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TRADING OPTIONS LIKE THE PROS

Learn How to Become the House

DAVID
BERNS

MICHAEL
GREEN

THE LITTLE BOOK



OF
TRADING
OPTIONS LIKE
THE PROS


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WILEY

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For my Carolee & Henry, who bring magic to us all.

—DB

To Jennifer, Ryan, Ella & Gavin.

The journey has been the reward.

—MG

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Preface



RETAIL OPTIONS TRADING HAS exploded in popularity over the past few years. But options are complex, and trading options can quickly become a black hole of losses. The goal of this book is to show new options traders how to quickly pivot from naïve strategies with a high probability of loss to a winning strategy deployed by professional options traders. After a quick review of the option ecosystem and the basics of options, we spend most of the book presenting a proven options trading strategy. This strategy is a bread-and-butter trade from the institutional world of hedge funds and market makers, and we show you how to execute it at home. We have also decided to support readers of this book beyond just the words found here, by making the option screener reviewed in this book available for free at www.tradingoptionslikethepros.com.

This book is intended for nonfinance professionals. We have avoided the use of advanced mathematics to keep this accessible for all. We have thrown in a few “Adult Swim” sections for those who want to go a bit deeper on topics, but these are not required reading, so feel free to skip these if you want to keep things light.

Let’s now quickly review what will be covered in each chapter.

Chapter 1. Trading Options: Allure vs. Reality. We review the recent rise of retail options trading, which has boomed on the heels of easy access to trading and an expansive social media ecosystem for amateur traders. We then illustrate how the combined human biases of loss aversion and overestimation of low-probability events leads novice traders into buying cheap options. We then show that most cheap options expire worthless, leaving amateur traders destined to perform poorly. This discussion lays the groundwork for the winning option strategy we will cover in this book: selling cheap options for small yet consistent wins.

Chapter 2. The Barebones Option Primer. We begin with a review of the defining characteristics of an option: calls versus puts, the underlying asset, strike, and expiry. We review the basic payoff structure of an option as a function of the underlying price at contract expiry. We bring time into the equation, showing how the value of an option contract evolves into expiry, which then forces us to break