Breakeven Strike i.e. 16300 PE and keeps trending lower, then limited loss would accrue on this Strategy on the down side.

However, in this Strategy, limited loss situation would arise, if either on the upside (*i.e. CE side*) or downside (*i.e. PE side*), the underlying breaks-out beyond the Breakeven Strike level of that particular side and closes by Expiry beyond the Long leg (*on either side*). Even if the underlying keeps trending beyond the Long Strike (*on either side*), the Limited Max Loss would remain the same on this Strategy.

Payoff Chart for Short Strangle



Payoff Chart for Iron Condor



Loss in this Strategy:

Since, this Strategy comprises of naked Short legs, therefore **if the underlying breaks the range defined by Shorting relevant Options, on either side, and starts trending after crossing beyond the Breakeven Strike of that side, then this Strategy will start yielding unlimited loss** as the underlying keep trending in that direction and expires outside the Breakeven Strike.

In this situation, the Short leg of that side Option (*where the BE Strike is breached*) becomes an ITM. The other side of Short

Loss in this Strategy:

Maximum loss in this Strategy occurs when the underlying breaks the range defined by Shorting relevant Options, on either side, and starts trending after crossing beyond the Breakeven Strike of that side and eventually closes by Expiry either: (i) at or higher than the CE Long leg of the Strategy; or (ii) at or lower than the PE Long Strike of the Strategy.

In this situation, both the Short & Long leg of that side Option (*where the BE Strike is breached*) becomes an ITM.

Option leg becomes even farther OTM. This situation generates the Unlimited Max Loss situation on the Strategy.

Level of starting unlimited loss on the upside (i.e. CE side):

If the underlying, gets bullish and breaches the Breakeven Strike on the CE side of the Strategy and closes higher than the BE Strike on the CE side, then this Strategy would yield loss on the upside. Higher the underlying would close by Expiry after breaching the BE Strike on the CE side, higher will be the loss. The loss situation is unlimited, if the underlying keeps trending higher by Expiry. This is because the CE Short Strike becomes an ITM (*while the CE Long Strike becomes an even farther OTM*).

Level of starting unlimited loss on the downside (i.e. PE side):

If the underlying, gets bearish and breaches the Breakeven Strike on the PE side of the Strategy and closes lower than the BE Strike on the PE side, then this Strategy would yield loss on the downside. Lower the underlying would close by Expiry after breaching the BE Strike on the PE side, higher will be the loss. The loss situation is unlimited, if the underlying keeps trending lower by Expiry. This is because the PE Short Strike becomes an ITM (*while the PE Long Strike becomes an even farther OTM*).

Impact on loss situation, due to Strike Difference:

Larger the difference between the Far OTM CE Short Strike and Far OTM PE Short Strike, smaller will be the Total Premium Credit received, hence smaller profit margin from the Strategy. However, larger Strike difference between the CE Short &

The other side of Options, both Long & Short leg becomes even farther OTM. This situation generates the Limited Max Loss situation on the Strategy.

Calculation of Max Loss:

The Max Loss on this Strategy will be limited and can be pre-calculated. Maximum Loss in this Strategy is calculated as:

Max Loss for CE side: is calculated as:

- *[Strike difference between CE Long and CE Short]*
minus
- *[aggregate of Net Premium Credit received on CE side & PE side on this Strategy].*

Max Loss for PE side: Is calculated as:

- *[Strike difference between PE Short Strike and PE Long Strike]*
minus
- *[aggregate of Net Premium Credit received on CE side & PE side on this Strategy].*

Impact on Max Loss situation, due to variation in Strike Difference between CE side & PE side:

If the Strike difference between Short leg & Long leg, on both CE side and PE side is same (eg: 300 point difference between CE Short & CE Long and 300 point difference between PE Short & PE Long), then the Max Loss would be same for the CE side as well as for the PE side. In such case, the amount so

PE Short legs, enlarges the Breakeven Strike on both CE side & PE side. Therefore, the profit range gets even wider with larger strike difference, which helps curtailing the loss probability. <u>Calculation of final loss amount on the Strategy:</u> If the underlying closes by Expiry, after breaching the Breakeven Strike on either side, then the Loss accrued on the Strategy on Expiry can be calculated as: • [the final premium value of Short Option of the momentum side on Expiry (<i>i.e. Short leg which becomes / expires as an ITM</i>)]¹⁸ minus • [the aggregate Premium Credit collected by Shorting both CE & PE Options for the Strategy] <i>For example: If ATM is at 17000, then for Short Strangle: If Nifty 16500 PE is sold at Rs. 100 per Lot & Nifty 17500 CE is sold at Rs. 50 per Lot, then the BE Strike of this Strategy will be:</i> <i>On CE side: 17650 CE Strike; and</i> <i>On PE side: 16350 PE Strike.</i> <i>Therefore, if by Expiry Nifty falls below 16350 and Expiry is at 15850 (as ATM), then PE Short leg of 16500 will be an ITM with final LTP of about Rs. 650 (because on Expiry, final LTP of this PE strike will be equal to its Intrinsic Value, which is</i>	determined, is said to be the Max Loss of the Strategy. However, if the Strike difference between Short leg & Long leg, on CE side and PE side is different (<i>eg: 300 point difference between CE Short & CE Long and 500 point difference between PE Short & PE Long</i>), then the Max Loss would be different for the CE side and the PE side. The side where the Strike difference is more, would have more Net Premium Credit and accordingly the BE Level of that side will also increase. But with increase in BE Level, the Max Loss situation on that side would also increase. In such case, the Max Loss of the side where Strike difference is more, would be the Max Loss of the Strategy. <u>Level of starting loss on the Strategy and Loss Zone:</u> If the underlying breaks-out and starts trending after crossing beyond the Breakeven Strike of either side, then this Strategy will start yielding loss. Thus, breaching the BE Level on either side, is the Level from which loss would start on the Strategy. <u>Loss Zone on the CE side:</u> If the underlying, gets bullish and breaches the Breakeven Strike on the CE side of the Strategy and closes higher than the BE Strike on the CE side, then this Strategy would yield loss on the upside. Higher the underlying would close by Expiry after breaching the BE Strike on
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¹⁸ The final LTP (i.e. Premium value) of the Option, if it expires as an ITM, would be equal to the Intrinsic Value (i.e. the difference between the relevant ITM Strike and ATM Strike on Expiry).

calculated as PE ITM Strike – ATM Strike = 16500 – 15850 = 650).

Thus, the Loss incurred in this Strategy will be: 650 – 150 = Rs. 350 per qty in a Lot, i.e. 350 x 50 = Rs. 17,500 per Lot.

the CE side, higher will be the loss. But if the underlying closes by Expiry, at or beyond the CE Long leg (on the higher strike side) then the Limited Max Loss situation would accrue on this Strategy (*i.e. applicable Max Loss on CE side, as per Max Loss calculations given above*).

Thus, the Loss zone on the CE side, is the BE Strike on the CE side till CE Long Strike and higher. If the underlying closes by Expiry within this Loss Zone, but towards the BE Strike on the CE side then the loss on the Strategy will be lower; but if the underlying closes towards the CE Long Strike within the zone, then the loss on the Strategy would be relatively more. In this Loss zone, the CE Short leg becomes an ITM, whereas the CE Long leg remains an OTM.

Loss Zone on the PE side: If the underlying, gets bearish and breaches the Breakeven Strike on the PE side of the Strategy and closes lower than the BE Strike on the PE side, then this Strategy would yield loss on the downside. Lower the underlying would close by Expiry after breaching the BE Strike on the PE side, higher will be the loss. But if the underlying closes by Expiry, at or beyond the PE Long leg (on the lower strike side) then the Limited Max Loss situation would accrue on this Strategy (*i.e. applicable Max Loss on PE side, as per Max Loss calculations given above*).

Thus, the Loss zone on the PE side, is the BE Strike on the PE side till PE Long Strike and lower. If the underlying closes by Expiry within this

	Loss Zone, but towards the BE Strike on the PE side then the loss on the Strategy will be lower; but if the underlying closes towards the PE Long Strike within the zone, then the loss on the Strategy would be relatively more. In this Loss zone, the PE Short leg becomes an ITM, whereas the PE Long leg remains an OTM. <u>Calculation of final loss amount on the Strategy within the Loss Zone:</u> If the underlying closes by Expiry within the Loss Zone (<i>either on CE side or PE Side</i>), then the Loss on Expiry will be calculated as: • [the final premium value of Short Option of the momentum side on Expiry (<i>i.e. Short leg which becomes / expires as an ITM</i>)]¹⁹ minus • [the Net Premium Credit collected on the overall Strategy]. <i>For example: If Nifty 17500 CE is sold at Rs. 250 per Lot & Nifty 17800 CE is bought at Rs. 150, for the CE side of this Strategy; and Nifty 16500 PE is sold at Rs. 200 per Lot & Nifty 16200 PE is bought at Rs. 100 per Lot, for the PE side of this Strategy, then:</i> • <i>the Net Premium Credit received on this Strategy will be:</i> $[(250+200) - (150+100)] = 450 - 250 = 200.$
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¹⁹ The final LTP (i.e. Premium value) of the Option, if it expires as an ITM, would be equal to the Intrinsic Value (i.e. the difference between the relevant ITM Strike and ATM Strike on Expiry).

- *BE Strike on CE side = $17500 + 200 = 17700$ CE*
- *BE Strike on PE side = $16500 - 200 = 16300$ PE*

In the aforesaid example:

Max Loss on the CE side (i.e. if the underlying breaches the Breakeven Strike of 17700 CE, will be: $[17800 - 17500] - [200] = 300 - 200 = 100$ per qty i.e. $100 \times 50 = \text{Rs } 5000$ per Lot. This Max Loss situation on the upside will arise if the underlying closes by Expiry at or higher than the CE Long Strike of 17800.

Max Loss on the PE side (i.e. if the underlying breaches the Breakeven Strike of 16300 PE, will be: $[16500 - 16200] - [200] = 300 - 200 = \text{Rs. } 100$ per qty i.e. $100 \times 50 = \text{Rs. } 5000$ per Lot. This Max Loss situation on the downside will arise if the underlying closes by Expiry at or lower than the PE Long Strike of 16200.

Here, because the Strike difference on both CE side and PE side (between the Short leg & Long leg) is the same (i.e. 300 on both side), therefore, the Max Loss on both CE side & PE side is same (i.e. Rs. 5000)

However, if by Expiry, Nifty rises above and closes at 17750 Strike (as ATM), i.e., within the Loss Zone on the CE side, then CE Short leg of 17500 will be an ITM with final LTP of about Rs. 250 (because on Expiry, final LTP of this CE strike will be equal to its Intrinsic Value, which is calculated as $\text{ATM Strike} - \text{CE ITM Strike} = 17750 - 17500 = 250$).

	<i>Thus, the Loss incurred in this Strategy will be: $250 - 200 = \text{Rs. } 50$ per qty in a Lot, i.e. $50 \times 50 = \text{Rs. } 2500$ per Lot.</i>
<u>Profit in this Strategy:</u> <u>Max Profit scenario & amount:</u> By Expiry of the relevant Options, if the underlying closes at between the Short CE Strike & Short PE Strike, then the entire Premium collected is the Max Profit in this Strategy. <u>Profit zone:</u> In the event the underlying moves beyond the Strike at which Shorts have been initiated but do not cross the Breakeven Strike of that side, then too this Strategy would yield some profit. Therefore, the overall profit zone on the Strategy ranges from BE Strike on the CE side to BE Strike on the PE side. If the underlying closes anywhere within this zone by Expiry, then the Strategy will generate profit. <u>On the CE side:</u> if the underlying closes, between the CE Short Strike and the BE level of the Strategy on the CE side range, then some profit would be generated by the Strategy. If the underlying closes by Expiry near the CE Short Strike within this zone, then profit will be relatively more; than if the underlying closes near the BE Strike range on the CE side within this zone. Therefore, the profit zone on the CE side is: when the underlying closes by Expiry between the CE Short Strike and the BE Strike level on the CE side. <u>On the PE side:</u> if the underlying closes, between the PE Short Strike and the BE level of the Strategy on the PE side profit zone, then some profit would be generated by the Strategy. If the underlying closes by Expiry near the PE Short Strike within the	<u>Profit in this Strategy:</u> <u>Max Profit scenario & amount:</u> By Expiry of the relevant Options, if the underlying remains within the Strikes at which Shorts have been initiated, then the entire Net Premium Credit collected is the Max Profit in this Strategy. <u>Profit zone:</u> In the event the underlying moves beyond the Strike at which Shorts have been initiated but do not cross the Breakeven Strike of that side, then too this Strategy would yield some profit. Therefore, the overall profit zone on the Strategy ranges from BE Strike on the CE side to BE Strike on the PE side. If the underlying closes anywhere within this zone by Expiry, then the Strategy will generate profit. <u>On the CE side:</u> if the underlying closes, between the CE Short Strike and the BE level of the Strategy on the CE side range, then some profit would be generated by the Strategy. This is the Profit zone on the CE side. If the underlying closes by Expiry near the CE Short Strike within this zone, then profit will be relatively more; than if the underlying closes near the BE Strike range on the CE side within this zone. Therefore, the profit zone on the CE side is: when the underlying closes by Expiry between the CE Short Strike and the BE Strike level on the CE side.

profit zone, then profit will be relatively more; than if the underlying closes within the profit zone, near the BE Strike on the PE side. Therefore, the profit zone on the PE side is: when the underlying closes by Expiry between the PE Short Strike and the BE Strike level on PE side.

Calculation of final profit on the Strategy in the Profit Zone:

If the underlying breaches the Strike at which Shorts have been initiated but do not cross the Breakeven Strike of that side and closes within the profit zone (of that side) by Expiry, then too this Strategy would yield some profit. This profit in such situation will be calculated as:

- [aggregate Premium Credit collected on the Strategy]

minus

- [final LTP value, on Expiry, of the Short Option, which expires as an ITM]²⁰.

For example: If ATM is at 17000, then for Short Strangle: If Nifty 16500 PE is sold at Rs. 100 per Lot & Nifty 17500 CE is sold at Rs. 50 per Lot, then the BE Strike of this Strategy will be:

On CE side: 17650 CE Strike; and

On PE side: 16350 PE Strike.

On the PE side: if the underlying closes, between the PE Short Strike and the BE level of the Strategy on the PE side profit zone, then some profit would be generated by the Strategy. If the underlying closes by Expiry near the PE Short Strike within the profit zone, then profit will be relatively more; than if the underlying closes within the profit zone, near the BE Strike on the PE side. Therefore, the profit zone on the PE side is: when the underlying closes by Expiry between the PE Short Strike and the BE Strike level on PE side.

Calculation of final profit on the Strategy in the Profit Zone:

If the underlying breaches the Strike at which Shorts have been initiated (*on either side*), but do not cross the Breakeven Strike of that side and closes within the profit zone (of that side) by Expiry, then too this Strategy would yield some profit. This profit in such situation will be calculated as:

- [aggregate Premium Credit collected on the Strategy]

minus

- [final LTP value, on Expiry, of the Short Option leg, which expires as an ITM]²¹.

²⁰ The final LTP (i.e. Premium value) of the Option, if it expires as an ITM, would be equal to the Intrinsic Value (i.e. the difference between the relevant ITM Strike and ATM Strike on Expiry).

²¹ The final LTP (i.e. Premium value) of the Option, if it expires as an ITM, would be equal to the Intrinsic Value (i.e. the difference between the relevant ITM Strike and ATM Strike on Expiry).

Thus, if the underlying by Expiry of the Options Shorted, remains within the defined Strike range in this Strategy and does not breach the Strikes at which Short have been initiated, then the entire Rs. 150 aggregate Premium shall be the Max Profit in this Strategy.

However, if Nifty moves higher than the 17500 CE Strike, but does not breach the Breakeven Strike of 17650 on the upper side and expire at 17600 Strike as ATM, then the Max Profit in this Strategy will be the final LTP of the 17500 CE Short leg (say Rs. 100) minus Rs. 150 (aggregate Premium Credit received on this Strategy) = Rs. 50 per qty in the Lot. Thus, overall profit on this Strategy got reduced (from total premium credit of Rs. 150 to Rs. 50) as the Strike at which Short was initiated was breached by Expiry (but loss in this Strategy did not occur because the Breakeven Strike was not breached by Expiry).

Impact on profit situation, due to Strike Difference:

Larger the difference between the Far OTM CE Short Strike and Far OTM PE Short Strike, smaller will be the net premium credit received, hence smaller profit margin from the Strategy. However, larger Strike difference between the CE Short & PE Short legs, enlarges the Breakeven Strike on both CE side & PE side. Therefore, the profit range gets even wider with larger Strike difference, which helps increasing the profit probability.

For example: If Nifty 17500 CE is sold at Rs. 250 per Lot & Nifty 17800 CE is bought at Rs. 150, for the CE side of this Strategy; and Nifty 16500 PE is sold at Rs. 200 per Lot & Nifty 16200 PE is bought at Rs. 100 per Lot, for the PE side of this Strategy, then:

- the Net Premium Credit received on this Strategy will be:

$$[(250+200) - (150+100)] = 450 - 250 = 200.$$
- BE Strike on CE side =
 $17500+200=17700 \text{ CE}$
- BE Strike on PE side = $16500-200 = 16300 \text{ PE}$

Thus, if the underlying by Expiry of the Options Shorted, remains within the defined Strike range in this Strategy and does not breach the Strikes at which Short have been initiated, then the entire Rs. 200 per Lot aggregate Net Premium Credit received on this Strategy shall be the Max Profit in this Strategy.

However, if Nifty moves higher than the 17500 CE Strike, but does not breach the Breakeven Strike of 17700 CE on the upper side and expire at 17600 ATM (which implies that 17500 CE became an ITM; and 17800 CE and both PE legs expire as OTMs and thus become zero), then the Profit in this Strategy will be the final LTP of the 17500 CE Short leg (say Rs. 100) minus Rs. 200 (aggregate Premium Credit received on this Strategy) = Rs. 100 per qty in the Lot. Thus, overall profit on this Strategy got reduced (from total premium credit of Rs. 200 to Rs. 100) as the Strike at which

	<i>Short was initiated was breached by Expiry (but loss in this Strategy did not occur because the Breakeven Strike was not breached by Expiry).</i> <u>Impact on profit situation, due to Strike Difference between CE Short & PE Short:</u> Larger the difference between the Far OTM CE Short Strike and Far OTM PE Short Strike, smaller will be the Net Premium Credit received, hence smaller profit margin from the Strategy. However, larger Strike difference between the CE Short & PE Short legs, enlarges the Breakeven Strike on both CE side & PE side. Therefore, the profit range gets even wider with larger Strike difference, which helps increasing the profit probability. The ratio between the Max Loss and the Max Reward gives the Risk & Reward ratio for this Strategy.
<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level on the upside (CE side):</u> [CE Short Strike + Total Premium Credit collected on both CE Short & PE Short leg] <u>BE Level on the downside (PE side):</u> [PE Short Strike - Total Premium Credit collected on both CE Short & PE Short leg] <u>Min Profit Level:</u> If underlying closes by Expiry just above the BE Level²² on the PE	<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level on the upside (CE side):</u> [CE Short Strike + Net Premium Credit collected on both CE & PE sides] <u>BE Level on the downside (PE side):</u> [PE Short Strike – Net Premium Credit collected on both CE & PE sides] <u>Min Profit Level:</u> If underlying closes by Expiry just above the BE Level²⁶ on the PE side or if the underlying closes

²² That is higher Strike than BE Strike Level on PE side.

²⁶ That is higher Strike than BE Strike Level on PE side.

side or if the underlying closes just below the BE Level on the CE side²³. Profit in such situation can be calculated as already explained above. Max Profit Level: If underlying closes by Expiry at or anywhere between the CE Short Strike and PE Short Strike. Profit Zone: If underlying closes by Expiry between the BE Level on PE side and BE Level on CE side. In this profit zone the following situation may arise: <u>If underlying closes by Expiry at or anywhere between the CE Short Strike and PE Short Strike:</u> Max profit on the Strategy would be generated (calculated as aforesaid). <u>If underlying closes between the PE Short Strike and BE Level on the PE side:</u> Then some profit would be generated on the overall Strategy. In such case higher profit would be generated on the Strategy if the underlying closes by Expiry near the PE Short Strike; and the profit would be less if the underlying closes towards the BE Level on the PE side. Profit in such situation can be calculated as already explained above. <u>If underlying closes between the CE Short Strike and BE Level on the CE side:</u> Then some profit would be generated on the overall Strategy. In such case higher profit would be generated on the Strategy if the underlying closes by Expiry near the CE Short Strike; and the profit would be less if the underlying closes towards the BE Level on the CE side. Profit in such situation can be calculated as already explained above.	just below the BE Level on the CE side²⁷. Profit in such situation can be calculated as already explained above. Max Profit Level: If underlying closes by Expiry at or anywhere between the CE Short Strike and PE Short Strike. Profit Zone: If underlying closes by Expiry between the BE Level on PE side and BE Level on CE side. In this profit zone the following situation may arise: <u>If underlying closes by Expiry at or anywhere between the CE Short Strike and PE Short Strike:</u> Max profit on the Strategy would be generated (calculated as aforesaid). <u>If underlying closes between the PE Short Strike and BE Level on the PE side:</u> Then some profit would be generated on the overall Strategy. In such case higher profit would be generated on the Strategy if the underlying closes by Expiry near the PE Short Strike; and the profit would be less if the underlying closes towards the BE Level on the PE side. Profit in such situation can be calculated as already explained above. <u>If underlying closes between the CE Short Strike and BE Level on the CE side:</u> Then some profit would be generated on the overall Strategy. In such case higher profit would be generated on the Strategy if the underlying closes by Expiry near the CE Short Strike; and the profit would be less if the
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²³ That is lower Strike than BE Strike Level on CE side.

²⁷ That is lower Strike than BE Strike Level on CE side.

<u>Loss Starting Level:</u> If underlying closes by Expiry below the BE Level on the PE side²⁴ or above the BE Level on the CE side²⁵. <u>Max Loss situation:</u> If the underlying closes by Expiry below the BE Level on the PE side or above the BE Level on the CE side, then the Max Loss may arise on this Strategy, in the following situation: <u>Max Loss on the PE side:</u> In case the underlying keeps falling below the BE Level on the PE side, then unlimited loss situation would arise on the lower side. Lower the underlying would close below the BE Level of the PE side, higher will be the loss on the overall Strategy. Loss on Expiry, in such situation can be calculated as already explained above. <u>Max Loss on the CE side:</u> In case the underlying keeps rising above the BE Level on the CE side, then unlimited loss situation would arise on the upside. Higher the underlying would close above the BE Level of the CE side, higher will be the loss on the overall Strategy. Loss on Expiry, in such situation can be calculated as already explained above.	underlying closes towards the BE Level on the CE side. Profit in such situation can be calculated as already explained above. <u>Loss Starting Level:</u> If underlying closes by Expiry below the BE Level on the PE side²⁸ or above the BE Level on the CE side²⁹. <u>Max Loss situation:</u> If the underlying closes by Expiry below the PE Long Strike on the PE side or above the CE Long Strike on the CE side, then the Max Loss may arise on this Strategy. <u>Loss Zone:</u> If underlying closes by Expiry below the BE Level on PE side and above the BE Level on the CE side. In this loss zone the following situation may arise: <u>If underlying closes by Expiry at or anywhere below the PE Long Strike:</u> Max loss on the Strategy would be generated (<i>calculated as aforesaid</i>). <u>If underlying closes below the BE Level on the PE side and above the PE Long Strike:</u> Then some loss would be generated on the overall Strategy. In such case lower would be the loss generated on the Strategy if the underlying closes by Expiry near the BE Level on the PE side; and the loss would be relatively more if the underlying closes towards the PE Long
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²⁴ That is lower Strike than BE Strike Level on PE side.

²⁵ That is higher Strike than BE Strike Level on CE side.

²⁸ That is lower Strike than BE Strike Level on PE side.

²⁹ That is higher Strike than BE Strike Level on CE side.

	Strike. Loss in such situation can be calculated as already explained above. <u>If underlying closes by Expiry at or anywhere above the CE Long Strike:</u> Max loss on the Strategy would be generated (calculated as aforesaid). <u>If underlying closes above the BE Level on the CE side and below the CE Long Strike:</u> Then some loss would be generated on the overall Strategy. In such case lower would be the loss generated on the Strategy, if the underlying closes by Expiry near the BE Level on the CE side; and the loss would be relatively more if the underlying closes towards the CE Long Strike. Loss in such situation can be calculated as already explained above.
<u>Options behaviour</u> • In this Strategy, two factors help in generating profit: (i) rangebound move in the underlying; and (ii) Theta impact on the primary leg. Therefore, this Strategy is a high winning probability Strategy if the defined range is maintained by the underlying. • If the underlying remains within the defined range in this Strategy (i.e. between the two Strikes Shorted in this Strategy), then it implies that by Expiry both these Strikes expires worthless as OTM (due to Theta impact on both primary leg being OTMs). Consequently, the entire aggregate Premium received on Shorting both CE & PE Strikes would be the maximum profit.	<u>Options behaviour:</u> • In this Strategy, two factors help in generating profit: (i) rangebound move in the underlying; and (ii) Theta impact on both the Short primary leg. Therefore, this Strategy is a high winning probability Strategy if the defined range is maintained by the underlying. • If the underlying remains within the defined range in this Strategy (i.e. between the two Strikes Shorted in this Strategy), then it implies that by Expiry both these Strikes expires worthless as OTM (due to Theta impact on both primary legs and both hedged legs, being OTMs). Consequently, the entire

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| <ul style="list-style-type: none"> • Further, the selection of these CE & PE Strikes must be such OTM Strikes which are not expected to be breached by the underlying by Expiry of the Options Shorted. Therefore, CE Short must be initiated on Far OTM Strike above the Resistance level and the PE Short must be initiated on Far OTM Strike below the Support level. • Further, as the Expiry approaches near, the Theta impact on the Far OTM Strike CE & PE starts to lose its Premium, and therefore generates profit. • Due to the increasing Theta impact with the approach of Options Expiry, this Strategy becomes suitable for deployment near Expiry if the view is aligned and favourable. • Thus, Short Strangles can be initiated (i) when market is rangebound; (ii) near Expiry i.e. in the last week or so before Expiry, to play until Expiry day; (iii) a day before Expiry, to benefit from Overnight Expiry Decay; (iv) On Expiry day, to benefit from full Theta decay of Expiry day effect. • Rise in Volatility may not adversely impact this Strategy eventually by Expiry, even if rise in Volatility would be unfavourable to both the Short legs before the Expiry (<i>as their Premium would rise or atleast will not fall as otherwise expected</i>). This is owing to the fact that if the both the legs continue to be an OTM until Expiry then even if rising Volatility increases their Premium value, then also it would eventually become zero and | <p>aggregate Net Premium received on this Strategy would be the maximum profit.</p> <ul style="list-style-type: none"> • Further, the selection of these CE & PE Strikes must be such OTM Strikes which are not expected to be breached by the underlying by Expiry of the Options Shorted. Therefore, CE Short must be initiated on Far OTM Strike above the Resistance level and the PE Short must be initiated on Far OTM Strike below the Support level. • Further, as the Expiry approaches near, the Theta impact on the Far OTM Strike CE & PE starts to lose its Premium, and therefore generates profit. • Due to the increasing Theta impact with the approach of Options Expiry, this Strategy becomes suitable for deployment near Expiry if the view is aligned and favourable. • Thus, this Strategy (which is hedged Short Strangles) can be preferred over Short Strangles to play out: (i) when market is rangebound; (ii) near Expiry i.e. in the last week or so before Expiry, to play until Expiry day; (iii) a day before Expiry, to benefit from Overnight Expiry Decay; (iv) On Expiry day, to benefit from full Theta decay of Expiry day effect. • Rise in Volatility may not adversely impact this Strategy, |
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yield profit to the extent of aggregate Premium credit on Expiry. • Falling state of Volatility will also help this Strategy to realise the profit quickly, as the drop in Volatility will erode the Premium value of both the Short legs and the aggregate Premium Credit would be realised as profit sooner as Theta impact too would eventually help fasten the erosion of the Premium. • Delta play between the two Short legs is separately discussed hereinbelow.	even if rise in Volatility would be favourable to the CE Long & PE Long hedged legs and not on the CE Short & PE Short primary legs. This is owing to the fact that if the both the primary & hedged legs of the CE and PE side positions continue to be an OTM until Expiry then even if rising Volatility increases their Premium value, then also it would eventually become zero and yield profit to the extent of Net Premium credit on Expiry. • Falling state of Volatility will also help this Strategy to realise the profit quickly, as the drop in Volatility will erode the Premium value of both the CE Short & PE Short primary legs (as well as of the hedged legs) and the Net Premium credit would be realised as profit sooner as Theta impact too would eventually help fasten the erosion of the Premium. • Delta neutral position is strived for in this Strategy. The Delta play between the CE Short and PE Short primary legs; as well the CE Long and PE Long hedged legs is separately discussed hereinbelow.
<u>Strike / Delta value:</u> The two Short legs, i.e. CE Short and PE Short must be Far OTMs, and can be initiated at such Strike levels which have more or less same LTP or Delta value. This equal Delta value Short legs helps to ensure a reasonable balance between the profit &	<u>Strike / Delta value:</u> The two Short legs, i.e. CE Short and PE Short must be Far OTMs, and can be initiated at such Strike levels which have more or less same LTP or Delta value. This equal Delta value Short legs helps to ensure a reasonable balance

loss scenario between the two Short legs in this Strategy. With approx. equal Delta values on CE Short and PE Short legs:

- when CE Short leg loses due to rise in its LTP (*i.e. when underlying rises*), the PE Short leg will help counter the losses on CE leg by generating profit as the LTP of PE would reduce; and
- when PE Short leg generates loss due to rise in its LTP (*i.e. when underlying falls*), the CE Short leg will help counter the losses on PE leg by generating profit as the LTP of CE would reduce.

Thus, the CE Short and the PE Short leg also acts as a natural hedge to the other leg, to the extent of the Breakeven Strike. Once the Breakeven Strike is breached by the underlying on either side, then the unlimited loss situation arises depending how long the underlying trends beyond Breakeven Even Strike until Expiry of the Options Shorted.

between the profit & loss scenario between the two Short legs in this Strategy.

Likewise, the two Long legs in this Strategy, i.e. CE Long and PE Long must be even Far OTMs, and can be initiated at such Strike levels which have more or less same LTP or Delta value. This equal Delta value Long legs helps to ensure a reasonable balance between the profit & loss scenario between the two Long legs in this Strategy as per the movement of the underlying.

Thus, with approx. equal Delta values on CE Short and PE Short legs; and equal Delta values on CE Long and PE Long legs, Delta neutrality is ensured in this Strategy to cater to maintain a balance between the profit and loss situation amongst the Short legs and amongst the Long legs resulting due to the movement of the underlying, i.e.:

- when CE Short leg loses due to rise in its LTP (*i.e. when underlying rises*), the PE Short leg will help counter the losses on CE Short leg by generating profit (*as the LTP of PE would reduce*) to almost similar amount as to the loss incurred on the CE Short leg, due to same Delta values of the CE Short and PE Short legs.
- at the same time in this Strategy, with the rise in the underlying, PE Long leg generates losses due to fall in its LTP, however, the CE Long leg will help counter the losses on PE Long leg by generating profit (*as the LTP of CE would rise*) to

	almost similar amount as to the loss incurred on the PE Long leg, due to same Delta values of the CE Long and PE Long legs; • when PE Short leg generates loss due to rise in its LTP (<i>i.e. when underlying falls</i>), the CE Short leg will help counter the losses on PE Short leg by generating profit as the LTP of CE Short leg would reduce to almost similar amount as to the loss incurred on the PE Short leg, due to same Delta values of the CE Short and PE Short legs; • at the same time in this Strategy, with the fall in the underlying, CE Long leg generates losses due to fall in its LTP, however, the PE Long leg will help counter the losses incurred on CE Long leg, by generating profit (<i>as the LTP of PE would rise</i>) to almost similar amount as to the loss incurred on the CE Long leg, due to same Delta values of the CE Long and PE Long legs. Further, the Delta difference between the primary leg and the hedged leg of the CE side (<i>and also between the primary and hedged leg for the PE side</i>) will help maintain a reasonable control on the Net Premium Credit scenario in this Strategy. Delta difference can be ensured by selecting appropriate distance between the primary leg Strike and the hedged leg Strike, separately for CE and PE side, for this Strategy. Since, in this Strategy (which is a Net Credit Strategy), besides the
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	rangebound movement of the underlying, Theta decay also plays an important role to ensure profit. Therefore, Far OTM CEs are selected for this Strategy. In order to benefit from Theta decay, the CE Short for the primary leg should be initiated at such a Strike which the underlying is expected to not breach by Expiry. Also, the primary leg should have sufficient Premium Credit for reasonable profit generation. Once, primary hedge is selected then the hedged leg must be simultaneously initiated at a suitable Strike distance.
<u>Selection of Option Strikes:</u> Selection of the CE & PE Strikes must be such OTM Strikes which are not expected to be breached by the underlying by Expiry of the Options Shorted. Therefore, CE Short must be initiated on OTM Strike above the Resistance level and the PE Short must be initiated on OTM Strike below the Support level. Further, CE Short and PE Short must be initiated at such Far OTMs Strike levels which have more or less same LTP or Delta value. This equal Delta value Short legs helps to ensure a reasonable balance between the profit & loss scenario between the two Short legs in this Strategy, and thus a natural hedge to each other until Breakeven Strike is not breached by the underlying in either direction. Basis aforesaid factors, suitable Far OTM CE & PE Option Strike levels of a particular Expiry series and nearly same Delta value may be selected for this Strategy. Since, the success of this Strategy	<u>Selection of Option Strikes:</u> Selection of the CE & PE Strikes must be such OTM Strikes which are not expected to be breached by the underlying by Expiry of the Options Shorted. Therefore, CE Short must be initiated on OTM Strike above the Resistance level and the PE Short must be initiated on OTM Strike below the Support level. Further, CE Short and PE Short must be initiated at such Far OTMs Strike levels which have more or less same LTP or Delta value. Likewise, CE Long and PE Long must be initiated at such Far OTMs Strike levels which have more or less same LTP or Delta value. This equal Delta value between both the Short legs and equal Delta value between both the Long legs, helps to ensure a reasonable balance between the profit & loss scenario between the two Short legs and between the two Long leg in this

is also mainly dependent on the quick arrival of the Theta decay (*besides rangebound movement of the underlying*), therefore closer Expiry series are preferable for this Strategy.

Strategy and therefore ensures Delta neutrality from the perspective of movement of the underlying, and thus a natural hedge to each other until Breakeven Strike is not breached by the underlying in either direction.

Further, when a rangebound view on the underlying has conviction (*i.e. the underlying would not breach the primary leg Short Strikes*), then a suitable **smaller Delta / Strike difference can be maintained** between the primary leg and the hedged leg, i.e. between CE Short & CE Long; and between PE Short & PE Long. This smaller Delta difference can be ensured by maintaining suitable smaller gap between the Strikes at which primary leg and the hedged leg are initiated of the same Expiry (*i.e. by opting for slightly closer Far OTM Strikes for the Long leg CE & PE side, having almost same premium value*). This smaller gap between the Short leg & Long leg (on each CE side & PE side) will bring the Risk to Reward Ratio much favourable. But the risk is that the Breakeven Strike gets shorter.

However, when the rangebound view on the underlying does not have conviction and there seems uncertainty about continuation of tight sideways move in the underlying, and it is not very sure in which direction the underlying may breakout, then a suitable **larger Delta/ Strike difference can be maintained** between the primary leg and the hedged leg, i.e. between CE Short & CE Long; and between PE Short & PE Long. This larger Delta difference can be

	maintained by maintaining suitable larger gap between the Strikes at which primary leg and the hedged leg are initiated of the same Expiry (i.e. by opting for farther OTM Long Strike for CE & PE side, having almost same premium value). Larger Strike difference between the primary leg and the hedged leg (<i>i.e. between the Short leg & Long leg on each CE side & PE side</i>) would ensure higher Net Premium Credit, which would ensure a larger Breakeven area. In such situation, Risk to Reward Ratio gets not so favourable. Basis aforesaid factors, suitable Far OTM CE & PE Option Strike levels of a particular Expiry series and nearly same Delta value may be selected for this Strategy. Since, the success of this Strategy is also mainly dependent on the quick arrival of the Theta decay (<i>besides rangebound movement of the underlying</i>), therefore closer Expiry series are preferable for this Strategy.
<u>If trade goes as per plan:</u> The underlying remains rangebound, then both the two Short legs will generate profit due to regular expansion and contraction of Time Value / Premium of the Far OTM Options due to such up & down movement of the underlying. Further, as the Expiry draws closer, the impact of Theta decay also starts to help generate profit in this Strategy, due to erosion in the Time Value / Premium of both the Short legs. Therefore, when until Expiry, the underlying remains within the range	<u>If trade goes as per plan:</u> The underlying remains rangebound, then both the two Short legs will generate profit due to regular expansion and contraction of Time Value / Premium of the Far OTM Options due to such up & down movement of the underlying. However, there will also be premium loss on both the hedged Long legs of the Strategy, but, the rangebound movement will still help achieve the maximum profit to the extent of aggregate Net Premium Credit in the Strategy.

defined by two Strikes Shorted, then the CE Short and PE Short leg expires worthless as OTMs generating full profit to the tune of the aggregate Premium Credit collected on this Strategy.

If underlying movement breaches the range but not the Breakeven Strike:

But if the underlying breaches either of the Strikes at which Shorts have been initiated but do not cross the Breakeven Strike of that side, then too this Strategy would yield some profit, however, such profit will be lesser than the aggregate Premium Credit collected on this Strategy by Shorting CEs & PEs. The profit generated on Expiry, in this situation when the underlying closes within the Profit Zone, shall be as per calculations already discussed above.

If trade does not go as per plan and the Breakeven Strike is breached by the underlying:

Since, this Strategy comprises of naked Short legs, therefore, if the underlying breaks the range defined by Shorting relevant Options, on either side, and starts trending after crossing beyond the Breakeven Strike of that side, then this Strategy will start yielding unlimited loss as the underlying keep trending in that direction and expires outside the Breakeven Strike. The unlimited Loss however can be calculated on Expiry, as per the calculations already discussed above. In such situations, when the underlying breaks the range in either side and gets trending beyond the Breakeven Strike of this Strategy, then some adjustments can be considered in order to contain the loss in this Strategy (*as discussed below here*).

Further, as the Expiry draws closer, the impact of Theta decay also starts to help generate profit in this Strategy, due to erosion in the Time Value / Premium of both the Short legs. However, there will also be premium loss on both the hedged Long legs of the Strategy due to Theta impact, but the Theta decay will still help achieve the maximum profit to the extent of aggregate Net Premium Credit in the Strategy.

Therefore, when until Expiry, the underlying remains within the range defined by two Strikes Shorted, then the CE Short and PE Short leg (*as well as both the Long legs*) expires worthless as OTMs generating full profit to the tune of the aggregate Net Premium Credit collected on this Strategy.

If underlying movement breaches the range but not the Breakeven Strike:

But if the underlying breaches either of the Strikes at which Shorts have been initiated but do not cross the Breakeven Strike of that side, then too this Strategy may yield some profit, however, such profit will be lesser than the aggregate Net Premium Credit collected on this Strategy. The profit generated on Expiry, in this situation when the underlying closes within the Profit Zone, shall be as per calculations already discussed above.

If trade does not go as per plan and the Breakeven Strike is breached by the underlying:

If the underlying breaks the range defined by Shorting relevant Options, on either side, and starts trending after

	crossing beyond the Breakeven Strike of that side, then this Strategy will start yielding loss. However, the loss in this Strategy will be limited because the Long position initiated on that side as the hedged leg will help curtail the loss arising from the Short leg whose side the Breakeven Strike has been breached by the underlying. The Loss however on Expiry will be limited and can be calculated on Expiry, as per the calculations already discussed above. In such situations, when the underlying breaks the range in either side and gets trending beyond the Breakeven Strike of this Strategy, then some adjustments can be considered in order to mitigate the loss in this Strategy (<i>as discussed below here</i>).
<u>Adjustments (if the Breakeven Strike is breached by the underlying and this Strategy does not go as per plan):</u> Since, this Strategy is a Premium Credit strategy, therefore, the aggregate Premium received (i.e. the sum of the Premium received on the CE Short and PE Short leg) need to be protected for profit from Expiry perspective. However, when the underlying breaks the range in either side and gets trending beyond the Breakeven Strike of this Strategy, then the potential unlimited loss situation may arise in this Strategy. The potential loss in this Strategy may be unlimited if the underlying keeps trending in one direction beyond the Breakeven Strike. This unlimited loss situation that may occur in this Strategy can be mitigated	<u>Adjustments (if the Breakeven Strike is breached by the underlying and this Strategy does not go as per plan):</u> Since, this Strategy is a combination of two Credit Spread (<i>i.e. on CE side & PE side</i>) and is an aggregate Net Premium Credit strategy, therefore, the aggregate Premium received (<i>i.e. the sum of the Net Premium received on the CE and PE leg</i>) need to be protected for profit from Expiry perspective. However, when the underlying breaks the range in either side and gets trending beyond the Breakeven Strike of this Strategy, then the potential Loss situation may arise in this Strategy, which would be limited to the extent of pre-calculated Max Loss as already discussed above.

through following adjustments: (i) Converting naked Short Strangle to Iron Condor; or (ii) Long Options; or (iii) Short CEs; or (iv) Short PEs. These adjustments are discussed below:

- (i) Conversion to Iron Condor: If the original view that the underlying would remain and close by Expiry within the range (*at best within the Breakeven Strike range of the Short Strangle*) appears to get uncertain, then immediately the naked Short Strangle must be converted to Iron Condor Strategy by initiating even Far OTM Long CEs and Long PEs (*of equal quantity as that of Short legs, and of same Expiry series as that of the Short Options*). This hedging of Short Strangle through Iron Condor will mitigate the potential risk of unlimited loss on Short Strangle into a pre-calculated Limited Loss situation. You may refer to the details of Iron Condor given on the other side of this Table for better understanding.

- (ii) Counter Adjustment through Long Option: If the underlying breaches the Breakeven Strike of this Strategy downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be trending downwardly with momentum, then **PEs can be bought** (*i.e. Long PEs to be initiated*). However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be trending upwardly with momentum,

Even though the potential Max Loss in this Strategy may be limited (as it is a hedged strategy), if the underlying keeps trending in one direction beyond the Breakeven Strike, but on aggregate basis when played with heavy volume, the limited Max Loss situation may yield substantial loss in absolute terms. This loss situation that may occur in this Strategy can be mitigated through following adjustments: (i) Long Options; or (ii) Short CEs; or (iii) Short PEs. These adjustments are discussed below:

- (i) Counter Adjustment through Long Option: If the underlying breaches the Breakeven Strike of this Strategy downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be trending downwardly with momentum, then **PEs can be bought** (*i.e. Long PE to be initiated of same Expiry series as original PE Long if the expiry is far, else of next farther Expiry series if Expiry is close*). However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be trending upwardly with momentum, then **CEs can be bought** (*i.e. Long CE to be initiated of same Expiry series as original CE Long if the Expiry is far, else of next farther Expiry series if Expiry is close*).

Buying CEs or PEs to protect the risk in this Strategy will add up additional debit positions, therefore this Long Options

then **CEs can be bought** (*i.e. Long CEs to be initiated*).

Buying CEs or PEs to protect the risk in this Strategy will add up debit position, therefore this Long Options position should only be prudent to initiate only if there is strong momentum in the direction where the underlying has breached the Breakeven Strike. This Long Options position will help overcome the potential unlimited loss amount that may incur in this Strategy. This adjustment through Long Options can be played by naked CEs or PEs (or by Bull or Bear Debit Strategy). Further, Long Options should be initiated at a Strike having Delta value higher than the current Delta value of the Short leg which has been breached by the underlying (*i.e. at a higher Strike than the PE sell Strike; and at a lower Strike than the CE sell Strike, as the case may be*), so if the underlying keep trending in direction it has breached the Short leg, the relevant Long Options position initiated as an adjustment should generate more profit than the loss generated by that Short leg. Adding naked Longs of higher Delta value in same quantity as on the Short leg, would convert that side into a Debit Vertical Spread. Also, depending upon the likely momentum in the underlying, suitable number of Long Options (CEs or PEs as the case may be) need to be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may

position should only be prudent to initiate only if there is strong momentum in the direction where the underlying has breached the Breakeven Strike. This Long Options position will help overcome the potential limited loss amount that may incur in this Strategy. This adjustment through Long Options can be played by naked CEs or PEs (or by Bull or Bear Debit Strategy). Further, Long Options should be initiated at a Strike having Delta value higher than the current Delta value of the Short leg which has been breached by the underlying (*i.e. at a higher Strike than the PE sell Strike; and at a lower Strike than the CE sell Strike, as the case may be*), so if the underlying keep trending in direction it has breached the Short leg, the relevant Long Options position initiated as an adjustment should generate more profit than the loss generated by that Short leg. Also, depending upon the likely momentum in the underlying, suitable number of Long Options (CEs or PEs as the case may be) need to be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Long Options position as an adjustment in comparison to the original number of Lots initiated on the Strategy. If the Long Options generates profit or reasonably minimizes the loss in this Strategy before Expiry, then it

be required to be added to Long Options position as an adjustment in comparison to the original number of Lots initiated on the Strategy. If the Long Options generates profit or reasonably minimizes the loss in this Strategy before Expiry, then it would be advisable to book the profit on this Long Options position and to exit this Strategy as a whole by booking minor loss or profit.

(iii) Counter Adjustment through Short Option:

If there seems to be a slow trend, after breaching the Breakeven Strike downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then Far OTM CEs **can be sold** (*i.e. Short CEs to be initiated*). However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be in a mild upwardly direction, then **PEs can be sold** (*i.e. Short PEs to be initiated*).

Idea in this adjustment is to pick up a suitable Far OTM Option for Shorting, such that this far OTM Option expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying after once

would be advisable to book the profit on this Long Options position and to exit this Strategy as a whole by booking minor loss or profit.

However, since the Max Loss situation in this Strategy is anyways limited, therefore instead of initiating Long Options as mentioned above, Shorting Options (i.e. Short CEs or Short PEs) as adjustments to mitigate limited Max Loss situation in this Strategy, as discussed below, can be considered.

(ii) Counter Adjustment through Short Option:

If there seems to be a slow trend, after breaching the Breakeven Strike downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then Far OTM CEs **can be sold** (*i.e. Short CEs to be initiated*). However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be in a mild upwardly direction, then Far OTM **PEs can be sold** (*i.e. Short PEs to be initiated*).

Idea in this adjustment is to pick up a suitable Far OTM Option for Shorting, such that this far OTM Option expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This additional Short

breaching the Breakeven Strike again reverses, then these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on the relevant Far OTM Options (CEs or PEs as the case may be), suitable number of Options can be Shorted as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to these additional Short Options position in comparison to the original number of Lots initiated on the Strategy. These additional Short Options position should be initiated at such Far OTM Strike(s), which may have reasonable Premium and is expected to expire worthless as OTM on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

- (iv) Adjustment through Pyramiding: If there seems to be a limited downward trend with momentum, after breaching the Breakeven Strike downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then additional Far OTM PEs **can be sold** (*i.e. Short PEs to be initiated*) below the Support area of the underlying,

Options position will help cover the potential loss that may be generated on this Strategy. Selection of a far OTM Option for this adjustment is important because even if the direction of the underlying after once breaching the Breakeven Strike again reverses, then these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on the relevant Far OTM Options (CEs or PEs as the case may be), suitable number of Options can be Shorted as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to these additional Short Options position in comparison to the original number of Lots initiated on the Strategy. These additional Short Options position should be initiated at such Far OTM Strike(s), which may have reasonable Premium and is expected to expire worthless as OTM on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

which is expected not to be breached by the underlying by Expiry. However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be trending with momentum upwardly upto a limited extent, then additional Far OTM CEs **can be sold** (*i.e. Short CEs to be initiated*) above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry.

Idea in this adjustment is to pick up a suitable much Far OTM Options for Shorting in the same direction in which the underlying has breached the Breakeven Strike, such that these additional far OTM Options (initiated as part of adjustments) expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. These additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of Far OTM Options for this adjustment is important because even if the trend of the underlying after breach of Breakeven Strike continues in that direction, these additional Short Options position must be at such Strike which can be expected to be not breached by the underlying by Expiry and to expire as OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the

(iii) Adjustment through

Pyramiding: If there seems to be a limited downward trend with momentum, after breaching the Breakeven Strike downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then additional Far OTM PEs **can be sold** (*i.e. Short PEs to be initiated of the same Expiry series as that of the original PE Short leg*) below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry. However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be trending with momentum upwardly upto a limited extent, then additional Far OTM CEs **can be sold** (*i.e. Short CEs to be initiated of the same Expiry series as that of the original CE Short leg*) above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry.

Idea in this adjustment is to pick up a suitable much far OTM Options for Shorting in the same direction in which the underlying has breached the Breakeven Strike, such that these additional far OTM Options (initiated as part of adjustments) expires worthless as an OTM on Expiry thereby giving full Premium at which Short is

likely mild trend of the underlying and the Premium available on relevant Far OTM Options (*i.e. in case of PE Shorts, below the Support area; and in case of CE Shorts, above the Resistance area*), suitable number of Options can be considered to be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these additional Short Options due to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short for this adjustment, in comparison to the original number of Lots initiated on the Strategy.

In this type of adjustment, additional Short Options positions can also be added in a pyramidal structure. That is:

- as the downtrend continues Far OTM PEs' Premium would rise, therefore, Short PEs positions can be added at subsequent lower Strike levels as the downtrend continues with lower PEs gaining decent Premium values. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16500 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 16400 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.*
- as the uptrend continues Far OTM CEs' Premium would rise,

initiated as profit. These additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of Far OTM Options for this adjustment is important because even if the trend of the underlying after breach of Breakeven Strike continues in that direction, these additional Short Options position must be at such Strike which can be expected to be not breached by the underlying by Expiry and to expire as OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on relevant Far OTM Options (*i.e. in case of PE Shorts, below the Support area; and in case of CE Shorts, above the Resistance area*), suitable number of Options can be considered to be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these additional Short Options due to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short for this adjustment, in comparison to the original number of Lots initiated on the Strategy.

In this type of adjustment, additional Short Options positions can also be added in a pyramidal structure. That is:

therefore, Short CE positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining decent Premium values. *For example, when the uptrend continues in Nifty, a Far OTM CE at 18000 having Premium of Rs. 50 can be sold, thereafter when the Nifty rises further, subsequent higher CE at 18200 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.*

This **Shorting of Options in a pyramiding manner** may ensure a broader Breakeven Strike (i.e. larger risk area protection) and thus greater probability of profiting due to Theta decay on these bunch of additional Short Options on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

- as the downtrend continues Far OTM PEs' Premium would rise, therefore, Short PEs positions can be added at subsequent lower Strike levels as the downtrend continues with lower PEs gaining decent Premium values. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16000 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 15800 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.*

- as the uptrend continues Far OTM CEs' Premium would rise, therefore, Short CEs positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining decent Premium values. *For example, when the uptrend continues in Nifty, a Far OTM CE at 18000 having Premium of Rs. 50 can be sold, thereafter when the Nifty rises further, subsequent higher CE at 18200 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.*

This **Shorting of Options in a pyramiding manner** may ensure a broader Breakeven Strike (i.e. larger risk area protection) and thus greater probability of

	profiting due to Theta decay on these bunch of additional Short Options on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.
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SHORT STRADDLE & IRONFLY / BUTTERFLY

When a view is formed that irrespective of the intermittent small directional movement of the underlying, eventually the underlying is expected to remain within a very tight defined range from its present price level; then such view can be played out by a neutral strategy employing Short Options positions at ATM CE & PE Strikes (or near ATM CE & PE same Strikes) which defines a very tight range within which the underlying is expected to remain by Expiry of those Options.

Thus, when the view on the underlying is that it is expected to remain within a tight/ narrow range upto the Expiry of relevant Options, and the same is played out by Shorting Naked ATM CE & PE Options (or near ATM CE & PE same Strikes) pertaining to that Expiry series (*by which the underlying is expected to remain in a range or sideways movement*), then such a Strategy is called **Short Straddle**. In Short Straddle Strategy, naked ATM CE & PE Options (or near ATM CE & PE same Strikes) are sold in equal quantity, on the same underlying pertaining to same Expiry series. In this Strategy, the expectation is that the underlying will remain, until the Expiry of the Options Shorted, within a very tight range from the present level (i.e. maximum within the Breakeven Strikes). Short Straddle involves naked Short positions on CE & PE Options (involving two legs only). Also, Short Straddle is a Strategy which generates Limited Profit, but can also generate Unlimited Loss if the tight range is breached by the underlying.

However, when the Short Straddle (naked Strategy) is hedged with Long Options on OTM CE & OTM PE Options (of Strikes having nearly same Delta values), then such Strategy is called **Iron Fly or Iron Butterfly Strategy** (also referred to as **Short Iron Fly or Short Iron Butterfly**)³⁰. In Iron Fly Strategy, there is (i) ATM CE Short (**CE primary leg**) and OTM CE Long (**CE hedged leg**), in equal quantity, on the same underlying pertaining to same Expiry series; and (ii) ATM PE Short (**PE primary leg**) and OTM PE Long (**PE hedged leg**),

³⁰Usually, when the OTM Long legs of both CE & PE sides are closer to the ATM in this Strategy, then it is referred to as Iron Fly; and when the Longs legs of both CE & PE sides are little farther away from the ATM in this Strategy, then it is referred to as Iron Butterfly Strategy.

in equal quantity, on the same underlying pertaining to same Expiry series. In essence, Iron Fly (like Iron Condor) is pairing of Bear Call Credit Spread Strategy and Bull Put Credit Spread Strategy (*which are having Short legs on a common Strike*); and in aggregate involves 4 legs. Like in Short Straddle, in Iron Fly too, the expectation is that the underlying will remain, until the Expiry of the Options Shorted, within a tight range from the current price level of the underlying (i.e. within the Breakeven Strike levels of the Strategy); however hedged legs are added to the both the Short legs of Short Straddle in order to ensure that:

- (i) if the underlying happens to slip upwardly beyond the Strike at which CE Short is initiated, by Expiry of the CE Options Shorted, then the CE hedged leg will cover up for the losses that may be incurred on the CE primary leg, thereby converting the unlimited Max Loss situation of Short Straddle into Limited Max Loss in IronFly; and
- (ii) if the underlying happens to slip downwardly beyond the Strike at which PE Short is initiated, by Expiry of the PE Options Shorted, then the PE hedged leg will cover up for the losses that may be incurred on the PE primary leg, thereby converting the unlimited Max Loss situation of Short Straddle into Limited Max Loss in IronFly.

Thus, Iron Fly is a Strategy which generates Limited Profit, but also has limited risk (as it will generate Limited Max Loss, if the range is breached by the underlying).

With this background, now let us delve into discussing the Short Straddle Strategy and Iron Fly Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Short Straddle Strategy	Iron Fly Strategy
<u>Trade Legs:</u> • <i>Short CE ATM Strike (primary CE leg); and</i> • <i>Short PE ATM Strike (primary PE leg)</i>	<u>Trade Legs:</u> • <i>Short CE ATM Strike (CE primary leg)</i> • <i>Long CE of OTM Strike (CE hedged leg); and</i> • <i>Short PE ATM (PE primary leg)</i>

Both Short legs would be of same Expiry series, and in equal number of Lots in both primary legs.	• <i>Long PE of OTM Strike (PE hedged leg)</i> All the 4 legs (<i>i.e. two Short legs & two Long legs</i>) would be of same Expiry series, with equal quantity in each of the aforesaid four legs. The Long Options for the hedged leg would be of nearly same Premium value. It is a hedged Short Straddle, making a pair of Bear CE Credit Strategy and Bull PE Credit Strategy.
Example: <i>If ATM is at 17000, then for Short Straddle:</i> • <i>Sell 10 Lot Nifty 17000 CE of Next Week Expiry (at Rs. 250 per Lot); and</i> • <i>Sell 10 Lot Nifty 17000 PE of Next Week Expiry (at Rs. 275 per Lot)</i>	Example: <i>If ATM is at 17000, then for Iron Fly:</i> • <i>Sell 5 Lot Nifty 17000 CE of Current Month Expiry series (at Rs. 250 per Lot)</i> • <i>Buy 5 Lot Nifty 17300 CE of Current Month Expiry series (at Rs. 100 per Lot); and</i> • <i>Sell 5 Lot Nifty 17000 PE of Current Month Expiry series (at Rs. 275 per Lot)</i> • <i>Buy 5 Lot Nifty 16700 PE of Current Month Expiry series (at Rs. 110 per Lot)</i>
Objective: Objective is to play a Neutral / Non-directional or sideways / rangebound view, through selling naked ATM CEs and PEs (both as the primary leg), as the expectation is that the underlying will remain, until the Expiry of the Options Shorted, within a tight range from the current price levels of the underlying and	Objective: Objective is to play a Neutral / Non-directional or sideways / rangebound view, through selling naked ATM CEs and PEs (both as the primary leg), as the expectation is that the underlying will remain, until the Expiry of the Options Shorted, within a tight range from the current price levels of the underlying and thus the Options Shorted would expire

thus the Options Shorted would expire within their Breakeven Strike range.

Since, maximum Time Value in absolute number is at ATM Strikes and also Theta is maximum at ATM Strikes, therefore if the technical view is that there will not be much directional move of the underlying until the expiry of the Options Shorted/ intended to be Shorted, then this Strategy may be implemented to harness profit from the aggregate Premium Credit collected on this Strategy by Shorting ATM Options due to tight rangebound move in the underlying coupled with Theta impact of Expiry.

It is a Credit Strategy, as both the Short legs get the credit of the Premium at which ATM Strike Options are sold. Accordingly, this Strategy generates limited profit to which may extend upto the maximum extent of Premium collected on both the Short legs.

However, if the underlying breaches the Breakeven Strike on either side (*CE side or PE side*), then this Strategy would get exposed to unlimited Loss potential. In such a situation, the deeper the trend continues, more would be the Loss generated on this Strategy.

within the Breakeven Strike range of this Strategy.

Since, maximum Time Value in absolute number is at ATM Strikes and also Theta is maximum at ATM Strikes, therefore if the technical view is that there will not be much directional move of the underlying until the Expiry of the Options Shorted/ intended to be Shorted, then this Strategy may be implemented to harness profit from the aggregate Premium Credit collected on this Strategy by Shorting ATM Options due to tight rangebound move in the underlying coupled with Theta impact of Expiry.

It is a Net Premium Credit Strategy, as both the Short legs get the credit of the Premium at which ATM Strike Options are sold; and both the Long hedged legs incur lower Premium debit on the Strategy. Accordingly, this Strategy generates limited profit to which may extend upto the maximum extent of Net Premium Credit collected on the Strategy.

Further, in this Strategy: in order to mitigate the risk / loss that may arise if the primary legs are breached by the underlying, equal number of OTM Long Options are also initiated simultaneously with the primary Short legs, such that this Strategy becomes hedged Short Straddle, comprising of a pair of Bear CE Credit Strategy and Bull PE Credit Strategy (*which are having Short legs on a common Strike*).

Thus, in effect, Iron Fly comprising of Bull PE Credit Strategy and Bear CE Credit Strategy, which converts the

	naked Short Straddle into a hedged Short Straddle so as to cover and limit the unlimited loss that may arise in a naked Short Straddle positions, to a limited Max Loss situation, if the underlying breaches the range defined by the primary leg (on either side) and gets trending in that direction.
<u>Demerits:</u> • It comprises of naked Short positions. • Since this Strategy is implemented by Shorting ATM CEs and PEs (or near ATM same Strike CEs & PEs), it requires more capital/ margin and also sufficient capital for MTM adjustments also need to be ensured. • This Strategy generates limited profit to the maximum extent of Premium collected on both the Short legs. Profit is generated on this Strategy only if the underlying remains within the tight range from the current price levels of the underlying (and the Options Shorted would expire within their Breakeven Strike range). • If the underlying breaks out and breaches the range beyond the Breakeven Strike of the Shorted Option, on either side, then this Strategy may yield unlimited loss. Thus, this Strategy is the kind with limited profit and unlimited loss. • During low Volatility period and close to Expiry period, sufficient Premium may not be available in	<u>Demerits:</u> • Since, in this Strategy on each CE and PE sides, there is one Short position initiated at a higher Premium (on ATM Strike or near ATM Strikes) and a Long position initiated at a OTM Strike with lower Premium, therefore, this Strategy have a Net Premium Credit (<i>i.e. Premium received on Short leg – Premium paid on Long leg</i>). This Net Credit Premium on Iron Fly Strategy is less than the aggregate Premium Credit on naked Short Straddle. Therefore, the quantum of profit is less in Iron Fly than in Short Straddle if the underlying remains on Expiry within the Breakeven Strike range defined by the Short legs (initiated on the same Strikes in Iron Fly and Short Straddle). • When Short Straddle is hedged and is played in the form of Iron Fly, then the profit gets squeezed (<i>due to lesser Net Premium Credit</i>) in Iron Fly, as compared to Short Straddle. Also, the Breakeven Level gets narrowed down in Iron Fly, thereby reducing the area upto which profit can occur (due to lesser Premium

ATM CEs and PEs, making this Strategy not viable from of profit amount perspective. • If there is a Volatility spike, then both the Short legs, will get adversely impacted as there will addition of Time Value in the premium of both the Options (<i>even if there is not much movement in the underlying in any particular direction</i>). This volatility spike may exhibit virtual loss on the Strategy.	Credit in Iron Fly), implying that if the underlying takes momentum in one side then the chances of breaching the Breakeven Strike on that side increases (<i>hence slightly enhancing loss probability; which ofcourse in Iron Fly is limited</i>). Thus, this Strategy has lesser profit potential than naked Short Straddle. • If there is a Volatility spike, then both the Short legs, will get adversely impacted but the Long leg would get favourably impacted, as there will addition of Time Value in the premium of both the Short & Long Options. This Volatility spike may exhibit virtual loss on the Strategy (<i>even if there is not much movement in the underlying in any particular direction</i>).
<u>Benefits of Short Straddle:</u> • This Strategy is suitable for a very tight rangebound / sideways view. A very narrow rangebound movement of the underlying within the tight range from the current price levels of the underlying (<i>i.e. within the Breakeven Strike range of this Strategy</i>), generates profit in both the ATM Short legs due to erosion of time value owing to such movement in the underlying. • With the passage of time, if the underlying remains within the narrow range as expected, then both the Short legs continues to be ATM Strikes or one near OTM & another near ITM, consequently generating	<u>Benefits of Iron Fly:</u> • It is a hedged Strategy (<i>i.e. Iron Fly is hedged Short Straddle</i>). Consequently, the unlimited Max Loss potential in naked Short Straddle gets capped to a pre-defined limited Max Loss in Iron Fly. • Since, it is a hedged Strategy, the capital / margin required is less as compared to Short Strangle and does not require much capital towards any MTM requirements. • Since, less capital is required to implement this Strategy as compared to Short Straddle, more quantity/ Lots can be initiated in

profit in this Strategy, due to the rising Theta impact. If by Expiry of the Options Shorted, if the underlying remains within the tight range in this Strategy and the Options Shorted would expire within their Breakeven Strike range, then both the Shorted legs would expire worthless as ATM (or one of them would become OTM and expire worthless and another as near ITM yet having less Premium left due to Theta effect on Expiry), generating profit on this Strategy or a lesser profit. • In this Strategy, two factors help in generating profit: (i) very tight rangebound move in the underlying; and (ii) Theta impact on the primary legs. Therefore, this Strategy can yield decent profit if the tight range is maintained by the underlying. • Due to the increasing Theta impact with the approach of Options Expiry, this Strategy becomes suitable for deployment near Expiry if the view is aligned and favourable. • It is a Credit Strategy. Since both Short legs comprises of selling ATM Strikes, the Premium on both Short legs is the amount of aggregate Premium collected. Accordingly, in this Strategy, the Credit of Premium need to be protected for profit in this Strategy. • The aggregate Credit Premium collected on both Short legs, increases the loss area in this Strategy by defining the Breakeven Strike. Thus, from Expiry perspective, the	this Strategy for same amount of capital as compared to the Short Straddle. • While this Strategy has 2 Short Options (as primary legs) and 2 Long Options (as hedged legs), this Strategy is a Net Premium Credit Strategy as the Shorts are initiated at higher Premium than the Longs on the respective CE / PE sides between their primary and hedged legs. • Since, this a hedged Strategy, therefore, any breakout by the underlying before Expiry on either side of the defined range is covered by the Long Options hedged leg on that side. Thus, this Strategy helps curtail the unlimited loss situation that may arise in Short Straddle owing to the Long Options positions added in this Strategy (<i>provided such Long Options do not loose their Premium significantly due to Volatility crash or Theta decay</i>). • This Strategy is suitable for a very tight rangebound / sideways view. A very narrow rangebound movement of the underlying within the tight range from the current price levels of the underlying (i.e. within the Breakeven Strike range of this Strategy), generates profit in both the ATM Short legs due to erosion of Time Value owing to such movement in the underlying. • With the passage of time, if the underlying remains within the narrow range as expected, then both the Short legs continues to be ATM
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underlying must not go down and cross below the Breakeven Strike of PE Short Strike and on the upper side the underlying must not go up and cross above the Breakeven Strike of CE Short Strike (*the Breakeven Strikes in this Strategy are discussed below*).

- Volatility crash is favourable on the Strategy, as the reduction in volatility causes erosion in the Time Value of both the primary Short legs, which yield profit on the Strategy.
- However, Volatility spike will cause addition of Time Value in the premium of both the Options (even if there is not much movement in the underlying in any particular direction), thus exhibiting virtual loss on the Strategy. But so long the Breakeven Strike is not breached on either side by Expiry, then inspite of increase in premium value and virtual loss on the Strategy due to volatility spike, there will not be an actual loss scenario on the Strategy.

Strikes or one near OTM & another near ITM, consequently generating profit in this Strategy due to the rising Theta impact. If by Expiry of the Options Shorted, if the underlying remains within the tight range in this Strategy and the Options Shorted would expire within their Breakeven Strike range, then both the Shorted legs would expire worthless as ATM (or one of them would become OTM and expire worthless and another as near ITM yet having less Premium left due to Theta effect on Expiry), generating profit on this Strategy.

- In this Strategy, two factors help in generating profit: (i) very tight rangebound move in the underlying; and (ii) Theta impact on the primary legs. Therefore, this Strategy can yield decent profit if the tight range is maintained by the underlying.
- Due to the increasing Theta impact with the approach of Options Expiry, this Strategy becomes suitable for deployment near Expiry if the view is aligned and favourable.
- Volatility crash is favourable on the Strategy, as the reduction in volatility causes erosion in the Time Value of both the primary leg (as well as the hedged leg), which eventually yield profit on the Strategy.
- However, Volatility spike will cause addition of Time Value in the premium of both the Long & Short legs (*even if there is not much*

	<i>movement in the underlying in any particular direction</i>), thus exhibiting some virtual loss on the Strategy. But so long the Breakeven Strike is not breached on either side by Expiry, then inspite of increase in premium value and virtual loss on the Strategy due to volatility spike, there will not be an actual loss scenario on the Strategy.
<u>Breakeven Strike of this Strategy from Expiry perspective:</u> This Strategy comprises of naked ATM CE Short; and a naked ATM PE Short (or Shorts initiated at same CE & PE Strike near ATM). This is an aggregate Credit Strategy as the Premium at which both Shorts are initiated, on aggregate basis is the total Premium Credit received. The CE Short leg determines the upper range; and the PE Short leg determines the lower range in this Strategy. The Breakeven on the upper side (i.e. CE side) and lower side (i.e. PE side), is determined as follows: • <u>The Breakeven Strike on the CE side (upper side) is:</u> The CE Strike (at which Short is initiated) + aggregate Premium Credit received on both CE & PE Shorts; and • <u>The Breakeven Strike on the PE side (lower side) is:</u> The PE Strike (at which Short is initiated) - aggregate Premium Credit received on both CE & PE Shorts. Thus, if by Expiry of the relevant Options which have been Shorted, if the underlying does not breach the aforesaid	<u>Breakeven Strike of this Strategy from Expiry perspective:</u> The CE side (upper side) comprises of CE Short primary leg at higher Premium and CE Long hedged leg at lower Premium. Thus, there is a Net Premium Credit on the CE side of Iron Fly. Likewise, the PE side (lower side) comprises of PE Short primary leg at higher Premium and PE Long hedged leg at lower Premium. Thus, there is a Net Premium Credit on the PE side of Iron Fly. The sum of the Net Premium Credit on the CE and PE Side is the aggregate Net Premium Credit received in this Strategy. Accordingly: • <u>the Breakeven Strike of the CE side in this Strategy (upper range) is:</u> CE Short primary leg + the aggregate Net Premium Credit in the Strategy; and • <u>the Breakeven Strike of the PE side in this Strategy (lower range) is:</u> PE Short primary leg - the aggregate Net Premium Credit in the Strategy.

Breakeven Strikes (either on the upper side or the lower side), then this Strategy would yield profit; but if by Expiry of the relevant Options, the underlying breaches either upper or lower side and goes beyond the relevant Breakeven Strike then the Strategy would yield loss. In case of continuous movement of the underlying after breaching of the Breakeven Strike on either side by the underlying, an unlimited loss situation would arise.

For example: If ATM is at 17000, then for Short Straddle: If Nifty 17000 PE is sold at Rs. 100 per Lot & Nifty 17000 CE is sold at Rs. 150 per Lot, then the BE Strike of this Strategy will be:

- *On CE side: $17000 + (100+150) = 17250$ CE Strike; and*
- *On PE side: $17000 - (100+150) = 16750$ PE Strike*

Thus, while this Strategy might yield total aggregate Premium of Rs. 250 per Lot as full profit if the underlying remains at 17000 on Expiry.

However, if Nifty crosses 17000 Strike upwardly then this Strategy would not yield loss so long the Breakeven Strike of 17250 is not breached upwardly by Nifty till Expiry of Options Shorted. Likewise, if Nifty crosses 17000 Strike downwardly then this Strategy would not yield loss so long the Breakeven Strike of 16750 is not breached downwardly by Nifty till Expiry of Options Shorted.

Therefore, in this Strategy, unlimited loss situation would arise, if either on the upside (i.e. CE side) or downside (i.e. PE

Thus, if by Expiry of the relevant Options, if the underlying does not breach the aforesaid Breakeven Strikes (*either on the upper side or the lower side*), then this Strategy would yield profit; but if by Expiry of the relevant Options, the underlying gets trending either on the upper side or lower side and goes beyond the relevant Breakeven Strike on that side, then the Strategy would yield loss.

In case of continuous movement of the underlying after breaching of the Breakeven Strike on either side by the underlying, and closing downwardly below the PE Long Strike or closing above the CE Long Strike, would yield quantified Max Loss on this Strategy (**Limited Loss situation**).

For example: If Nifty 17000 CE is sold at Rs. 250 per Lot & Nifty 17300 CE is bought at Rs. 150, for the CE side of this Strategy; and

Nifty 17000 PE is sold at Rs. 200 per Lot & Nifty 16700 PE is bought at Rs. 100 per Lot, for the PE side of this Strategy, then:

the Net Premium Credit received on this Strategy will be: $[(250+200) - (150+100)] = 450 - 250 = 200$

- *Breakeven Strike of this Strategy on upper range (CE side) will be: $17000 + 200 = 17200$ CE*
- *Breakeven Strike of this Strategy on lower range (PE side) will be: $17000 - 200 = 16800$ PE*

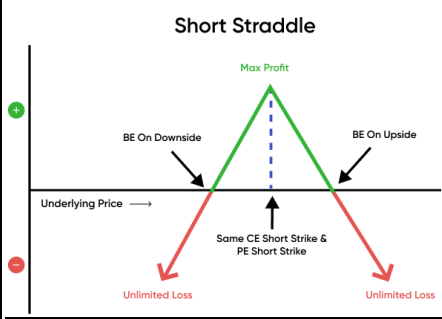
Thus, in the aforementioned example: if the underlying breaches the upper Breakeven Strike i.e. 17200 CE and

side), the underlying breaks-out and closes by Expiry beyond the Breakeven Strike level of that particular side.

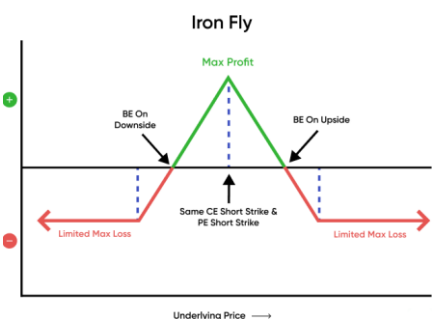
keeps trending higher then the loss caused on account of 17000 CE Short primary leg would get mitigated to some extent by the 17300 CE Long hedged leg. However, if the uptrend continues and the underlying closes by Expiry beyond the CE Long leg, then only limited max Loss on the CE side would accrue on the Strategy. Thus, this Strategy helps avoiding an unlimited loss situation, in the event of a continuous uptrend.

Likewise, if the underlying breaches the lower Breakeven Strike i.e. 16800 PE and keeps trending lower, then the loss caused on account of 17000 PE Short primary leg would get mitigated to some extent by the 16700 PE Long hedged leg. However, if the downtrend continues and the underlying closes by Expiry beyond the PE Long leg, then only limited max Loss on the PE side would accrue on the Strategy. Thus, this Strategy helps avoiding an unlimited loss situation, in the event of a continuous downtrend.

Payoff Chart for Short Straddle



Payoff Chart for Iron Fly



Loss in this Strategy:

Since, this Strategy comprises of naked Short legs, therefore if the underlying breaks the Breakeven Strike range defined by Shorting relevant Options, on either side, and starts trending after crossing beyond the Breakeven Strike of that side, then this Strategy will start yielding unlimited loss as the underlying keep trending in that direction and closes by Expiry outside the Breakeven Strike.

In this situation, the Short leg of that side Option (*where the BE Strike is breached*) becomes an ITM. The other side Short Option leg becomes even farther OTM. This situation generates the Unlimited Max Loss situation on the Strategy.

Level of starting unlimited loss on the upside (i.e. CE side):

If the underlying, gets bullish and breaches the Breakeven Strike on the CE side of the Strategy and closes higher than the BE Strike on the CE side, then this Strategy would yield loss on the upside. Higher the underlying would close by Expiry after breaching the BE Strike on the CE side, higher will be the loss. The loss situation is unlimited, if the underlying keeps trending higher by Expiry. This is because the CE Short Strike becomes an ITM (*while the CE Long Strike becomes an even farther OTM*).

Level of starting unlimited loss on the downside (i.e. PE side):

If the underlying, gets bearish and breaches the Breakeven Strike on the PE side of the Strategy and closes lower than the BE Strike on the PE side, then this Strategy would yield loss on the

Loss in this Strategy:

Max Loss on this Strategy occurs when the underlying breaches the Breakeven Strike of either side and eventually closes by Expiry at or higher than the CE Long leg of the Strategy or if the underlying closes at or lower than the PE Long Strike of the Strategy.

In this situation, both the Short & Long leg of that side Option (*where the BE Strike is breached*) becomes an ITM. The other side Options, both Long & Short leg becomes even farther OTM. This situation generates the Limited Max Loss situation on the Strategy.

Calculation of Max Loss:

Maximum loss in this Strategy will be limited and can be pre-calculated. The Maximum Loss in this Strategy is calculated as:

Max Loss for CE side: is calculated as:

- [*Strike difference between CE Long Strike and CE Short Strike*]
- minus**
- [*aggregate of Net Premium Credit received on CE side & PE side on this Strategy*].

Max Loss for PE side: is calculated as:

- [*Strike difference between PE Short Strike and PE Long Strike*]
- minus**
- [*aggregate of Net Premium Credit received on CE side & PE side on this Strategy*]

downside. Lower the underlying would close by Expiry after breaching the BE Strike on the PE side, higher will be the loss. The loss situation is unlimited, if the underlying keeps trending lower by Expiry. This is because the PE Short Strike becomes an ITM (<i>while the PE Long Strike becomes an even farther OTM</i>). <u>Calculation of final loss amount on the Strategy:</u> If the underlying closes by Expiry, after breaching the Breakeven Strike on either side, then the Loss accrued on the Strategy on Expiry can be calculated as: • [the final premium value of Short Option of the momentum side on Expiry (<i>i.e. Short leg which becomes / expires as an ITM</i>)]³¹ minus • the aggregate Premium Credit collected by Shorting both CE & PE Options. More the underlying closes beyond the BE Strike on either side, higher will be the loss generated by the Short leg of that side Option. <i>For example: If ATM is at 17000, then for Short Straddle:</i> <i>If Nifty 17000 PE is sold at Rs. 100 per Lot & Nifty 17000 CE is sold at Rs. 150 per Lot, then the BE Strike of this Strategy will be (basis the total Premium Credit of Rs 250 per Lot collected on the Strategy):</i>	<u>Impact on Max Loss situation, due to variation in Strike Difference between CE side & PE side:</u> If the Strike difference between Short leg & Long leg, on both CE side and PE side is same (<i>eg: 300 point difference between CE Short & CE Long and 300 point difference between PE Short & PE Long</i>), then the Max Loss would be same for the CE side as well as for the PE side. In such case, the amount so determined, is said to be the Max Loss of the Strategy. However, if the Strike difference between Short leg & Long leg, on CE side and PE side is different (<i>eg: 300 point difference between CE Short & CE Long and 500 point difference between PE Short & PE Long</i>), then the Max Loss would be different for the CE side and the PE side. The side where the Strike difference is more, would have more Net Premium Credit and accordingly the BE Level of that side will also increase. But with increase in BE Level, the Max Loss situation on that side would also increase. In such case, the Max Loss of the side where Strike difference is more, would be the Max Loss of the Strategy. <u>Level of starting loss on the Strategy and Loss Zone:</u> If the underlying breaks-out and starts trending after crossing beyond the Breakeven Strike of either side, then this Strategy will start yielding loss. Thus, breaching the BE Level on either side, is
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³¹ The final LTP (i.e. Premium value) of the Option, if it expires as an ITM, would be equal to the Intrinsic Value (i.e. the difference between the relevant ITM Strike and ATM Strike on Expiry).

*BE on CE side: 17250 CE Strike; and
BE on PE side: 16750 PE Strike.*

Therefore, if by Expiry Nifty falls below 16750 and Expiry is at 16500 (as ATM), then PE Short leg of 17000 will be an ITM with final LTP of about Rs. 500 (because on Expiry, final LTP of this PE strike will be equal to its Intrinsic Value, which is calculated as PE ITM Strike – ATM Strike = 17000 – 16500 = 500).

Thus, the Loss incurred in this strategy will be: $500 - 250 = \text{Rs. } 250$ per qty in a Lot, i.e. $250 \times 50 = \text{Rs. } 12,500$ per Lot.

the Level from which loss would start on the Strategy.

Loss Zone on the CE side: If the underlying, gets bullish and breaches the Breakeven Strike on the CE side of the Strategy and closes higher than the BE Strike on the CE side, then this Strategy would yield loss on the upside. Higher the underlying would close by Expiry after breaching the BE Strike on the CE side, higher will be the loss. But if the underlying closes by Expiry, at or beyond the CE Long leg then the Limited Max Loss situation would accrue on this Strategy (i.e. *applicable Max Loss on CE side, as per Max Loss calculations given above*).

Thus, the Loss zone on the CE side, is the BE Strike on the CE side till CE Long Strike and higher. If the underlying closes by Expiry within this Loss Zone, but towards the BE Strike on the CE side then the loss on the Strategy will be lower; but if the underlying closes towards the CE Long Strike within the zone, then the loss on the Strategy would be relatively more. In this Loss zone, the CE Short leg becomes an ITM, whereas the CE Long leg remains an OTM.

Loss Zone on the PE side: If the underlying, gets bearish and breaches the Breakeven Strike on the PE side of the Strategy and closes lower than the BE Strike on the PE side, then this Strategy would yield loss on the downside. Lower the underlying would close by Expiry after breaching the BE Strike on the PE side, higher will be the loss. But if the underlying closes by Expiry, at or beyond the PE Long leg then the Limited Max

	Loss situation would accrue on this Strategy (<i>i.e. applicable Max Loss on PE side, as per Max Loss calculations given above</i>). Thus, the Loss zone on the PE side, is the BE Strike on the PE side till PE Long Strike and lower. If the underlying closes by Expiry within this Loss Zone, but towards the BE Strike on the PE side then the loss on the Strategy will be lower; but if the underlying closes towards the PE Long Strike within the zone, then the loss on the Strategy would be relatively more. In this Loss zone, the PE Short leg becomes an ITM, whereas the PE Long leg remains an OTM. <u>Calculation of final loss amount on the Strategy within the Loss Zone:</u> If the underlying closes by Expiry within the Loss Zone (<i>either on CE side or PE Side</i>), then the Loss on Expiry will be calculated as: • [the final premium value of Short Option of the momentum side on Expiry (<i>i.e. Short leg which becomes / expires as an ITM</i>)]³² minus • the Net Premium Credit collected on the overall Strategy. <i>For example: If Nifty 17000 CE is sold at Rs. 250 per Lot & Nifty 17300 CE is bought at Rs. 150, for the CE side of this Strategy; and Nifty 17000 PE is sold at Rs. 200 per Lot & Nifty 16700 PE is bought</i>
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³² The final LTP (i.e. Premium value) of the Option, if it expires as an ITM, would be equal to the Intrinsic Value (i.e. the difference between the relevant ITM Strike and ATM Strike on Expiry).

at Rs. 100 per Lot, for the PE side of this Strategy, then:

- the Net Premium Credit received on this Strategy will be: $[(250+200) - (150+100)] = 450 - 250 = 200$
- BE Strike on CE side = $17000 + 200 = 17200$ CE
- BE Strike on PE side = $17000 - 200 = 16800$ PE

In the aforesaid example:

Max Loss on the CE side (i.e. if the underlying breaches the CE Long Strike of 17300 CE on the upside, will be: $[17300 - 17000] - [200] = 300 - 200 = 100$ per qty i.e. $\text{Rs } 100 \times 50 = \text{Rs. } 5000$ per Lot

Max Loss on the PE side (i.e. if the underlying breaches the PE Long Strike of 16700 PE on the downside, will be: $[17000 - 16700] - [200] = 300 - 200 = \text{Rs. } 100$ qty i.e. $\text{Rs } 100 \times 50 = \text{Rs. } 5000$ per Lot

Here, because the Strike difference on both CE side and PE side (between the Short leg & Long leg) is the same (i.e. 300 on both side), therefore, the Max Loss on both CE side & PE side is same (i.e. Rs. 5000)

However, if by Expiry, Nifty rises above and closes at 17250 Strike (as ATM), i.e., within the Loss Zone on the CE side, then CE Short leg of 17000 will be an ITM with final LTP of about Rs. 250 (because on Expiry, final LTP of this CE Strike will be equal to its Intrinsic Value, which is calculated as $\text{ATM Strike} - \text{CE ITM Strike} = 17250 - 17000 = 250$).

	<i>Thus, the Loss incurred in this Strategy will be: $250 - 200 = \text{Rs. } 50 \text{ per qty in a Lot}$, i.e. $50 \times 50 = \text{Rs. } 2500 \text{ per Lot}$.</i>
<u>Profit in this Strategy:</u> <u>Max Profit scenario:</u> By Expiry of the relevant Options which have been Shorted, if the underlying closes at the same Strike (on which Shorts have been initiated), then the entire Premium Credit collected on the Strategy, shall be the Max Profit in this Strategy. <u>Max Profit Level:</u> Thus, Max Profit level: Is the Strike at which Shorts have been initiated. If underlying closes by Expiry at this Strike, then Max Reward is generated by the Strategy. <u>Profit zone:</u> In the event the underlying moves beyond the Strike at which Shorts have been initiated but do not cross the Breakeven Strike of that side, then too this Strategy would yield some profit. Therefore, the overall profit zone on the Strategy ranges from BE Strike on the CE side to BE Strike on the PE side. If the underlying closes anywhere within this zone by Expiry, then the Strategy will generate profit. <u>On the CE side:</u> if the underlying closes, between the CE Short Strike and the BE level of the Strategy on the CE side range, then some profit would be generated by the Strategy. If the underlying closes by Expiry near the CE Short Strike within this zone, then profit will be relatively more; than if the underlying closes near the BE Strike range on the CE side within	<u>Profit in this Strategy:</u> <u>Max Profit scenario:</u> The aggregate Net Premium Credit received on this Strategy, which is notionally credited at the time of initiating this Strategy, is the Maximum Profit / Reward in this Strategy, i.e. aggregate Premium Credit received on the Strategy (i.e. <i>sum of Premium Credit received on CE Short & PE Short legs</i>) minus aggregate Premium Paid on this Strategy (i.e. <i>sum of Premium paid on CE Long & PE Long legs</i>). <u>Max Profit Level:</u> Thus, Max Profit level: Is the Strike at which Shorts have been initiated. If underlying closes by Expiry at this Strike, then Max Reward is generated by the Strategy. <u>Profit zone:</u> In the event the underlying moves beyond the Strike at which Shorts have been initiated but do not cross the Breakeven Strike of that side, then too this Strategy would yield some profit. Therefore, the overall profit zone on the Strategy ranges from BE Strike on the CE side to BE Strike on the PE side. If the underlying closes anywhere within this zone by Expiry, then the Strategy will generate profit. <u>On the CE side:</u> if the underlying closes, between the CE Short Strike and the BE level of the Strategy on the CE side range, then some profit would be generated by the Strategy. This is the

this zone. Therefore, the profit zone on the CE side is: when the underlying closes by Expiry between the CE Short Strike and the BE Strike level on the CE side.

On the PE side: if the underlying closes, between the PE Short Strike and the BE level of the Strategy on the PE side profit zone, then some profit would be generated by the Strategy. If the underlying closes by Expiry near the PE Short Strike within the profit zone, then profit will be relatively more; than if the underlying closes within the profit zone, near the BE Strike on the PE side. Therefore, the profit zone on the PE side is: when the underlying closes by Expiry between the PE Short Strike and the BE Strike level on PE side.

Calculation of final profit on the Strategy in the Profit Zone:

If the underlying goes beyond the Strike at which Shorts have been initiated, but do not cross the Breakeven Strike of that side and closes within the profit zone (of that side) by Expiry, then too this Strategy would yield some profit. This profit in such situation will be calculated as:

- [aggregate Premium Credit collected on the Strategy]
- minus**
- [final LTP value, on Expiry, of the Option, which expires as an ITM]³³

For example: If ATM is at 17000, then for Short Straddle: If Nifty 17000 PE is sold at

Profit zone on the CE side. If the underlying closes by Expiry near the CE Short Strike within this zone, then profit will be relatively more; than if the underlying closes near the BE Strike range on the CE side within this zone. Therefore, the profit zone on the CE side is: when the underlying closes by Expiry between the CE Short Strike and the BE Strike level on the CE side.

On the PE side: if the underlying closes, between the PE Short Strike and the BE level of the Strategy on the PE side profit zone, then some profit would be generated by the Strategy. If the underlying closes by Expiry near the PE Short Strike within the profit zone, then profit will be relatively more; than if the underlying closes within the profit zone, near the BE Strike on the PE side. Therefore, the profit zone on the PE side is: when the underlying closes by Expiry between the PE Short Strike and the BE Strike level on PE side.

Calculation of final profit on the Strategy in the Profit Zone:

If the underlying breaches the Strike at which Shorts have been initiated (*on either side*), but do not cross the Breakeven Strike of that side and closes within the profit zone (of that side) by Expiry, then too this Strategy would yield some profit. This profit in such situation will be calculated as:

³³ The final LTP (i.e. Premium value) of the Option, if it expires as an ITM, would be equal to the Intrinsic Value (i.e. the difference between the relevant ITM Strike and ATM Strike on Expiry).

Rs. 100 per Lot & Nifty 17000 CE is sold at Rs. 150 per Lot, then the BE Strike of this Strategy will be:

On CE side: 17250 CE Strike; and

On PE side: 16750 PE Strike.

Thus, if the underlying by Expiry of the Options Shorted, closes at the same Strike on which the two Short legs are initiated and consequently both the Short legs expire as an OTM/ ATM, then the entire Rs. 250 aggregate Premium shall be the Max Profit in this Strategy.

However, if Nifty moves higher than the 17000 CE Strike, but does not breach the Breakeven Strike of 17250 on the upper side and expire at 17200 ATM, then the Max Profit in this Strategy will be the final LTP of the 17000 CE Short leg (which would be an ITM having higher Premium by Expiry, say Rs. 200) minus Rs. 250 (aggregate Premium Credit received on this Strategy) = Rs. 50 per Lot.

Thus, overall profit on this Strategy got reduced (from a total Premium Credit of Rs. 250 on the overall Strategy, to Rs. 50 only) as the Strike at which Short was initiated was breached by Expiry (but loss in this Strategy did not occur because the Breakeven Strike of 17250 CE was not breached by Expiry).

- [the Net Premium Credit collected on the overall Strategy]

minus

- [final LTP value of the Short Option leg, on Expiry, which expires as an ITM]³⁴

For example: If Nifty 17000 CE is sold at Rs. 250 per Lot & Nifty 17300 CE is bought at Rs. 150, for the CE side of this Strategy; and Nifty 17000 PE is sold at Rs. 200 per Lot & Nifty 16700 PE is bought at Rs. 100 per Lot, for the PE side of this Strategy, then

- *the Net Premium Credit received on this Strategy will be: $[(250+200) - (150+100)] = 450 - 250 = 200$*
- *BE Strike on CE side = $17000 + 200 = 17200$ CE*
- *BE Strike on PE side = $17000 - 200 = 16800$ PE*

Thus, if the underlying by Expiry of the Options Shorted, closes at the same Strike on which the two Short legs are initiated and consequently both the Short primary legs expire as ATM/ OTM, then the entire Rs. 200 per Lot aggregate Net Premium Credit received on this Strategy shall be the Max Profit in this Strategy.

However, if Nifty moves higher than the 17000 CE Strike, but does not breach the Breakeven Strike of 17200 CE on the upper side and expire at 17150 ATM (which implies that 17000 CE Short leg becomes an ITM; and 17300 CE Long leg

³⁴ The final LTP (i.e. Premium value) of the Option, if it expires as an ITM, would be equal to the Intrinsic Value (i.e. the difference between the relevant ITM Strike and ATM Strike on Expiry).

	<i>and both PE legs (i.e. 17000 PE Short & 16700 PE Long) expire as OTMs and thus become zero), then the Max Profit in this Strategy will be the [final LTP of the 17000 CE Short leg minus aggregate Net Premium Credit of Rs. 200 per Lot received on this Strategy].</i> <i>The final LTP of the 17000 CE Short leg on Expiry will be equivalent to its Intrinsic Value (which is determined as ATM – ITM CE) i.e. 17150 – 17000 = Rs. 150).</i> <i>Thus, the profit on this Strategy, as per aforesaid formula would be: Rs 200 (aggregate Premium Credit received on this Strategy) minus Rs. 150 (final premium value of 17000 CE on Expiry) = Rs. 50 per qty in the Lot.</i> <i>Thus, overall profit on this Strategy got reduced (from a Net Premium Credit of Rs. 200 on the overall Strategy, to Rs. 50 only) as the Strike at which Short was initiated was breached by Expiry (but loss in this Strategy did not occur because the Breakeven Strike was not breached by Expiry).</i> The ratio between the Max Loss and the Max Reward gives the Risk & Reward ratio for this Strategy.
<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level on the upside (CE side):</u> [CE Short Strike + Total Premium Credit collected on both CE Short & PE Short leg] <u>BE Level on the downside (PE side):</u> [PE Short Strike - Total Premium Credit	<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level on the upside (CE side):</u> [CE Short Strike + Net Premium Credit collected on both CE & PE sides] <u>BE Level on the downside (PE side):</u> [PE Short Strike – Net Premium Credit collected on both CE & PE sides]

collected on both CE Short & PE Short leg] Min Profit Level: If underlying closes by Expiry just above the BE Level³⁵ on the PE side or if the underlying closes just below the BE Level on the CE side³⁶. Max Profit Level: If underlying closes by Expiry at the same Strike on which CE Short & PE Short positions were initiated in this Strategy. Profit Zone: If underlying closes by Expiry between the BE Level on PE side and BE Level on CE side. In this profit zone the following situation may arise: <u>If underlying closes by Expiry at the Strike on which CE Short and PE Short are initiated:</u> Max profit on the Strategy would be generated (as calculated aforesaid). <u>If underlying closes between the PE Short Strike and BE Level on the PE side:</u> Then some profit would be generated on the overall Strategy. In such case higher profit would be generated on the Strategy if the underlying closes by Expiry near the PE Short Strike; and the profit would be less if the underlying closes towards the BE Level on the PE side. Profit in such situation can be calculated as already explained above. <u>If underlying closes between the CE Short Strike and BE Level on the CE side:</u> Then some profit would be generated on the	Min Profit Level: If underlying closes by Expiry just above the BE Level³⁹ on the PE side or if the underlying closes just below the BE Level on the CE side⁴⁰. Max Profit Level: If underlying closes by Expiry at the same Strike on which CE Short & PE Short positions were initiated in this Strategy. Profit Zone: If underlying closes by Expiry between the BE Level on PE side and BE Level on CE side. In this profit zone the following situation may arise: <u>If underlying closes by Expiry at the Strike on which CE Short and PE Short are initiated:</u> Max profit on the Strategy would be generated (as calculated aforesaid). <u>If underlying closes between the PE Short Strike and BE Level on the PE side:</u> Then some profit would be generated on the overall Strategy. In such case higher profit would be generated on the Strategy if the underlying closes by Expiry near the PE Short Strike; and the profit would be less if the underlying closes towards the BE Level on the PE side. <u>If underlying closes between the CE Short Strike and BE Level on the CE side:</u> Then some profit would be generated on the overall Strategy. In such case higher profit would be generated on the Strategy if the underlying closes by Expiry near the CE Short Strike; and the
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³⁵ That is higher Strike than BE Strike Level on PE side.

³⁶ That is lower Strike than BE Strike Level on CE side.

³⁹ That is higher Strike than BE Strike Level on PE side.

⁴⁰ That is lower Strike than BE Strike Level on CE side.

overall Strategy. In such case higher profit would be generated on the Strategy if the underlying closes by Expiry near the CE Short Strike; and the profit would be less if the underlying closes towards the BE Level on the CE side. Profit in such situation can be calculated as already explained above.

Loss Starting Level: If underlying closes by Expiry below the BE Level on the PE side³⁷ or above the BE Level on the CE side³⁸.

Max Loss situation: If the underlying closes by Expiry below the BE Level on the PE side or if the underlying closes above the BE Level on the CE Strike, then the Max Loss situation may arise on this Strategy, in the following situation:

Max Loss on the PE side: In case the underlying keeps falling below the BE Level on the PE side, then unlimited loss situation would arise on the lower side. Lower the underlying would close below the BE Level of the PE side, higher will be the loss on the overall Strategy. Loss on Expiry, in such situation can be calculated as already explained above.

Max Loss on the CE side: In case the underlying keeps rising above the BE Level on the CE side, then unlimited loss situation would arise on the upside. Higher the underlying would close above the BE Level of the CE side, higher will be the loss on the overall Strategy. Loss on

profit would be less if the underlying closes towards the BE Level on the CE side.

Loss Starting Level: If underlying closes by Expiry below the BE Level on the PE side⁴¹ or above the BE Level on the CE side⁴².

Max Loss situation: If the underlying closes by Expiry below the PE Long Strike on the PE side or above the CE Long Strike on the CE side, then the Max Loss may arise on this Strategy

Loss Zone: If underlying closes by Expiry below the BE Level on PE side or above the BE Level on the CE side. In this loss zone the following situation may arise:

If underlying closes by Expiry at or anywhere below the PE Long Strike: Max loss on the Strategy would be generated (calculated as aforesaid).

If underlying closes below the BE Level on the PE side and above the PE Long Strike: Then some loss would be generated on the overall Strategy. In such case lower would be the loss generated on the Strategy if the underlying closes by Expiry near the BE Level on the PE side; and the loss would be relatively more if the underlying closes towards the PE Long Strike.

If underlying closes by Expiry at or anywhere above the CE Long Strike: Max

³⁷ That is lower Strike than BE Strike Level on PE side.

³⁸ That is higher Strike than BE Strike Level on CE side.

⁴¹ That is lower Strike than BE Strike Level on PE side.

⁴² That is higher Strike than BE Strike Level on CE side.

Expiry, in such situation can be calculated as already explained above.	loss on the Strategy would be generated (<i>calculated as aforesaid</i>). <u><i>If underlying closes above the BE Level on the CE side and below the CE Long Strike:</i></u> Then some loss would be generated on the overall Strategy. In such case lower would be the loss generated on the Strategy, if the underlying closes by Expiry near the BE Level on the CE side; and the loss would be relatively more if the underlying closes towards the CE Long Strike.
<u>Options behaviour:</u> • In this Strategy, two factors help in generating profit: (i) tight rangebound move in the underlying; and (ii) Theta impact on the primary legs. Therefore, this Strategy is a highly profitable Strategy if the narrow range is maintained by the underlying. • If the underlying remains within the narrow range in this Strategy (<i>i.e. between the Breakeven Strikes in this Strategy</i>), then it implies that by Expiry, either: (i) both these Strikes expires worthless as OTM / ATM (due to Theta impact on both primary leg being OTMs). Consequently, the entire aggregate Premium received on Shorting both CE & PE Strikes would be the maximum profit if underlying closes on Expiry at the Strike on which both Short legs have been initiated; or (ii) one primary leg would expire worthless as an OTM and another as a near ITM, in which case lesser	<u>Options behaviour:</u> • In this Strategy, two factors help in generating profit: (i) tight rangebound move in the underlying; and (ii) Theta impact on the primary legs. Therefore, this Strategy is a highly profitable Strategy if the narrow range is maintained by the underlying. • If the underlying remains within the narrow range in this Strategy (<i>i.e. between the Breakeven Strikes in this Strategy</i>), then it implies that by Expiry, either: (i) both these Strikes expires worthless as OTM / ATM (due to Theta impact on both primary leg being OTM/ ATM). Consequently, the entire Net Premium received on Shorting both CE & PE Strikes would be the maximum profit if underlying closes on Expiry at the Strike on which both Short legs have been initiated; or (ii) one primary leg would expire worthless as an OTM and another as a near ITM, in which case lesser profit (than the

profit (than the Maximum Profit) is generated on this Strategy. • Further, as the Expiry approaches near, the Theta impact on the ATM Strike CE & PE starts causing them to loose their Premium, and therefore generates profit. • Due to the increasing Theta impact with the approach of Options Expiry, this Strategy becomes suitable for deployment near Expiry if the narrow rangebound view on the underlying is aligned and favourable. • Thus, Short Straddles can be initiated when market is in a very narrow rangebound limits, especially: (i) near Expiry i.e. in the last week or so before Expiry, to play until Expiry day; or (ii) a day before Expiry, to benefit from Overnight Expiry Decay; or (iii) On Expiry day, to benefit from full Theta decay of Expiry day effect. • Rise in Volatility may not adversely impact this Strategy, because even if rise in Volatility would be unfavourable to both the Short legs before the Expiry (as their Premium would rise or will not fall as otherwise expected), the Premium value of Options Shorted would reduce near Expiry due to Theta impact. This is owing to the fact that if the Short legs are ATM / OTM on Expiry then even if rising Volatility increases their Premium value, then also it would eventually become zero	Maximum Profit) is generated on this Strategy. • Further, as the Expiry approaches near, the Theta impact on the ATM Strike CE & PE starts causing them to loose their Premium, and therefore generates profit. • Due to the increasing Theta impact with the approach of Options Expiry, this Strategy becomes suitable for deployment near Expiry if the narrow rangebound view on the underlying is aligned and favourable. • Thus, this Strategy (which is hedged Short Straddle) can be preferred over Short Straddle to play out when market is in a very narrow rangebound limits, especially: (i) near Expiry i.e. in the last week or so before Expiry, to play until Expiry day; or (ii) a day before Expiry, to benefit from Overnight Expiry Decay; or (iii) On Expiry day, to benefit from full Theta decay of Expiry day effect. • Rise in Volatility may not adversely impact this Strategy, even if rise in Volatility would be favourable to the CE Long & PE Long hedged legs and not on the CE Short & PE Short primary legs. This is owing to the fact that if the both the primary & hedged legs of the CE and PE side positions continue to be an ATM/ OTM until Expiry then even if rising Volatility increases their Premium value, then also it would eventually become zero and yield
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and yield profit to the extent of aggregate Premium credit on Expiry. • Falling state of Volatility will also help this Strategy to realise the profit quickly, as the drop in Volatility will erode the Premium value of both the Short legs and the aggregate Premium credit would be realised as profit sooner as Theta impact too would fasten the erosion of the Premium. • The Delta play between the CE Short and PE Short primary legs is separately discussed hereinbelow.	profit to the extent of Net Premium credit on Expiry. • Falling state of Volatility will also help this Strategy to realise the profit quickly, as the drop in Volatility will erode the Premium value of both the CE Short & PE Short primary legs (as well as of the hedged legs) and the Net Premium credit would be realised as profit sooner as Theta impact too would fasten the erosion of the Premium. • The Delta play amongst the primary legs, as well as amongst the hedged legs, is separately discussed hereinbelow.
<u>Strike / Delta value:</u> Since, both the Short legs are on the same Strike, their Delta values help maintain a balance between the profit & loss scenario between the two Short legs. In this Strategy, ATM CE & PE are Shorted (which have nearly same Delta value equal to 0.5 per Lot basis), therefore, in this Strategy, with the movement of the underlying within the narrow range, the Delta values on CE Short and PE Short legs acts natural hedge to each other, in the following manner: • when CE Short leg loses due to rise in its LTP (i.e. when underlying rises and CE Short Strike becomes an ITM), the PE Short leg will help counter the losses on CE leg by generating profit as the LTP of PE would reduce (as the PE Short Strike becomes an OTM, when underlying rises); and	<u>Strike / Delta value:</u> Since, both the Short legs are on the same Strike, their Delta values help maintain a balance between the profit & loss scenario between the two Short legs. In this Strategy, ATM CE & PE are Shorted (which have nearly same Delta value equal to 0.5 per Lot basis), therefore, in this Strategy, with the movement of the underlying within the narrow range, the Delta values on CE Short and PE Short legs acts natural hedge to each other, in the following manner: • when CE Short leg loses due to rise in its LTP (i.e. when underlying rises and CE Short Strike becomes an ITM), the PE Short leg will help counter the losses on CE leg by generating profit as the LTP of PE would reduce (as the PE Short

- when PE Short leg generates loss due to rise in its LTP (i.e. when underlying falls and PE Short Strike becomes an ITM), the CE Short leg will help counter the losses on PE leg by generating profit as the LTP of CE would reduce (as the CE Short Strike becomes an OTM, when underlying falls).

Thus, such fluctuations of CE Short and the PE Short leg, from near ITM to OTM, acts as a natural hedge to the other leg in more or less same Delta ratio (*which Delta ratio keeps inter-changing between the CE Short and PE Short leg, as they switch from OTM to ITM*), so long the Breakeven Strike is not breached by the underlying on either side. Once the Breakeven Strike is breached by the underlying on either side, then the unlimited loss situation arises depending how long the underlying trends beyond Breakeven Even Strike until Expiry of the Options Shorted.

Strike becomes an OTM, when underlying rises); and

- when PE Short leg generates loss due to rise in its LTP (i.e. when underlying falls and PE Short Strike becomes an ITM), the CE Short leg will help counter the losses on PE leg by generating profit as the LTP of CE would reduce (as the CE Short Strike becomes an OTM, when underlying falls).

Thus, such fluctuations of CE Short and the PE Short leg, from near ITM to OTM, acts as a natural hedge to the other leg in more or less same Delta ratio (*which Delta ratio keeps inter-changing between the CE Short and PE Short leg, as they switch from OTM to ITM*), so long the Breakeven Strike is not breached by the underlying on either side.

Also, the two Long legs in this Strategy, i.e. CE Long and PE Long which are initiated on Far OTMs, can be initiated at such Strike levels which have more or less same LTP or Delta value. This equal Delta value Long legs helps to ensure a reasonable balance between the profit & loss scenario between the two Long legs in this Strategy as per the movement of the underlying.

Thus, with approx. equal Delta values on CE Long and PE Long legs, Delta neutrality is ensured in this Strategy to cater to maintain a balance between the profit and loss situation amongst the Long legs resulting due to the movement of the underlying, i.e.:

- with the rise in the underlying, PE Long leg generates losses due to fall

	in its LTP, however, the CE Long leg will help counter the losses on PE Long leg by generating profit (as the LTP of CE would rise) to almost similar amount as to the loss incurred on the PE Long leg, due to same Delta values of the CE Long and PE Long legs; • with the fall in the underlying, CE Long leg generates losses due to fall in its LTP, however, the PE Long leg will help counter the losses incurred on CE Long leg, by generating profit (as the LTP of PE would rise) to almost similar amount as to the loss incurred on the CE Long leg, due to same Delta values of the CE Long and PE Long legs. Further, the Delta difference between the primary leg and the hedged leg of the CE side (and also between the primary and hedged leg for the PE side) will help maintain a reasonable control on the Net Premium Credit scenario in this Strategy. Delta difference can be ensured by selecting appropriate distance Far OTMs for the hedged leg Strike, separately for CE and PE side, for this Strategy.
<u>Selection of Option Strikes:</u> This Strategy is dependent of higher Time value and maximum Theta impact, thus it usually comprises of naked ATM CE Short; and naked ATM PE Short legs. However, this Strategy can also be implemented by initiating naked Shorts at same Strike CE & PE near ATM.	<u>Selection of Option Strikes:</u> This Strategy is dependent of higher Time value and maximum Theta impact, thus it usually comprises of naked ATM CE Short; and naked ATM PE Short legs, for the primary leg. However, the primary leg in this this Strategy can also be implemented by initiating naked

Since, the success of this Strategy is also mainly dependent on the quick arrival of the Theta decay (besides narrow rangebound movement of the underlying), therefore closer Expiry series are preferable for this Strategy.

Shorts at same Strike CE & PE near ATM.

Since, the Short primary leg is initiated at the ATM Strike, the Delta neutrality is maintained in the Short legs of this Strategy.

Further, CE Long and PE Long must be initiated at such OTM Strike levels which have more or less same LTP or Delta value. This equal Delta value between both the Long legs, helps to ensure a reasonable balance between the profit & loss scenario between the two Long leg in this Strategy and therefore ensures Delta neutrality (and approx. same Theta decay) from the perspective of movement of the underlying and approach of Expiry, and thus a natural hedge to each other until Breakeven Strike is not breached by the underlying in either direction.

Further, when a tight rangebound view on the underlying has conviction (*i.e. the underlying would not breach the primary leg ATM Short Strikes*), then a suitable **smaller Delta / Strike difference can be maintained** between the primary leg and the hedged leg, i.e. between CE Short & CE Long; and between PE Short & PE Long. This smaller Delta difference can be ensured by maintaining suitable smaller gap between the Strikes at which primary leg and the hedged leg are initiated of the same Expiry (*i.e. by opting for Near OTM Long Strikes for CE & PE side, having almost same premium value*). This smaller gap will bring the Risk to Reward Ratio much

	favourable. But the risk is that the Breakeven Strike gets shorter. However, when tight rangebound view on the underlying does not have conviction and there seems uncertainty about continuation of tight sideways move in the underlying, and it is not very sure in which direction the underlying may breakout, then a suitable larger Delta/ Strike difference can be maintained between the primary leg and the hedged leg, i.e. between CE Short & CE Long; and between PE Short & PE Long. This larger Delta difference can be maintained by maintaining suitable larger gap between the Strikes at which primary leg and the hedged leg are initiated of the same Expiry (i.e. by opting for farther OTM Long Strike for CE & PE side, having almost same premium value). Larger Strike difference between the primary leg and the hedged leg would ensure higher Net Premium Credit, therefore offers a larger Breakeven area. In such situation, Risk to Reward Ratio is not so favourable. Basis aforesaid factors, suitable Far OTM CE & PE Option Strike for the hedged leg with nearly same Delta & Theta value may be selected for this Strategy (besides ATMs for the Short legs). Since, the success of this Strategy is also mainly dependent on the quick arrival of the Theta decay (besides narrow rangebound movement of the underlying), therefore closer Expiry series are preferable for this Strategy.
<u>If trade goes as per plan:</u>	<u>If trade goes as per plan:</u>

The underlying remains within the narrow rangebound, then both the two Short legs will generate profit due to regular expansion and contraction of Time Value / Premium of the ATM Options due to such up & down movement of the underlying.

Further, as the Expiry draws closer, the impact of Theta decay also starts to help generate profit in this Strategy, due to erosion in the Time Value / Premium of both the Short legs.

Therefore, when until Expiry, the underlying remains within the tight range and the underlying closes on Expiry at the Strike on which the CE Short and PE Short legs have been initiated, then the both the Short leg Strikes would expire worthless as ATMs/ OTMs generating full profit to the tune of the aggregate Premium collected on this Strategy.

If underlying movement breaches the Short Strike but not the Breakeven Strike:

But if the underlying breaches either of the Strikes at which Shorts have been initiated but do not cross the Breakeven Strike of that side, then too this Strategy would yield some profit.

In such event too, some profit will be generated by this Strategy, however, such profit will be lesser than the aggregate Premium collected on this Strategy by Shorting CEs & PEs. The limited profit however can be calculated on Expiry, as per the calculations discussed above.

If trade does not go as per plan and the Breakeven Strike is breached by the underlying:

The underlying remains within the narrow rangebound, then both the two Short legs will generate profit due to regular expansion and contraction of Time Value / Premium of the ATM Options due to such up & down movement of the underlying. However, there will also be premium loss on both the hedged Long legs of the Strategy, but, the rangebound movement will still help achieve the maximum profit to the extent of aggregate Net Premium Credit in the Strategy by Expiry.

Further, as the Expiry draws closer, the impact of Theta decay also starts to help generate profit in this Strategy, due to erosion in the Time Value / Premium of both the Short legs. However, there will also be premium loss on both the hedged Long legs of the Strategy due to Theta impact, but the Theta decay will still help achieve the maximum profit to the extent of aggregate Net Premium Credit in the Strategy.

Therefore, when until Expiry, the underlying remains within the tight range and the underlying closes on Expiry at the Strike on which the CE Short and PE Short leg have been initiated, then the both the Short leg Strikes would expire worthless as ATMs/ OTMs generating full profit to the tune of the aggregate Premium collected on this Strategy.

If underlying movement breaches the Short Strike but not the Breakeven Strike:

But if the underlying breaches either of the Strikes at which Shorts have been initiated but do not cross the Breakeven

Since, this Strategy comprises of naked Short legs, therefore if the underlying breaks the Breakeven Strike, on either side, and starts trending after crossing beyond the Breakeven Strike of that side, then this Strategy will start yielding unlimited loss as the underlying keep trending in that direction and expires outside the Breakeven Strike. The unlimited Loss however can be calculated on Expiry, as per the calculations discussed above. In such situations, when the underlying breaks the range in either side and gets trending beyond the Breakeven Strike of this Strategy, then some adjustments can be considered in order to contain the loss in this Strategy (<i>as discussed below here</i>).	Strike of that side, then too this Strategy may yield some profit. In such event too, some profit will be generated by this Strategy, however, such profit will be lesser than the aggregate Net Premium collected on this Strategy. The limited profit however can be calculated on Expiry, as per the calculations discussed above. <u>If trade does not go as per plan and the Breakeven Strike is breached by the underlying:</u> If the underlying breaks the Breakeven Strike range, on either side, and starts trending after crossing beyond the Breakeven Strike of that side, then this Strategy will start yielding loss. However, the loss in this Strategy will be limited because the Long position initiated on that side as the hedged leg will help curtail the loss arising from the Short leg whose side the Breakeven Strike has been breached by the underlying. The Loss, however, on Expiry will be limited and can be calculated on Expiry, as per the calculations already discussed above. In such situations, when the underlying breaks the range in either side and gets trending beyond the Breakeven Strike of this Strategy, then some adjustments can be considered in order to mitigate the loss in this Strategy (<i>as discussed below here</i>).
<u>Adjustments (if the Breakeven Strike is breached by the underlying and this Strategy does not go as per plan):</u>	<u>Adjustments (if the Breakeven Strike is breached by the underlying and this Strategy does not go as per plan):</u>

Since, this Strategy is a Premium Credit strategy, therefore, the aggregate Premium Credit received (*i.e. the sum of the Premium Credit received on the CE Short and PE Short leg*) need to be protected for profit from Expiry perspective.

However, when the underlying breaks the range in either side and gets trending beyond the Breakeven Strike of this Strategy, then the potential unlimited loss situation may arise in this Strategy.

The potential loss in this Strategy may be unlimited if the underlying keeps trending in one direction beyond the Breakeven Strike. This unlimited loss situation that may occur in this Strategy can be mitigated through following adjustments: (i) Conversion to Iron Fly (*i.e. hedging Short Straddle*); or (ii) Long Options; or (iii) Short CEs; or (iv) Short PEs. These adjustments are discussed below:

- (i) Conversion to Iron Fly: If the original view that the underlying would remain and close by Expiry within the tight range (*at best within the Breakeven Strike range of the Short Straddle*) appears to get uncertain, then immediately the naked Short Straddle must be converted to Iron Fly Strategy by initiating OTM Long CEs and OTM Long PEs (*of equal quantity as that of Short legs, and of same Expiry series as that of the Short Options*). This hedging of Short Straddle through Iron Fly will mitigate the potential risk of unlimited loss on Short Straddle

Since, this Strategy is a combination of two Credit Spread and is an aggregate Net Premium Credit strategy, therefore, the aggregate Premium Credit received (*i.e. the sum of the Net Premium Credit received on the CE and PE leg*) need to be protected for profit from Expiry perspective.

However, when the underlying breaks the range in either side and gets trending beyond the Breakeven Strike of this Strategy, then the potential Loss situation may arise in this Strategy, which would be limited to the extent of pre-calculated Max Loss as already discussed above.

Even though the potential Max Loss in this Strategy may be limited (as it is a hedged strategy), if the underlying keeps trending in one direction beyond the Breakeven Strike, but on aggregate basis when played with heavy volume, the limited Max Loss situation may yield substantial loss in absolute terms.

This loss situation that may occur in this Strategy can be mitigated through following adjustments: (i) Long Options; or (ii) Short CEs; or (iii) Short PEs. These adjustments are discussed below:

- (i) Counter Adjustment through Long Option: If the underlying breaches the Breakeven Strike of this Strategy downwardly *i.e. breaking the lower range (on the PE side) in this Strategy* and the underlying seems to be trending downwardly with momentum, then **PEs can be bought** (*i.e. Long PE to be initiated of same Expiry series as original PE Long if the expiry is far, else of next farther Expiry*)

into a pre-calculated Limited Loss situation. You may refer to the details of Iron Fly given on the other side of this Table for better understanding.

- (ii) Counter Adjustment through Long Option: If the underlying breaches the Breakeven Strike of this Strategy downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be trending downwardly with momentum, then **PEs can be bought** (*i.e. Long PE to be initiated*). However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be trending upwardly with momentum, then **CEs can be bought** (*i.e. Long CE to be initiated*).

Buying CEs or PEs to protect the risk in this Strategy will add up debit position, therefore this Long Options position should only be prudent to initiate only if there is strong momentum in the direction where the underlying has breached the Breakeven Strike. This Long Options position will help overcome the potential unlimited loss amount that may incur in this Strategy. This adjustment through Long Options can be played by naked CEs or PEs (or by Bull or Bear Debit Strategy). Further, Long Options should be initiated at a Strike having Delta value higher than the current Delta value of the Short leg which has been breached

series if Expiry is close). However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be trending upwardly with momentum, then **CEs can be bought** (*i.e. Long CE to be initiated of same Expiry series as original CE Long if the expiry is far, else of next farther Expiry series if Expiry is close*).

Buying CEs or PEs to protect the risk in this Strategy will add up additional debit positions, therefore this Long Options position should only be prudent to initiate only if there is strong momentum in the direction where the underlying has breached the Breakeven Strike. This Long Options position will help overcome the potential limited loss amount that may incur in this Strategy. This adjustment through Long Options can be played by naked CEs or PEs (or by Bull or Bear Debit Strategy). Further, Long Options should be initiated at a Strike having Delta value higher than the current Delta value of the Short leg which has been breached by the underlying (i.e. at a higher Strike than the PE sell Strike; and at a lower Strike than the CE sell Strike, as the case may be), so if the underlying keep trending in direction it has breached the Short leg, the relevant Long Options position initiated as an adjustment should generate more profit than the loss generated by that Short leg. Also, depending upon the likely

by the underlying (i.e. at a higher Strike than the PE sell Strike; and at a lower Strike than the CE sell Strike, as the case may be), so if the underlying keep trending in direction it has breached the Short leg, the relevant Long Options position initiated as an adjustment should generate more profit than the loss generated by that Short leg. Adding naked Longs of higher Delta value in same quantity as on the Short leg, would convert that side into a Debit Vertical Spread. Also, depending upon the likely momentum in the underlying, suitable number of Long Options (CEs or PEs as the case may be) need to be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to Long Options position as an adjustment in comparison to the original number of Lots initiated on the Strategy. If the Long Options generates profit or reasonably minimizes the loss in this Strategy before Expiry, then it would be advisable to book the profit on this Long Options position and to exit this Strategy as a whole by booking minor loss or profit.

- (iii) Counter Adjustment through Short Option: If there seems to be a slow trend, after breaching the Breakeven Strike downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be in a mild

momentum in the underlying, suitable number of Long Options (CEs or PEs as the case may be) need to be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to Long Options position as an adjustment in comparison to the original number of Lots initiated on the Strategy. If the Long Options generates profit or reasonably minimizes the loss in this Strategy before Expiry, then it would be advisable to book the profit on this Long Options position and to exit this Strategy as a whole by booking minor loss or profit.

However, since the Max Loss situation in this Strategy is anyways limited, therefore instead of initiating Long Options as mentioned above, Shorting Options (i.e. Short CEs or Short PEs) as adjustments to mitigate limited Max Loss situation in this Strategy, as discussed below, can be considered.

- (ii) Counter Adjustment through Short Option: If there seems to be a slow trend, after breaching the Breakeven Strike downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then Far OTM CEs **can be sold** (i.e. *Short CEs to be initiated*). However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to

downwardly direction, then **Far OTM CEs can be sold** (*i.e. Short CEs to be initiated*). However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be in a mild upwardly direction, then **PEs can be sold** (*i.e. Short PEs to be initiated*).

Idea in this adjustment is to pick up a suitable Far OTM Option for Shorting, such that this far OTM Option expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying after once breaching the Breakeven Strike again reverses, then these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on the relevant Far OTM Options (CEs or PEs as the case may be), suitable number of Options can be Shorted as an adjustment to absorb or outweigh the loss in the Strategy.

be in a mild upwardly direction, then **Far OTM PEs can be sold** (*i.e. Short PEs to be initiated*).

Idea in this adjustment is to pick up a suitable Far OTM Option for Shorting, such that this far OTM Option expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying after once breaching the Breakeven Strike again reverses, then these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on the relevant Far OTM Options (CEs or PEs as the case may be), suitable number of Options can be Shorted as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to these additional Short Options position in comparison to the original number of Lots initiated on the Strategy. These additional Short Options position should be initiated at such Far OTM Strike(s), which may have reasonable Premium and is expected to expire

Generally, at least 2 to 4 times more Lot quantity may be required to be added to these additional Short Options position in comparison to the original number of Lots initiated on the Strategy. These additional Short Options position should be initiated at such Far OTM Strike(s), which may have reasonable Premium and is expected to expire worthless as OTM on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

- (iv) Adjustment through Pyramiding: If there seems to be a limited trend but with momentum, after breaching the Breakeven Strike downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then additional Far OTM PEs **can be sold** (*i.e. Short PEs to be initiated*) below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry. However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be trending upwardly with momentum but to a limited extent, then additional Far OTM CEs **can be sold** (*i.e. Short CEs to be initiated*) above the Resistance area of the underlying, which is expected

worthless as OTM on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

- (iii) Adjustment through Pyramiding: If there seems to be a limited trend but with momentum, after breaching the Breakeven Strike downwardly i.e. breaking the lower range (on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then additional Far OTM PEs **can be sold** (*i.e. Short PEs to be initiated of the same Expiry series as that of the original PE Short leg*) below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry. However, if the underlying breaches the Breakeven Strike of this Strategy upwardly i.e. breaking the upper range (on the CE side) in this Strategy and the underlying seems to be trending upwardly with momentum but to a limited extent, then additional Far OTM CEs **can be sold** (*i.e. Short CEs to be initiated of the same Expiry series as that of the original CE Short leg*) above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry.

Idea in this adjustment is to pick up a suitable much far OTM Options for Shorting in the same direction in which the underlying has breached the Breakeven Strike, such that these additional far OTM Options (initiated as part of adjustments)

not to be breached by the underlying by Expiry.

Idea in this adjustment is to pick up a suitable much far OTM Options for Shorting in the same direction in which the underlying has breached the Breakeven Strike, such that these additional Far OTM Options (initiated as part of adjustments) expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. These additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of far OTM Options for this adjustment is important because even if the trend of the underlying after breach of Breakeven Strike continues in that direction, these additional Short Options position must be at such Strike which can be expected to be not breached by the underlying by Expiry and to expire as OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on relevant Far OTM Options (*i.e. in case of PE Shorts, below the Support area; and in case of CE Shorts, above the Resistance area*), suitable number of Options can be considered to be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these additional Short Options due

expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. These additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of Far OTM Options for this adjustment is important because even if the trend of the underlying after breach of Breakeven Strike continues in that direction, these additional Short Options position must be at such Strike which can be expected to be not breached by the underlying by Expiry and to expire as OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on relevant Far OTM Options (*i.e. in case of PE Shorts, below the Support area; and in case of CE Shorts, above the Resistance area*), suitable number of Options can be considered to be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these additional Short Options due to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short for this adjustment, in comparison to the original number of Lots initiated on the Strategy.

In this type of adjustment, additional Short Options positions can also be added in a pyramidal structure. That is:

to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short for this adjustment, in comparison to the original number of Lots initiated on the Strategy.

In this type of adjustment, additional Short Options positions can also be added in a pyramidal structure. That is:

- as the downtrend continues Far OTM PEs' Premium would rise, therefore, Short PEs positions can be added at subsequent lower Strike levels as the downtrend continues with lower PEs gaining decent Premium values. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16000 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 15800 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.*
- as the uptrend continues Far OTM CEs' Premium would rise, therefore, Short CEs positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining decent Premium values. *For example, when the uptrend continues in Nifty, a Far OTM CE at 18000 having Premium of Rs. 50 can*

- as the downtrend continues Far OTM PEs' Premium would rise, therefore, Short PEs positions can be added at subsequent lower Strike levels as the downtrend continues with lower PEs gaining decent Premium values. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16000 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 15800 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.*
- as the uptrend continues Far OTM CEs' Premium would rise, therefore, Short CEs positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining decent Premium values. *For example, when the uptrend continues in Nifty, a Far OTM CE at 18000 having Premium of Rs. 50 can be sold, thereafter when the Nifty rises further, subsequent higher CE at 18200 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.*

This **Shorting of Options in a pyramiding manner** may ensure a broader Breakeven Strike (i.e. larger risk area protection) and thus greater probability of profiting due

be sold, thereafter when the Nifty rises further, subsequent higher CE at 18200 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.

This **Shorting of Options in a pyramiding manner** may ensure a broader Breakeven Strike (i.e. larger risk area protection) and thus greater probability of profiting due to Theta decay on these bunch of additional Short Options on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

to Theta decay on these bunch of additional Short Options on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

LONG STRANGLE & REVERSE IRON CONDOR

When a view is formed that the underlying would soon likely to take a directional move in any one direction, may be on account of any news, outcome, event etc., but it is not certain in which direction that momentum movement of the underlying is likely to occur, then such view can be played out by a neutral strategy employing Long Options positions in Far OTM Strikes with the expectation that the underlying by Expiry would make its one sided strong momentum move.

Thus, when the view on the underlying is that it is expected to make one sided strong momentum move but it is not certain that in which direction the underlying would make such a move; and such situation is played out through Long positions in Naked Far OTM CE & PE Options pertaining to that Expiry series (*by which the underlying is expected to make such one sided strong momentum move*), then such a Strategy is called **Long Strangle**. In Long Strangle Strategy, Far OTM CE & Far OTM PE are bought in equal quantity, on the same underlying pertaining to same Expiry series. In this Strategy, the expectation is that the underlying will soon make a sudden one-sided strong momentum move, and would trend much beyond the current level either upwardly or downwardly by the Expiry of the Long Options, crossing beyond the Breakeven Strikes of the Long Options. Long Strangle involves naked Long positions on Far OTM CE & PE Options (involving two legs only). This Strategy has Unlimited Profit potential if the underlying moves swiftly with strong momentum on either side; but it may also generate pre-calculated Limited Max Loss if the Breakeven range is not breached by the underlying with good momentum.

However, when the Long Strangle (naked Strategy) is hedged with Short Options on even Far OTM Strikes (*than the Strikes at which Long has been or intended to be initiated as part of Long Strangle Strategy*), then such Strategy is called **Reverse Iron Condor** (also called as, **Long Iron Condor**). In Reverse Iron Condor Strategy, there is (i) Far OTM CE Long (**CE primary leg**) and even Far OTM CE Short (**CE hedged leg**), in equal quantity, on the same underlying pertaining to same Expiry series; and (ii) Far OTM PE Long (**PE primary leg**) and even Far OTM PE Short (**PE hedged leg**), in equal quantity, on the same underlying pertaining to same Expiry series. In essence, Reverse Iron Condor is

pairing of Bull Call Debit Spread Strategy and Bear Put Debit Spread Strategy; and in aggregate involves 4 legs. Like in Long Strangle, in Reverse Iron Condor too, the expectation is that the underlying will soon make a sudden one sided strong momentum move, and would trend much beyond the current level either upwardly or downwardly by the Expiry of the Long Options, crossing beyond the Breakeven Strikes of the Long Options; however hedged legs are added to the both the Long legs of Long Strangle in order to ensure that if the underlying do not soon make a sudden one sided strong momentum move as expected on either direction, such that the Breakeven Strike of Reverse Iron Condor Strategy is not crossed-over by the underlying by Expiry, then the CE hedged leg and PE hedged leg will cover up for the losses that may be incurred on the CE & PE primary legs. Thus, Reverse Iron Condor Strategy reduces the Loss amount in Long Strangle if the Breakeven range is not breached by the underlying with good momentum. However, in doing so, the Unlimited Profit potential in naked Long Strangle is also reduced to pre-calculated Limited Profit in Reverse Iron Condor, if the underlying moves swiftly with strong momentum on either side.

With this background, now let us delve into discussing the Long Strangle Strategy and Reverse Iron Condor Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Long Strangle Strategy	Reverse Iron Condor Strategy
<u>Trade Legs:</u> • Long CE of Far OTM Strike (primary CE leg); and • Long PE of Far OTM Strike (primary PE leg) Equal number of Lots in both primary legs; and both Long legs must be of same Expiry series. Further, CE Long and PE Long must be of nearly same Premium value.	<u>Trade Legs:</u> • Long CE of Far OTM lower Strike with higher Premium (CE primary leg) • Short CE of even Far OTM higher Strike with lower Premium (CE hedged leg) • Long PE of higher Far OTM Strike with higher Premium (PE primary leg) • Short PE of even Far OTM lower Strike with lower Premium (PE hedged leg)

	All the 4 legs (<i>i.e. two Long primary legs & two Short hedged legs</i>) would be of same Expiry series, with equal quantity in each of the aforesaid four legs. CE Long and PE Long must be of nearly same Premium value. Also, CE Short and PE Short must be of nearly same Premium value. It is a hedged Long Strangle, making a pair of Bull CE Debit Spread Strategy and Bear PE Debit Spread Strategy.
Example: <i>If ATM is at 17000, then for Long Strangle:</i> • Buy 2 Lots Nifty 17500 CE of Next Month Expiry (at Rs. 200 per Lot); and • Buy 2 Lots Nifty 16500 PE of Next Month Expiry (at Rs. 220 per Lot)	Example: <i>If ATM is at 17000, then for Reverse Iron Condor:</i> • Buy 10 Lots Nifty 17500 CE of Current Month Expiry (at Rs. 150 per Lot) • Sell 10 Lots Nifty 17800 CE of Current Month Expiry (at Rs. 120 per Lot) • Buy 10 Lots Nifty 16500 PE of Current Month Expiry (at Rs. 170 per Lot) • Sell 10 Lots Nifty 16200 PE of Current Month Expiry (at Rs. 135 per Lot)
Objective: Objective is to play a Neutral / uncertain strong momentum one-sided directional move on the underlying on account of any event, news, outcomes etc., through buying Far OTM CEs and PEs (both as the primary leg), as the expectation is that the underlying will	Objective: Objective is to play a Neutral / uncertain strong momentum one-sided directional move on the underlying on account of any event, news, outcomes etc., through buying Far OTM CEs and PEs (both as the primary leg), as the expectation is that the underlying will soon make a sudden

soon make a sudden strong momentum one-sided directional move, and would trend in that direction until the Expiry of the Long Options. It is an aggregate Debit Strategy, as both the Long legs are initiated by paying the Premium. On arrival of a soon strong momentum one-sided directional move on the underlying, either of the Far OTM Long primary leg becomes an ITM and the other Far OTM Long position becomes an even farther OTM. The Long position leg which becomes an ITM crosses beyond the Breakeven Strike of this Strategy and generates profit; and the other Long position leg which becomes an even farther OTM Options generates loss. Further, due to the sudden strong momentum trending move of the underlying one of the Long Options position can generate unlimited profit, whereas the other Long Options position which becomes an even farther OTM can only yield loss limited to the extent of the premium paid on buying this Long Option. Thus, the net profit between the two Long Options, is the profit generated in this Strategy. Accordingly, this Strategy can generate limited loss to the maximum extent of the aggregate Premium paid on both the Long legs, but if the underlying takes a strong momentum one-sided trending	strong momentum one-sided directional move, and would trend in that direction until the Expiry of the Long Options, just like in a naked Long Strangle Strategy. However, in this Strategy: in order to mitigate the risk / loss that may arise if the underlying fails to breach the Breakeven Strike on the primary legs by Expiry, a pair of Short Options are also initiated simultaneously with the primary Long legs, such that this Strategy becomes hedged Long Strangle, comprising of a pair of Bull CE Debit Spread Strategy and Bear PE Debit Spread Strategy. Therefore, if the underlying fails to breach the Breakeven Strike of the Long Options, then even Far OTM Short Options on the hedged leg would expire as an OTM too, thereby reducing the loss caused to the maximum extent of Premium paid on the Long out of the Credit or Premium received on the Short legs. Thus, in effect, Reverse Iron Condor comprising of Bull CE Debit Spread Strategy and Bear PE Debit Spread Strategy, converts the naked Long Strangle into a hedged Long Strangle so as to cover and limit the loss that may arise in a naked Long Strangle positions, if the underlying fails to breach the Breakeven Strike of the Long Strangle due to non-arrival of a strong momentum trend in either direction. This Strategy comprising of two Long Options (on Far OTM Strikes) and two
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move, then this Strategy is capable of generating unlimited profit.

Short Options (on even farther OTM Strikes) makes this strategy a Net Debit Strategy, because both the Long Options are initiated by paying higher Premiums, and the Short Options are initiated by collecting lesser Premiums.

On arrival of a soon strong momentum one-sided directional move on the underlying, either side of Far OTM Long primary leg becomes an ITM and the other side Far OTM Long position & Short position becomes an even farther OTM. When the underlying crosses beyond the Breakeven Strike of this Strategy on either side such that the one of the Long Option side (*i.e. CE side or PE side, as the case may be*) becomes an ITM, then this Strategy generates profit; because the Long Option which becomes an ITM generates higher profit than the Net premium paid on the Strategy. However, in this Strategy the profit potential gets limited (due to the Short legs added to otherwise naked Long Strangle).

Accordingly, this Strategy can generate limited loss to the maximum extent of the aggregate Net Premium paid on both this Strategy, but if the underlying takes a strong momentum one-sided trending move, then this Strategy is capable of generating limited profit potential. Both the max profit & max loss in this Strategy can be pre-calculated from Expiry perspective.

Demerits:

Demerits:

• It comprises of naked Long positions. • This Strategy is workable/ profitable only when there is a strong conviction that soon there will be arrival of a strong momentum one-sided trending move of the underlying. However, even if the underlying move one-sided but there is no momentum or if the underlying gets into a rangebound movement, then this Strategy would yield loss due to erosion of Time Value. • Thus, with the passage of time, if the underlying does not move with momentum, then both the Long legs may continue to be OTM Strikes and starts generating loss due to the rising Theta impact. If by Expiry of the Long Options, if the underlying fails to make the one-sided momentum trending move and do not cross the Breakeven Strike of this Strategy on either side, then both the Long legs would expire worthless as OTM, generating entire aggregate Premium paid on this Strategy as loss. • <i>Therefore</i>, two factors which are most detrimental to this Strategy are: (i) rangebound move in the underlying; and (ii) Theta impact on the primary legs. Therefore, this Strategy is heavily dependent on	• Since, in this Strategy on each CE and PE sides, there is one Long position initiated at a higher Premium; and a Short position initiated at a lower Premium. Thus, each of the CE and PE legs have a Net Premium Debit (<i>i.e. Premium paid on Long leg – Premium received on Short leg</i>). This Net Debit Premium on Reverse Iron Condor Strategy is less than the aggregate Premium Debit on Long Strangle. • When Long Strangle is hedged and made up like Reverse Iron Condor, then the unlimited profit potential in Long Strangle, gets converted into limited profit in Reverse Iron Condor. • This Strategy is workable/ profitable only when there is a strong conviction that soon there will be arrival of a strong momentum one-sided trending move of the underlying. From Expiry perspective, for this Strategy to be profitable it is required that the underlying must either trend downwardly and cross below the Breakeven Strike of this Strategy on the PE side; or the underlying must trend upwardly and cross above the Breakeven Strike of this Strategy on the CE side (<i>the Breakeven Strikes in this Strategy are discussed below here</i>). • However, if (i) the underlying move one-sided but there is no
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strong momentum one-sided trending move of the underlying.

- Due to the increasing Theta impact with the approach of Options Expiry, this Strategy may be avoided for positional holding near Expiry.
- It is an aggregate Debit Strategy. Since both Long legs comprises of buying Far OTM Strikes, the Premium on both Long legs is the amount of aggregate Premium paid for this Strategy. Accordingly, from Expiry perspective, the aggregate Premium paid need to be first covered up as profit in this Strategy, to become overall profitable in this Strategy.
- The aggregate of the Premium paid on both Long legs, increases the Breakeven Strike to be crossed-over to make this Strategy profitable from Expiry perspective. Thus, from Expiry perspective, it is required that the underlying must either trend downwardly and cross below the Breakeven Strike of this Strategy on the PE Long side; or the underlying must trend upwardly and cross above the Breakeven Strike of this Strategy on the CE Long side, for this Strategy to generate profit (*the Breakeven Strikes in this Strategy are discussed below here*).

momentum; or the underlying gets into a rangebound movement, then this Strategy would yield limited loss (to the extent of Net Premium paid on this Strategy) due to erosion of Time Value.

- Thus, with the passage of time, if the underlying does not move with momentum, then both the Long legs may continue to be OTM Strikes and starts generating loss due to the rising Theta impact. At the same time, both the Short legs will generate profit due to Theta decay in aforesaid situation. Thus, if by Expiry of the Options, if the underlying fails to make the one-sided momentum trending move and do not cross the Breakeven Strike of this Strategy on either side, then both the Long legs and Short legs would expire worthless as OTM, generating maximum loss to the extent of aggregate Net Premium paid on this Strategy.
- Therefore, two factors which are most detrimental to this Strategy are: (i) rangebound move in the underlying; and (ii) Theta impact on the primary legs. Therefore, this Strategy is heavily dependent on strong momentum one-sided trending move of the underlying.
- Due to the increasing Theta impact with the approach of Options Expiry, this Strategy may be avoided for positional holding near Expiry.

• When the Volatility is in a falling state, then there will be erosion caused to the Premium of the Long Options (<i>or it may act as a deterrence to let the Premium of the Long Options rise</i>), thereby making this Strategy not viable from profit perspective.	• When the Volatility is in a falling state, then there will be erosion caused to the Premium of the Long Options (<i>or it may act as a deterrence to let the Premium of the Long Options rise</i>), thereby making this Strategy not viable from profit perspective, as even though the erosion would also be caused in the Premium Credit on the Short legs but the fall in Volatility may expedite loss of Net Premium Debit made on this Strategy.
<u>Benefits of Long Strangle:</u> • This is a neutral Strategy i.e. when the view is uncertain in which direction the underlying can move with strong momentum as a result of any news, event or outcome etc., this Strategy can be implemented. • Since this Strategy is implemented through buying Far OTM CEs and PEs (Long Options), it requires less capital/ margin and does not need any further capital towards MTM adjustments. • If the view goes as expected, then this Strategy is capable of generating unlimited profit if the trend in one side continues until Expiry of Options, but if the view fails then it can cause a limited loss to the maximum extent of aggregate Premium paid on both the Long legs. Thus, this Strategy is the kind with unlimited profit and limited loss.	<u>Benefits of Reverse Iron Condor:</u> • This is a neutral Strategy i.e. when the view is uncertain in which direction the underlying can move with strong momentum as a result of any news, event or outcome etc., this Strategy can be implemented. • It is a hedged Strategy (i.e. Reverse Iron Condor is hedged Long Strangle). When Long Strangle is hedged and made up like Reverse Iron Condor, then Max Loss in naked Long Strangle gets capped to a smaller Max Loss. Also, the Breakeven Level gets narrowed down in Reverse Iron Condor, thereby requiring relatively lesser move in the underlying to cross-over the Breakeven for generating profit (<i>hence enhancing profit probability</i>). • Since, it is a hedged Strategy, the capital / margin required is less and does not require capital towards any MTM requirements.

• Rise in Volatility is favourable for this Strategy as rise in Volatility will help the Premium of the Long Options to rise (or to not cause them fall much). If there is huge Volatility spike, then both the premium value of both CE Long and PE Long legs would rise exponentially, even if there is no significant move in the underlying. • Thus, rise in Volatility and one-sided strong momentum trending move is the requirement for profitability in this Strategy.	• If the view goes as expected, then this Strategy is capable of generating reasonable profit if the trend in one side continues until Expiry of Options. • Since this a hedged Strategy, therefore, if the underlying fails to breakout the Breakeven Strike by the Expiry on either side, then the hedged leg helps mitigate the loss of the Premium paid on the primary legs through the Credit of Premium received on the Short hedged legs. Thus, this Strategy helps curtail the loss that may arise on the Long Options, due to the Short hedged legs added in this Strategy (<i>which are likely to generate profit due to erosion in their Premium due to Volatility crash or Theta decay</i>). • Rise in Volatility is favourable for this Strategy as rise in Volatility will help the Premium of the Long Options to rise (or to not cause them fall much). If there is huge Volatility spike, then both the premium value of both CE Long and PE Long legs would rise exponentially, even if there is no significant move in the underlying. • Thus, rise in Volatility and one-sided strong momentum trending move is the requirement for profitability in this Strategy.
<u>Breakeven Strike of this Strategy from Expiry perspective:</u>	<u>Breakeven Strike of this Strategy from Expiry perspective:</u>

This Strategy comprises of naked CE Long at Far OTM Strike; and a naked PE long at Far OTM Strike. This is an aggregate Debit Strategy as the Premium at which both Longs are initiated, on aggregate basis is the total Premium paid on this Strategy. The aggregate Premium paid on this Strategy determines the Breakeven Strike range which need to be crossed over by the underlying on either side in order to make this Strategy profitable. The Breakeven Strike range on the upper side and the lower side are calculated as follows in this Strategy: • <u>The Breakeven Strike on the CE side (upper side) is:</u> The CE Strike (at which Long is initiated) + aggregate Premium paid on both CE & PE Longs; and • <u>The Breakeven Strike on the PE side (lower side) is:</u> The PE Strike (at which Long is initiated) - aggregate Premium paid on both CE & PE Longs. Thus, if by Expiry of the Long Options, the underlying successfully crosses-over the aforesaid Breakeven Strikes (<i>either on the upper side or the lower side</i>), then this Strategy would yield profit. Further, in case of continuous trending movement of the underlying after successfully crosses-over the Breakeven Strike on either side by the underlying, an unlimited profit situation would arise.	The CE side comprises of CE Long primary leg at higher Premium and CE Short hedged leg at lower Premium. Thus, there is a Net Premium Debit on the CE side of Reverse Iron Condor. Likewise, the PE side comprises of PE Long primary leg at higher Premium and PE Short hedged leg at lower Premium. Thus, there is a Net Premium Debit on the PE side of Reverse Iron Condor. The sum of the Net Premium Debit on the CE and PE Side is the aggregate Net Premium Debit paid in this Strategy. Accordingly: • <u><i>the Breakeven Strike of the CE side in this Strategy (upper range) is:</i></u> CE Long primary leg Strike + the aggregate Net Premium Debit in the Strategy; and • <u><i>the Breakeven Strike of the PE side in this Strategy (lower range) is:</i></u> PE Short primary leg Strike - the aggregate Net Premium Debit in the Strategy. Thus, if by Expiry of the Long Options, the underlying successfully crosses-over the aforesaid Breakeven Strikes (<i>either on the upper side or the lower side</i>), then this Strategy would yield profit. However, if by Expiry of these Options, the underlying fails to cross-over either upper or lower side of the Breakeven Strikes, then the Strategy would yield loss, which may extend upto the maximum loss level equivalent to the total Net Premium paid on the Strategy.
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However, if by Expiry of these Long Options, the underlying fails to cross-over either upper or lower side of the Breakeven Strikes, then the Strategy would yield loss, which may extend upto the maximum loss level equivalent to the aggregate Premium paid on the Strategy.

For example: If ATM is at 17000, then for Long Strangle: If Nifty 16500 PE is bought at Rs. 100 per Lot & Nifty 17500 CE is bought at Rs. 50 per Lot, then the aggregate Premium paid on this Strategy would be Rs. 100 + Rs 50 = Rs. 150 per Lot.

Thus, the BE Strike of this Strategy will be:

- On CE side: $17500 + (100+50) = 17650$ CE Strike; and
- On PE side: $16500 - (100+50) = 16350$ PE Strike

Thus, if by Expiry, the underlying successfully crosses-over the aforesaid Breakeven Strikes (*either on the upper side or the lower side*), then this Strategy would yield profit; but if by Expiry, the underlying fails to successfully cross-over the relevant Breakeven Strike on either side, then the Strategy would yield loss (*which may extend to the maximum extent of Rs. 150 per Lot, i.e. the total Premium paid on this Strategy*).

Thus, in the aforementioned example: if the underlying goes higher until Expiry

For example: If ATM is at 17000, then for Reverse Iron Condor: If Nifty 17500 CE is bought at Rs. 250 per Lot & Nifty 17800 CE is sold at Rs. 150, for the CE side of this Strategy; and Nifty 16500 PE is bought at Rs. 200 per Lot & Nifty 16200 PE is sold at Rs. 100 per Lot, for the PE side of this Strategy, then:

the Net Premium Debit paid on this Strategy will be: $[(250+200) - (150+100)] = 450 - 250 = 200$

- *Breakeven Strike of this Strategy on upper range (CE side) will be: $17500 + 200 = 17700$ CE*
- *Breakeven Strike of this Strategy on lower range (PE side) will be: $16500 - 200 = 16300$ PE*

Thus, if by Expiry, the underlying successfully crosses-over the aforesaid Breakeven Strikes (either on the upper side or the lower side), then this Strategy would yield profit; but if by Expiry, the underlying fails to successfully cross-over the relevant Breakeven Strike on either side, then the Strategy would yield loss (*which may be upto a maximum extent of the Rs. 200 per Lot, i.e. the net Premium paid of this Strategy*).

Thus, in the aforementioned example: if the underlying goes higher until Expiry and successfully crosses-over the upper Breakeven Strike i.e. 17700 CE and keeps trending higher then the Strategy will be in profit; but if the underlying by Expiry fails to breach the Breakeven Strike of 17700, then this Strategy will incur loss

and successfully crosses-over the upper Breakeven Strike i.e. 17650 CE and keeps trending higher then the Strategy will be in profit; but if the underlying by Expiry fails to cross-over the Breakeven Strike of 17650, then this Strategy will incur loss (<i>which may extend to the maximum extent of total Premium paid on this Strategy (i.e. Rs. 150 per Lot)</i>). Likewise, if the underlying goes lower until Expiry and successfully crosses-over the lower Breakeven Strike i.e. 16350 PE and keeps trending lower then the Strategy will be in profit; but if the underlying by Expiry fails to successfully cross-over the Breakeven Strike of 16350, then this Strategy will incur loss (<i>which may extend to the maximum extent of total Premium paid on this Strategy (i.e. Rs. 150 per Lot)</i>).	(<i>which may be upto a maximum extent of Net Premium paid on this Strategy (i.e. Rs. 200 per Lot)</i>). Likewise, if the underlying goes lower until Expiry and successfully crosses-over the lower Breakeven Strike i.e. 16300 PE and keeps trending lower then the Strategy will be in profit; but if the underlying by Expiry fails to breach the Breakeven Strike of 16300, then this Strategy will incur loss (<i>which may be upto a maximum extent of Net Premium paid on this Strategy (i.e. Rs. 200 per Lot)</i>).
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<u>Payoff Chart of Long Strangle</u> The chart shows a V-shaped payoff curve. The horizontal axis is 'Underlying Price' and the vertical axis represents profit/loss. The bottom of the V is labeled 'Limited Max Loss'. The left side of the V is labeled 'BE On Downside' and the right side is 'BE On Upside'. The left vertical segment is labeled 'PE Long Strike Price' and the right vertical segment is 'CE Long Strike Price'. The upward-sloping parts of the V are labeled 'Unlimited Profit'.	<u>Payoff Chart of Reverse Iron Condor</u> The chart shows an inverted V-shaped payoff curve. The horizontal axis is 'Underlying Price' and the vertical axis represents profit/loss. The top of the inverted V is labeled 'Limited Max Profit'. The bottom of the inverted V is labeled 'Limited Max Loss'. The left side of the inverted V is labeled 'BE On Downside' and the right side is 'BE On Upside'. The left vertical segment is labeled 'Put Long Strike Price' and the right vertical segment is 'Call Long Strike Price'. The downward-sloping parts of the inverted V are labeled 'Limited Max Profit'. The horizontal segments at the top are labeled 'Put Short Strike Price' and 'Call Short Strike Price'.
<u>Loss in this Strategy from Expiry perspective:</u> <u>Max Loss:</u> Since, this Strategy comprises of naked Long legs, for which the Premiums are paid, therefore, the aggregate Premium paid for both the	<u>Loss in this Strategy from Expiry perspective:</u> <u>Max Loss:</u> Since, this Strategy comprises of Long legs and Short legs on both CE side & PE side, therefore a Net Premium Debit is incurred on the overall Strategy.

Long legs in this Strategy is the maximum loss that may occur.

Thus, Maximum Loss in this Strategy will be limited and can be pre-calculated. The Maximum Loss in this Strategy is equivalent to the Total Premium paid on this Strategy, i.e.

Max Loss on Long Strangle = [Premium Paid on CE Long leg + Premium Paid on PE Long Leg]

Max Loss scenario:

The situation of this Max Loss would occur if by Expiry of the Long Options, the underlying closes between both the Long CE Strike and PE Long Strike of this Strategy.

Loss zone:

If the underlying closes by Expiry within the two Breakeven Levels i.e. on the CE side and on the PE side, then loss would be incurred on the Strategy. Therefore, the Loss Zone of this Strategy lies between the BE Level of the CE side and BE Level of the PE side.

Loss Zone on the CE side: if the underlying closes higher than the CE Long leg but below the BE Strike on the CE side, then too some loss would be incurred on the Strategy. Thus, on the CE side, CE Long Strike to BE Strike on the CE side of the Strategy is a Loss zone. Lower loss would be generated on the Strategy if the underlying by Expiry closes towards the BE Strike on CE side; and higher loss would be generated on

This Net Premium paid on the overall Strategy is the maximum loss that may occur on the Strategy.

Thus, Maximum Loss in this Strategy will be limited and can be pre-calculated. The Maximum Loss in this Strategy is equivalent to the Net Premium paid on this Strategy, i.e.

Max Loss on Reverse Iron Condor = [Aggregate Premium Paid on CE Long leg & PE Long Leg] minus [Aggregate Premium Credit received on CE Short leg & PE Short Leg]

Max Loss scenario:

The situation of this Max Loss would occur if by Expiry of the Options, the underlying closes between both the Long CE Strike and PE Long Strike of this Strategy.

Loss zone:

If the underlying closes by Expiry within the two Breakeven Levels i.e. on the CE side and on the PE side, then loss would be incurred on the Strategy. Therefore, the Loss Zone of this Strategy lies between the BE Level of the CE side and BE Level of the PE side.

Loss Zone on the CE side: if the underlying closes higher than the CE Long leg but below the BE Strike on the CE side, then too some loss would be incurred on the Strategy. Thus, on the CE side, CE Long Strike to BE Strike on the CE side of the Strategy is a Loss zone. Lower loss would be generated on the Strategy if the

the Strategy if the underlying closes near or lower than the CE Long Strike. <u>Loss Zone on the PE side:</u> if the underlying closes lower than the PE Long leg but above the BE Strike on the PE side, then too some loss would be incurred on the Strategy. Thus, on the PE side, PE Long Strike to BE Strike of the Strategy on the PE side is a Loss zone. Lower loss would be generated on the Strategy if the underlying by Expiry closes towards the BE Strike on PE side; and higher loss would be generated on the Strategy if the underlying closes near or higher than the PE Long Strike. <u>Impact on Max Loss amount, due to Strike Difference:</u> Larger the difference between CE Long and PE Long Strike, smaller will be the premium debit incurred on the Strategy, and therefore lower Max Loss from Expiry perspective. However, with larger Strike difference, the Breakeven required for profit from Expiry perspective would also expand, thereby requiring longer sustained momentum in order to bring this Strategy to profit (<i>i.e. reducing the profit probability</i>). Thus, pre-calculated loss and BE Levels on the Strategy will help decide, the Strike at which this Strategy must be initiated. <u>For example:</u> If ATM is at 17000, then for Long Strangle: If Nifty 16500 PE is bought at Rs. 100 per Lot & Nifty 17500 CE is bought at Rs. 50 per Lot, then the	underlying by Expiry closes towards the BE Strike on CE side; and higher loss would be generated on the Strategy if the underlying closes near or lower than the CE Long Strike. <u>Loss Zone on the PE side:</u> if the underlying closes lower than the PE Long leg but above the BE Strike on the PE side, then too some loss would be incurred on the Strategy. Thus, on the PE side, PE Long Strike to BE Strike of the Strategy on the PE side is a Loss zone. Lower loss would be generated on the Strategy if the underlying by Expiry closes towards the BE Strike on PE side; and higher loss would be generated on the Strategy if the underlying closes near or higher than the PE Long Strike. <u>Impact on Max Loss amount, due to Strike Difference:</u> Larger the difference between CE Long and PE Long Strike, smaller will be the premium debit incurred on the Strategy, and therefore lower Max Loss from Expiry perspective. However, with larger Strike difference, the Breakeven required for profit from Expiry perspective would also expand, thereby requiring longer sustained momentum in order to bring this Strategy to profit (<i>i.e. reducing the profit probability</i>). Thus, pre-calculated loss and BE Levels on the Strategy will help decide, the Strike at which this Strategy must be initiated. <u>For example:</u> If ATM is at 17000, then for Reverse Iron Condor: If Nifty 17500 CE is
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aggregate premium paid on this Strategy is Rs. 150 per Lot.

Thus, in this Strategy, if: (a) the Nifty fails to cross-over above the Breakeven strike of 17650 upwardly by the Expiry; and (b) the underlying fails to cross-over below the Breakeven strike of 16350 downwardly by the Expiry, then this Strategy would yield loss. Further, if Nifty closes by Expiry between 16500 and 17500 Strikes, then Max Loss equivalent to total aggregate Premium of Rs. 150 per Lot would be incurred on the Strategy.

bought at Rs. 250 per Lot and Nifty 17800 CE is sold at Rs. 150, for the CE side of the Strategy; and Nifty 16500 PE is bought at Rs. 200 per Lot & Nifty 16200 PE is sold at Rs. 100 per Lot, for the PE side of this Strategy, then:

the Net Premium Debit paid on this Strategy will be: $[(250+200) - (150+100)] = 450 - 250 = 200$

In the aforesaid example:

If the underlying fails to successfully cross-over the Breakeven Strike of 17700 or 16300 by Expiry, then this Strategy would yield loss. Further, if Nifty closes by Expiry between 16500 and 17500 Strikes, then Max Loss equivalent to the Net Premium of Rs. 200 per Lot paid on this Strategy would be incurred.

Profit in this Strategy from Expiry perspective:

Max Profit scenario: If by Expiry of the Long Options, the underlying successfully crosses-over the Breakeven Strikes of the Strategy (*either on the upper side or the lower side*), then this Strategy would yield profit. More trending the underlying gets in one direction with momentum, crossing beyond the BE Strike level of the Strategy on that side, higher the profit that will be generated. Thus, the Max Profit potential on this Strategy is unlimited, provided the strong momentum makes either CE side Long

Profit in this Strategy from Expiry perspective:

Max Profit scenario: If by Expiry of the Options, the underlying successfully crosses-over the Breakeven Strikes of the Strategy (*either on the upper side or the lower side*), then this Strategy would yield profit. More trending the underlying gets in one direction with momentum, crossing beyond the BE Strike level of the Strategy on that side, higher the profit that will be generated. However, the Max Profit potential on this Strategy is limited (*as against unlimited profit in naked Long Strangle, in case of continuous trending momentum on any particular side*) and the

Strike or PE side Long Strike a deep ITM. Thus, in case of continuous trending movement of the underlying after breaching of the Breakeven Strike on either side by the underlying, an unlimited profit situation would arise from Expiry perspective. This situation implies that the Long leg Strike on the side of the momentum, ends up being an ITM on Expiry (<i>and the other side Long Option expires worthless as an OTM</i>). <u>Calculation of final Profit generated on the Strategy:</u> If the underlying closes by Expiry, after breaching the Breakeven Strike on either side, then the final Profit accrued on the Strategy on Expiry can be calculated as: • [the final premium value of Long Option of the momentum side on Expiry (<i>i.e. Long leg which becomes / expires as an ITM</i>)]⁴³ minus • [the aggregate Premium paid for the Strategy] <i>For example: If ATM is at 17000, then for Long Strangle: If Nifty 16500 PE is bought at Rs. 100 per Lot & Nifty 17500 CE is bought at Rs. 50 per Lot, then the BE Strike of this Strategy will be:</i>	max profit on this Strategy can be pre-calculated. <u>Max Profit Level:</u> If the underlying by Expiry closes either at or beyond the Short leg of any particular side (<i>i.e. CE Short leg on the upside and PE Short leg on the downside</i>), then the Strategy would yield Max Profit, which is limited. In this situation, both the Long leg & Short leg of that side Option (<i>where the BE Strike is breached</i>) becomes an ITM. The other side of Options, both Long & Short leg becomes even farther OTM. This situation generates the Limited Max Profit situation on the Strategy. However, in this Strategy, even if the underlying gets trending on one side but it crosses beyond the Short leg of the Strategy on that side, then no higher profit would be generated on this Strategy from Expiry perspective other than the pre-calculated Max Profit that can be generated on this Strategy. Thus, this Strategy is a limited max profit Strategy; and the max profit on this Strategy can be pre-calculated. <u>Calculation of Max Profit on the Strategy:</u> The Max Profit potential of this Strategy can be calculated as: • [Strike difference between Long & Short leg of CE / PE side]
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⁴³ The final premium of an Option which would expire as an ITM would be equivalent to its Intrinsic Value (*which is the difference between the ATM Strike on Expiry and the Strike of the relevant Option which expired as an ITM*).

On CE side: $17500 + (100+50) = 17650$
CE Strike; and

On PE side: $16500 - (100+50) = 16350$
PE Strike

Thus, in this Strategy, if:

(a) Nifty crosses above the Breakeven Strike of 17650 Strike upwardly by Expiry, then 17500 CE Long leg expires as an ITM generating profit (as CE Long leg Premium would rise) and the PE 16500 Long expires as even farther OTM generating loss (as PE Long leg Premium would fall), thereby giving a net profit in this Strategy due to upward trending move in the Nifty. The more deeper the CE Long leg goes as an ITM by Expiry, more profitable the Strategy would be. The maximum profit on Expiry would be the difference between: [the final LTP of the CE Long position] and [the aggregate Premium paid on the Strategy]; or

(b) Nifty crosses below the Breakeven Strike of 16350 Strike downwardly by Expiry, then 16500 PE Long leg expires as an ITM generating profit (as PE Long leg Premium would rise) and the CE 17500 Long expires as even farther OTM generating loss (as CE Long leg Premium would fall), thereby giving a net profit in this Strategy due to downward trending move in the Nifty. Deeper the PE Long leg goes as an ITM by Expiry, more

minus

- [the Net Premium paid for the Strategy]

Using the above formula, the Max Profit potential for each of CE side and PE side can be separately calculated. Thus, we can determine the Max Profit potential on any particular side of this Strategy. However, if the Strike difference between Long & Short leg is same for both CE side and PE side, then calculation of Max Profit as per aforesaid formula, would be same for both CE side and PE side.

Impact on Max Profit situation, due to variation in Strike Difference between CE side & PE side:

If the Strike difference between Long leg & Short leg, on both CE side and PE side is same (eg: 300 point difference between CE Long & CE Short and similarly 300 point difference between PE Long & PE Short), then the Max Profit would be same for the CE side as well as for the PE side. In such case, the amount so determined, is said to be the Max Profit of the Strategy.

However, if the Strike difference between Long leg & Short leg, on CE side and PE side is different (eg: 300 point difference between CE Long & CE Short and 500 point difference between PE Long & PE Short), then the Max Loss would be different for the CE side and the PE side. The side where the Strike difference is more, would have more Net Premium Debit and accordingly the BE Level of that

profitable the Strategy would be. The maximum profit on Expiry would be the difference between: [the final LTP of the PE Long position] and [the aggregate Premium paid on the Strategy].

Profit Level:

Profit would accrue on this Strategy, from Expiry perspective, if underlying closes after successfully crossing-over the Breakeven Strike of either side, such that the Long Option of atleast one side expires as an ITM.

Impact on profitability, due to Strike Difference:

Larger the difference between CE Long and PE Long Strike, smaller will be the premium debit incurred on the Strategy, and therefore lower Max Loss from Expiry perspective. However, with larger Strike difference, the Breakeven required for profit from Expiry perspective would also expand, thereby requiring longer sustained momentum in order to bring this Strategy to profit (*i.e. reducing the profit probability*). Thus, pre-calculated loss and BE Levels on the Strategy will help decide, the Strike at which this Strategy must be initiated.

side will also increase. But with increase in BE Level, the Max Profit situation on that side would also increase. In such case, the Max Profit of the side where Strike difference is more, would be the Max Profit of the Strategy.

Profit Zone:

The profitability from Expiry perspective would arise in the Strategy, if the underlying closes above the Breakeven Strike level of this Strategy on the CE side⁴⁴; or if the underlying closes below the Breakeven Strike level of this Strategy on the PE side⁴⁵. Therefore, profit would be realised on this Spread if the underlying closes by Expiry after successfully crossing-over the BE Strike of this Strategy on either side.

Profit zone on CE side: Thus, if the underlying by Expiry crosses above the BE Strike on the CE side and closes between the BE Strike on CE side and at or higher than the CE Short Strike, then the Strategy would generate profit on the CE side. Therefore, this is the Profit zone on the CE side. However, if the underlying closes by Expiry at or above the CE Short Strike then Max Profit would be generated on this Strategy. The profit in this zone would be less, if the underlying closes just above the BE Strike level on the CE side; but if the underlying closes near the CE Short Strike level, then the Strategy would generate higher profit (*which may extend*

⁴⁴ That is higher Strike than the BE Level on the CE side.

⁴⁵ That is lower Strike than the BE Level on the PE side.

upto Max Profit, if the underlying closes at or above the CE Short Strike by Expiry).

Profit zone on PE side: Similarly, if the underlying by Expiry crosses below the BE Strike on the PE side and closes between the BE Strike on PE side and at or lower than the PE Short Strike, then the Strategy would generate profit on the PE side. Therefore, this is the Profit zone on the PE side. However, if the underlying closes by Expiry at or below the PE Short Strike then Max Profit would be generated on this Strategy. The profit in this zone would be less, if the underlying closes just below the BE Strike level on the PE side; but if the underlying closes near the PE Short Strike level, then the Strategy would generate higher profit (*which may extend upto Max Profit, if the underlying closes at or below the PE Short Strike by Expiry*).

Calculation of Profit generated on the Strategy within Profit Zone:

On arrival of a strong momentum one-sided directional move on the underlying, that side of Far OTM Long primary leg becomes an ITM and the other side Far OTM Long position & Short position becomes an even farther OTM. The Option side which is in the direction of the momentum (*i.e. Long Option on the CE side or PE side, as the case may be*) which becomes an ITM due to movement in the underlying generates profit; and the other Option side which becomes an even farther OTM Options generates loss.

	Thus, if the underlying by Expiry successfully closes beyond the BE Strike Level of either side and closes within the profit zone of that side, then the final profit on the Strategy at Expiry can be calculated as: • [the final premium value of Long Option of the momentum side on Expiry (<i>i.e. Long leg which becomes / expires as an ITM</i>)]⁴⁶ minus • [the Net Premium paid for the Strategy] <u>For example:</u> If ATM is at 17000, then for Reverse Iron Condor: If Nifty 17500 CE is bought at Rs. 250 per Lot & Nifty 17800 CE is sold at Rs. 150, for the CE side of this Strategy; and Nifty 16500 PE is bought at Rs. 200 per Lot & Nifty 16200 PE is sold at Rs. 100 per Lot, for the PE side of this Strategy, then: • the Net Premium Debit paid on this Strategy will be: $[(250+200) - (150+100)] = 450 - 250 = \text{Rs. } 200$ per Lot • Breakeven Strike of this Strategy on upper range will be: $17500 + 200 = 17700$ CE • Breakeven Strike of this Strategy on lower range will be: $16500 - 200 = 16300$ PE
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⁴⁶ The final premium of an Option which would expire as an ITM would be equivalent to its Intrinsic Value (*which is the difference between the ATM Strike on Expiry and the Strike of the relevant Option which expired as an ITM*).

- *Max Profit would be: $[300-200] = 100$ per Lot, provided the underlying either closes by Expiry at or above the CE Short leg; or the underlying closes at or below the PE Short leg of this Strategy.*

Thus, in this Strategy, if:

(a) Nifty crosses above the Breakeven Strike of 17700 Strike upwardly by Expiry, then 17500 CE Long leg expires as an ITM generating profit (as CE Long leg Premium would rise) and the PE 16500 Long expires as even farther OTM generating loss (as PE Long leg Premium would fall), thereby giving a net profit in this Strategy due to upward trending move in the Nifty. Deeper the CE Long leg goes as an ITM by Expiry, more profitable the Strategy would be. However, the maximum profit on Expiry on CE side would be: $[17800-17500] - [200] = \text{Rs. } 100$ per Lot. This max profit on CE side would be realized on Expiry, if the underlying trends higher and closes at or above the CE Short leg. But if the underlying closes at 17750 on Expiry i.e. in the Profit Zone on the CE side, then the CE Long leg of 17500 would be an ITM with final premium value on Expiry of Rs. 250 (because on Expiry, the final premium value is equal to the Intrinsic Value of the ITM, which is calculated as $\text{ATM} - \text{ITM CE Strike}$). Therefore, the final premium value of 17500 CE would be $[17750-17500]=250$. Thus, the final overall profit on the Strategy would be: 17500

	<i>CE final premium value – Net premium paid on the Strategy = 250 – 200 = Rs. 50 per qty in a Lot i.e. 50 x 50 = Rs 2500 in a Lot.</i> <i>(b) Nifty crosses below the Breakeven Strike of 16300 Strike downwardly by Expiry, then 16500 PE Long leg expires as an ITM generating profit (as PE Long leg Premium would rise) and the CE 17500 Long expires as even farther OTM generating loss (as CE Long leg Premium would fall), thereby giving a net profit in this Strategy due to downward trending move in the Nifty. Deeper the PE Long leg goes as an ITM by Expiry, more profitable the Strategy would be. However, the maximum profit on PE side on Expiry would be: [16500 - 16200] – [200] = Rs. 100 per Lot. This max profit on PE side would be realized on Expiry, if the underlying trends lower and closes at or below the PE Short leg. But if the underlying closes at 16250 on Expiry i.e. in the Profit Zone on the PE side, then the PE Long leg of 16500 would be an ITM with final premium value on Expiry of Rs. 250 (because on Expiry, the final premium value is equal to the Intrinsic Value of the ITM, which is calculated as ITM PE Strike – ATM). Therefore, the final premium value of 16500 PE would be [16500-16250=250]. Thus, the final overall profit on the Strategy would be: 16500 PE final premium value – Net premium paid on the Strategy = 250 –</i>
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	<i>200 = Rs. 50 per qty in a Lot i.e. 50 x</i> <i>50 = Rs 2500 in a Lot.</i>
<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level on CE side:</u> [CE Long Strike + Total Premium Debit paid on the Strategy] <u>BE Level on PE side:</u> [PE Long Strike - Total Premium Debit paid on the Strategy] <u>Min Profit Level:</u> If underlying closes by Expiry just above the BE Level on CE side (<i>i.e. higher CE Strike than BE Strike</i>) or if the underlying closes by Expiry just below the BE Level on PE side (<i>i.e. lower PE Strike than BE Strike</i>). <u>Max Profit Level:</u> Max Profit is unlimited if the underlying successfully crosses-over the BE Strike Level on either CE side or PE Side (<i>such that one side Strike becomes an ITM</i>). Max profit situation arises as the underlying closes by Expiry anywhere higher than the BE Strike Level on the CE side; or anywhere lower than the BE Strike Level on the PE side. Deeper the CE Long or PE Long becomes an ITM, higher will be the profit generated on this Strategy. <u>Loss Zone:</u> If underlying closes by Expiry anywhere between the BE Level on the CE side and the BE Strike on the PE side, then loss would be incurred on this Strategy.	<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level on CE side:</u> [CE Long Strike + Net Premium Debit paid on the Strategy] <u>BE Level on PE side:</u> [PE Long Strike - Net Premium Debit paid on the Strategy] <u>Min Profit Level:</u> If underlying closes by Expiry just above the BE Level on CE side (<i>i.e. higher CE Strike than BE Strike</i>) or if the underlying closes by Expiry just below the BE Level on PE side (<i>i.e. lower PE Strike than BE Strike</i>). <u>Max Profit Level:</u> Max Profit is limited, and the same is realised on the Strategy if the underlying successfully crosses-over the Short Strike Level on either CE side or PE Side (<i>such that one side becomes an ITM</i>), by Expiry. Anywhere deeper the underlying may close beyond the Short leg, the Max Profit shall be limited to the pre-calculated Max Profit Level on that side. <u>Profit Zone:</u> If underlying closes by Expiry anywhere between the BE Strike on the CE side and at or higher than the CE Short Strike. Similarly, on the PE side, if the underlying closes by Expiry anywhere between the BE Strike on the PE side and at or lower than the PE Short Strike. <u>Loss Zone:</u> If underlying closes by Expiry anywhere between the BE Level on the CE

<u>Max Loss Zone:</u> If underlying closes by Expiry anywhere between the CE Long Strike and the PE Long Strike, then Max Loss would be incurred on this Strategy.	side and the BE Strike on the PE side, then loss would be incurred on this Strategy. <u>Max Loss Zone:</u> If underlying closes by Expiry anywhere between the CE Long Strike and the PE Long Strike, then Max Loss would be incurred on this Strategy.
<u>Options behaviour:</u> • In this Strategy, three factors help in generating profit: (i) strong momentum trending move of the underlying; and (ii) the momentum trend should arrive soon, otherwise Theta decay would adversely impact the probability of profit; and (iii) Volatility should either rise or remain constant, but should not go into steep falling state. Therefore, profitability in this Strategy is heavily dependent on these factors. • Further, the selection of these CE & PE Strikes must be such OTM Strikes which are not too Far and must be within the Most Impacted Radius Zone where the Long Options would get positively impacted on arrival of momentum. • Further, as the Expiry approaches near, the Theta impact on the Far OTM Strike CE & PE would cause erosion on the Premium values of the Long Options. Thus, near Expiry this Strategy must be avoided unless when quick strong momentum is expected within a	<u>Options behaviour:</u> • In this Strategy, three factors help in generating profit: (i) strong momentum trending move of the underlying; and (ii) the momentum trend should arrive soon, otherwise Theta decay would adversely impact the probability of profit; and (iii) Volatility should either rise or remain constant, but should not go into steep falling state. Therefore, profitability in this Strategy is heavily dependent on these factors. • Further, the selection of these CE & PE Strikes must be such OTM Strikes which are not too far and must be within the Most Impacted Radius Zone where the Long Options would get positively impacted on arrival of momentum. • Further, as the Expiry approaches near, the Theta impact on the Far OTM Strike CE & PE would cause erosion on the Premium values of the Long Options. However, since in this Strategy the Long leg is hedged with Short positions therefore, the Theta also impacts the Far OTM CE & PE Short legs thereby helping to absorb

short holding period after this Strategy is initiated. • Rise in Volatility is favourable for this Strategy as rise in Volatility will help the Premium of the Long Options to rise (or to not cause them fall much). • Delta play between the two Long legs is separately discussed hereinbelow.	the loss on the Long Options leg through profit on the Short leg. Thus, near Expiry this Strategy must be avoided unless when quick strong momentum (or huge gapup/gapdown) is expected within a very short span of time (like next day or so) after this Strategy is initiated. • Rise in Volatility is favourable for this Strategy as rise in Volatility will help the Premium of the Long Options to rise (or to not cause them fall much). • Delta neutral position is strived for in this Strategy at the time of initiating this Strategy. The Delta play between the CE Long and PE Long primary legs; as well the CE Short and PE Short hedged legs is separately discussed hereinbelow.
<u>Strike / Delta value:</u> The two Long legs, i.e. CE Long and PE Long must be Far OTMs, and can be initiated at such Strike levels which have more or less same LTP or Delta value. This equal Delta value Long legs helps to ensure a reasonable balance between the profit & loss scenario between the two Long legs in this Strategy, until the momentum arrives. This is because, if there is uncertainty with regard to which direction the underlying is going to push forward its strong momentum move, then it is better to initiate both Long primary legs with equal Delta values, thereby maintaining Delta	<u>Strike / Delta value:</u> The two Long legs, i.e. CE Long and PE Long are OTMs, and can be initiated at such Strike levels which have more or less same LTP or Delta value. This equal Delta value Long legs helps to ensure uniformity in the profitability irrespective in whichever direction the momentum in the underlying arrives. Likewise, the two Short hedged legs in this Strategy, i.e. CE Short and PE Short must be even Far OTMs, and can be initiated at such Strike levels which have more or less same LTP or Delta value. This equal Delta value Short legs helps to ensure uniformity in profitability in one side (<i>where momentum arrives</i>) and the loss incidence on the other

neutrality at the time of initiating the Strategy. However, if basis our I we have a bias towards a particular direction in which the underlying may likely move, then we can initiate that side Long leg (CE or PE, as the case may be) with slightly higher Delta value than the other leg. This will help to achieve greater profit on the side with higher Delta, and lesser loss on the side with lesser Delta, if the underlying makes a move in the direction we expected it to go. Higher Delta Option, will be relatively a Near OTM Strike, then the other side Option (<i>which will be relatively Far OTM</i>). <i>For example: If ATM is at 17000, and our view is strong bullish move expected on Nifty, then we can initiate Long Strangle with:</i> • <i>higher Delta value of 0.15 on CE Long (eg: Nifty 17200 CE bought at Rs. 200 per Lot); and</i> • <i>lower Delta value of 0.35 on PE Long (eg: Nifty 16500 PE is bought at Rs. 100 per Lot).</i> <i>Thus, in the aforesaid example: once the Breakeven Strike of 17500 is successfully crossed-over by the underlying on the CE side, then the unlimited profit situation arises depending how long the underlying trends beyond Breakeven Strike until Expiry of the Options. Nifty CE 17200 rises more due to higher Delta value with the upward momentum and becomes an ITM, generating more profit; while PE</i>	<i>side (which is not favoured by the momentum in the underlying).</i> Thus, with approx. equal Delta values on CE Long and PE Long legs; and equal Delta values on CE Short and PE Short legs, Delta neutrality is ensured in this Strategy to maintain balance between the profit and loss situation amongst the two sides, i.e.: • when CE Long leg gets profitable due to rise in its LTP (<i>i.e. when underlying rises with momentum</i>), greater profitability is achieved as the CE Long Option moves up the higher Delta ladder (as it slides deeper in the money). However, with the rise in the underlying, the PE Long leg generates loss (<i>as the LTP of PE would reduce</i>) and the PE Long leg slides down lower Delta as it goes deeper out of the money. But the rate at which greater profitability on CE side is generated <i>vis-à-vis</i> loss on the PE Long Option, gets wider and wider, as the underlying moves higher, because CE Long would move through ascending Delta values, whereas the PE Long would slide down through descending Delta values. Further, while CE Long option generates profit as the underlying moves higher, however, the CE Short hedged leg incurs loss and accordingly net profit is generated between the CE Long & Short leg. Similarly, as the underlying moves higher, the PE Long option
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16500 falls relatively less due to being at lower Delta, thereby the Strategy overall generates profit.

generates loss however, the PE Short hedged leg generates profit and accordingly the loss generated by the PE Long is absorbed to some extent by the PE Short leg. But the Delta neutrality ensured at the time of initiating the Strategy helps to generate increased profit on CE side and reduced loss on the PE side, as the underlying keeps trending higher.

- Likewise, when PE Long leg gets profitable due to rise in its LTP (*i.e. when underlying falls with momentum*), greater profitability is achieved as the PE Long Option moves up the higher Delta ladder (as it slides deeper in the money). However, with the fall in the underlying, the CE Long leg generates loss (as the LTP of CE would reduce) and the CE Long leg slides down lower Delta as it goes deeper out of the money. But the rate at which greater profitability on PE side is generated *vis-à-vis* loss on the CE Long Option, gets wider and wider, as the underlying moves lower, because PE Long would move through ascending Delta value, whereas the CE Long would slide down through descending Delta value. Further, while PE Long Option generates profit as the underlying moves lower, however, the PE Short hedged leg incurs loss and accordingly net profit is generated between the PE Long &

	Short leg. Similarly, as the underlying moves lower, the CE Long option generates loss however, the CE Short hedged leg generates profit and accordingly the loss generated by the CE Long is absorbed to some extent by the CE Short leg. But the Delta neutrality ensured at the time of initiating the Strategy helps to generate increased profit on PE side and reduced loss on the CE side, as the underlying keeps trending lower. <i>For example: If ATM is at 17000, then for ensuring Delta neutrality in Reverse Iron Condor:</i> • <i>For Long leg: If Nifty 17500 CE is bought at Rs. 250 per Lot with Delta of 0.45 (single Lot basis), then Nifty 16500 PE buy can be initiated with approx. Rs. 200 per Lot having similar Delta value of approx. 0.45 (single Lot basis); and</i> • <i>For Short leg: if Nifty 17800 CE is sold at Rs. 150 per Lot at Delta of 0.3 (single Lot basis), then Nifty 16200 PE sell can be initiated at approx. Rs. 180 per Lot having similar Delta value of approx. 0.29 (single Lot basis).</i>
<u>Selection of Option Strikes:</u> Selection of the CE & PE Strikes must be such OTM Strikes which have equal LTP / Delta values in order to maintain Delta neutrality at the time of initiating	<u>Selection of Option Strikes:</u> Selection of the CE & PE Long legs and CE & PE Short legs Strikes must be such OTM Strikes which have equal LTP / Delta values in order to maintain Delta

the Strategy, if the view is neutral and non-biased.

However, if the view is biased on one particular side, then that side Option can be initiated at a higher Delta than the other.

The Far OTM Strikes must be within the Most Impacted Radius Zone, wherein the positive impact of the momentum can be harnessed.

A reasonable Strike difference must be ensured between the CE Long & PE Long Strikes. Larger the difference between CE Long and PE Long Strike, smaller will be the premium debit incurred on the Strategy, and therefore lower Max Loss from Expiry perspective. However, with larger Strike difference, the Breakeven required for profit from Expiry perspective would also expand, thereby requiring longer sustained momentum in order to bring this Strategy to profit (*i.e. reducing the profit probability*). Thus, pre-calculated loss and BE Levels on the Strategy will help decide, the Strike at which this Strategy must be initiated.

Basis aforesaid factors, suitable Far OTM CE & PE Option Strike levels of a particular Expiry series may be selected for this Strategy. Since, the success of this Strategy is also mainly dependent on the low Theta decay, therefore farther Expiry series (or larger time to Expiry Options) would be preferable for this Strategy.

neutrality at the time of initiating the Strategy.

The Far OTM Long Strikes must be within the Most Impacted Radius Zone, wherein the positive impact of the momentum can be harnessed.

A reasonable Strike difference must be ensured between the CE Long & PE Long Strikes. Larger the difference between CE Long and PE Long Strike, smaller will be the premium debit incurred on the Strategy, and therefore lower Max Loss from Expiry perspective. However, with larger Strike difference, the Breakeven required for profit from Expiry perspective would also expand, thereby requiring longer sustained momentum in order to bring this Strategy to profit (*i.e. reducing the profit probability*). Thus, pre-calculated loss and BE Levels on the Strategy will help decide, the Strike at which this Strategy must be initiated.

Basis aforesaid factors, suitable Far OTM CE & PE Option Strike levels of a particular Expiry series may be selected for this Strategy. Since, the success of this Strategy is also mainly dependent on the low Theta decay, therefore farther Expiry series (or larger time to Expiry Options) would be preferable for this Strategy.

<u>If trade goes as per plan as trends beyond the Breakeven Strike, from Expiry perspective:</u> If by Expiry of the Long Options, if the underlying starts trending strongly with momentum on one side and breaches the Breakeven Strikes of the Strategy on that particular side (<i>i.e. either upwardly on the CE side or downwardly on the PE side</i>), then this Strategy would yield profit. The strength and length of the momentum would decide the quantum of profit in this Strategy. Therefore, in case of continuous trending movement of the underlying after successfully crossing-over the Breakeven Strike on any one side by the underlying, an unlimited profit situation may arise from Expiry perspective. <u>If underlying movement fails to breach the Breakeven Strike, from Expiry perspective:</u> However, if by Expiry of these Long Options, the underlying fails to cross-over the Breakeven Strikes either upwardly on the CE side or downwardly on the PE side, then the Strategy would yield loss (<i>which may extend upto a maximum extent of the aggregate Premium paid on the Strategy</i>). In such situations, when the underlying does not seem to be trending enough to be able to cross-over the Breakeven Strike on either side by Expiry, then	<u>If trade goes as per plan as trends beyond the Breakeven Strike, from Expiry perspective:</u> If by Expiry of the Long Options, if the underlying starts trending strongly with momentum on one side and breaches the Breakeven Strikes of the Strategy on that particular side (<i>i.e. either upwardly on the CE side or downwardly on the PE side</i>), then this Strategy would yield profit. The strength and length of the momentum would decide the quantum of profit in this Strategy. Therefore, in case of continuous trending movement of the underlying after successfully crossing-over the Breakeven Strike on any one side by the underlying, a limited profit situation may arise from Expiry perspective. <u>If underlying movement fails to breach the Breakeven Strike, from Expiry perspective:</u> However, if by Expiry of these Long Options, the underlying fails to cross-over the Breakeven Strikes either upwardly on the CE side or downwardly on the PE side, then the Strategy would yield loss (<i>which may extend upto a maximum extent of the Net Premium paid on the Strategy</i>). In such situations, when the underlying does not seem to be trending enough to be able to cross-over the Breakeven Strike on either side by Expiry, then some adjustments can be considered in order to
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some adjustments can be considered in order to contain the loss in this Strategy <i>(as discussed below here)</i>.	contain the loss in this Strategy <i>(as discussed below here)</i>.
<u>Adjustments (if the Breakeven Strike is not breached by the underlying and this Strategy does not go as per plan):</u> Since, this Strategy is a Premium Debit Strategy, therefore, the aggregate Premium paid (<i>i.e. the sum of the Premium paid on the CE Long and PE Long leg</i>) need to be first recovered from the profit in this Strategy, from Expiry perspective, in order for this Strategy to be overall profitable by Expiry. However, when underlying does not seem to be trending enough to be able to cross-over the Breakeven Strike on either side by Expiry, then the potential loss (<i>limited to the maximum extent of the aggregate Premium paid on this Strategy</i>) situation can be handled by making following adjustments: (i) Converting naked Long Strangle into Reverse Iron Condor (<i>i.e hedged Long Strangle</i>); or (ii) Short both CEs & PEs; or (iii) Short CEs; or (iv) Short PEs. These adjustments are discussed below: (i) <u>Conversion to Reverse Iron Condor</u>: If the original view that the underlying would breakout beyond the Breakeven Strike of the Strategy on either side, appears to get uncertain, then immediately the naked Long Strangle must be converted to Reverse Iron Condor Strategy by initiating even Far	<u>Adjustments (if the Breakeven Strike is not breached by the underlying and this Strategy does not go as per plan):</u> Since, this Strategy is a Premium Debit Strategy, therefore, the Net Premium paid (<i>i.e. the sum of the Net Premium paid on the CE leg and PE leg</i>) need to be first recovered from the profit in this Strategy, from Expiry perspective, in order for this Strategy to be overall profitable by Expiry. However, when underlying does not seem to be trending enough to be able to cross-over the Breakeven Strike on either side by Expiry, then the potential loss (<i>limited to the maximum extent of the Net Premium paid on this Strategy</i>) situation can be handled by making following adjustments: (i) Short both CEs & PEs; or (ii) Short CEs; or (iii) Short PEs. These adjustments are discussed below: (i) <u>Counter Adjustment through Short Option (both sides)</u>: If the underlying do not seem to be breaching the Breakeven Strike of this Strategy and seems to remain until Expiry of the Long Options, within a range, then, both Far OTM CEs and PEs can be sold (<i>i.e. additional Short CE & PE to be initiated</i>). These additional Short CEs and PEs must be even Far OTMs than the Short Options on the hedged leg, and of the same or closer Expiry series than that of the Long Options

OTM Short CEs and Short PEs (*of equal quantity as that of Long legs, and of same Expiry series as that of the Long Options*). This hedging of Long Strangle through Reverse Iron Condor will mitigate the potential risk of loss on the Long Strangle into a pre-calculated even much Limited Loss situation. You may refer to the details of Reverse Iron Condor given on the other side of this Table for better understanding.

Counter Adjustment through Short Option (both sides): If the underlying do not seem to be breaching the Breakeven Strike of this Strategy and seems to remain until Expiry of the Long Options, within a range, then, both **Far OTM CEs and PEs can be sold** (Short CE & PE to be initiated). These Short CEs and PEs must be even Far OTMs than the Long Options initiated as the primary leg, and of the same or closer Expiry series than that of the Long Options leg.

Further, these Short CEs & PEs can be initiated on such sufficient quantities to receive aggregate Premium Credit which is equal to or more than the aggregate Debit incurred on this Strategy through Long Options leg. This way the Long Strangle gets converted into Reverse Iron Condor or both side

leg. This way the Reverse Iron Condor gets converted into both side Ratio Spreads (*with more Shorts than Longs on both CE side & PE side*).

Further, these additional Short CEs & PEs can be initiated in such sufficient quantities to receive aggregate Premium Credit which is equal to or more than the Net Debit incurred on this Strategy. With this adjustment, the Reverse Iron Condor gets converted into both side Ratio Spreads (*with more Shorts than Longs on both CE side & PE side*)

Idea in this adjustment is to pick suitable Far OTM CEs & PEs for Shorting, such that these Far OTM Options expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying breaks out and breaches the Breakeven Strike on any side, then in that situation too these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Thus, suitable number of Short Options (additional CEs and PEs

Ratio Spreads (*with more Shorts than Longs on both CE side & PE side*).

Idea in this adjustment is to pick up a suitable Far OTM CEs & PEs for Shorting, such that these Far OTM Options expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying breaks-out and breaches the Breakeven Strike on any side, then in that situation too these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Thus, suitable number of Short Options (CEs and PEs Short) need to be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short Options position as an adjustment in comparison to the original number of Lots initiated on the Strategy. If the Short Options generates profit and

Short) need to be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short Options position as an adjustment in comparison to the original number of Lots initiated on the Strategy. If the Short Options generates profit and reasonably minimizes the loss in this Strategy before Expiry, then it would be advisable to book the profit and to exit this Strategy. However, selling Options will require higher margin / capital and MTM requirements will also have to be met.

- (ii) Counter Adjustment through Short Option (one side): If there seems to be a slow trend on the downward, such that the Breakeven Strike does not seem to be breached downwardly (i.e. on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then Far OTM CEs **can be sold** (i.e. additional Short CEs to be initiated).

However, If there seems to be a slow uptrend, such that the Breakeven Strike does not seem to be breached upwardly (i.e. on the CE side) in this Strategy and the underlying seems to be in a mild upwardly direction, then Far OTM PEs **can be sold** (i.e. additional Short PEs to be initiated).

Idea in this adjustment is to pick up a suitable far OTM Option for

reasonably minimizes the loss in this Strategy before Expiry, then it would be advisable to book the profit and to exit this Strategy. However, selling Options will require higher margin / capital and MTM requirements will also have to be met.

- (ii) Counter Adjustment through Short Option (one side): If there seems to be a slow trend on the downward, such that the Breakeven Strike does not seem to be breached downwardly (i.e. on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then Far OTM CEs **can be sold** (Short CEs to be initiated).

However, If there seems to be a slow uptrend, such that the Breakeven Strike does not seem to be breached upwardly (i.e. on the CE side) in this Strategy and the underlying seems to be in a mild upwardly direction, then Far OTM PEs **can be sold** (Short PEs to be initiated).

Idea in this adjustment is to pick up a suitable Far OTM Option for Shorting, such that this far OTM Option expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This Short Options position will help cover the potential loss that may be

Shorting, such that this far OTM Option expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a far OTM Option for this adjustment is important because even if the direction of the underlying reverses on the opposite side (i.e. against the additional Short Options position), then these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on the relevant Far OTM Options (CEs or PEs as the case may be), suitable number of Options can be Shorted as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to these additional Short Options position in comparison to the original number of Lots initiated on the Strategy. These additional Short Options position should be initiated at such Far OTM Strike(s), which may have reasonable Premium and is expected to expire worthless as OTM on Expiry. However, selling additional Options

generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying reverses on the opposite side (i.e. against the Short Options position), then these Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on the relevant Far OTM Options (CEs or PEs as the case may be), suitable number of Options can be Shorted as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to these additional Short Options position in comparison to the original number of Lots initiated on the Strategy. These Short Options position should be initiated at such Far OTM Strike(s), which may have reasonable Premium and is expected to expire worthless as OTM on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

will require higher margin / capital and MTM requirements will also have to be met.

(iii) Adjustment through Pyramiding: If the underlying seems to be moving in one direction (and not really hovering in a range) but with limited momentum and does not seem to be able to breach the Breakeven Strike in that direction (CE or PE, as the case may be) by Expiry, then Far OTM Options of that direction (in which the underlying has been slowly advancing) can be Shorted. That is: If there seems to be a limited trend with momentum in the downward direction, but the underlying does not seem to be able to breach the Breakeven Strike on the PE side by Expiry, then additional Far OTM **PEs can be sold** (i.e. additional Short PEs to be initiated) below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry. Likewise, If there seems to be a limited trend with momentum in the upward direction, but the underlying does not seem to be able to breach the Breakeven Strike on the CE side by Expiry, then additional Far OTM **CEs can be sold** (i.e. additional Short CEs to be initiated) above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry.

Idea in this adjustment is to pick up suitable Far OTM Options for

(iii) Adjustment through Pyramiding:

If the underlying seems to be moving in one direction (and not really hovering in a range) but with limited momentum and does not seem to be able to breach the Breakeven Strike in that direction (CE or PE, as the case may be) by Expiry, then Far OTM Options of that direction (in which the underlying has been slowly advancing) can be Shorted. That is: If there seems to be a limited trend with momentum in the downward direction, but the underlying does not seem to be able to breach the Breakeven Strike on the PE side by Expiry, then Far OTM **PEs can be sold** (Short PEs to be initiated) below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry. Likewise, If there seems to be a limited trend with momentum in the upward direction, but the underlying does not seem to be able to breach the Breakeven Strike on the CE side by Expiry, then Far OTM **CEs can be sold** (Short CEs to be initiated) above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry.

Idea in this adjustment is to pick up suitable Far OTM Options for Shorting in the same direction in which the underlying is

Shorting in the same direction in which the underlying is advancing, such that these Far OTM Short Options (initiated as part of adjustments) expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. These Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of Far OTM Options for this adjustment is important because even if the trend of the underlying gets into trending momentum in the same direction and breaches the Breakeven Strike and continues further in that direction, then too these additional Short Options position must be at such Strike which can be expected to be not breached by the underlying by Expiry and to expire as OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the max loss in the original Strategy and the likely mild trend of the underlying and the Premium available on relevant Far OTM Options (*i.e. in case of PE Shorts, below the Support area; and in case of CE Shorts, above the Resistance area*), suitable number of Options can be considered to be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these additional Short Options due to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to

advancing, such that these Far OTM Short Options (initiated as part of adjustments) expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. These Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of Far OTM Options for this adjustment is important because even if the trend of the underlying gets into trending momentum in the same direction and breaches the Breakeven Strike and continues further in that direction, then too these Short Options position must be at such Strike which can be expected to be not breached by the underlying by Expiry and to expire as OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the max loss in the original Strategy and the likely mild trend of the underlying and the Premium available on relevant Far OTM Options (*i.e. in case of PE Shorts, below the Support area; and in case of CE Shorts, above the Resistance area*), suitable number of Options can be considered to be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these Short Options due to time decay on Expiry. Generally, at least 2 to 4 times more Lot quantity may be required to be added to

be added to Short for this adjustment, in comparison to the original number of Lots initiated on the Strategy.

In this type of adjustment, Short Options positions can also be added in a pyramidal structure.

That is:

- as the downtrend continues Far OTM PE's Premium would rise, therefore, additional Short PE positions can be added at subsequent lower Strike levels as the downtrend continues with lower PE's gaining decent Premium values. *For example, when the downtrend continues in Nifty, a ITM PE at 16000 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 15800 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.*
- as the uptrend continues Far OTM CE's Premium would rise, therefore, additional Short CE positions can be added at subsequent higher Strike levels as the uptrend continues with higher CE's gaining decent Premium values. *For example, when the uptrend continues, a Far OTM CE at 17800 having Premium of Rs. 50 can be sold, thereafter when the Nifty rises further, subsequent*

Short for this adjustment, in comparison to the original number of Lots initiated on the Strategy.

In this type of adjustment, Short Options positions can also be added in a pyramidal structure. That is:

- as the downtrend continues Far OTM PEs' Premium would rise, therefore, Short PEs positions can be added at subsequent lower Strike levels as the downtrend continues with lower PEs gaining decent Premium Is. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16000 Ig Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 15800 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.*
- as the uptrend continues Far OTM CEs' Premium would rise, therefore, Short CEs positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining premium values. *For example, when the uptrend continues in Nifty, a Far OTM CEI7800 having Premium of Rs. 50 can*

higher CE at 17900 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.

This **Shorting of Options in a pyramiding manner** may ensure a broader Breakeven Strike for the Short leg (i.e. larger risk area protection) and thus greater probability of profiting due to Theta decay on these bunch of Short Options on Expiry. However, selling Options will require higher margin / capital and MTM requirements will also have to be met.

be sold, thereafter when the Nifty rises further, subsequent higher CE at 17900 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.

This **Shorting of Options in a pyramiding manner** may ensure a broader Breakeven Strike for the Short leg (i.e. larger risk area protection) and thus greater probability of profiting due to Theta decay on these bunch of Short Options on Expiry. However, selling Options will require higher margin / capital and MTM requirements will also have to be met.

LONG STRADDLE & REVERSE IRONFLY / BUTTERFLY

When a view is formed that the underlying would soon likely to take a directional move in any one direction, may be on account of any news, outcome, event etc., but it is not certain in which direction that momentum movement of the underlying is likely to occur, then such view can be played out by a neutral strategy employing Long Options positions at ATM Strikes with the expectation that the underlying would in response to any expected, news, outcome etc would very soon take one sided strong momentum move.

Thus, when the view on the underlying is that it is expected to make one sided strong momentum move very soon, but it is not certain that in which direction the underlying would make such a move; and such situation is played out through Long positions in Naked ATM CE & PE Options, then such a Strategy is called **Long Straddle**. In Long Straddle Strategy, ATM CE & ATM PE are bought in equal quantity, on the same underlying pertaining to same Expiry series. In this Strategy, the expectation is that the underlying will soon make a sudden one-sided strong momentum move, and would trend much beyond the current level either upwardly or downwardly very shortly, crossing beyond the Breakeven Strikes of the Long Options (on either side). Long Straddle involves naked Long positions on ATM CE & PE Options (involving two legs only). This Strategy has Unlimited Profit potential if the underlying moves swiftly with strong momentum on either side; but it may also generate pre-calculated Limited Max Loss if the Breakeven range is not breached by the underlying with good momentum.

However, when the Long Straddle (naked Strategy) is hedged with Short Options on OTM Strikes (on both CE & PE side), then such Strategy is called **Reverse Iron Fly or Reverse Iron Butterfly (also referred to as Long Iron Fly or Long Iron Butterfly)**⁴⁷. In Reverse Iron Butterfly Strategy, there is (i) ATM CE Long (CE **primary leg**) and OTM CE Short (CE **hedged leg**), in equal quantity,

⁴⁷Usually, when the OTM Short legs of both CE & PE sides are closer to the ATM in this Strategy, then it is referred to as Reverse Iron Fly; and when the Short legs of both CE & PE sides are little farther away from the ATM in this Strategy, then it is referred to as Reverse Iron Butterfly Strategy.

on the same underlying pertaining to same Expiry series; and (ii) ATM PE Long (**PE primary leg**) and OTM PE Short (**PE hedged leg**), in equal quantity, on the same underlying pertaining to same Expiry series. In essence, Reverse Iron Butterfly is pairing of Bull Call Debit Spread Strategy and Bear Put Debit Spread Strategy joined at the ATM; and in aggregate involves 4 legs. Like in Long Straddle, in Reverse Iron Butterfly too, the expectation is that the underlying will soon make a sudden one sided strong momentum move, and may trend much beyond the current level either upwardly or downwardly within a short span of time, crossing beyond the Breakeven Strikes of the Long Options on either side; however the hedged legs are added to the both the Long legs of Long Straddle in order to ensure that if the underlying do not soon make a sudden one sided strong momentum move as expected on either direction, such that the Breakeven Strike of Reverse Iron Fly Strategy is not crossed-over by the underlying by Expiry, then the CE hedged leg and PE hedged leg will cover up for the losses that may be incurred on the CE & PE primary legs. Thus, Reverse Iron Butterfly Strategy reduces the Loss amount in Long Straddle if the Breakeven range is not breached by the underlying with good momentum. However, in doing so, the Unlimited Profit potential in naked Long Straddle is also reduced to pre-calculated Limited Profit in Reverse Iron Butterfly, if the underlying moves swiftly with strong momentum on either side.

With this background, now let us delve into discussing the Long Straddle Strategy and Reverse Iron Fly Strategy in detail. Both these Strategies are analysed and discussed side-by-side in the table below:

Long Straddle Strategy	Reverse Iron Fly / Butterfly Strategy
Trade Legs: - Long ATM CE Strike (<i>primary CE leg</i>); and - Long ATM PE Strike (primary PE leg) Equal number of Lots in both primary legs; and both Long legs must be of same Expiry series.	Trade Legs: - Long ATM CE Strike with higher Premium (<i>CE primary leg</i>) - Short OTM CE i.e. higher Strike with lower Premium (<i>CE hedged leg</i>) - Long ATM PE Strike with higher Premium (<i>PE primary leg</i>)

	• Short OTM PE i.e. lower Strike with lower Premium (<i>PE hedged leg</i>) All the 4 legs (<i>i.e. two Long primary legs & two Short hedged legs</i>) would be of same Expiry series, with equal quantity in each of the aforesaid four legs. CE Long and PE Long would be ATM Strike; and CE Short and PE Short must be of nearly same Premium value. It is a hedged Long Straddle, making a pair of Bull CE Debit Spread Strategy and Bear PE Debit Spread Strategy, joined at the ATM Strike.
Example: <i>If ATM is at 17000, then for Long Straddle:</i> • Buy 5 Lots Nifty 17000 CE of Next Week Expiry; and • Buy 5 Lots Nifty 17000 PE of Next Week Expiry	Example: <i>If ATM is at 17000, then for Reverse Iron Butterfly:</i> • Buy 4 Lots Nifty 17000 ATM CE of Current Week Expiry (at Rs. 220 per Lot) • Sell 4 Lots Nifty 17500 CE of Current Week Expiry (at Rs. 120 per Lot) • Buy 4 Lots Nifty 17000 ATM PE of Current Week Expiry (at Rs. 250 per Lot) • Sell 4 Lots Nifty 16500 PE of Current Week Expiry (at Rs. 160 per Lot)
Objective: Objective is to play a Neutral / uncertain strong momentum one-sided directional move on the underlying on account of any event, news, outcomes etc., likely to occur very shortly,	Objective: Objective is to play a Neutral / uncertain strong momentum one-sided directional move on the underlying on account of any event, news, outcomes etc., through buying ATM CEs and PEs (both as the primary

through buying ATM CEs and PEs (both as the primary leg), as the expectation is that the underlying will soon make a sudden strong momentum one-sided directional move (*or a huge gapup or gapdown*).

It is an aggregate Debit Strategy, as both the Long legs are initiated by paying the Premium.

On arrival of a soon strong momentum one-sided directional move on the underlying (*or a huge gapup or gapdown*), either of the ATM Long primary leg becomes an ITM and the other ATM Long primary leg becomes a Far OTM. The Long position leg which becomes an ITM crosses beyond the Breakeven Strike of this Strategy and generates profit; and the other Long position leg which becomes a Far OTM generates loss.

Further, due to the sudden strong momentum trending move of the underlying (*or a huge gapup or gapdown*), one of the Long Options position can generate huge profit, whereas the other Long Options position which becomes a Far OTM can only yield loss limited to the extent of the premium paid on buying this Long Option. Thus, the net profit between the two Long Options, is the profit generated in this Strategy.

Accordingly, this Strategy can generate limited loss to the maximum extent of the aggregate Premium paid on both

leg), as the expectation is that the underlying will soon make a sudden strong momentum one-sided directional move (*or a huge gapup or gapdown*), and may trend in that direction, just like in a naked Long Straddle Strategy.

However, in this Strategy: in order to mitigate the risk / loss that may arise if the underlying fails to breach the Breakeven Strike on the primary legs by Expiry, a pair of Short Options are also initiated simultaneously with the primary Long legs, such that this Strategy becomes hedged Long Straddle, comprising of a pair of Bull CE Debit Spread Strategy and Bear PE Debit Spread Strategy, joined at the ATM through the Long legs. Therefore, if the underlying fails to breach the Breakeven Strike of the Long Options, then OTM Short Options on the hedged leg would expire as an OTM too, thereby reducing the loss caused to the maximum extent of Premium paid on the Long legs, out of the Credit or Premium received on the Short legs.

Thus, in effect, Reverse Iron Fly comprising of Bull CE Debit Spread Strategy and Bear PE Debit Spread Strategy, converts the naked Long Straddle into a hedged Long Straddle so as to cover and limit the loss that may arise in a naked Long Straddle position, if the underlying fails to breach the Breakeven Strike of the Long Straddle due to non-arrival of a strong momentum trend in either direction.

the Long legs, but if the underlying takes a strong momentum one-sided trending move (or a huge gapup or gapdown), then this Strategy is capable of generating huge profit.	This Strategy comprising of two Long Options (on ATM Strikes) and two Short Options (on OTM Strikes) makes this strategy a Net Debit Strategy, because both the Long Options are initiated by paying higher Premiums, and the Short Options are initiated by collecting lesser Premiums. On arrival of a soon strong momentum one-sided directional move on the underlying (or a huge gapup or gapdown), either side of ATM Long primary leg becomes an ITM and the other side ATM Long position & Short position becomes an even farther OTM. When the underlying crosses beyond the Breakeven Strike of this Strategy on either side such that the one of the Long Option side (<i>i.e. CE side or PE side, as the case may be</i>) becomes an ITM, then this Strategy generates profit; because the Long Option which becomes an ITM generates higher profit than the Net premium paid on the Strategy. However, in this Strategy the profit potential gets limited (due to the Short legs added to otherwise naked Long Straddle). Accordingly, this Strategy can generate limited loss to the maximum extent of the aggregate Net Premium paid on this Strategy, but if the underlying takes a strong momentum one-sided trending move (or a huge gapup or gapdown), then this Strategy is capable of generating good profit, which is capable of yielding a limited pre-calculated max profit. Both the max profit & max loss in this Strategy can be pre-calculated from Expiry perspective.
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Demerits:

- It comprises of naked Long positions.
- This Strategy is workable/ profitable only when there is a strong conviction that soon there will be arrival of a strong momentum one-sided trending move of the underlying (or a huge gapup or gapdown). However, if (i) the underlying moves one-sided but there is no momentum; or the underlying gets into a rangebound movement, then this Strategy would yield loss due to erosion of Time Value on both primary legs.
- This Strategy requires more Premium to be paid, as against the Long Strangle (or even Reverse Iron Fly).
- Thus, if the underlying does not soon move with strong momentum (or fails to make a huge gapup or gapdown), then both the Long legs may continue to be ATM Strikes (*or one primary leg may be a near ITM and another near OTM*), which situation would generate loss in this Strategy. Further, as the time passes and Expiry approaches near, and the underlying fails to make the one-sided momentum trending move and do not cross the Breakeven Strike of this

Demerits:

- Since, in this Strategy on each CE and PE sides, there is one Long position initiated at a higher Premium ATM; and a Short position initiated at a lower Premium OTM. Thus, each of the CE and PE legs have a Net Premium Debit (*i.e. Premium paid on Long leg – Premium received on Short leg*). This Net Debit Premium on Reverse Iron Fly Strategy is less than the aggregate Premium Debit on Long Straddle.
- Since, this Strategy is a Net Debit Strategy, therefore, from Expiry perspective, the aggregate Net Premium paid need to be first covered up as profit in this Strategy, to become overall profitable in this Strategy.
- This Strategy is workable/ profitable only when there is a strong conviction that soon there will be arrival of a strong momentum one-sided trending move of the underlying (or a huge gapup or gapdown). From Expiry perspective, for this Strategy to be profitable it is required that the underlying must either trend downwardly and cross below the Breakeven Strike of this Strategy on the PE side; or the underlying must trend upwardly and cross above the Breakeven Strike of this Strategy on the CE side (*the Breakeven Strikes in this Strategy are discussed below here*).

Strategy on either side, then the impact of Theta and failure to cross-over the Breakeven Strike both would cause loss of the entire aggregate Premium paid on this Strategy. • Therefore, two factors which are most detrimental to this Strategy are: (i) rangebound move in the underlying; and (ii) Theta impact on the primary legs. Therefore, this Strategy is heavily dependent on soon arrival of strong momentum one-sided trending move of the underlying (or a huge gapup or gapdown). • Due to the increasing Theta impact with the approach of Options Expiry, this Strategy may be avoided for positional holding near Expiry. • It is an aggregate Debit Strategy. Since both Long legs comprises of buying the ATM Strikes, the Premium on both Long legs is the amount of aggregate Premium paid for this Strategy. Accordingly, from Expiry perspective, the aggregate Premium paid need to be first covered up as profit in this Strategy, to become overall profitable in this Strategy. • The aggregate of the Premium paid on both Long legs defines a higher Breakeven Strike to be	• However, if (i) the underlying move one-sided but there is no momentum; or the underlying gets into a rangebound movement, then this Strategy would yield limited loss (to the extent of Net Premium paid on this Strategy) due to erosion of Time Value. • Thus, with the passage of time, if the underlying does not move with momentum, then both the Long legs may continue to be ATM Strikes (<i>or one side Options may be a near ITM and another side Options may be a near OTM</i>) and the primary leg starts generating loss due to the rising Theta impact. At the same time, both the Short legs will generate profit due to Theta decay in aforesaid situation. Thus, if by Expiry of the Options, if the underlying fails to make the one-sided momentum trending move (or huge gapup/ gapdown) and do not cross the Breakeven Strike of this Strategy on either side, then both the Long legs and may expire as ATM/OTM and both the Short legs would expire worthless as OTM, thereby this Strategy may generate maximum loss to the extent of aggregate Net Premium paid on this Strategy. • Therefore, two factors which are most detrimental to this Strategy are: (i) rangebound move in the underlying; and (ii) Theta impact on the primary legs. Therefore, this Strategy is heavily
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crossed-over to make this Strategy profitable from Expiry perspective. Thus, from Expiry perspective, it is required that the underlying must either trend downwardly and cross below the Breakeven Strike of this Strategy on the PE Long side (<i>or take a huge gapdown</i>); or the underlying must trend upwardly and cross above the Breakeven Strike of this Strategy on the CE Long side (<i>or take a huge gapup</i>). • When the Volatility is in a falling state, then there will be erosion caused to the Premium of the Long Options (or it may act as a deterrence to let the Premium of the Long Options rise), thereby making this Strategy not viable from profit perspective.	dependent on strong momentum one-sided trending move of the underlying (or a huge gapup/ gapdown). • Due to the increasing Theta impact with the approach of Options Expiry, this Strategy may be avoided for positional holding near Expiry. • When the Volatility is in a falling state, then there will be erosion caused to the Premium of the Long Options (or it may act as a deterrence to let the Premium of the Long Options rise), thereby making this Strategy not viable from profit perspective, as even though the erosion would also be caused in the Premium Credit on the Short legs but the fall in Volatility may expedite loss of Net Premium Debit made on this Strategy.
<u>Benefits of Long Straddle:</u> • This is a neutral Strategy i.e. when the view is uncertain in which direction the underlying can move with strong momentum (<i>or might take a huge gapup or gapdown</i>) as a result of any news, event or outcome etc., this Strategy can be implemented. This is mainly targeted for a very quick arrival of momentum or gapup/gapdown within a very short span of time. • Since this Strategy is implemented through buying ATM CEs and PEs (Long Options), it requires	<u>Benefits of Reverse Iron Fly:</u> • This is a neutral Strategy i.e. when the view is uncertain in which direction the underlying can move with strong momentum (or might take a huge gapup or gapdown) as a result of any news, event or outcome etc., this Strategy can be implemented. • It is a hedged Strategy (i.e. Reverse Iron Fly is hedged Long Straddle). • Since, it is a hedged Strategy, the capital / margin required is less and does not require capital towards any MTM requirements.

less capital/ margin and does not need any further capital towards MTM adjustments. • If the view goes as expected, then this Strategy is capable of generating huge profit if the trend in one side continues (or if there is a huge gapup or gapdown), but if the view fails then it can cause a limited loss to the maximum extent of aggregate Premium paid on both the Long legs. Thus, this Strategy is the kind with unlimited profit and limited loss. • Rise in Volatility is favourable for this Strategy as rise in Volatility will help the Premium of the Long Options to rise (or to not cause them fall much). • Thus, rise in Volatility and one-sided strong momentum trending move (or likely huge gapup or gapdown) is the requirement for profitability in this Strategy. Further, if there is huge Volatility spike, then the premium value of both CE Long and PE Long legs would rise exponentially, even if there is no significant move in the underlying.	• If the view goes as expected, then this Strategy is capable of generating reasonable profit if the trend in one side continues until Expiry of Options. • Since this a hedged Strategy, therefore, if the underlying fails to breakout the Breakeven Strike by the Expiry on either side, then the hedged leg helps mitigate the loss of the Premium paid on the primary legs through the Credit of Premium received on the Short hedged legs. Thus, this Strategy helps curtail the loss that may arise on the Long Options, due to the Short hedged legs added in this Strategy (<i>which are likely to generate profit due to erosion in their Premium due to Volatility crash or Theta decay</i>). • Rise in Volatility is favourable for this Strategy as rise in Volatility will help the Premium of the Long Options to rise (or to not cause them fall much). • Thus, rise in Volatility and one-sided strong momentum trending move is the requirement for profitability in this Strategy. Further, if there is huge Volatility spike, then the premium value of both CE Long and PE Long legs would rise exponentially, even if there is no significant move in the underlying.
<u>Breakeven Strike of this Strategy from Expiry perspective:</u>	<u>Breakeven Strike of this Strategy from Expiry perspective:</u>

This Strategy comprises of naked CE Long at ATM Strike; and a naked PE long at ATM Strike. This is an aggregate Debit Strategy as the Premium at which both Longs are initiated, on aggregate basis is the total Premium paid on this Strategy.

The aggregate Premium paid on this Strategy determines the Breakeven Strike range which need to be crossed over by the underlying on either side in order to make this Strategy profitable. The Breakeven Strike range on the upper side and the lower side are calculated as follows in this Strategy:

- the Breakeven Strike on the CE side (upper side) is: [The CE Strike (at which Long is initiated) + aggregate Premium paid on both CE & PE Long]; and
- the Breakeven Strike on the PE side (lower side) is: [The PE Strike (at which Long is initiated) - aggregate Premium paid on both CE & PE Longs].

Thus, if by Expiry of the Long Options, the underlying successfully crosses-over the aforesaid Breakeven Strikes (*either on the upper side or the lower side*), then this Strategy would yield profit. Further, in case of continuous trending movement of the underlying after successfully crossing-over the Breakeven Strike on either side by the underlying (*or a huge gapup or gapdown, which crosses-over the*

The CE side comprises of CE Long primary leg at higher Premium and CE short hedged leg at lower Premium. Thus, there is a Net Premium Debit on the CE side of Reverse IronFly.

Likewise, the PE side comprises of PE Long primary leg at higher Premium and PE Short hedged leg at lower Premium. Thus, there is a Net Premium Debit on the PE side of Reverse Iron Fly.

The sum of the Net Premium Debit on the CE and PE Side is the aggregate Net Premium Debit paid in this Strategy. Accordingly:

- the Breakeven Strike of the CE side in this Strategy (upper range) is: [CE Long primary leg Strike + the aggregate Net Premium Debit in the strategy]; and
- the Breakeven Strike of the PE side in this Strategy (lower range) is: [PE Short primary leg Strike - the aggregate Net Premium Debit in the Strategy].

Thus, if by Expiry of the Long Options, the underlying successfully crosses-over the aforesaid Breakeven Strikes (*either on the upper side or the lower side*), then this Strategy would yield profit. However, if by Expiry of these Options, the underlying fails to cross-over either upper or lower side of the Breakeven Strikes, then the Strategy would yield loss (*which may extend to the maximum extent of the Net Premium paid on the Strategy*).

For example: If ATM is at 17000 for Reverse Iron Fly:

Breakeven Strike), a huge / unlimited profit situation might arise.

However, if by Expiry of these Long Options, the underlying fails to cross-over either upper or lower side of the Breakeven Strikes, then the Strategy would yield loss (*which may extend to the maximum extent of the aggregate Premium paid on the Strategy*).

Example: If ATM is at 17000, then for Long Straddle: If Nifty 17000 PE is bought at Rs. 300 per Lot & Nifty 17000 CE is bought at Rs. 350 per Lot, then the aggregate Premium paid on this Strategy would be Rs. 300 + Rs 350 = Rs. 650 per Lot.

Thus, the BE Strike of this Strategy will be:

- On CE side: $17000 + (300+350) = 17650$ CE Strike; and
- On PE side: $17000 - (300+350) = 16350$ PE Strike

Thus, if by Expiry, the underlying successfully crosses-over the aforesaid Breakeven Strikes (*either on the upper side or the lower side*), then this Strategy would yield profit; but if by Expiry, the underlying fails to successfully cross-over the relevant Breakeven Strike on either side, then the Strategy would yield loss (*which may extend to the maximum extent of Rs. 650 per Lot, i.e. the total Premium paid on this Strategy*).

Thus, in the aforementioned example: if the underlying goes higher until

Nifty 17000 is bought at Rs. 350 per Lot & Nifty 17500 CE is sold at Rs. 200 per Lot; and

Nifty 17000 PE is bought at Rs. 300 per Lot & Nifty 16500 PE is sold at Rs. 150 per Lot, then:

the Net Premium Debit paid on this Strategy will be: $[(350+300) - (200+150)] = 650 - 350 = 300$

Thus, the BE Strike of this Strategy will be:

- On CE side: $17000 + 300 = 17300$ CE Strike; and
- On PE side: $17000 - 300 = 16700$ PE Strike

Thus, if by Expiry, the underlying successfully crosses-over the aforesaid Breakeven Strikes (*either on the upper side or the lower side*), then this Strategy would yield profit; but if by Expiry, the underlying fails to successfully cross-over the relevant Breakeven Strike on either side, then the Strategy would yield loss (*which may extend to the maximum extent of Rs. 300 per Lot, i.e. the net Premium paid on this Strategy*).

Thus, in the aforementioned example: if the underlying goes higher until Expiry and successfully crosses-over the upper Breakeven Strike i.e. 17300 CE and keeps trending higher then the Strategy will be in profit; but if the underlying by Expiry fails to successfully cross-over the Breakeven Strike of 17300, then this Strategy will incur loss (*which may extend to the*

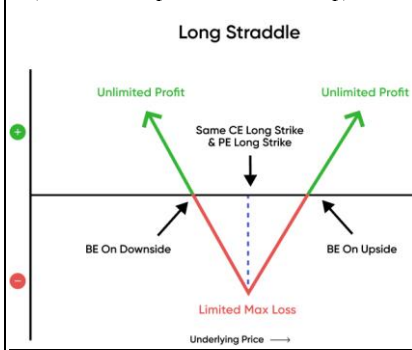
Expiry and successfully crosses-over the upper Breakeven Strike i.e. 17650 CE and keeps trending higher, then the Strategy will be in profit; but if the underlying by Expiry fails to cross-over the Breakeven Strike of 17650, then this Strategy will incur loss (*which may extend to the maximum extent of total Premium paid on this Strategy (i.e. Rs. 650 per Lot)*).

Likewise, if the underlying goes lower until Expiry and successfully crosses-over the lower Breakeven Strike i.e. 16350 PE and keeps trending lower, then the Strategy will be in profit; but if the underlying by Expiry fails to successfully cross-over the Breakeven Strike of 16350, then this Strategy will incur loss (*which may extend to the maximum extent of total Premium paid on this Strategy (i.e. Rs. 650 per Lot)*).

maximum extent of Net Premium paid on this Strategy (i.e. Rs. 300 per Lot).

Likewise, if the underlying goes lower until Expiry and successfully crosses-over the lower Breakeven Strike i.e. 16700 PE and keeps trending lower, then the Strategy will be in profit; but if the underlying by Expiry fails to successfully cross-over the Breakeven Strike of 16700, then this Strategy will incur loss (*which may extend to the maximum extent of Net Premium paid on this Strategy (i.e. Rs. 300 per Lot)*).

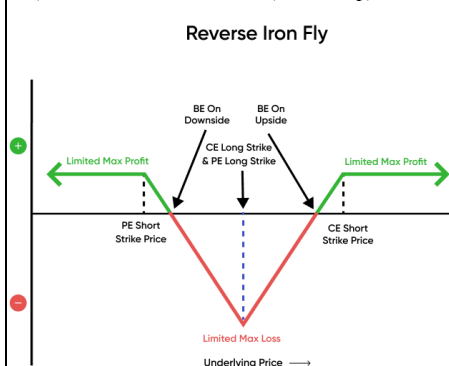
Payoff of Long Straddle Strategy



Loss in this Strategy from Expiry perspective:

Max Loss: Since, this Strategy comprises of naked Long legs, for

Payoff of Reverse Iron Fly Strategy



Loss in this Strategy from Expiry perspective:

Max Loss: If by Expiry of these Options, the underlying fails to cross-over either

which the Premiums are paid, therefore, the aggregate Premium paid for both the Long legs in this Strategy is the maximum loss that may occur. Thus, Maximum Loss in this Strategy will be limited and can be pre-calculated. The Maximum Loss in this Strategy is equivalent to the Total Premium paid on this Strategy, i.e.

Max Loss on Long Straddle = [Premium Paid on CE Long leg + Premium Paid on PE Long Leg]

Max Loss scenario:

The situation of this Max Loss would occur if by Expiry of the Long Options, the underlying closes at the Strike on which Long legs have been initiated.

Loss zone:

If the underlying closes by Expiry within the two Breakeven Levels i.e. on the CE side and on the PE side, then loss would be incurred on the Strategy. Therefore, the Loss Zone of this Strategy lies between the BE Level of the CE side and BE Level of the PE side.

Loss Zone on the CE side: if the underlying closes higher than the CE Long leg but below the BE Strike on the CE side, then loss would be incurred on the Strategy. Thus, on the CE side, CE Long Strike to BE Strike on the CE side of the Strategy is a Loss zone. Lower loss would be generated on the Strategy if the underlying by Expiry closes towards the BE Strike on CE

upper or lower side of the Breakeven Strikes, then the Strategy would yield loss (*which may extend to the maximum extent of the aggregate Net Premium paid on this Strategy*).

Thus, Maximum Loss in this Strategy will be limited and can be pre-calculated. The Maximum Loss in this Strategy is the Net Premium paid on this Strategy.

Max Loss on Reverse Iron Fly = [Aggregate Premium Paid on CE Long leg & PE Long Leg] **minus** [Aggregate Premium Credit received on CE Short leg & PE Short Leg]

Max Loss scenario:

The situation of this Max Loss would occur if by Expiry of the Long Options, the underlying closes at the Strike on which Long legs have been initiated.

Loss zone:

If the underlying closes by Expiry within the two Breakeven Levels i.e. on the CE side and on the PE side, then loss would be incurred on the Strategy. Therefore, the Loss Zone of this Strategy lies between the BE Level of the CE side and BE Level of the PE side.

Loss Zone on the CE side: if the underlying closes higher than the CE Long leg but below the BE Strike on the CE side, then loss would be incurred on the Strategy. Thus, on the CE side, CE Long Strike to BE Strike on the CE side of the Strategy is a Loss zone. Lower loss would be generated on the Strategy if the underlying by Expiry closes towards the BE Strike on CE side;

side; and higher loss would be generated on the Strategy if the underlying closes near or at the CE Long Strike.

Loss zone on the PE side: if the underlying closes lower than the PE Long leg but above the BE Strike on the PE side, then some loss would be incurred on the Strategy. Thus, on the PE side, PE Long Strike to BE Strike of the Strategy on the PE side is a Loss zone. Lower loss would be generated on the Strategy if the underlying by Expiry closes towards the BE Strike on PE side; and higher loss would be generated on the Strategy if the underlying closes near or at the PE Long Strike.

For example: If ATM is at 17000, then for Long Straddle: If Nifty 17000 PE is bought at Rs. 300 per Lot & Nifty 17000 CE is bought at Rs. 350 per Lot, then the aggregate Premium paid on this Strategy would be Rs. $300 + 350 = \text{Rs. } 650$ per Lot.

Thus, the BE Strike of this Strategy will be:

- On CE side: $17000 + (300+350) = 17650$ CE Strike; and
- On PE side: $17000 - (300+350) = 16350$ PE Strike

Thus, in this Strategy, if: (a) the Nifty fails to cross-over above the Breakeven strike of 17650 upwardly by the Expiry; or (b) if underlying fails to cross-over

and higher loss would be generated on the Strategy if the underlying closes near or at the CE Long Strike.

Loss zone on the PE side: if the underlying closes lower than the PE Long leg but above the BE Strike on the PE side, then some loss would be incurred on the Strategy. Thus, on the PE side, PE Long Strike to BE Strike of the Strategy on the PE side is a Loss zone. Lower loss would be generated on the Strategy if the underlying by Expiry closes towards the BE Strike on PE side; and higher loss will be generated on the Strategy if the underlying closes near or at the PE Long Strike.

Example: If ATM is at 17000, then for Ice Iron Fly:

Nifty 17000 CE is bought at Rs. 350 per Lot & Nifty 17500 CE is sold at Rs. 200 per Lot; and

Nifty 17000 PE is bought at Rs. 300 per Lot & Nifty 16500 PE is sold at Rs. 150 per Lot, then:

the Net Premium Debit paid on this Strategy will be: $[(350+300) - (200+150)] = 650 - 350 = 300$

In the aforesaid example:

If the underlying fails to breach the Breakeven Strike of 17300 or 16700 Expiry, then this Strategy would yield loss. Further, if Nifty closes by Expiry at 17000 Strike (i.e. the Strike at which Long legs have been initiated), then Max Loss equivalent to total aggregate Premium of Rs. 300 per Lot would be incurred on this Strategy.

<i>below the Breakeven strike of 16350 downwardly by the Expiry, then this Strategy would yield loss. Further, if Nifty closes by Expiry at 17000 Strike (i.e. the Strike at which Long legs have been initiated), then Max Loss equivalent to total aggregate Premium of Rs. 650 per Lot would be incurred on this Strategy.</i>	
<u>Profit Reward in this Strategy from Expiry perspective:</u> <u>Max Profit:</u> If by Expiry of the Long Options, if the underlying successfully crosses-over the Breakeven Strikes of the Strategy (<i>either on the upper side or the lower side</i>), then this Strategy would yield profit. More trending the underlying gets in one direction with momentum, crossing beyond the BE Strike level of the Strategy on that side, higher the profit that will be generated. Thus, the Max Profit potential on this Strategy is unlimited, provided the strong momentum makes either CE side Long Strike or PE side Long Strike a deep ITM. Thus, in case of huge gapup / gapdown or a continuous trending movement of the underlying after breaching of the Breakeven Strike on either side by the underlying, a huge / unlimited profit situation might arise from Expiry perspective. This situation implies that the Long leg Strike on the side of the momentum, ends up being an ITM on	<u>Profit in this Strategy from Expiry perspective:</u> <u>Max Profit:</u> If by Expiry of the Options, the underlying successfully crosses-over the Breakeven Strikes of the Strategy (<i>either on the upper side or the lower side</i>), then this Strategy would yield profit. More trending the underlying gets in one direction with momentum (or in case of huge gapup / gapdown), crossing beyond the BE Strike level of the Strategy on that side, higher the profit that will be generated. However, the Max Profit potential on this Strategy is limited (<i>as against unlimited profit in naked Long Straddle, in case of continuous trending momentum on any particular side</i>) and the max profit on this Strategy can be pre-calculated. <u>Max Profit Level:</u> If the underlying by Expiry closes either at or beyond the Short leg of any particular side (<i>i.e. CE Short leg on the upside and PE Short leg on the downside</i>), then the Strategy would yield Max Profit, which is limited. In this situation, both the Long leg & Short leg of that side Option (<i>where the BE Strike</i>

Expiry (and the other side Long Option expires worthless as an OTM).

Calculation of final Profit generated on the Strategy:

If the underlying closes by Expiry, after breaching the Breakeven Strike on either side, then the final Profit accrued on the Strategy on Expiry can be calculated as:

- [the final premium value of Long Option of the momentum side on Expiry (i.e. Long leg which becomes / expires as an ITM)]⁴⁸

minus

- [the aggregate Premium paid for the Strategy]

For example: If ATM is at 17000, then for Long Straddle: If Nifty 17000 PE is bought at Rs. 300 per Lot & Nifty 17000 CE is bought at Rs. 350 per Lot, then the aggregate Premium paid on this Strategy would be Rs. 300 + Rs 350 = Rs. 650 per Lot.

Also, the BE Strike of this Strategy i.e. on CE side, 17650 CE Strike; and on PE side, 16350.

Thus, in this Strategy, if:

- (a) Nifty crosses above the Breakeven Strike of 17650 Strike upwardly by

is breached) becomes an ITM. The other side of Options, both Long & Short leg becomes even farther OTM. This situation generates the Limited Max Profit situation on the Strategy. However, in this Strategy, even if the underlying gets trending on one side but it crosses beyond the Short leg of the Strategy on that side, then no higher profit would be generated on this Strategy from Expiry perspective other than the pre-calculated Max Profit that can be generated on this Strategy. Thus, this Strategy is a limited max profit Strategy; and the max profit on this Strategy can be pre-calculated.

Calculation of Max Profit on the Strategy:

The Max Profit potential of this Strategy can be pre-calculated as:

- [Strike difference between Long & Short leg of CE / PE side]

minus

- [the Net Premium paid for the Strategy]

Using the above formula, the Max Profit potential for each of CE side and PE side can be separately calculated. Thus, we can determine the Max Profit potential on any particular side of this Strategy. However, if the Strike difference between Long & Short leg is same for both CE side and PE side, then calculation of Max Profit as per

⁴⁸ The final premium of an Option which would expire as an ITM would be equivalent to its Intrinsic Value (which is the difference between the ATM Strike on Expiry and the Strike of the relevant Option which expired as an ITM).

<i>Expiry, and at Expiry Nifty is at 18000; then 17000 CE Long leg expires as a deep ITM generating profit (as CE Long leg Premium would rise) and the PE 17000 Long expires as far OTM generating loss (as PE Long leg Premium would fall), thereby giving a net profit in this Strategy due to upward trending move in the Nifty. Deeper the CE Long leg goes as an ITM by Expiry, more profitable the Strategy would be. The maximum profit on Expiry would be the difference between: [the final LTP of the CE Long position] and [the aggregate Premium paid on the Strategy]; or</i> (b) <i>Nifty crosses below the Breakeven Strike of 16350 Strike downwardly by Expiry, and at Expiry if Nifty closes at 16000; then 17000 PE Long leg expires as a deep ITM generating profit (as PE Long Premium would rise) and the CE 17000 Long expires as far OTM generating loss (as CE Long leg Premium would fall), thereby giving a net profit in this Strategy due to downward trending move in the Nifty. Deeper the PE Long leg goes as an ITM by Expiry, more profitable the Strategy would be. The maximum profit on Expiry would be the difference between: [the final LTP of the PE Long position] and [the aggregate Premium paid on the Strategy].</i>	aforesaid formula, would be same for both CE side and PE side. <u>Impact on Max Profit situation, due to variation in Strike Difference between CE side & PE side:</u> If the Strike difference between Long leg & Short leg, on both CE side and PE side is same (eg: 300 point difference between CE Long & CE Short and similarly 300 point difference between PE Long & PE Short), then the Max Profit would be same for the CE side as well as for the PE side. In such case, the amount so determined, is said to be the Max Profit of the Strategy. However, if the Strike difference between Long leg & Short leg, on CE side and PE side is different (eg: 300 point difference between CE Long & CE Short and 500 point difference between PE Long & PE Short), then the Max Loss would be different for the CE side and the PE side. The side where the Strike difference is more, would have more Net Premium Debit and accordingly the BE Level of that side will also increase. But with increase in BE Level, the Max Profit situation on that side would also increase. In such case, the Max Profit of the side where Strike difference is more, would be the Max Profit of the Strategy. <u>Profit Zone:</u> The profitability from Expiry perspective would arise in the Strategy, if the underlying closes above the Breakeven Strike level of this Strategy on the CE
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Profit Level:

Profit would accrue on this Strategy, from Expiry perspective, if underlying closes after successfully crossing-over the Breakeven Strike of either side, such that the Long Option of atleast one side expires as an ITM.

side⁴⁹; or if the underlying closes below the Breakeven Strike level of this Strategy on the PE side⁵⁰. Therefore, profit would be realised on this Spread if the underlying closes by Expiry after successfully crossing-over the BE Strike of this Strategy on either side.

Profit zone on CE side: Thus, if the underlying by Expiry crosses above the BE Strike on the CE side and closes between the BE Strike on CE side and at or higher than the CE Short Strike, then the Strategy would generate profit on the CE side. Therefore, this is the Profit zone on the CE side. However, if the underlying closes by Expiry at or above the CE Short Strike then Max Profit would be generated on this Strategy. The profit in this zone would be less, if the underlying closes just above the BE Strike level on the CE side; but if the underlying closes near the CE Short Strike level, then the Strategy would generate higher profit (*which may extend upto Max Profit, if the underlying closes at or above the CE Short Strike by Expiry*).

Profit zone on PE side: Similarly, if the underlying by Expiry crosses below the BE Strike on the PE side and closes between the BE Strike on PE side and at or lower than the PE Short Strike, then the Strategy would generate profit on the PE side. Therefore, this is the Profit zone on the PE side. However, if the underlying closes by Expiry at or below the PE Short Strike then

⁴⁹ That is higher Strike than the BE Level on the CE side.

⁵⁰ That is lower Strike than the BE Level on the PE side.

	Max Profit would be generated on this Strategy. The profit in this zone would be less, if the underlying closes just below the BE Strike level on the PE side; but if the underlying closes near the PE Short Strike level, then the Strategy would generate higher profit (<i>which may extend upto Max Profit, if the underlying closes at or below the PE Short Strike by Expiry</i>). <u>Calculation of Profit generated on the Strategy within Profit Zone:</u> On arrival of a strong momentum one-sided directional move on the underlying, that side of ATM Long primary leg becomes an ITM and the other side ATM Long position & Short position becomes Far OTMs. The Option side which is in the direction of the momentum (<i>i.e. Long Option on the CE side or PE side, as the case may be</i>) which becomes an ITM due to movement in the underlying generates profit; and the other Option side which becomes Far OTMs generates loss. Thus, if the underlying by Expiry successfully closes beyond the BE Strike Level of either side and closes within the profit zone of that side, then the final profit on the Strategy at Expiry can be calculated as: • [the final premium value Long Option of the momentum side on Expiry (<i>i.e. Long leg which becomes / expires as an ITM</i>)] minus • [the Net Premium paid for the Strategy]
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For example: If ATM is at 17000, then for Reverse Iron Fly: If Nifty 17000 CE is bought at Rs. 350 per Lot & Nifty 17500 CE is sold at Rs. 200 per Lot; and

Nifty 17000 PE is bought at Rs. 300 per Lot & Nifty 16500 PE is sold at Rs. 150 per Lot, then:

- the Net Premium Debit paid on this Strategy will be: $[(350+300) - (200+150)] = 650 - 350 = 100$ per Lot
- Breakeven Strike of this Strategy on upper range will be: $17000 + 300 = 17300$ CE
- Breakeven Strike of this Strategy on lower range will be: $17000 - 300 = 16700$ PE

Thus, in this Strategy, if:

- (a) Nifty crosses above the Breakeven Strike of 17300 Strike upwardly by Expiry, then 17000 CE Long leg expires as an ITM generating profit, as CE Long leg Premium would rise) and the PE 17000 Long expires as Far OTM generating loss (as PE Long premium would fall), thereby giving a net profit in this Strategy due to upward trending move in the Nifty. Deeper the CE Long leg goes as an ITM by Expiry, more profitable the Strategy would be. However, the maximum profit that can be realised on the CE side by Expiry would be: $[17500 \text{ CE} - 17000 \text{ CE}] - [300] = \text{Rs. } 200$ per Lot. Thus, overall profit in such situation on the Strategy would be Rs. 200 per qty in the Lot

	<i>i.e. $50 \times 200 = \text{Rs. } 10,000$ per Lot. This max profit on CE side would be realized on Expiry, if the underlying trends higher and closes at or above the CE Short leg. But if the underlying closes at 17400 on Expiry i.e. in the Profit Zone on the CE side, then the CE Long leg of 17000 would be an ITM with final premium value on Expiry of Rs. 400 (because on Expiry, the final premium value is equal to the Intrinsic Value of the ITM, which is calculated as $\text{ATM} - \text{ITM CE Strike}$). Therefore, the final premium value of 17000 CE would be : $[17400 - 17000 = 400]$. Thus, the final overall profit on the Strategy would be: 17000 CE final premium value – Net premium paid on the Strategy = $400 - 300 = \text{Rs. } 100$ per qty in a Lot i.e. $50 \times 100 = \text{Rs } 5000$ in a Lot.</i> <i>(b) Nifty crosses below the Breakeven Strike of 16700 Strike downwardly by Expiry, then 17000 PE Long leg expires as an ITM generating profit (as PE Long leg Premium would rise) and the CE 17000 Long expires as Far OTM generating loss (as CE Long leg Premium would fall), thereby giving a net profit in this Strategy due to downward trending move in the Nifty. Deeper the PE Long leg goes as an ITM by Expiry, more profitable the Strategy would be. However, the maximum profit on the PE side by Expiry would be: $[17000 \text{ PE} - 16500 \text{ PE}] - [300] = \text{Rs. } 200$ per</i>
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	<i>Lot. Thus, overall profit in such situation on the Strategy would be Rs. 200 per qty in the Lot i.e. $50 \times 200 = \text{Rs. } 10,000$ per Lot. This max profit on PE side would be realized on Expiry, if the underlying trends lower and closes at or below the PE Short leg. But if the underlying closes at 16600 on Expiry i.e. in the Profit Zone on the PE side, then the PE Long leg of 17000 would be an ITM with final premium value on Expiry of Rs. 400 (because on Expiry, the final premium value is equal to the Intrinsic Value of the ITM, which is calculated as $\text{ITM PE Strike} - \text{ATM}$). Therefore, the final premium value of 17000 PE would be $[17000 - 16600 = 400]$. Thus, the final overall profit on the Strategy would be: $17000 \text{ PE final premium value} - \text{Net premium paid on the Strategy} = 400 - 300 = \text{Rs. } 100$ per qty in a Lot i.e. $50 \times 100 = \text{Rs } 5000$ in a Lot.</i>
<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level on CE side:</u> [CE Long Strike + Total Premium Debit paid on the Strategy] <u>BE Level on PE side:</u> [PE Long Strike - Total Premium Debit paid on the Strategy] <u>Min Profit Level:</u> If underlying closes by Expiry just above the BE Level on CE side (<i>i.e. higher CE Strike than BE Strike</i>) or if the underlying closes by Expiry just below the BE Level on PE	<u>Profit & Loss Levels on the Strategy, from Expiry perspective:</u> <u>BE Level on CE side:</u> [CE Long Strike + Net Premium Debit paid on the Strategy] <u>BE Level on PE side:</u> [PE Long Strike – Net Premium Debit paid on the Strategy] <u>Min Profit Level:</u> If underlying closes by Expiry just above the BE Level on CE side (<i>i.e. higher CE Strike than BE Strike</i>) or if the underlying closes by Expiry just below the BE Level on PE side (<i>i.e. lower PE Strike than BE Strike</i>).

side (<i>i.e. lower PE Strike than BE Strike</i>). <u>Max Profit Level:</u> Max Profit is unlimited if the underlying successfully crosses-over the BE Strike Level on either CE side or PE Side (<i>such that one side Strike becomes an ITM</i>). Max profit situation arises as the underlying closes by Expiry anywhere higher than the BE Strike Level on the CE side; or anywhere lower than the BE Strike Level on the PE side. Deeper the CE Long or PE Long becomes an ITM, higher will be the profit generated on this Strategy. <u>Loss Zone:</u> If the underlying closes by Expiry anywhere between the BE Level on the CE side and the BE Strike on the PE side, then loss would be incurred on this Strategy. <u>Max Loss Zone:</u> If underlying closes by Expiry at the Strike on which CE Long and PE Long legs have been initiated, then Max Loss would be incurred on this Strategy.	<u>Max Profit Level:</u> Max Profit is limited if the underlying successfully crosses-over the Short Strike on either CE side or PE Side (<i>such that one side both Long & Short Strikes becomes an ITM</i>). Anywhere deeper the underlying may close beyond the Short leg, the Max Profit shall be limited to the pre-calculated Max Profit Level on that side. <u>Loss Zone:</u> If the underlying closes by Expiry anywhere between the BE Level on the CE side and the BE Strike on the PE side, then loss would be incurred on this Strategy. <u>Max Loss Zone:</u> If underlying closes by Expiry at the Strike on which CE Long and PE Long legs have been initiated, then Max Loss would be incurred on this Strategy.
<u>Options behaviour:</u> • In this Strategy, three factors help in generating profit: (i) strong momentum trending move of the underlying (or huge gapup / gapdown); and (ii) the momentum trend should arrive soon, otherwise Theta decay would adversely impact the probability of profit; and (iii)	<u>Options behaviour:</u> • In this Strategy, three factors help in generating profit: (i) strong momentum trending move of the underlying (or huge gapup / gapdown; and (ii) the momentum trend should arrive soon, otherwise Theta decay would adversely impact the probability of profit; and (iii) Volatility should either rise or remain

Volatility should either rise or remain constant, but should not go into steep falling state. Therefore, profitability in this Strategy is heavily dependent on these factors.

- Further, since the CE & PE Strikes are ATM, it results in higher Premium being paid; and consequently this Strategy in order to generate profit, need very strong momentum to arrive soon such that the underlying crosses-over the Breakeven Strike.
- Further, as the Expiry approaches near, the Theta impact on the ATM Strike CE & PE is highest (*if the underlying becomes sideways and both the primary Long legs remains an ATM*), would cause erosion on the Premium values of the Long Options. Thus, near Expiry this Strategy must be avoided unless when quick strong momentum (or huge gapup/ gapdown) is expected within a very short span of time (like next day or so) after this Strategy is initiated.
- Rise in Volatility is favourable for this Strategy as rise in Volatility will help the Premium of the Long Options to rise (or to not cause them fall much).

constant, but should not go into steep falling state. Therefore, profitability in this Strategy is heavily dependent on these factors.

- Further, since the CE & PE Strikes are ATM, it results in higher Premium being paid; and consequently this Strategy in order to generate profit, need very strong momentum to arrive soon such that the underlying crosses-over the Breakeven Strike. However, the Net Premium paid in this Strategy is lesser than the Total Premium paid on a naked Long Straddle, hence the Breakeven Strikes are shorter than the Long Straddle and max loss is lesser in this Strategy than the Long Straddle.
- Further, as the Expiry approaches near, the Theta impact on the ATM Strike CE & PE is highest (*if the underlying becomes sideways and both the primary Long legs remains an ATM*), would cause erosion on the Premium values of the Long Options. However, since in this Strategy the Long leg is hedged with Short positions therefore, the Theta also impacts the OTM CE & PE Short legs thereby helping to absorb the loss on the Long Options leg through profit on the Short leg. Thus, near Expiry this Strategy must be avoided unless when quick strong momentum (or huge gapup/ gapdown) is expected within a very short span of time (like next day or so) after this Strategy is initiated.

• Delta play between the two Long legs is separately discussed hereinbelow.	• Rise in Volatility is favourable for this Strategy as rise in Volatility will help the Premium of the Long Options to rise (or to not cause them fall much). • Delta neutral position is strived for in this Strategy at the time of initiating this Strategy. The Delta play between the CE Long and PE Long primary legs; as well the CE Short and PE Short hedged legs is separately discussed hereinbelow.
<u>Strike / Delta value:</u> The two Long legs, i.e. CE Long and PE Long are ATMs, and consequently have same Delta value of 0.5 (on single Lot basis). This equal Delta value Long legs helps to ensure uniformity in the profitability irrespective in whichever direction the momentum in the underlying arrives. This is because, if there is uncertainty with regard to which direction the underlying is going to push forward its strong momentum move, then it is better to initiate both Long primary legs with equal Delta values, thereby maintaining Delta neutrality at the time of initiating the Strategy (<i>which is ensured by initiating the Long legs at ATMs</i>). <u>Long Strap Strategy:</u> If the view on the underlying is biased on the bullish side, then even an additional Long CE leg can also be introduced along with Long Straddle. Consequently, there will be 2 Long	<u>Strike / Delta value:</u> The two Long legs, i.e. CE Long and PE Long are ATMs, and consequently have same Delta value of 0.5 (on single Lot basis). This equal Delta value Long legs helps to ensure uniformity in the profitability irrespective in whichever direction the momentum in the underlying arrives. Likewise, the two Short hedged legs in this Strategy, i.e. CE Short and PE Short must be Far OTMs, and can be initiated at such Strike levels which have more or less same LTP or Delta value. This equal Delta value Short legs helps to ensure uniformity in profitability in one side (<i>where momentum arrives</i>) and the loss incidence on the other side (<i>which is not favoured by the momentum move in the underlying</i>). This is because, if there is uncertainty with regard to which direction the underlying is going to push forward its strong momentum move, then it is better to initiate both Long primary legs with equal Delta values as well as both Short legs with equal Delta values, thereby maintaining

CEs against 1 Long PE, all at ATM Strike. This structure is called a **Long Strap**. The view here is that if the bullish momentum arrives, then the 2 Long CEs would generate much higher profit than the loss on the PE Long leg. And if the bearish momentum arrives, then the PE Long would be able to generate sufficient profit which must be able to cover the cost of the entire Strategy. The cost of the Strategy is the total premium debit incurred on the Strategy to initiated 2 Long CEs and a Long PE. From Expiry perspective in order to be profitable, in the Long Strap the momentum on the underlying must be strong enough to close beyond the BE Strike on either side. The BE Strike on either side will be:

- BE Strike for CE side: CE Strike + total Premium paid on the Strategy
- BE Strike for PE side: PE Strike + total Premium paid on the Strategy.

Thus, the profit potential on either side is unlimited, if the underlying moves with strong momentum on either side; however, if the underlying closes by Expiry between the BE Strikes on CE side & PE side, the max loss to the extent of total Premium paid on the Long Strap would be incurred.

Delta neutrality at the time of initiating the Strategy.

Thus, with approx. equal Delta values on CE Long and PE Long legs; and equal Delta values on CE Short and PE Short legs, Delta neutrality is ensured in this Strategy to maintain a balance between the profit and loss situation amongst the two sides, i.e.:

- when CE Long leg gets profitable due to rise in its LTP (i.e. when underlying rises with momentum), greater profitability is achieved as the CE Long Option moves up the higher Delta ladder (as it slides deeper in the money). However, with the rise in the underlying, the PE Long leg generates loss (as the LTP of PE would reduce) and the PE Long leg slides down lower Delta as it goes deeper out of the money. But the rate at which greater profitability on CE side is generated *vis-à-vis* loss on the PE Long Option, gets wider and wider, as the underlying moves higher, because CE Long would move through ascending Delta values, whereas the PE Long would slide down through descending Delta values. Further, while CE Long leg generates profit as the underlying moves higher, however, the CE Short hedged leg incurs loss and accordingly net profit is generated between the CE Long & Short leg. Similarly, as the underlying moves higher, the PE Long leg generates loss, however, the PE Short hedged leg generates profit and

	accordingly the loss generated by the PE Long is absorbed to some extent by the PE Short leg. But the Delta neutrality ensured at the time of initiating the Strategy helps to generate increased profit on CE side and reduced loss on the PE side, as the underlying keeps trending higher. • Likewise, when PE Long leg gets profitable due to rise in its LTP (i.e. when underlying falls with momentum), greater profitability is achieved as the PE Long Option moves up the higher Delta ladder (as it slides deeper in the money). However, with the fall in the underlying, the CE Long leg generates loss (as the LTP of CE would reduce) and the CE Long leg slides down lower Delta as it goes deeper out of the money. But the rate at which greater profitability on PE side is generated <i>vis-à-vis</i> loss on the CE Long Option, gets wider and wider, as the underlying moves lower, because PE Long would move through ascending Delta values, whereas the CE Long would slide down through descending Delta values. Further, while PE Long Option generates profit as the underlying moves lower, however, the PE Short hedged leg incurs loss and accordingly net profit is generated between the PE Long & Short leg. Similarly, as the underlying moves lower, the CE Long option generates loss however, the CE Short hedged leg
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	generates profit and accordingly the loss generated by the CE Long is absorbed to some extent by the CE Short leg. But the Delta neutrality ensured at the time of initiating the Strategy helps to generate increased profit on PE side and reduced loss on the CE side, as the underlying keeps trending lower. <i>For example: If ATM is at 17000, then for ensuring Delta neutrality in Reverse Iron Fly:</i> • <i>For Long leg: If Nifty 17000 ATM CE is bought at Rs. 350 per Lot and Nifty 17000 ATM PE is bought at Rs. 300 per Lot, both having ATM Delta value of 0.50 (single Lot basis); and</i> • <i>For Short leg: if Nifty 17500 CE is sold at Rs. 250 per Lot at Delta of 0.3 (single Lot basis), then Nifty 16500 PE sell can be initiated at around Rs. 150 per Lot having similar Delta value of approx. 0.29 (single Lot basis)</i>
<u>Selection of Option Strikes:</u> In this Strategy, ATM CE & PE Strikes (<i>which have equal Delta values</i>) are used for initiating Long Options for both the primary legs. This is done in order to maintain Delta neutrality at the time of initiating the Strategy, if the view is neutral and uncertain, but expecting huge gapup/ gapdown (or very strong trending momentum in a very short span of time).	<u>Selection of Option Strikes:</u> Selection of the CE & PE Long legs are ATMs with same Delta value; and CE & PE Short legs Strikes must be such OTM Strikes which have equal LTP / Delta values in order to maintain Delta neutrality at the time of initiating the Strategy, if the view is neutral and uncertain, but expecting huge gapup/ gapdown (or very strong trending momentum in a very short span of time). However, depending on the expected time within which strong one-sided momentum

However, depending on the expected time within which strong one-sided momentum is expected to arrive, choice of closer or farther Expiry series for initiating Long Options must be considered. If holding time is very less, then current Expiry series can be considered; but if holding time is more than 10-15 days or so then it is better to not loose Premium on account of Theta and therefore farther Expiry series ATM Options may be employed for this Strategy. Basis aforesaid factors, suitable ATM CE & PE Option Strike levels of a particular Expiry series may be selected for this Strategy. Since, the success of this Strategy is also mainly dependent on the low Theta decay, therefore farther Expiry series (or larger time to Expiry Options) would be preferable for this Strategy.	is expected to arrive, choice of closer or farther Expiry series for initiating Long Options must be considered. If holding time is very less, then current Expiry series can be considered; but if holding time is more than 10-15 days or so then it is better to not loose Premium on account of Theta and therefore farther Expiry series ATM Options may be employed for this Strategy. Basis aforesaid factors, ATM CE & PE Option Strike levels for the Long leg and suitable OTM CE & PE for Short leg of a particular Expiry series may be selected for this Strategy. Since, the success of this Strategy is also mainly dependent on the low Theta decay, therefore farther Expiry series (or larger time to Expiry Options) would be preferable for this Strategy.
<u>If trade goes as per plan as trends beyond the Breakeven Strike, from Expiry perspective:</u> If the underlying starts trending strongly with momentum on one side (<i>or if takes a huge gapup / gapdown</i>) and successfully breaches the Breakeven Strikes of the Strategy on that particular side (<i>i.e. either upwardly on the CE side or downwardly on the PE side</i>), then this Strategy would yield profit. The strength and length of the	<u>If trade goes as per plan as trends beyond the Breakeven Strike, from Expiry perspective:</u> If by Expiry of the Long Options, if the underlying starts trending strongly with momentum on one side (<i>or if takes a huge gapup / gapdown</i>) and successfully breaches the Breakeven Strikes of the Strategy on that particular side (<i>i.e. either upwardly on the CE side or downwardly on the PE side</i>), then this Strategy would yield profit. The strength and length of the momentum

momentum would decide the quantum of profit in this Strategy. Therefore, in case of continuous trending movement of the underlying (or due to huge gapup/ gapdown) after breaching of the Breakeven Strike on any one side by the underlying, a huge / unlimited profit situation may arise from Expiry perspective. <u>If underlying's movement fails to breach the Breakeven Strike, from Expiry perspective:</u> However, if by Expiry of these Long Options, the underlying fails to cross-over the Breakeven Strikes either upwardly on the CE side or downwardly on the PE side, then the Strategy would yield loss(<i>which may extend upto a maximum extent of the Total Premium paid on the Strategy</i>). In such situations, when the underlying does not seem to be trending enough to be able to cross-over the Breakeven Strike on either side by Expiry, then some adjustments can be considered in order to contain the loss in this Strategy (<i>as discussed below here</i>).	would decide the quantum of profit in this Strategy. Therefore, in case of continuous trending movement of the underlying (or if takes a huge gapup / gapdown) after breaching of the Breakeven Strike on any one side by the underlying, a limited profit situation may arise on this Strategy from Expiry perspective. <u>If underlying's movement fails to breach the Breakeven Strike, from Expiry perspective:</u> However, if by Expiry of the Options, the underlying fails to cross-over the Breakeven Strikes either upwardly on the CE side or downwardly on the PE side, then the Strategy would yield loss(<i>which may extend upto a maximum extent of the Net Premium paid on the Strategy</i>). In such situations, when the underlying does not seem to be trending enough to be able to cross-over the Breakeven Strike on either side by Expiry, then some adjustments can be considered in order to contain the loss in this Strategy (<i>as discussed below here</i>).
<u>Adjustments (if the Breakeven Strike is not breached by the underlying and this Strategy does not go as per plan):</u> Since, this Strategy is an aggregate Premium Debit strategy, therefore, the aggregate Premium paid (i.e. the sum of the Premium paid on the CE Long and PE Long leg) need to be first	<u>Adjustments (if the Breakeven Strike is not breached by the underlying and this Strategy does not go as per plan):</u> Since, this Strategy is a Premium Debit strategy, therefore, the Net Premium paid (<i>i.e. the difference between the total Premium paid on the CE & PE Long leg and the total premium credit received on the CE & PE</i>

recovered from the profit in this Strategy, from Expiry perspective, in order for this Strategy to be overall profitable by Expiry. However, when underlying does not seem to be trending enough to be able to cross-over the Breakeven Strike on either side by Expiry, then the potential loss (limited to the maximum extent of the aggregate Premium paid on this Strategy) situation can be handled by making following adjustments: (i) Converting Long Straddle into Reverse Iron Fly (<i>i.e hedged Long Straddle</i>); or (ii) Short both CEs & PEs; or (iii) Short CEs; or (iv) Short PEs. These adjustments are discussed below: (i) <u>Conversion to Reverse Iron Fly</u>: If the original view that the underlying would breakout beyond the Breakeven Strike of the Strategy on either side, appears to get uncertain, then immediately the naked Long Straddle must be converted to Reverse Iron Fly Strategy by initiating OTM Short CEs and Short PEs (<i>of equal quantity as that of Long legs, and of same Expiry series as that of the Long Options</i>). This hedging of Long Straddle through conversion into Reverse Iron Fly will mitigate the potential risk of loss on the Long Straddle into a pre-calculated even much Limited Loss situation. You may refer to the details of Reverse Iron Fly given on the other side of	<i>Short leg</i>) need to be first recovered from the profit in this Strategy, from Expiry perspective, in order for this Strategy to be overall profitable by Expiry. However, when underlying does not seem to be trending enough to be able to cross-over the Breakeven Strike on either side by Expiry, then the potential loss (<i>limited to the maximum extent of the Net Premium paid on this Strategy</i>) situation can be handled by making following adjustments: (i) Short both CEs & PEs; or (ii) Short CEs; or (iii) Short PEs. These adjustments are discussed below: (i) <u>Counter Adjustment through Short Option (both sides)</u>: If the underlying do not seem to be breaching the Breakeven Strike of this Strategy and seems to remain until Expiry of the Long Options, within a range, then, additional Far OTM CEs and PEs can be sold (<i>i.e. additional Short CE & PE to be initiated</i>). These additional Short CEs and PEs must be even Far OTMs than the Short Options on the hedged leg, and of the same or closer Expiry series than that of the Long Options leg. Further, these additional Short CEs & PEs can be initiated on equal quantities but in such sufficient quantities to receive aggregate Credit which is equal to or more than the Net Debit incurred on this Strategy. With this adjustment, the Reverse Iron Fly gets converted into both side
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this Table for better understanding.

- (ii) Counter Adjustment through Short Option (both sides): If the underlying do not seem to be breaching the Breakeven Strike of this Strategy and seems to remain until Expiry of the Long Options, within a range, then, both **Far OTM CEs and PEs can be sold** (Short CE & PE to be initiated). These Short CEs and PEs must be Far OTMs, and of the same or closer Expiry series than that of the Long Options leg.

Further, these Short CEs & PEs can be initiated on equal quantities but in such sufficient quantities to receive aggregate Credit which is equal to or more than the aggregate Debit incurred on this Strategy through Long Options leg. This way the Long Straddle gets converted into Reverse Iron Fly or both side Ratio Spreads (*with more Shorts than Longs on both CE side & PE side*).

Idea in this adjustment is to pick up a suitable Far OTM CEs & PEs for Shorting, such that these Far OTM Options expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This Short Options position will help cover the potential loss that may be generated on this Strategy.

Ratio Spreads (*with more Shorts than Longs on both CE side & PE side*).

Idea in this adjustment is to pick suitable Far OTM CEs & PEs for Shorting, such that these Far OTM Options expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This additional Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying breakout and breaches the Breakeven Strike on any side, then in that situation too these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Thus, suitable number of Short Options (additional CEs and PEs Short) need to be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short Options position as an adjustment in comparison to the original number of Lots initiated on the Strategy. If the Short Options generates profit and reasonably minimizes the loss in this Strategy before Expiry, then it would be advisable to book the profit and to

Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying breaks-out and breaches the Breakeven Strike on any side, then in that situation too these additional Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Thus, suitable number of Short Options (CEs and PEs Short) need to be considered to be added as an adjustment to absorb or outweigh the loss in the Strategy. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short Options position as an adjustment in comparison to the original number of Lots initiated on the Strategy. If the Short Options generates profit and reasonably minimizes the loss in this Strategy before Expiry, then it would be advisable to book the profit and to exit this Strategy. However, selling Options will require higher margin / capital and MTM requirements will also have to be met. (iii) <u>Counter Adjustment through Short Option (one side):</u> If there seems to be a slow trend on the downward, such that the Breakeven Strike does not seem to be breached downwardly (i.e. on	exit this Strategy. However, selling Options will require higher margin / capital and MTM requirements will also have to be met. (ii) <u>Counter Adjustment through Short Option (one side):</u> If there seems to be a slow trend on the downward, such that the Breakeven Strike does not seem to be breached downwardly (i.e. on the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then Far OTM CEs can be sold (i.e. additional Short CEs to be initiated). However, If there seems to be a slow uptrend, such that the Breakeven Strike does not seem to be breached upwardly (i.e. on the CE side) in this Strategy and the underlying seems to be in a mild upwardly direction, then Far OTM PEs can be sold (i.e. additional Short PEs to be initiated). Idea in this adjustment is to pick up a suitable Far OTM Option for Shorting, such that this Far OTM Option expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying reverses on the opposite side (i.e. against the additional Short Options position), then these additional Short
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the PE side) in this Strategy and the underlying seems to be in a mild downwardly direction, then Far OTM CEs **can be sold** (Short CEs to be initiated). However, if there seems to be a slow uptrend, such that the Breakeven Strike does not seem to be breached upwardly (i.e. on the CE side) in this Strategy and the underlying seems to be in a mild upwardly direction, then Far OTM PEs **can be sold** (Short PEs to be initiated).

Idea in this adjustment is to pick up a suitable Far OTM Option for Shorting, such that this far OTM Option expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. This Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of a Far OTM Option for this adjustment is important because even if the direction of the underlying reverses on the opposite side (i.e. against the Short Options position), then these Short Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend

Options positions (initiated as part of adjustments) must be such which can be expected to expire as an OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the potential loss in the original Strategy and the likely mild trend of the underlying and the Premium available on the relevant Far OTM Options (CEs or PEs as the case may be), suitable number of Options can be Shorted as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to these additional Short Options position in comparison to the original number of Lots initiated on the Strategy. These additional Short Options position should be initiated at such Far OTM Strike(s), which may have reasonable Premium and is expected to expire worthless as OTM on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

- (iii) Adjustment through Pyramiding: If the underlying seems to be moving in one direction (and not really hovering in a range) but with limited momentum and does not seem to be able to breach the Breakeven Strike in that direction (CE or PE, as the case may be), then Far OTM Options of that direction (in which the underlying has been trending) can be

of the underlying and the Premium available on the relevant Far OTM Options (CEs or PEs as the case may be), suitable number of Options can be Shorted as an adjustment to absorb or outweigh the loss in the Strategy. Generally, at least 2 to 4 times more Lot quantity may be required to be added to these additional Short Options position in comparison to the original number of Lots initiated on the Strategy. These Short Options position should be initiated at such Far OTM Strike(s), which may have reasonable Premium and is expected to expire worthless as OTM on Expiry. However, selling additional Options will require higher margin / capital and MTM requirements will also have to be met.

(iv) Adjustment through Pyramiding:

If the underlying seems to be moving in one direction (and not really hovering in a range) but with limited momentum and does not seem to be able to breach the Breakeven Strike in that direction (CE or PE, as the case may be) by Expiry, then Far OTM Options of that direction (in which the underlying has been trending) can be Shorted. That is: If there seems to be a limited trend with momentum in the downward direction, but the underlying does

Shorted. That is: If there seems to be a limited trend with momentum in the downward direction, but the underlying does not seem to be able to breach the Breakeven Strike on the PE side, then additional Far OTM **PEs can be sold** (i.e. additional Short PEs to be initiated) below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry. Likewise, If there seems to be a limited trend with momentum in the upward direction, but the underlying does not seem to be able to breach the Breakeven Strike on the CE side by Expiry, then additional Far OTM **CEs can be sold** (i.e. additional Short CEs to be initiated) above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry.

Idea in this adjustment is to pick up suitable Far OTM Options for Shorting in the same direction in which the underlying is advancing, such that these Far OTM Short Options (initiated as part of adjustments) expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. These Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of Far OTM Options for this adjustment is important because even if the trend of the underlying gets into trending

not seem to be able to breach the Breakeven Strike on the PE side by Expiry, then Far OTM **PEs can be sold** (Short PEs to be initiated) below the Support area of the underlying, which is expected not to be breached by the underlying by Expiry. Likewise, if there seems to be a limited trend with momentum in the upward direction, but the underlying does not seem to be able to breach the Breakeven Strike on the CE side by Expiry, then Far OTM **CEs can be sold** (Short CEs to be initiated) above the Resistance area of the underlying, which is expected not to be breached by the underlying by Expiry.

Idea in this adjustment is to pick up suitable Far OTM Options for Shorting in the same direction in which the underlying is advancing, such that these Far OTM Short Options (initiated as part of adjustments) expires worthless as an OTM on Expiry thereby giving full Premium at which Short is initiated as profit. These Short Options position will help cover the potential loss that may be generated on this Strategy. Selection of Far OTM Options for this adjustment is important because even if the trend of the underlying gets into trending momentum in the same direction

momentum in the same direction and breaches the Breakeven Strike and continues further in that direction, then too these additional Short Options position must be at such Strike which can be expected to be not breached by the underlying by Expiry and to expire as OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the max loss in the original Strategy and the likely mild trend of the underlying and the Premium available on relevant Far OTM Options (*i.e. in case of PE Shorts, below the Support area; and in case of CE Shorts, above the Resistance area*), suitable number of Options can be considered to be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these additional Short Options due to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short for this adjustment, in comparison to the original number of Lots initiated on the Strategy.

In this type of adjustment, Short Options positions can also be added in a pyramidal structure. That is:

- as the downtrend continues Far OTM PEs' Premium would rise, therefore, additional Short PEs positions can be added at subsequent lower Strike levels as

and breaches the Breakeven Strike and continues further in that direction, then too these Short Options position must be at such Strike which can be expected to be not breached by the underlying by Expiry and to expire as OTM on Expiry, thereby generating profit to the extent of its Premium on Expiry. Also, depending upon the max loss in the original Strategy and the likely mild trend of the underlying and the Premium available on relevant Far OTM Options (*i.e. in case of PE Shorts, below the Support area; and in case of CE Shorts, above the Resistance area*), suitable number of Options can be considered to be Shorted as an adjustment to absorb or outweigh the potential loss in the Strategy, by the profit yielded by these Short Options due to time decay on Expiry. Generally, atleast 2 to 4 times more Lot quantity may be required to be added to Short for this adjustment, in comparison to the original number of Lots initiated on the Strategy.

In this type of adjustment, Short Options positions can also be added in a pyramidal structure. That is:

- as the downtrend continues Far OTM PEs' Premium

the downtrend continues with lower PEs gaining decent Premium values. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16000 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 15800 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.*

- as the uptrend continues Far OTM CEs' Premium would rise, therefore, additional Short CEs positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining decent Premium values. *For example, when the uptrend continues in Nifty, a Far OTM CE at 17800 having Premium of Rs. 50 can be sold, thereafter when the Nifty rises further, subsequent higher CE at 17900 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.*

This Shorting of Options in a pyramiding manner may ensure a broader Breakeven Strike for the Short leg (*i.e.* larger risk area protection) and thus greater probability of profiting due to Theta decay on these bunch of Short Options on Expiry.

would rise, therefore, Short PEs positions can be added at subsequent lower Strike levels as the downtrend continues with lower PEs gaining decent Premium values. *For example, when the downtrend continues in Nifty, a Far OTM PE at 16000 having Premium of Rs. 50 can be sold, thereafter when the Nifty slips down further, subsequent lower PE at 15800 (whose Premium would have become 50 due to continuous downtrend) can be sold in equal or double quantity and so on.*

- as the uptrend continues Far OTM CEs' Premium would rise, therefore, Short CEs positions can be added at subsequent higher Strike levels as the uptrend continues with higher CEs gaining decent Premium values. *For example, when the uptrend continues in Nifty, a Far OTM CE at 17800 having Premium of Rs. 50 can be sold, thereafter when the Nifty rises further, subsequent higher CE at 17900 (whose Premium would have become 50 due to continuous uptrend) can be sold in equal or double quantity and so on.*

However, selling Options will require higher margin / capital and MTM requirements will also have to be met.

This Shorting of Options in a pyramiding manner may ensure a broader Breakeven Strike for the Short leg (i.e. larger risk area protection) and thus greater probability of profiting due to Theta decay on these bunch of Short Options on Expiry. However, selling Options will require higher margin / capital and MTM requirements will also have to be met.	
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OVERVIEW ON A FEW MORE STRATEGIES

In this Chapter, we have discussed above about various facets of about 24 different Conventional Strategies, which every trader must understand. These are few most common, very popular, quite dependable Strategies; and these essentially forms the backbone or the basic design on which many other Strategies are formed / can be formed to play relevant market dynamics.

If the understanding about the basic design, logic and objective of the aforementioned Conventional Strategies is clear, then we are prepared to understand few other popular Conventional Strategies. We will give an overview about these few other popular Strategies here, so as to enable you to gain basic acquaintance with these Strategies; and should you desire to know more about them, I am confident that by now you are sufficiently equipped to decode any aspect of these Strategies with your own further analysis.

Let us proceed to explore few other popular Strategies, which you can add to your knowledge bank.

Call Ratio Backspread	Put Ratio Backspread
We have already discussed above, Call Ratio Spread, which has more Shorts than Longs (and is usually a Credit Spread) and are initiated to play a mild bullish view on the underlying. However, if the view is bullish, then instead of Call Ratio Credit Spread, a trader must consider Call Ratio Backspread Strategy. In Call Ratio Backspread, bullish expectation on the underlying is played by having more Long CEs than CE Short, typically in the ratio of 2:1, 3:2, or 3:1 etc. This may comprise of 2 OTM CE Long primary leg and 1 ITM CE Short as hedged leg on same Expiry series; or 2	We have already discussed above, Put Ratio Spread, which has more Shorts than Longs (and is usually a Credit Spread) and are initiated to play a mild bearish view on the underlying. Backspread Strategy. In Put Ratio Backspread, bearish expectation on the underlying is played by having more Long PEs than PE Short, typically in the ratio of 2:1, 3:2, or 3:1 etc. This may comprise of 2 OTM PE Long primary leg and 1 ITM PE Short as hedged leg on same Expiry series; or 2 ITM PE Long and 1 OTM PE Short, etc. Thus, Put Ratio Backspread is a Net Premium Debit Strategy (<i>i.e. with more</i>

ITM CE Long and 1 OTM CE Short. Thus, Call Ratio Backspread is a Net Premium Debit Strategy (<i>i.e. with more Premium paid for the CE Long than Premium Credit collected on the Short leg, due to different quantity initiated on Long leg and Short leg</i>). In this Strategy, the upside profit potential is unlimited and the downside risk is limited to the maximum extent of the Net Premium Debit incurred on the Strategy. It is a Vega positive Strategy.	<i>Premium paid for the PE Long than Premium Credit collected on the PE Short leg, due to different quantity initiated on Long leg and Short leg</i>). In this Strategy, the downside profit potential is unlimited and the upside risk is limited to the maximum extent of the Net Premium Debit incurred on the Strategy. It is a Vega positive Strategy.
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Call Butterfly	Put Butterfly
We have already discussed above, Iron Butterfly, which is a hedged Short Straddle, comprising a pair of Bear Call Credit Spread and Bull PE Credit Spread. This Strategy has 4 legs, in which Short CE & PE are joined at ATM Strike and Long CE & PE legs are OTM Strike. Further, this is played to benefit from a narrow range and neutral view on the underlying for limited profit, running risk of limited loss. However, such narrow range and neutral view on the underlying for limited profit, running risk of limited loss, can also be played only on CE side, through Call Butterfly Strategy. In this Strategy, 2 Short CEs are initiated at ATM and 1 Long CE as Near ITM and 1 Long CE as Near OTM, all on same Expiry series. Both the Long CEs	We have already discussed above, Iron Butterfly, which is a hedged Short Straddle, comprising a pair of Bear Call Credit Spread and Bull PE Credit Spread. This Strategy has 4 legs, in which Short CE & PE are joined at ATM Strike and Long CE & PE legs are OTM Strike. Further, this is played to benefit from a narrow range and neutral view on the underlying for limited profit, running risk of limited loss. However, such narrow range and neutral view on the underlying for limited profit, running risk of limited loss, can also be played only on PE side, through Put Butterfly Strategy. In this Strategy, 2 Short PEs are initiated at ATM and 1 Long PE as Near ITM and 1 Long PE as Near OTM, all on same Expiry series. Both the Long PEs

maintain the same Strike difference from the ATM Short leg. Thus, essentially it is a pairing of a Bull CE Debit Spread and a Bear CE Credit Spread, joined on the common Short Strike. It is a Net Premium Debit Strategy, therefore, the max loss is capped to the extent of Net Premium paid on the Strategy. The payoff of this Strategy, from Expiry perspective, looks same as Iron Butterfly (and Put Butterfly). In this Strategy: (i) max profit generated at Short leg; (ii) max loss is accrued beyond either Long CE Strikes; and (iii) profit zone of this Strategy is between the two BE Strikes. Volatility crash and Theta decay is favourable for this Strategy.	maintain the same Strike difference from the ATM Short leg. Thus, essentially it is a pairing of a Bear PE Debit Spread and a Bull PE Credit Spread, joined on the common Short Strike. It is a Net Premium Debit Strategy, therefore, the max loss is capped to the extent of Net Premium paid on the Strategy. The payoff of this Strategy, from Expiry perspective, looks same as Iron Butterfly (and Call Butterfly). In this Strategy: (i) max profit generated at Short leg; (ii) max loss is accrued beyond either Long PE Strikes; and (iii) profit zone of this Strategy is between the two BE Strikes. Volatility crash and Theta decay is favourable for this Strategy.
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Call Brokenwing Butterfly Spread	Put Brokenwing Butterfly Spread
It is an uneven/ unbalanced Call Butterfly Strategy, to play a tight range to bearish view on the underlying for limited profit, running risk of limited loss. Like, a Call Butterfly Strategy, this Strategy too is a pairing of a Bull CE Debit Spread and a Bear CE Credit Spread, joined on the common Short Strike. However, this Strategy comprises of 1 Long CE as Near ITM and 2 Short CEs are initiated at Near OTM and 1 Long CE Near OTM which is around two Strikes higher than the CE Short leg, all	It is an uneven/ unbalanced Put Butterfly Strategy, to play a tight range to bullish view on the underlying for limited profit, running risk of limited loss. Like, a Put Butterfly Strategy, this Strategy too is a pairing of a Bear PE Debit Spread and a Bull PE Credit Spread, joined on the common Short Strike. However, this Strategy comprises of 1 Long PE as Near ITM and 2 Short PEs are initiated at Near OTM and 1 Long PE Near OTM which is around two Strikes lower than the PE Short leg, all on same Expiry series. Thus, essentially, the

on same Expiry series. Thus, essentially, the Long CEs do not maintain the same Strike difference from the Short leg, and thus this Spread is referred to as brokenwing. This Strategy is ensured to be initiated with Net Premium Credit, hence there is no downside risk in this Strategy. Max profit is generated at the Short Strike. Further, limited max loss in this Strategy is yielded if the underlying closes by Expiry higher than the OTM CE Long Strike. Volatility crash and Theta decay is favourable for this Strategy.	Long PEs do not maintain the same Strike difference from the Short leg, and thus this Spread is referred to as brokenwing. This Strategy is ensured to be initiated with Net Premium Credit, hence there is no upside risk in this Strategy. Max profit is generated at the Short Strike. Further, limited max loss in this Strategy is yielded if the underlying closes by Expiry lower than the OTM PE Long Strike. Volatility crash and Theta decay is favourable for this Strategy.
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STRATEGIES DEPICTED ON BOILER-PLATE OPTIONS CHAIN

We have discussed in this Chapter about +30 different Strategies, which not only pertains to different Strikes but for some Strategy even different Expiry series. A lot of these Strategies are a mix of two or more Strategies or a reversal of some other Strategies. It is very interesting to see the implementation of different thoughts in designing a particular Strategy and utilisation of different strategy-mix to develop altogether a different Strategy for a different objective and risk & reward. This understanding is extremely crucial for a trader to evolve as a pro.

For a beginner it may appear to be a difficult task to have all these Conventional Strategies on his fingertips. The basic design of some of these Strategies may also appear to be so close to each other that they appear get confusing at times. While it may appear to be little confusing initially or you may get a feeling that every Strategy you learnt is getting messed up in your head; but be assured that with time all this will surely be within your grip because it is definitely not so complex as it appears to be.

In another attempt to simplify learning about these confusing-looking aspects about Options, we have tried to bring all the hedged Strategies discussed in this Chapter at one place by plotting it on a boiler-plate Options Chain, to help you to better place these Strategies in your memory bank by just looking / remembering the following Table.

In the Table below, we have provided Options Chain of two different Expiry series. On the left-hand side, we have a Option Chain of a closer Expiry series and on the right-hand side we have a Options Chain of a relatively farther Expiry series. In these Options Chain, we have plotted different types of CE & PE Options (i.e. ITM, ATM & OTM). Have a closer look in the diagram given below:

<u>Options Chain of Closer Expiry</u> (Example: Current Month Expiry series)		<u>Options Chain of Farther Expiry</u> (Example: Next Month Expiry series)	
CE Side	PE Side	CE Side	PE Side
Deep ITM (A) Near ITM (B)	Far OTM (N) OTM (M)	Deep ITM (AA) Near ITM (BB)	Far OTM (NN) OTM (MM)
CE ATM (C)	PE ATM (L)	CE ATM (CC)	PE ATM (LL)
OTM (D) Far OTM (E)	Near ITM (K) Deep ITM (J)	OTM (DD) Far OTM (EE)	Near ITM (KK) Deep ITM (JJ)
- Here we have given some random codes (denoting through capitalized alphabets) to each of the different types of Options, in each of the above Options Chain. - Closer Expiry Options are denoted with a single alphabet letter and farther Expiry series is denoted with double alphabet letters, as you can see in the table above. - The alphabets primarily denotes only category of Options, not a particular Strike (or same Strike between closer and farther Expiry series) - Delta values in an Options Chain on CE side increases from Far OTM to Deep ITM (i.e. from E to A or EE to AA). Delta values in an Options Chain on PE side increases from Far OTM to Deep ITM (i.e. from N to J or NN to JJ)			

Now, just for the sake of quick recollection of all the popular Conventional hedged Strategies, with their relevant trade legs, we have used the codes depicted in the above Table, to showcase different option types which are employed in

creation of trading positions for different Conventional Strategies. The following Table gives a summary pointer of the trade legs for each of the Conventional Strategies, as a quick reference point:

Sl. No	Strategy	Trade Legs
1	Covered Call (bullish view)	- Long Futures (<i>current Expiry</i>) and Short B or C; or - Long Futures (<i>farther Expiry</i>) and Short BB or CC
2	Poor Man's Covered Call (bullish view) It can be used as an alternate to regular Covered Call to cap the downside risk	- Long A and Short B or C; or - Long AA and Short BB or CC <i>Long leg must have a Delta value close to 1 per Lot basis. This can be done by taking more Long ITMs than 1 single Deep ITM.</i>
3	Collar-PE side (bullish view) It is used for covering the downside risk in a Covered Call	- Long Futures (<i>current Expiry</i>) & Short D and Long M or N; or - Long Futures (<i>farther Expiry</i>) & Short DD and Long MM or NN <i>It is a combination of Covered Call and Protective Put</i>
4	Covered Put (bearish view)	- Short Futures (<i>current Expiry</i>) and Short K or L; or - Short Futures (<i>farther Expiry</i>) and Short KK or LL
5	Poor Man's Covered Put (bearish view) It can be used as an alternate to regular Covered Put to cap the upside risk	- Long J and Short K or L; or - Long JJ and Short KK or LL <i>Long leg must have a Delta value close to 1 per Lot basis. This can be done by taking more Long ITMs than 1 single Deep ITM.</i>

6	Collar-CE side <i>(bearish view)</i> It is for covering the upside risk in a Covered Put	• Short Futures (<i>current Expiry</i>) & Short M and Long D or E; or • Short Futures (<i>farther Expiry</i>) & Short MM and Long DD or EE <i>It is a combination of Covered Put and Long Call</i>
7	Bull CE Debit Spread <i>(bullish view)</i>	• Long C and Short D or E; or • Long D and Short E; or • Long CC and Short DD or EE; or • Long DD and Short EE
8	Bear PE Debit Spread <i>(bearish view)</i>	• Long L and Short M or N; or • Long M and Short N; or • Long LL and Short MM or NN; or • Long MM and Short NN
9	Bull PE Credit Spread <i>(rangebound to mild bullish view)</i>	• Short M and Long N; or • Short MM and Long NN
10	Bear CE Credit Spread <i>(rangebound to mild bearish view)</i>	• Short D and Long E; or • Short DD and Long EE
11	CE Ratio (Credit) Spread <i>(rangebound to mild bullish view)</i>	• few Long D and more Short E (in ratio of 1:2 or 2:3 or 1:3 or 1:4 etc); or • few Long DD and more Short EE (in ratio of 1:2 or 2:3 or 1:3 or 1:4 etc)
12	CE Ratio (Debit) Backspread <i>(bullish view)</i>	• more Long D or E and few Short B (in ratio of 2:1 or 3:2 or 3:1 or 4:1 etc); or • more Long B and few Short D or E (in ratio of 2:1 or 3:2 or 3:1 or 4:1 etc); or

		• more Long DD or EE and few Short BB (in ratio of 2:1 or 3:2 or 3:1 or 4:1 etc); or • more Long BB and few Short DD or EE (in ratio of 2:1 or 3:2 or 3:1 or 4:1 etc)
13	PE Ratio (Credit) Spread <i>(rangebound to mild bearish view)</i>	• few Long M and more Short N (in ratio of 1:2 or 2:3 or 1:3 or 1:4 etc); or • few Long MM and more Short NN (in ratio of 1:2 or 2:3 or 1:3 or 1:4 etc)
14	PE Ratio (Debit) Backspread <i>(bearish view)</i>	• more Long M or N and few Short K (in ratio of 2:1 or 3:2 or 3:1 or 4:1 etc); or • more Long K and few Short M or N (in ratio of 2:1 or 3:2 or 3:1 or 4:1 etc); or • more Long MM or NN and few Short KK (in ratio of 2:1 or 3:2 or 3:1 or 4:1 etc); or • more Long KK and few Short MM or NN (in ratio of 2:1 or 3:2 or 3:1 or 4:1 etc)
15	CE Calendar Long Spread <i>(rangebound to mild bullish view)</i>	• Short C and Long CC
16	CE Diagonal Spread <i>(rangebound to mild bullish view)</i>	• Short D and Long EE; or • Short E and Long EE
17	Reverse CE Calendar (Short) Spread <i>(rangebound to mild bearish view)</i>	• Long C and Short CC
18	PE Calendar Long Spread <i>(rangebound to mild bearish view)</i>	• Short L and Long LL

19	PE Diagonal Spread <i>(rangebound to mild bearish view)</i>	• Short M and Long NN; or • Short N and Long NN
20	Reverse PE Calendar (Short) Spread <i>(rangebound to mild bullish view)</i>	• Long L and Short LL
21	Short Straddle <i>(underlying to remain in tight range)</i>	• Short C and Short L
22	Iron Fly <i>(underlying to remain in tight range)</i> It is a hedged Short Straddle	• Short C & Short L and Long D & Long M <i>It is a pairing of Bear Call Credit Spread and Bull Put Credit Spread, joined at both ATM Strikes through the Short leg</i>
23	Call Butterfly Spread <i>(underlying to remain in tight range)</i> It is a substitute of Iron Fly, designed for only CE side play	• Short C and Long B & Long D (<i>in the ratio of 2 Shorts to 1 Long each</i>), where B & D Strikes are equidistant from the C Strike <i>It is a pairing of Bull Call Debit Spread and a Bear Call Credit Spread, joined at the CE ATM Strike through the Short leg</i>
24	Call Brokenwing Butterfly Spread <i>(underlying to remain in tight range with bearish bias)</i> It is an unbalanced Call Butterfly Spread with Longs not equidistant from Short leg	• Short D and Long B & Long E (<i>in the ratio of 2 Shorts to 1 Long each</i>), where B & D Strikes are at shorter Strike difference than D & E <i>It is a pairing of Bull Call Debit Spread and a Bear Call Credit Spread, joined at the common Short leg</i>
25	Put Butterfly Spread <i>(underlying to remain in tight range)</i> It is a substitute of Iron Fly, designed for only PE side play	• Short L and Long K & Long M (<i>in the ratio of 2 Shorts to 1 Long each</i>), where K & M Strikes are equidistant from the L Strike <i>It is a pairing of Bear Put Debit Spread and a Bull Put Credit Spread, joined at</i>

		<i>the PE ATM Strike through the Short leg</i>
26	Put Brokenwing Butterfly Spread <i>(underlying to remain in tight range with bullish bias)</i> It is an unbalanced Put Butterfly Spread with Longs not equidistant from Short leg	• Short M and Long K & Long N (<i>in the ratio of 2 Shorts to 1 Long each</i>), where K & M Strikes are at shorter Strike difference than M & N <i>It is a pairing of Bull Call Debit Spread and a Bear Call Credit Spread, joined at the common Short leg</i>
27	Short Strangle <i>(underlying to remain within wide range)</i>	• Short D and Short M; or • Short E and Short N
28	Iron Condor <i>(underlying to remain within wide range)</i> It is a hedged Short Strangle	• Short D & Short M and Long E & Long N <i>It is a pairing of Bear Call Credit Spread and Bull Put Credit Spread</i>
29	Long Straddle <i>(underlying may breakout on either side)</i>	• Long C and Long L; or • Long CC and Long LL
30	Reverse Iron Fly <i>(underlying may breakout on either side)</i> It is a hedged Long Straddle	• Long C & Long L and Short D or E & Short M or N; or • Long CC & Long LL and Short DD or EE & Short MM or NN <i>It is a pairing of Bull Call Debit Spread and a Bear Put Debit Spread, joined at both the ATM Strike through the Long leg</i>
31	Long Strangle <i>(underlying may breakout massively on either side)</i>	• Long D and Long M; or • Long E and Long N; or • Long DD and Long MM; or • Long EE and Long NN

32	Reverse Iron Condor <i>(underlying may breakout massively on either side)</i> It is a hedged Long Strangle	• Long D & Long M and Short E & Short N; or • Long DD & Long MM and Short EE & Short NN <i>It is a pairing of Bull Call Debit Spread and a Bear Put Debit Spread</i>
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Trust this table helps to clearly and quickly figure out the relevance of different Strategies and their applicability to play a particular trend in the underlying and to be able to place the relevant trade legs which comprises that Strategy.

CONCLUSION

Thus, we have explored around **+30 Conventional Strategies** in Chapter 3, which can be successfully deployed to play out the specific market condition for which they are designed. I am sure, you must have gained a deep insight into the constructs of these Conventional Strategies and the knowledge & understanding about these basic Strategies will certainly help you to shape up your trading career in a big way.

Further, as already mentioned above and as you must have noted that in order to be able to dissect a Strategy or to initiate/ manage a trading position, every trader must have a sound understanding about the relevant aspects, viz. the net premium position, the net Delta position on inception, the inter-play of Greeks, behaviour of Options to different market scenarios, profit & loss levels, risk and reward potential etc. A sound understanding of these concepts helps a great deal in planning and managing a trade, and to eventually evolve as a pro. It is, therefore, a sincere request to revisit any of the Chapters (in this Volume or Volume-I) on any of the aforementioned aspects, if the same is still not very clear. I am sure, a thorough read would help you absorb the concept and include the same in your knowledge bank, which will be your arsenal in the battlefield of trading.

In **Volume III**, we would learn about certain advanced customised Strategies, which cater to different market conditions and technical view on the underlying. These Strategies must be considered by traders; and after learning and analysing them well, can consider to deploy them to play out relevant market condition. Get your copy of Volume III to explore **+20 Advanced Customised Strategies and about 10 unique Expiry day Strategies**.

FINAL WORD

With discussions on the various Conventional Strategies, we have come to the end of Volume II of the Book.

In **Volume II of the Book** we have discussed in detail about various concepts which are and can be used to design a trading Strategy and also to adjust trading positions should the need arise. Besides setting the fundamental blocks of designing and development of different F&O Strategies and adjustment techniques, Volume II also covered detailed discussions on about 30+ Conventional Strategies.

Having said this, it is important to understand that in order to fully comprehend and implement the contents, concepts, techniques and Strategies covered in Volume II of the Book, a learner must have a sound understanding about the basic aspects of F&O instrument and F&O trading. **Volume I of the Book**, aims to equip the learners with clear understanding about **various aspects of F&O instruments, practically relevant concepts of trading F&O, procedural aspects of placing different orders for trading purposes** and finally preparing and arming the traders with beforehand understanding about the **Risk Management rules & procedures** which a trader must follow.

Further, with the background on the F&O concepts covered in Volume I and hedging and adjustment techniques together with detailed study on 30+ Conventional Strategies – **you are ready to understand complex nature of Advanced Customised Strategies we have discussed in detail in Volume III of the Book**. Volume III is primarily aimed to equip the traders to design different trading Strategies for all kind of market situations, both naked and hedged with risk adjustment techniques, for positional as well as intraday trading including trading Expiry days. Volume III comprises of about **20+ Advanced Customised Strategies** and about **10 unique Expiry Day Strategies**.

Therefore, before starting to deploy capital on F&O trading or to implement trading Strategies discussed in Volume II of the Book, we urge the

learners to first equip themselves with the basic features of F&O instruments, core concepts of F&O trading, procedural aspects of F&O trading and the Risk Management procedures explained in Volume I of the Book. And once the traders are equipped with the concepts covered in Volume II of the Book, you may start exploring Advanced Customised Strategies and unique Expiry Day Strategies covered in Volume III.

We, sincerely, believe that the concepts, techniques, Strategies explained collectively in all the 3 Volumes of the Book, offers a one-stop learning solution and comprehensive material on F&O trading, which would not only shorten the learning curve to a great extent but would also be extremely beneficial for the learners to evolve as a successful trader. This gives us the confidence to urge that **this learning kit must be available with every trader, not just for their learning needs, but also as a reference material for referring to varied concepts & practicalities pertaining to F&O trading.**

I would love to hear from you—please feel free to write to me at intelligentmoneywise@gmail.com and do consider sharing your valuable feedback on Amazon (or the platform where you purchased Volume 2).

Wishing you all the very best for your trading career !

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