Timing is Everything…

StockEarnings.com

October 26, 2017

Welcome to "TIMING IS EVERYTHING", an exploration of how understanding the role of time in an earnings play:

- can significantly enhance your profitability
- has made the volatility-rush one of our favorite earnings plays

-- Ryan Nocera & Mitch Firestone, stockearnings.com

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Timing is Everything

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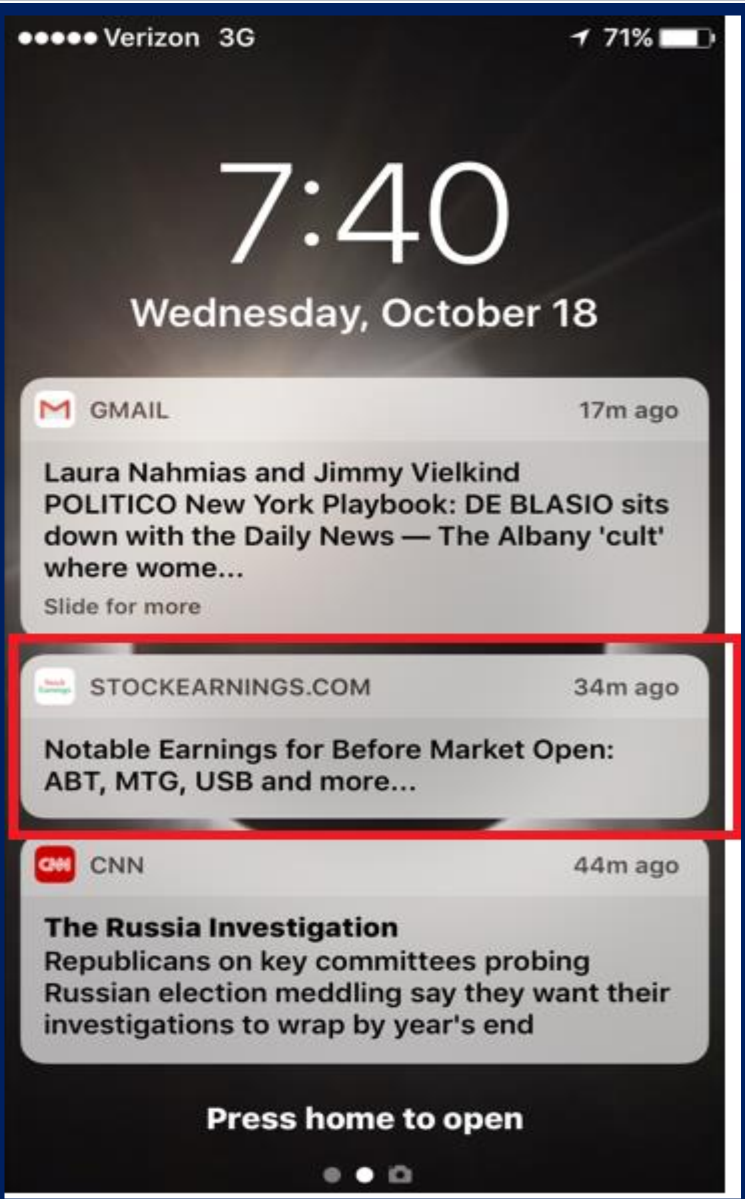

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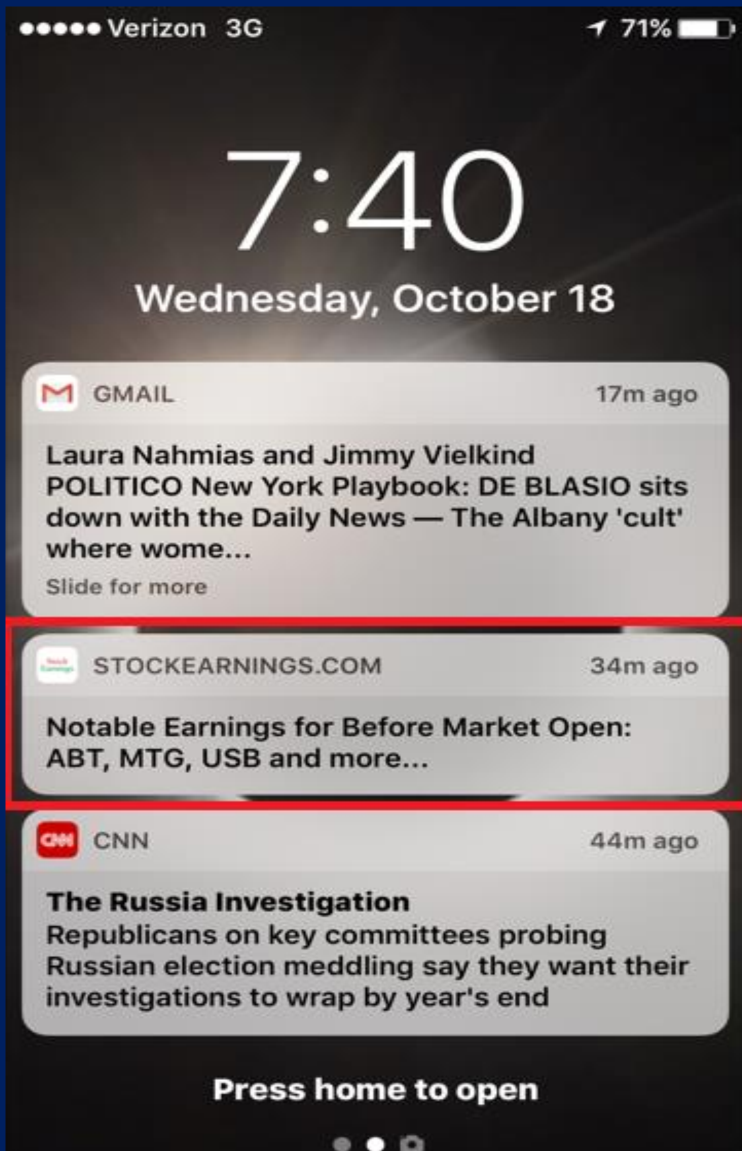

STOCKEARNINGS.COM -- IV RUSH ALERT!!
October xx, 5794
LULU -- EA Th Nov 30, postmarket

Adjusted IV Rush Cycle 29 days, +- 1 day(s)
Enter option debit position (single or spread) Oct 31-Nov 2
Exit date range Nov 27-29
(we'll update if there's an early, significant volatility spike)

SAMPLE FOR DEMONSTRATION ONLY

Earnings Trades – General Concepts

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- Price moves after earnings announcements (EA) are unpredictable, due to how ways Wall Street gauges them:
  - The *"Consensus"* estimate (EPS & total revenues)
  - The "*Whisper" number* (EPS)
  - *Lower revenues/unit sales* affect an otherwise favorable EA
  - *Guidance*, in the EA text and/or the *earnings call*
  - *Company sentiment* – utterly unpredictable. Sentiment can be so glum that all news is judged as bad, but sometimes anything better than a plane crash is good, except when it isn't.
  - Broader overall market/economic sentiment or geopolitical events.

General Concepts (cont'd)

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- Demand for options increases into earnings, for objective, tactical reasons, and emotional motives:
  - *Objective, Tactical* -- Institutions hedge positions in their general portfolio-management activities
  - *Anxiety* by retail traders seeking to hedge their positions
  - *Anticipation* – speculators, both smaller retail & big-block traders, seek to capitalize on big earnings moves
- Increased options demand fuels a rise in implied volatility (IV), the key component affecting an option's time-value (extrinsic value).
- IV rises as we approach the date of a company's earnings announcement (EA).

General Concepts (cont'd)

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- Two broad classes of earnings-related trades:
  - Positional trades, linked to the price-move after the EA (often a straddle is used, buying a call and a put at the same expiry & strike, taking into account the anticipated post-EA price-move)
  - Non-positional trades, keyed to the relatively reliable behavior of IV in the quarterly earnings cycle :
    - ***The volatility CRUSH*** – occurs last couple of days of the run-up to the EA. At that time IV is generally at or very close to its peak. This is a credit position, where one sells a put or a call, and then buys an offsetting option of the same type so that one isn't unhedged. Post-EA the position is closed at hopefully a much lower price than the initial credit, resulting in a profit. One needs to take into account the anticipated price-move, which is a key data-set provided by StockEarnings.
    - ***The volatility RUSH*** – based on a significant rise in IV in the weeks preceding an EA. The basic IV crush trade is often non-positional and targets capturing future, higher-IV. But the trade can also be done positionally where one has a good read on price action, making it even more profitable.

Volatility Rush: Guidelines, Rules & Enhancements (I)

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- Start with major companies, liquid stocks at least 1MM shares avg daily volume, though really prefer 2x or 3x), whose options are also liquid (sometimes a range of options expiry dates will be available that meet criteria, sometimes only the monthly
  - better, easier fills – generally seek around mid-point; sometimes you have to throw the market maker a little sweetener to get filled…make it a small one…better stocks limits the frequency and cost of this
  - better bid/ask spreads – seek <5% of the bid whenever possible
- Lean towards underlyings where there are often price moves of > 10% in the 20 days prior to their EAs in the last 18 months (6 earnings cycles) -- *variable*
- Lean towards an average increase in near-month ATM IV for ABC of >30 % in the 20 days prior to the EAs in the last 18 months (6 earnings cycles) – seek far more than this & adjust the timing
- ***Screen for higher projected 1-day move (at least 3-5%) in stockearnings.com, which will generally suggest a higher IV rise***

Tendencies & Rhythms

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- Individual stocks and ETFs are like people…they differ between each other. While there are certainly reasonable, general guidelines for the IV-rush or any other trade, the trade particulars should be adjusted for each symbol's:
  - Tendencies – ABC's price shows an avg 3% rise the next trading day following 23 of the last 28 EAs (82%) – all available in stockearnings.com's direct symbol look-up and the screener
  - Rhythms – there are behaviors common to all symbols, but they occur at/for different (1) times, (2) durations and (3) different magnitudes comparing one symbol to the next

    →a NEW STOCKEARNINGS.COM FEATURE
  - Price Action
  - EXAMPLES (GOOG, AMZN, SLB)

Volatility Rush: Guidelines, Rules & Enhancements (II)

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- Note ABC's EA date and ex-Div date
- Note the IV cycle as IV rises for the last several earnings periods (3+ years). Determine an average, safe time-period that lets you capture a significant rise in IV a high % of the time (don't be greedy!)
- Place the upcoming EA date in your chart & work backwards to determine the trade entry date based on IV-cycle.
- Note as trade entry date approaches ABC's IV rank (IV at the time relative to its magnitude for the past year) to guide strategy selection. Very low IV → buy singles, medium volatility → debit spread
- Form a price-action thesis, i.e., a directional bias for the underlying as another input in strategy selection using your core trading methodology, e.g., trend lines, moving averages, indicators/oscillators, supply & demand, etc.
- If your price-action thesis permits a strong positional bias, you can create a positional trade, e.g., buying singles or doing a vertical debit spread. If no positional bias, use a price-neutral strategy like a straddle. Such a strategy has a very low delta and is not unduly affected by moves in ABC price.

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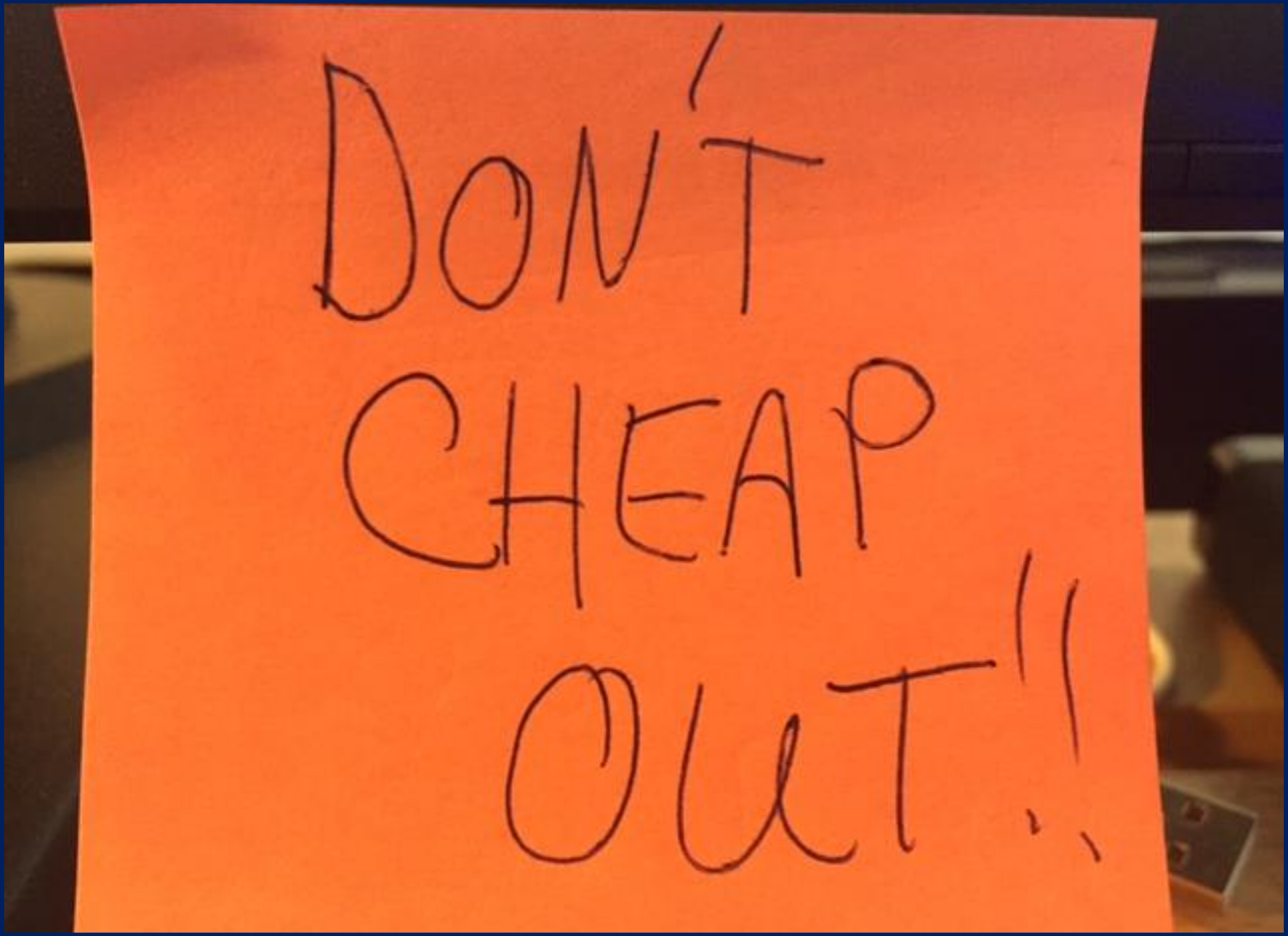
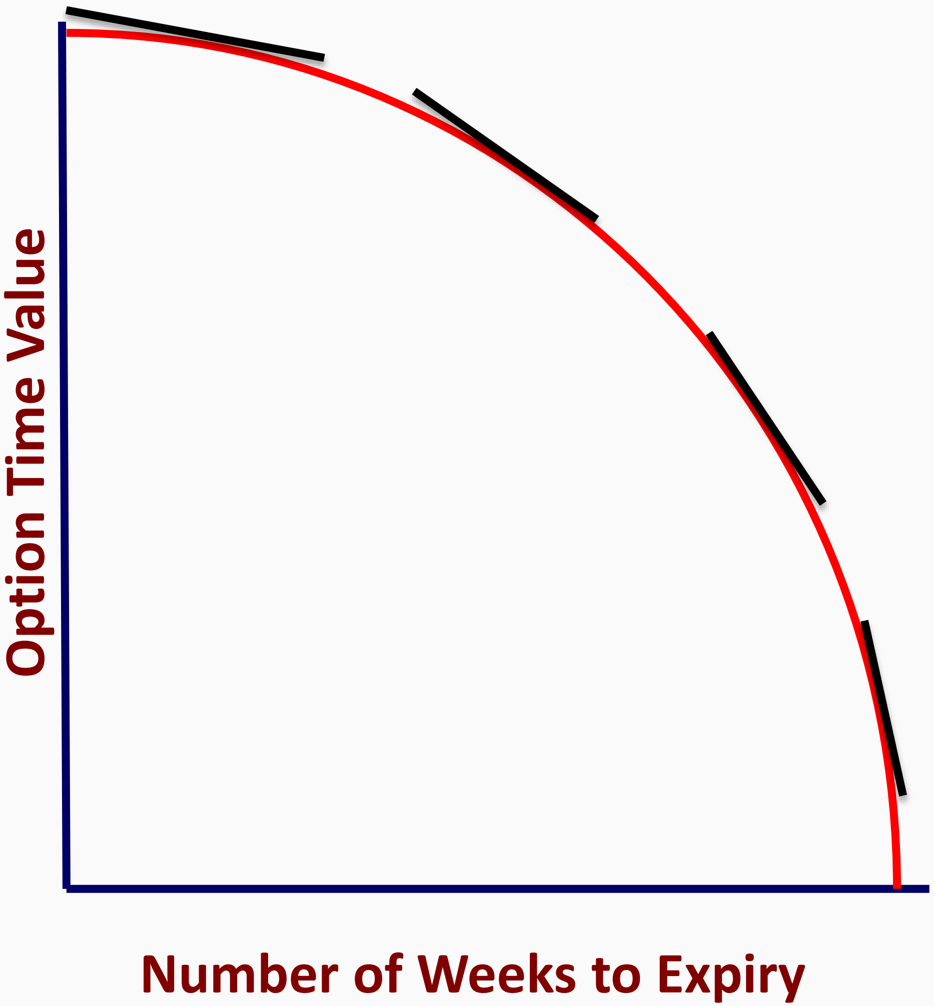


Q: Theta – Friend or Foe?
A: Yes

- **Options - wasting assets**
- **Time premium decays as time passes**
- ***Theta – 1-day's worth of time-decay;* accelerates as one approaches expiry**
- **Early (high) on the curve, theta is low, increases as curve slopes more aggressively downward, & is very high at the bottom (with little time to expiry)**



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- Options - wasting assets
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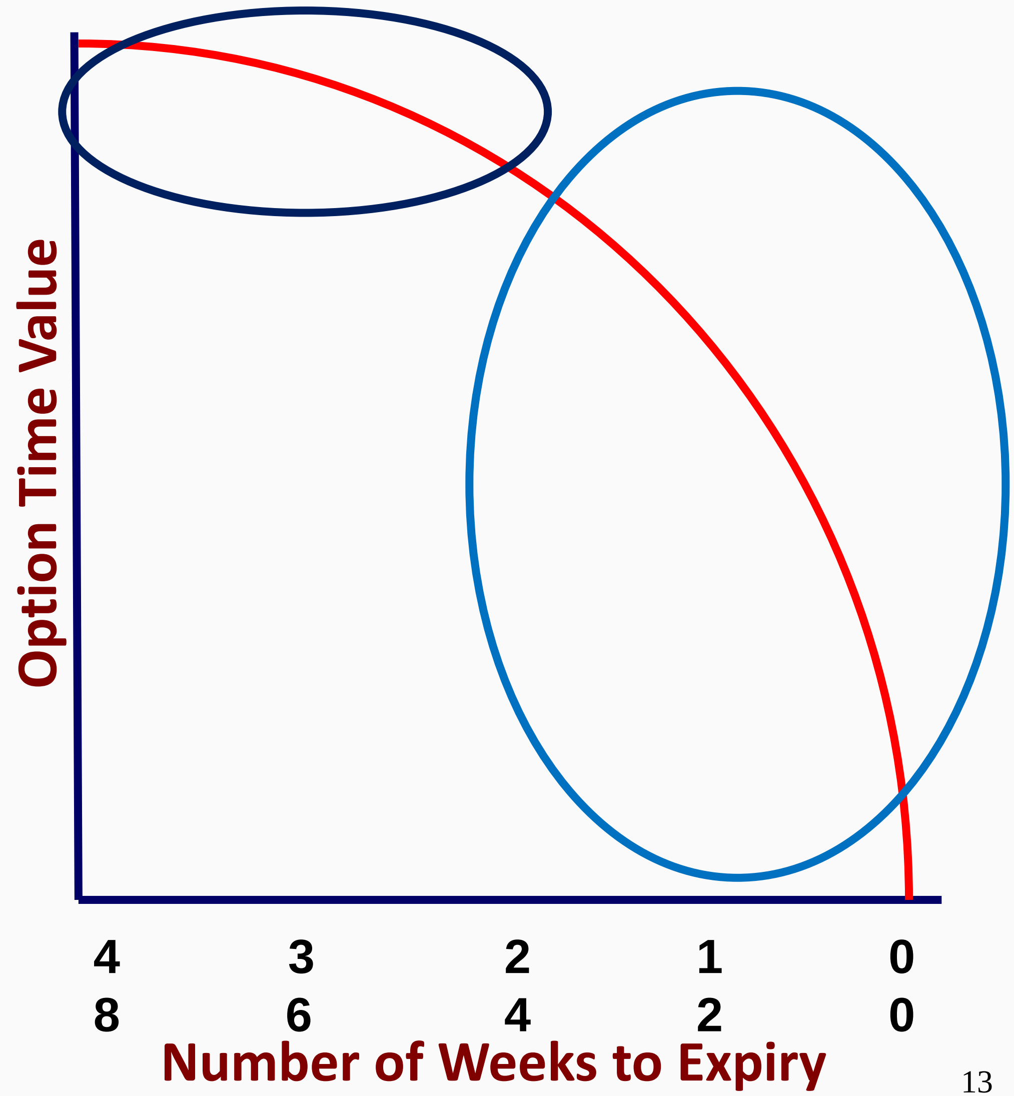
- Theta – 1-day's worth of time-decay; accelerates as one approaches expiry
- Early on the curve, theta is low, increases as curve slopes more aggressively downward, & is very high at the bottom
- Varies between symbols
  - 8, 6, 4, 2
  - 6, 4.5, 3.0, 1.5
  - 4, 3, 2, 1



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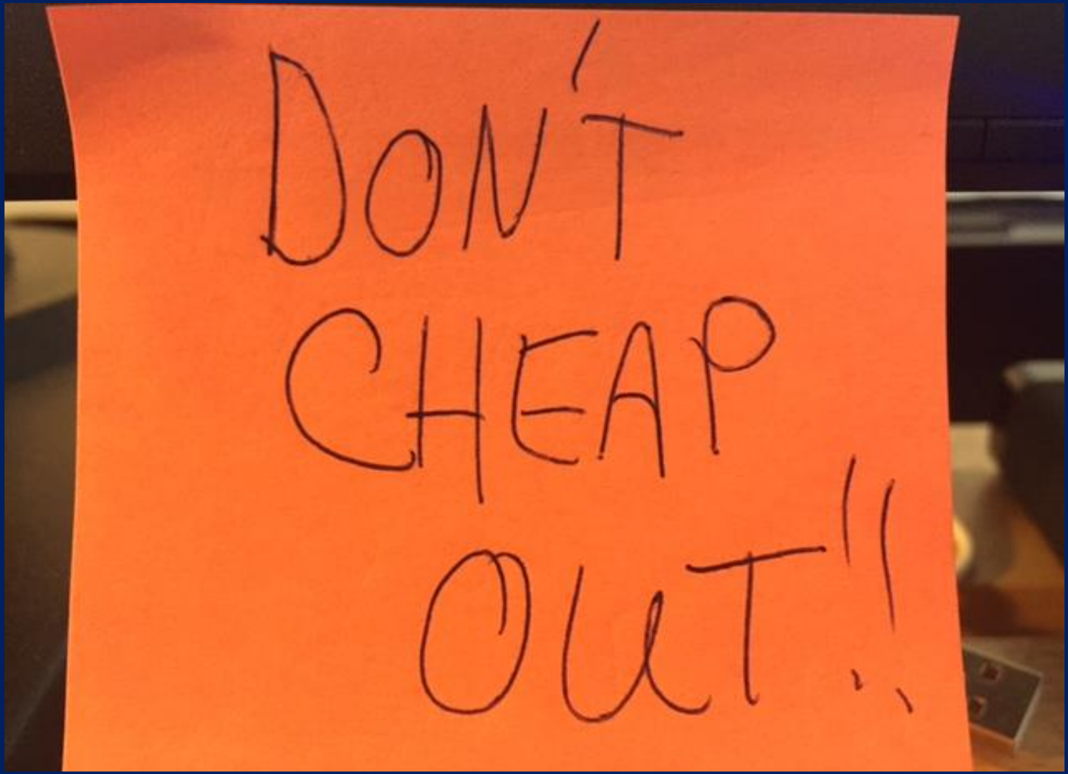
Buy enough time so that Theta (time-decay) doesn't ruin your trade…you'll spend more, but you'll get back more when you close the trade.

Doing the IV-rush
on the über-cheap won't work because time-decay will overtake the gain from IV.



Don’t Cheap Out!!!

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- When buying puts/calls or any debit spread, be a “thrifty shopper.” Look for value & Don’t Cheap Out.
- Paying for more time always makes sense, e.g., you may pay $2 for one month of time vs a total of $2.80-$3.00 for two months. Advantages:
    - unit price for the time is less
    - rate of time-decay starts out SIGNIFICANTLY less, saving you $ as the IV-rush plays out
- While you paid more for time, when you close the trade, you’ll get more back and lose less during the trade, letting you keep more profit from the IV-rise. You may pay $2.50 vs $1, but at the end of the trade you recover:
    - $2.20 (a loss of 0.30 time-value) in the first instance
    - $0.25 (a loss of 0.75 time-value) in the second instance

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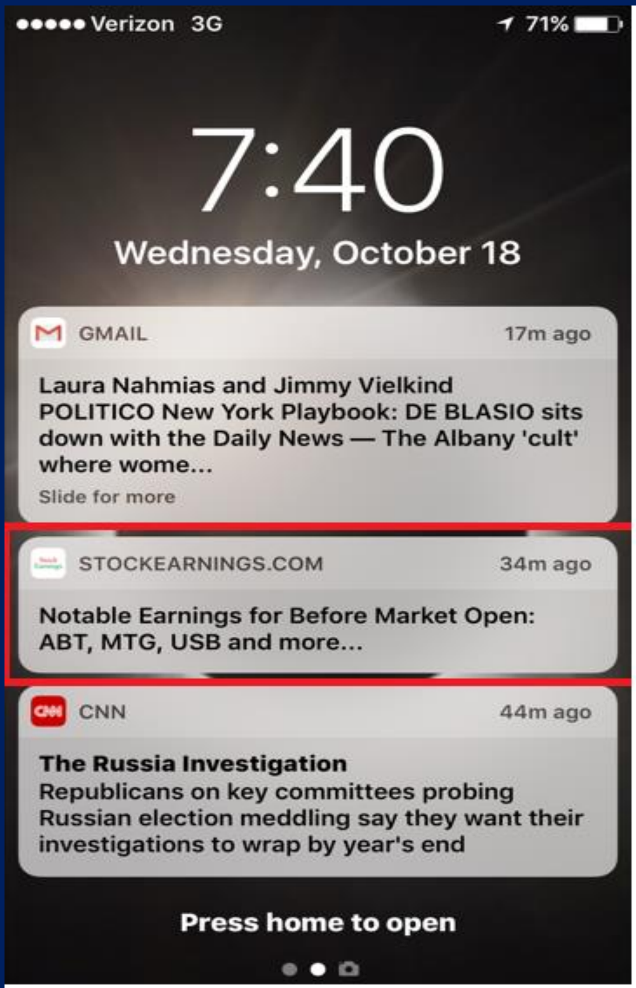

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IV rank = VL **L M H VH, Trend: weak confirmed UT, positional trade if LULU reaches 63.84 (put or bear-put vertical) or 60.09 (long) by entry period, otherwise go neutral**

Clarification

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At the end of the presentation there were questions that deserve further clarification:

Q: Someone asked about the timing of the buys to get into trades and the charts presented, and whether the term "days" refers to CALENDAR days and/or TRADING days.

A: In general, and in the presentation, use of "days" with options refers to CALENDAR days. In an options platform, all references to days-til-expiration are calendar days. Similarly, the daily charts from the presentation showing where the rise in IV starts leading into earnings are calendar days. To show the comparison between calendar and trading days, in the last trend line on the AMZN IV-chart included in the chart section there is a label that includes (1) how much TIME (CALENDAR DAYS) is covered as well as how many PRICE BARS (TRADING DAYS) are covered . You can see that the line reflects 44 (calendar days), but 31 bars (trading days). Given that this is a daily chart & the line covers 7+ calendar weeks, the 44 calendar days are made up of 31 trading days (BARS) plus 13 weekend days (SATs/SUNs)

Q: Someone asked when we begin introducing further insight about trades to the StockEarnings platform & phone alerts will these also include shorter duration trades.

A: The focus of the presentation was the IV-rush trade, which by design capitalizes on the rise in IV in the weeks leading up to an earnings announcement. But we will also be providing data and strategy suggestions for other types of earnings trades, too. Future presentations will concern other strategies.

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Thanks for attending and your attention. It’s a always a pleasure talking trading with our friends and clients…

Questions, Comments, Suggestions, want to see this info on the website and receive phone alerts re IV-rush trades as part of our of subscription service, reach out to us!!

- support@stockearnings.com